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Stamp Duty Land Tax: non-UK resident surcharge consultation

Response by the Chartered Institute of Taxation

1 Introduction

- 1.1 The CIOT responds to the consultation on a 1% Stamp Duty Land Tax (SDLT) surcharge on non-UK residents purchasing residential property in England and Northern Ireland.¹
- 1.2 It is understood that this consultation is outside the policy consultation annual cycle as the intention is to introduce the surcharge in a future (unspecified) Finance Bill. Therefore, the consultation is not stated as taking place at a particular stage of development in the annual cycle.
- 1.3 As an educational charity, our primary purpose is to promote education in taxation. One of the key aims of the CIOT is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 1.4 Our stated objectives for the tax system include the following that are of particular relevance to this consultation:
 - A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
 - Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
 - A responsive and competent tax administration, with a minimum of bureaucracy.

2 Executive summary

- 2.1 The stated policy intent of the introduction of the surcharge is to help control house price inflation and thereby assist UK residents in getting onto the housing ladder in line with the government's wider objectives on home ownership. The effect of recent SDLT changes to residential property should be evaluated as a precursor to introducing the new surcharge that will apply as an extra layer on top of those existing rates. In addition, a policy measure aimed at house price inflation should be considered in the context of other recent taxation

¹ SDLT ceased to apply to land transactions in Scotland from 1 April 2015 when it was replaced by Land and Buildings Transaction Tax (LBTT). Similarly, Land Transaction Tax (LTT) replaced SDLT in Wales from 1 April 2018.

changes affecting non-UK resident purchasers including the restriction on deductibility of interest, the introduction in 2015 (and the extension in 2019) of non-resident capital gains tax and the extension of the inheritance tax relevant property regime to non-UK companies owning residential property in 2017. The full impact of these measures has yet to be seen.

- 2.2 SDLT has become a highly complex tax that has been the subject of technical change in virtually every year since its introduction. The introduction of the higher rates in 2016 and first-time buyers' relief in 2018 compounded that complexity by requiring that, in the context of a transaction tax, decisions need to be made about the intended future use of the property being acquired.
- 2.3 In terms of routine administration, the brunt of this complexity is borne by conveyancers who generally complete SDLT returns (in the recently reduced timeframe of 14 days after the effective date of the transaction) but often do not have tax expertise.
- 2.4 We also raise the possibility of these proposals being contrary to EU law. This is because the surcharge would mean that the SDLT rules treat non-UK residents differently to UK residents in respect of identical transactions involving residential property in England and Northern Ireland.
- 2.5 The proposed residence test for individuals is to treat individuals as non-UK resident if they spent fewer than 183 days in the UK in the 12 months ending with the date of the transaction. This test has the advantages of relative simplicity and ease of application in the context of a specific transaction date determining liability. The Statutory Residence Test (SRT) that applies for income and capital gains tax is, on the other hand, a backward looking test applied at the end of a tax year and therefore not easily adapted to a transaction-based tax, as recognised by the consultation. There is therefore some logic in adopting the simpler test for non-UK resident individuals.
- 2.6 However, it appears to be consistent with the policy intent to provide for a refund of the surcharge where:
 - an individual is UK resident under the SRT in the tax year in which the transaction occurs; and
 - where an individual is resident for more than 183 days in any rolling 365-day period commencing 12 months before and ending 12 months after the transaction.
- 2.7 While it is recognised that trustees and advisers of settlements will generally be more familiar with the Statutory Residence Test (SRT), the SRT requires many aspects to be assessed over the tax year (for example does the taxpayer have a home in the UK in any 90-day period in the tax year). Therefore, a rewrite of these factors for an alternative 12-month period will be prohibitively complex. It seems therefore that using the alternative 183-day test for individual trustees (as for individuals) is, on balance, to be preferred.
- 2.8 The proposed company residence test is based on incorporation or the location of central management and control. The test of central management or control is not easily applied at the effective date of the transaction. Alternative approaches might be to ascertain central management and control by reference to the current or preceding accounting period or by reference to the 12 months leading up to the transaction date.
- 2.9 It is proposed that, to ensure consistency of treatment between non-UK residents acquiring residential property directly and indirectly, a UK resident close company (broadly one that is under the control of one or more non-UK resident persons) will also be liable to the surcharge. To achieve this end, current statutory rules for close companies will apply. These rules although established, are extremely complex and difficult to apply by reference to a specific transaction date rather than an accounting period. Their application will require detailed tax advice and analysis within a 14-day filing period. Consequently, the objective of consistency needs

