

Number 8

Stamp Duty: More Tax on Land (and Transitional Provisions)

As trailed in last year's Budget, this year's Budget and the Finance Bill 2003 contain provisions for a new stamp tax to be called Stamp Duty Land Tax ("SDLT"). The Inland Revenue currently says this will take effect on 1 December 2003 (and in this bulletin we assume that will be the date), but there will be important transitional provisions for transactions before then, so the date of Royal Assent (some time in early to mid July) will also be important.

The proposal for SDLT is a complete rewriting of stamp duty law and procedure in relation to UK land and interests in UK land, but this bulletin will focus on:

- 1 mainstream transactions on which SDLT will fall more heavily than stamp duty did; and
- 2 the transitional provisions e.g. for agreements before 1 December 2003.

More Tax

Stamp duty is a tax on documents. SDLT is to be a tax on "transactions" and so liability may arise whether or not there is a document and whether any document is held in the UK or elsewhere. Subject to limited exemptions, SDLT will apply to the acquisition by transfer or creation of the following chargeable interests:

- 1 an estate, interest (legal or equitable), right or power in or over land in the UK; and
- 2 the benefit of an obligation, restriction or condition affecting the value of any such estate, interest, right or power.

So SDLT will apply to more than just freehold and leasehold transfers and the creation and surrender of leases.

SDLT will also apply to the surrender, release or variation of any chargeable interest, which means, for example, that it will apply to the variation of a lease. Similarly it will apply to the creation, surrender, release or variation of a restrictive covenant or condition affecting the value of land. Stamp duty has in the past applied to options but SDLT will also apply to "pre-emption rights" where they prevent the grantor of the right from entering into, or restrict the right of the grantor to enter into, a land transaction.

The timing of SDLT's commencement is of particular importance for transactions which may be subject to SDLT but were not subject to stamp duty, or where the SDLT payable may be more than would have been payable as stamp duty: for example:

- 1 granting of leases - because the proposal is for new leases to attract SDLT on the premium at a rate of up to 4% as before, but also on the "net present value" of the aggregate of the rents over the lease term at a rate of 1%. This will result in a substantial increase in the tax payable under SDLT for new leases and may encourage shorter lease terms and, given the obligatory nature of

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SDLT (there is intended to be no vestige of the partially “voluntary” nature of stamp duty) greater focus on whether a landlord can grant a licence instead of a lease in particular cases;

- 2 exchanges of land – under the proposals SDLT would be payable on both of the properties being exchanged, whereas under previous practice (if structured correctly) stamp duty was payable only on the more expensive property. For SDLT there is to be an exception, subject to conditions, for residential part exchanges with house builders;
- 3 sub-sales and “resting on contract” present complications. The intention in the proposals is to remove the existing stamp duty exemption for sub-sales (the effect of the existing exemption was that in a sequence of initial sale and one or more sub-sales before completion only the final sale determined the amount of stamp duty, with the intention of avoiding double charging of stamp duty). The Inland Revenue’s ongoing consultation on this aspect seems to be limited in scope, for example to providing an SDLT exemption in relation to complex developments;
- 4 sales of companies and other vehicles with substantial property interests have been a concern since the 2002 Budget proposed applying the property rates of stamp duty to transfers of shares in such entities. Since then there has been consultation but we understand this issue is still a matter for consultation and it is not dealt with in the Finance Bill 2003. It is therefore unclear whether a new regime for property entities will be introduced or indeed how broadly it would be applied (e.g. would it be limited to true “single purpose vehicles” for holding property or could it extend to other businesses with a high property content, such as hotels, restaurants or serviced office accommodation providers?) For parties buying or selling who wish to avoid risk it would be prudent to contract if possible before the Finance Act achieves Royal Assent and, whether or not that can be achieved, at least complete before 1 December 2003;
- 5 transactions where the final price is contingent or uncertain – up to now under the “contingency principle” if there is a contingency with a maximum price then stamp duty would be charged on that maximum even if the maximum is not ultimately payable, and there is no mechanism for subsequent variation. Equally if a minimum price is stated but no other, under the “contingency principle” the minimum would be used for determining stamp duty. Since 1994 for transactions where the final price cannot be determined at all from the conveyance or lease, the market value is used for determining the stamp duty. This has meant for example that it is important to avoid mentioning a maximum price that is higher than the market value. The new proposal is for SDLT to be paid in relation to a contingent or uncertain price on the basis of a “reasonable estimate” of the likely price if it is uncertain, or if the maximum is known then SDLT would be charged on the maximum even though it is contingent. But there would also be provisions for variation of the SDLT payable, a repayment or additional payment of SDLT if the final price is different and a right to apply to defer payment. Transactions that involve contingent prices, such as “overage”, will need to take account of this aspect of SDLT and it will not be effective for SDLT purposes to specify a low minimum;
- 6 the kinds of consideration (what is used to pay the price for a land transaction) that will be charged to SDLT will be wider than for stamp duty because SDLT will be payable on any consideration in “money or money’s worth” and will include the carrying out of works or services; and
- 7 for SDLT there will also be new clawbacks of charity and demerger relief.

Transitional Provisions

The key determining date for SDLT is the “effective date” of the transaction. For transactions that are completed before being “substantially performed” (e.g. taking possession of substantially all of the property or payment of substantially all of the price) the effective date will be the date of completion.

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For transactions that are not completed before being “substantially performed” it will be the date of “substantial performance”. But SDLT will not be payable on transactions:

- 1 which are completed before 1 December 2003; or
- 2 which are completed on or after 1 December 2003 but are effected in pursuance of a contract entered into before the date of Royal Assent (July 2003) unless:
 - (a) there is a variation of the contract or assignment of rights under the contract on or after the date of Royal Assent; or
 - (b) the transaction is effected in consequence of the exercise of any option, right of pre-emption or similar right after the date of Royal Assent (surprisingly the Bill does not say “on or after” the date of Royal Assent, though that may change); or
 - (c) where the purchaser under the transaction is a person other than the purchaser under the contract because of a further contract made on or after the date of Royal Assent – this relates to sub-sales and “resting on contract”.

Despite its limitations, this exemption for pre-Royal Assent contracts may be useful.

Substantial performance before 1 December 2003 will not mean that completion on or after 1 December 2003 is free of SDLT – in that case the date of substantial performance is ignored and the effective date is the date of completion.

The transitional provisions create considerable problems of interpretation in relation to sub-sales and transactions where the parties are “resting on contract”, even for contracts entered into before Royal Assent. Purchasers under such contracts and purchasers from sellers who are sub-selling should take advice as soon as possible to establish their position under the transitional provisions.

There are further provisions applying to options and pre-emption rights exercised on or after 1 December 2003 and for those provisions it is important whether the option or pre-emption right was acquired on or after 17 April 2003 because if it was, the price for grant of the option or pre-emption right will be treated as part of the consideration chargeable to SDLT for the transaction resulting from exercise of the option or pre-emption right, and a similar treatment will apply to the price for any variation of such an option or right of pre-emption.

Of course the Finance Bill 2003 may be changed in Committee before Royal Assent (this bulletin reflects the position up to 16 June 2003), but there is clearly a need to begin planning for SDLT now.

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June 2003

Readers are advised to take specific advice before acting in reliance on the matters set out in this briefing.

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