

MODERNISING STAMP DUTY ON LAND AND BUILDINGS IN THE UNITED KINGDOM

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Background

The Inland Revenue issued a consultative document in April 2002 on the subject of modernising stamp duty on land and buildings in the UK. Various indications of the future for stamp duty can be gleaned from this document and the subsequent discussion process.

Towards the end of 2003, or the beginning of 2004, it will no longer be necessary to send in documents to the Stamp Office in the present way. Instead, there will be a standard form for notification which will be available electronically. Payment will be accepted by cheque, cash, BACs, CHAPs, as at present. Other electronic means of accepting payment are already being explored. Methods will be introduced to ensure that land registries can check that payment has been made in advance of registration. In due course, as a second part of this process, the land registries themselves will introduce electronic systems for conveyancing and other registration procedures. The aim is that these systems should replace the need to notify the Inland Revenue separately of a chargeable transaction.

Scope

A key feature of the changes overall is a new form of stamp duty transactions involving land and buildings in the United Kingdom. It should extend to transfers of substantial interests in entities (such as companies) owning mainly UK land. More particularly, in the consultative paper the Stamp Office suggest that the new rules would be likely to apply to:-

- the transfer of *substantial* interests (for example acquisitions of shareholdings of 30% or more), in
- certain *qualifying entities* including companies, partnerships, and other (possibly non-UK) vehicles,
- whose *major activity* involves the ownership or exploitation of UK land and buildings, and
- whose assets consist *primarily* of interests in UK land and buildings (for example at least 70% of gross assets).

Stamp tax, because that is what it will become, will be a modern purchase tax paid by a purchaser or a lessee. (At the moment there is no person responsible for the payment of stamp duty, because it is a tax on documents, and therefore, in practice, the person who seeks to rely on the document in question would typically seek to

have the document taxed. But that is a matter of commercial expedience, not law.)

The consultation process has now been underway since April 2002, and the intentions of the Revenue are clearer. They want the new stamp tax to be a global tax. This means that they want it to be payable by the purchaser or the lessee wherever such a person may be resident, if the transaction relates to UK land. In other words, they are aware of techniques by which entities based in locations such as Ireland or the Channel Islands are set up to acquire UK property in circumstances where stamp duty is avoided and the “knock out” provisions of s.14(4) Stamp Act 1891 are irrelevant because the structures involve no UK nexus. As stated, the new stamp tax is to be on “substantial interests”. This means that whether land is held through a company, a unit trust, a partnership or however, stamp tax will arise on the acquisition of a substantial interest. It is not clear whether the Inland Revenue are fully focused on the meaning of the word “acquisition” in these circumstances. After all, in Australia, where a stamp tax has been in existence for some time, the relevant legislation appears to be wider than that proposed by the UK Revenue. For example, it is not clear that if a structure were created involving a series of companies, a land transaction would automatically be caught by the new rules: there may not be sufficient “tracing” down to the company that holds the land interest to produce a charge in these circumstances.

The 2003 Budget is likely to describe in more detail the changes which will probably come into effect by the end of October 2003 or perhaps some time in February 2004. The Law Society have asked for a transitional period to be introduced which would allow property practitioners to become used to the new forms that will be used initially. The general feeling is that it is unlikely that there will be a consolidated Stamp Tax Act, but if this were to be the case, after all, then this would not be enacted until some time in 2004 at the earliest.

The new rule will be that the trigger point for the tax will be either the payment for the transaction (with an exemption for deposits) or else will be the time of substantial performance. On the face of it, therefore, all current stamp duty planning is likely to need sufficient rethinking, since the new tax will impact on any transaction involving land by reference to the cash paid or by reference to the transaction occurring: we shall all need to start afresh with what is in essence an entirely new tax.

What is left in the meantime?

Before the new stamp tax takes effect, there remain some planning ideas.

Resting on contract

Section 115 Finance Act 2002 brings to an end schemes involving resting on contract (exchanging but not completing), but only where there is a contract or agreement for the sale of an estate or interest in land and

the amount of the consideration exceeds £10m. or is part of a larger transaction where the consideration exceeds £10m. Consequently, the position remains that contracts may be exchanged without stamp duty where the consideration is £10m. or less. In certain circumstances this is enough. The vendor and the purchaser simply agree to exchange contracts, the equitable interest passes by operation of law and with care (and subject to the circumstances) the purchaser has all that it needs.