to be balanced against the complexities of the application of the test and the consequences for the smooth operation of the conveyancing process.

- 2.10 It is noted that the government is considering an upfront relief for Crown employees who are on overseas postings. It is not clear to us why that relief should not apply equally to employees on fixed term secondment overseas in the private sector who are subject to UK income tax.
- 2.11 The need for SDLT refunds is effectively built into these proposals (in addition to the current need to reclaim SDLT for the higher rates) and will impose administrative burdens and costs on both taxpayers directly and upon HMRC systems and resourcing. We assume that these costs will be recognised and evaluated in the context of the case for introducing the surcharge, as part of the information and impact note when these proposals are finalised.

3 Policy intent

- 3.1 The stated policy intent behind the introduction of the surcharge is to help control house price inflation and thereby assist UK residents in getting onto the housing ladder in line with the government's wider objectives on home ownership. The consultation points to evidence that purchases of property by non-UK residents are inflating house prices for UK residents. The source of this evidence is not set out in the consultation document. However, the following links to evidence have been provided by HMT as part of the consultative meetings:

<https://www.kcl.ac.uk/sspp/research/economics/People/FilipaPaper-June2017.pdf>

<https://www.london.gov.uk/moderngovmb/documents/s58641/08b2c%20University%20of%20York%20data%20report.pdf>

The economic and demographic analyses are outside our remit. However, we make the following observations. The assessment of the economic effect of the surcharge in terms of house price inflation should be considered from the supply side as well as demand including the effects on the supply of new homes, (particularly affordable housing) and the build to rent sector in terms of forward funding by overseas buyers. The research above, published in June 2017, inevitably considers data based on earlier transactions. The effect of Brexit and changes to the taxation of residential property are unlikely to be fully reflected in the data.

- 3.2 The higher rates of SDLT for purchases of additional residential property and first time buyers' relief in 2017 were also part of the government's policy of supporting home ownership. As set out in the tax policy making process paper published on 6 December 2017² the government recognises the critical need to monitor and evaluate tax policy. It seems appropriate therefore that previous SDLT measures should be evaluated as a precursor to introducing the new surcharge that will apply as an extra layer on top of those existing rates. In addition, a policy measure aimed at house price inflation should be evaluated in the context of other recent taxation changes affecting non-UK resident purchasers including the restriction on deductibility of interest, the introduction in 2015 (and extension in 2019) of non-resident capital gains tax and the extension of the inheritance tax relevant property regime to non-UK companies owning residential property in 2017. The full impact of these measures is yet to be seen.

² <https://www.gov.uk/government/publications/the-new-budget-timetable-and-the-tax-policy-making-process/the-new-budget-timetable-and-the-tax-policy-making-process#the-consultation-process>

