

Stamp Duty Land Tax - An unexpected consequence for rural property transactions?

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CATEGORY:
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Background

Last year's Budget contained very little of note. One of the most significant changes was the proposed 5% rate of SDLT for residential property purchases over £1m. This new rate is due to apply from 6 April 2011. The rate for non residential property remains at 4%.

This change may pose something of a problem for those involved in rural property transactions where only part of the asset being purchased can be classified as 'residential'.

Residential property

The definition of residential property is a building or structure that is used or is suitable for use as a dwelling together with any related land that is garden or necessary for the reasonable enjoyment of that dwelling having regard to its size and character. Land in excess of 0.5 hectares will be scrutinised. This mirrors the test for private residence relief for capital gains tax purposes.

Significantly, where six or more properties form part of a single transaction, the SDLT rules, rates and thresholds for non residential property apply.

Problem

Parties negotiating a transaction that is subject to SDLT will have to agree the value that is to be apportioned to the residential and non residential components. With differential rates of SDLT, this puts the parties on a potential collision course, which is unlikely to have been anticipated when the Chancellor stood up to deliver his Budget speech last year.

A seller will want a high value attributed in the contract to the principal house and curtilage if this will qualify for principal private residence relief as it will reduce the seller's capital gains tax exposure. In contrast, the buyer will want as low a value as possible attributed to the principal house and a tight definition of curtilage as this will minimise the additional 1% SDLT that will apply from 6 April of this year.

Where the subject of a transaction is a rural estate with a mixture of commercial property, agricultural land, woodland and six or more residential properties, the rate of SDLT should remain unaffected by the proposed changes. If there are fewer residential properties there could be an issue.

Commentary

For selling agents, these difficulties may have a bearing on how best to lot a sale. A seller will, in any event, want to retain the right to determine the apportionment of the sale price to ensure that his capital gains tax exposure is minimised; this will need to be negotiated as a term within the sale contract.

This means that, so far as a buyer is concerned, agreeing the apportionment of the purchase price will become an essential part of the initial negotiation process between agents. Buying agents would be advised to consider this apportionment in their offer letters for mixed use properties.

For any transaction where substantial performance (the date of completion or the date of payment of over 90% of the purchase price) is to take place after 5 April 2011, there should be an agreed apportionment of the price between the residential and non residential components in the heads of terms. This can be imported into the sale contract and will avoid any problems arising at an advanced stage of the transaction.

All of this should be considered in the knowledge that HMRC will look at a transaction in the round and may amend or even ignore any apportionment if they do not consider it to be a 'just and reasonable' reflection of true value.

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