Split title

If one wants to take this resting on contract technique a step further, then one can use the so-called “split title” arrangements involving a lease. The vendor would grant a long lease to a nominee for itself. Provided the nominee was not connected with it no *ad valorem* stamp duty would arise. There would then be a contract for the assignment of the long lease to a purchaser, and the relevant contract would not be completed. Assuming that the consideration did not exceed £10m, no *ad valorem* stamp duty would arise. In due course, the freehold reversion could be passed over to the purchaser or a subsidiary of the purchaser. The Stamp Office seem resigned to the fact that this technique avoids stamp duty and is not caught by s.90 Finance Act 1965 (contemplation of sale). Their resignation is probably tempered by the fact that this planning cannot survive the introduction of the new stamp tax: the payment of the consideration would, in effect, produce a stamp tax charge in the new regime.

Variation of the split title scheme

A slightly more provocative version of the split title scheme involves, again, the creation of a long lease in favour of a nominee. The long lease would be, say, for a peppercorn. This would drive down the value of the freehold reversion. The freehold reversion would then be sold to the purchaser for its market value (next to nothing). In due course, the purchaser might then make a substantial payment to the vendor in consideration of the vendor (in its capacity as lessee) agreeing to a cancellation of its lease for the consideration in question. This arrangement should not involve a conveyance on sale (it is merely a cancellation), and consequently ad valorem stamp duty is avoided. This technique is aggressive but probably effective.

Reducing rent with a stamp duty-free payment

Another clever idea takes advantage of the ability to make a payment to reduce rent in circumstances where the payment does not give rise to stamp duty. Accordingly, the vendor would grant a long lease to a subsidiary and perhaps it would be agreed that a considerable rent (say £30m.) would be paid in the first year with, say, 12% rental increases over a period of time and then a peppercorn rent in due course. In these circumstances that lease might then be sold to the purchaser for, say, £500,000. The scheme would then unravel by the purchaser of the lease paying a large sum of money, say, £30m., to reduce the rent. The payment is entirely free of stamp duty: it does not fall within the charging provisions of the legislation. The reduction

might be to reduce the rent (as stated) from £30m. in Year 1 to a small rent of, say, £100,000 per year. Anything less than this might lead to the conclusion that there had in effect been a chargeable surrender and regrant after all. In due course a subsidiary of the purchaser could then acquire the freehold interest. In these circumstances £30m. is moved to the vendors free of stamp duty.

Foreign Partnerships

One fairly straightforward technique for avoiding duty used to be to transfer land into a company and then to sell shares in that company at a rate of ½% (or nil if the company were foreign). Section 119 Finance Act 2000 put an end to this. However, it may be possible to “re-invent” this idea by utilising a foreign partnership instead of a foreign company. The vendor contributes property to the partnership. The Stamp Office generally accepts that this is stamp duty-free on the basis, for example, that s.241 Finance Act 1994 (exchanges) has no relevance. There is then a sale of the relevant partnership interest in circumstances where s.14(4) Stamp Act 1891 does not apply. In due course the partnership may be dissolved in circumstances where no stamp duty arises having regard to the ratio of the case of *IRC v. Macleod* (pure winding up – no consideration). Care needs to be taken in relation to this arrangement if interest relief is needed in the hands of a foreign purchaser, as it will be necessary to take additional steps in these circumstances.

Finance Act 2002

The Finance Act 2002 introduced a number of anti-avoidance provisions. These included a prohibition on group relief on intra-group transfers under s.42 Finance Act 1930 where there is a transfer of land and buildings followed by an onward sale of the transferee company within two years if it retains the land. The legislation is very poorly drafted, and there seems nothing to prevent a transfer of land down two or more tiers of companies in circumstances where the transferee company that leaves the group will not own the land directly. In relation to moving assets up the chain (in a reconstruction and “s.110 liquidation”) it is clear that there should be no new clawback rules under the new anti-s.76 provisions introduced by FA 2002, if the land which is being transferred up the chain leaves the holding company pursuant to relief under ss.75 or 76 FA 1986. But the Stamp Office seem to take the view that where there is a direct distribution then the clawback provisions in s.113 Finance Act 2002 may apply after all.

Conclusion

Stamp duty (or stamp tax) is undergoing a significant change and all of us involved in this area need to keep an eye on matters in anticipation of significant new legislation towards the end of 2003 or the beginning of 2004.

Caveat

The ideas in this article are intended to stimulate thinking: they should be implemented with great care.