- 3.3 One of the ten steps towards making tax policy better in the *Better Budgets*³ report is to ensure that an effective and routine post-legislative review takes place to determine whether or not measures are achieving their objectives at an acceptable cost. As part of this exercise the report also recommends that data is made more accessible to allow outside researchers to evaluate policy. It would be helpful therefore to publish more widely the source of the evidence that non-UK resident buyers are inflating house prices to the detriment of UK residents.
- 3.4 SDLT has become a highly complex tax that has been the subject of technical change in virtually every year since its introduction. The introduction of the higher rates in 2016 and first-time buyers' relief in 2018 compounded that complexity by requiring that, in the context of a transaction tax, decisions need to be made about the intended future use of the property being acquired. The need to make judgements about the future use of property and now, the residence status of the buyer, is not readily compatible with a transaction tax and undermines the coherence of the SDLT code. The surcharge adds 1% to the rate of SDLT that would otherwise have applied thereby effectively doubling the number of SDLT rates that can apply to the acquisition of residential property.
- 3.5 In terms of routine administration, the brunt of this complexity is borne by conveyancers who generally complete SDLT returns (in the recently reduced timeframe of 14 days after the effective date of the transaction) but who may not have tax expertise. It is recognised that the current proposals are as far as possible intended to be as simple as possible for taxpayers who are not engaging professional advisers and for conveyancers. However, the fact remains that the complexity of the SDLT code will be compounded by the surcharge with potentially adverse consequences for the conveyancing process.

4 EU law and other possible conflicts

- 4.1 We raise the possibility of these proposals being contrary to EU law⁴. This is because the surcharge would mean that the SDLT rules treat non-UK residents differently to UK residents in respect of identical transactions involving residential property in England and Northern Ireland.
- 4.2 It is accepted that the EU fundamental freedoms can be restricted if there is a justification for doing so, the measure is proportionate and is reasonably necessary to achieve the stated aim. The policy aims of this measure are around housing policy and a stated aim is to help to control house price inflation. We understand that it is the government's view that the implementation of the surcharge would not breach any EU law fundamental freedoms, on the grounds that it is justifiable and proportionate in relation to giving effect to the government's housing policy, so it could be implemented before the UK leaves the EU. We cannot easily see that this proposed measure is justifiable or proportionate in relation to housing policy. Thus we consider that the surcharge could be liable to challenge under EU law.

We have considered the case of *Staatssecretaris van Economische Zaken and another v Q* [2015] STC 2196 where it was held to be legitimate to have a national focused heritage exemption. However, in that case the discrimination related to the situs of the land rather than the residence status of the taxpayer. The proposed

³ https://www.instituteforgovernment.org.uk/sites/default/files/publications/Better_Budgets_report_WEB.pdf Better Budgets is a collaboration between the Chartered Institute of Taxation, the Institute for Fiscal Studies and the Institute for Government.

⁴ We understand that it is still government policy that the UK should leave the EU on the basis of the Withdrawal Agreement negotiated between the EU and UK and finalised on 14 November 2018. If the Withdrawal Agreement is approved by Parliament and, therefore, comes into effect on the UK's exit from the EU, the fundamental freedoms will continue to apply during the transition period. This period will run at least until the end of 2020.

difference in treatment if the surcharge is implemented would appear to us to undermine the relevant freedoms and we are not immediately aware of any cases that support the conclusion that it would be considered justified or proportionate.

- 4.3 The compatibility of the proposed surcharge with human rights legislation and existing trade agreements should be part of the assessment of impacts.

5 Question 1: Do you have any views on the proposed SDLT residence test for non-UK resident individuals?

Question 2: Would you prefer to see a different residence test applied? If so, what test and why?

- 5.1 The proposed residence test is to treat individuals as non-UK resident if they spent fewer than 183 days (a day being the end of a day based on presence at midnight) in the UK in the 12 months ending with the effective date (the earlier of completion or substantial performance). Adopting an additional test of residence in itself adds to complexity, however this test has the advantages of relative simplicity and ease of application in the context of a specific transaction date determining liability. One alternative, the statutory residence test (SRT), on the other hand, is a backward looking test applied at the end of a tax year and therefore not easily adapted to a transaction-based tax, as recognised by the consultation. There is therefore some logic in adopting the simpler test for non-UK resident individuals.
- 5.2 While having the advantage of relative simplicity, the test is something of a blunt instrument as it does not distinguish differences in the nature of the population being targeted for example, a non-UK national who spends little time in the UK (both before or after purchase) meets the test for non-UK residency and therefore the imposition of the surcharge (presumably in accordance with the policy intent) as may a UK expatriate working abroad temporarily who buys a house in anticipation of permanent or long term return to the UK (presumably outside the policy intent). In addition, the test presents difficulties where there are joint purchasers with differing status as acknowledged in the consultation. To the extent that liability falls on taxpayers outside the policy intent, it will be necessary to extend the refund mechanism (see our suggestions at para14) or to include specific exemptions (see [para 13]).
- 5.3 The proposed residence test for non-UK resident individuals is fewer than 183 days in the UK in the 12 months ending with the effective date. The effective date is the earlier of completion or substantial performance (FA 2003 sections 44(3) and (4)). Where the contract is substantially performed and subsequently completed by a conveyance, both the contract and the conveyance are notifiable transactions and tax is chargeable on the conveyance to the extent, if any, that the amount of SDLT chargeable on it is greater than the amount chargeable on the contract (FA 2003 section 44(8)). How will the residence test apply in these circumstances? Will the day count end at the date of substantial performance or at completion?
- 5.4 Guidance will be required on the type of evidence required by HMRC to establish residence, both for the day counting test and for refund eligibility, such as flight details, boarding passes. The guidance will need to be published well in advance of the surcharge coming into effect given that the test applies to the 12 months prior to the effective date of the transaction.
- 5.5 The consultation refers to the government's consideration of alternatives tests but only specifically considers the SRT. We are aware that other jurisdictions have adopted tests based on citizenship or nationality. However, these alternatives would appear to be potentially incompatible with EU and human rights

legislation and pose the same difficulties as the current proposed residence test (such as imposing liability for joint purchases involving UK citizens).

- 5.6 We have not responded to Question 3 (How will the proposed surcharge on residential properties affect purchase decisions of non-UK resident individuals in England and Northern Ireland?) or to Question 4 (Do you agree that a rate of 1% for the surcharge is set at the right level to balance between the government's objectives on home ownership and the UK remaining an open and dynamic economy?) as these questions fall outside our main areas of expertise.

6 Question 5: Do you have any views on the proposed company residence test for the surcharge?

Question 6: Would you prefer to see a different residence test applied? If so, what test and why?

- 6.1 The proposed company residence test is based on incorporation or the location of central management and control (Corporation Tax Act 2009 Part 2 Chapter 3). If the company is not UK resident under these tests, it will be treated as a non-UK resident purchaser and subject to the surcharge.
- 6.2 The test of central management or control is not easily applied at the effective date of the transaction, for example, would a board meeting held outside the UK on that date indicate non-UK residence in this context? Alternative approaches might be to ascertain central management and control by reference to the current or preceding accounting period or by reference to the 12 months leading up to the transaction date.

7 Question 7: Do you have any views on non-UK resident individuals using UK resident companies to purchase residential properties?

- 7.1 Our members indicate that recent changes to the taxation of corporate entities that hold residential property, particularly the introduction of the non-resident CGT charge and the removal from excluded property treatment for inheritance tax of non-UK companies owned by non-UK domiciliaries, may point towards the use of a UK company for non-UK resident buyers acquiring UK residential property in a corporate entity. However, other factors such as the current political uncertainty in relation to Brexit and concerns around the extent and pace of change to the taxation of UK residential property, may also affect the choice of jurisdiction.

8 Question 8: Do you have any views on the suitability of using the close company test as the basis for determining whether a company is under the control of non-UK resident persons?

Question 9: Do you have any views on applying the attribution of rights rules at section 451 CTA 2010 between persons of differing residence status?

Question 10: Do you have any views on potential problems which might arise when using the definition of control at section 450 CTA 2010?

- 8.1 It is proposed that, to ensure consistency of treatment between non-UK residents acquiring residential property directly and indirectly, a UK resident close company under the control of one or more non-UK resident persons, will be liable to the surcharge.

8.2 It should be recognised that the close company definition (CTA 2010 section 439), although established, is extremely complex and difficult to apply by reference to a specific transaction date rather than an accounting period. The initial definition involves a great many additional defined terms, such as control, participator and loan creditor; the application of the rules requires the attribution of the rights of associated persons. The interaction of the attribution rules and the proposed SDLT tests for residence of individuals or trustees who 'control' the company will require detailed specialist tax advice and analysis. The objective of consistency needs to be balanced against the complexities of the application of the test.

8.3 Where the surcharge has applied as a consequence of these rules but the residency status of a participator changes through spending 183 days or more in the UK in the 12 months following the transaction, consistency of approach also requires that a refund should be available (see further at paragraph 14 below).

9 Question 11: Do you have any views on whether any of the exemptions at S442 to S447 CTA 2010 should remain in place or be removed for the purposes of the surcharge?

9.1 We have no comments on the exemptions the application of which is largely a matter of policy. However, we note that the exemption for non-UK resident companies appears necessary to eliminate a double charge.

10 Question 12: Would you prefer to see a different test applied (for UK resident companies with non-UK resident participators)? If so, what test and why?

10.1 As we note above, the consistency objective needs to be balanced against the adoption of the close company attribution test that was not designed to apply to a transaction based tax.

11 Question 13: Do you have any comments on the proposed treatment of partnerships as joint purchasers?

Question 14: Do you think there should be different test applied for purchases by partnerships? If so, what test and why?

11.1 It is not clear from the consultation (paragraph 3.30) whether the rules in Part 3 of Schedule 15 will apply to reduce or remove the amount subject to the surcharge. Confirmation is requested.

12 Question 15: Do you have any views on the proposed SDLT treatment where the acquisition is made by a trust?

Question 16: Do you agree that the Statutory Residence Test (SRT) for individual trustees will work for SDLT if references to tax year are replaced by references to the 12- month period ending with the date of the transaction? If not, why not? What alternatives would you propose?

12.1 While it is recognised that trustees and advisers of settlements will generally be more familiar with the SRT, the latter test requires many aspects to be assessed over the tax year (for example does the taxpayer have a home in the UK in any 90-day period in the tax year). Therefore, a rewrite of these factors for a different 12-month period will be prohibitively complex. It seems therefore that using the alternative 183 day test for

individual trustees is to be preferred with the availability of a refund in the additional circumstances proposed under Question 20 below.

- 12.2 In relation to Question 17 (How will the proposed surcharge on residential properties affect purchase decisions of non-UK resident non-natural persons (companies, trusts and partnerships) in England and Northern Ireland?) our observations at Question 7 are relevant here also.

13 Question 18: Do you have any comments about the proposed reliefs from the surcharge?

Question 19: Are there any other categories of individual which you think the Government should consider providing a relief for and, if so, why?

- 13.1 It is noted that the government is considering an upfront relief for Crown employees who are on overseas postings. It is not clear to us why that relief should not apply equally to employees on fixed term secondment overseas in the private sector who are subject to UK income tax.

14 Question 20: Do you have any views on the proposed refunds available for those who have paid the surcharge?

Question 21: Do you have any views on the criteria the government is suggesting determining whether a purchaser would be eligible for a refund?

- 14.1 We consider that it would be consistent with the policy intent to expand the eligibility for a refund of the surcharge to include circumstances where:

- an individual is UK resident under SRT in the tax year in which the transaction occurs;

It seems both consistent with the policy intent and equitable as residence under the SRT can be established by virtue of a home in the UK such that the surcharged transaction could itself lead to SRT residence.

- where an individual is resident for more than 183 days in any 365-day period commencing 12 months before and ending 12 months after the transaction.

The current test for a refund looks back to the 12 months prior to the transaction and forward to the 12 months' post transaction. If 100 days are spent in the UK before the transaction and 100 days afterwards, no refund would be available despite spending more than 183 consecutive days in the UK. This suggestion addresses this inequity.

- 14.2 In addition, although the consultation states that a refund will not be available where a UK company is liable to the surcharge as a result of the close company test, the reason for this approach is not stated. It appears consistent with the policy objective to allow a refund where the surcharge has applied as a consequence of these rules but the residency status of a participator changes through spending 183 days or more in the UK in the 12 months following the transaction.

15 Question 22: Do you have any views about how the reliefs will apply in relation to the surcharge?

15.1 First time buyers' relief

It is not clear why the surcharge should apply to a non-UK resident individual who qualifies for first time buyers' relief as one of the conditions for that relief is that the buyer intends to occupy the property as their main residence. Although it should be possible for the taxpayer to subsequently claim a refund, the objection to upfront relief from the surcharge outlined in the consultation at paragraph 4.13 is that the future intentions of the purchaser may or may not be carried through. It seems inconsistent to use this uncertainty to deny an upfront relief from the surcharge while first time buyers' relief relies upon the intention.

15.2 Multiple dwellings relief (MDR)

The consultation refers to the minimum rate of tax for MDR of 1% that will remain at the same level. It is noted in passing that if the transaction is a higher 3% rates transaction, the higher rates apply and therefore the minimum rate would be 3% increasing to 4% with the surcharge.

15.3 Exercise of collective rights by tenants (collective enfranchisement)

We note that the analysis at paragraphs 5.14 – 5.17 of the consultation document does not cover the potential application of FA 2003 section 117(6) (6 or more dwellings are the subject of a single transaction treated as non-residential) that could apply to a collective enfranchisement that includes non-UK resident tenants, whether or not under a particular statutory procedure and whether or not involving a company strictly as bare trustee (as distinct from nominated or appointed) or corporately.

Leaving aside the application of section 116(7), if the purchaser is acting as nominee or bare trustee for the tenants it is proposed that the surcharge will apply to the whole of the consideration if any of the leaseholders are non-resident. It does not seem equitable that tenants acting together to exercise a statutory right to purchase the freehold of a block should incur the surcharge because one of the tenants is non-UK resident for surcharge purposes. An alternative might be to apply the surcharge if a minimum threshold proportion, say 25%, of the participating tenants were non-UK resident.

16 Question 23: Do you have any views on the proposed treatment where there is an interaction between existing SDLT rules and the surcharge?

16.1 In accordance with other provisions in tax code, and, in particular, FA 2003 Schedule 4ZA paragraph 9: Spouses and civil partners purchasing from one another) we consider that there should be an exemption for a transfer from one spouse or civil partner to another spouse or civil partner who is non-UK resident.

16.2 The consultation does not address the scope of residential property for the purposes of the surcharge. It is understood that the scope will be aligned, at least in part, with that of the higher rates in FA 2003 Schedule 4ZA thereby excluding, for example, the grant of a lease of no more than 21 years.

17 Question 24: Do you have any views on the proposed approach for administration and compliance for the surcharge above? Question 25: Are there any other changes to the administrative and compliance provisions in SDLT that the government should consider changing for the purposes of the surcharge?

17.1 The further need for SDLT refunds is effectively built into these proposals (in addition to the current need to reclaim SDLT for the higher rates) and will impose administrative burdens and costs on both taxpayers directly

and upon HMRC systems and resourcing. We assume that these costs will be recognised and evaluated in the context of the case for introducing the surcharge, as part of the information and impact note when these proposals are finalised.

- 17.2 In some cases, it may be necessary to make separate refund claims for both the higher rates and for the 1% surcharge.
- 17.3 We note that changes will be required to the SDLT return including the possibility of a new code or codes for a surcharged transaction. Using codes to designate the nature of a transaction has the advantage of simplifying and reducing the length of the return. However, where a code represents a relatively complex set of circumstances including conditions for residency, there is nothing on the face of the return that focuses the mind of the buyer on the representations being made. It may be preferable to include specific questions on the return to make the relevant circumstances explicit.

18 Acknowledgement of submission

- 18.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

19 The Chartered Institute of Taxation

- 19.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 18,500 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation

10 May 2019