

Patrica Lancaster & John Dingle

By Email

10 April 2016

Dear John and Patricia

PROPERTY TRANSACTION

I write further to our email correspondence and meeting last week in connection with the disposal of property from the pension fund. I have made a number of enquiries on your behalf in respect of the rules surrounding stamp duty land tax (SDLT) and advise as follows:

Of the options discussed, the simplest and perhaps most tax efficient option would be for the pension scheme to loan to either Valandry or Landing Properties up to 50% of the assets of the scheme. I have had prepared a deed of adherence to admit both companies to the scheme, which leaves it to your discretion and the advice of White Hart Associates regarding the most suitable choice of company.

Stamp Duty

HMRC under the property regulations defines residential property as a building that is used or suitable for use as a dwelling, or is in the process of being constructed or adapted for such use, it can also include land that is or forms part of the garden or grounds of a building including any building or structure on such land.

A purpose built office which is not presently suitable for use as a dwelling is not affected by the change in stamp duty rules. However, if consent of change of use is obtained prior to 1 April 2016 then it could be argued that the property is being adapted for such residential use and therefore SDLT residential rules may apply.

I set out below the SDLT effect of different options below:

1. Option 1 - Disposal of the property now - prior to 1 April 2016.
2. Option 2 - Disposal of the property with change of use consent post 1 April.
3. Option 3 - Disposal of the property estimated uplifted value with change of use consent post 1 April.

SDLT option 1.

Effective date	Purchase Price (£)	Percentage rate (%)	Total SDLT due (£)
31 March 2016	285,000	3	8,550

SDLT option 2.

Effective date	Purchase Price (£)	Percentage rate (%)	Total SDLT due (£)
1 April 2016	285,000	5.4	12,800

SDLT option 3.

Effective date	Purchase Price (£)	Percentage rate (%)	Total SDLT due (£)
1 April 2016	570,000 (assumed)	6.2	35,600

As you will note, the transfer of property after 1 April under change of use would give rise to an additional SDLT payment of £4250. However, by obtaining a change of use certificate this should increase the value of the property and were we to assume that the change of use increases the value of the property to say, £570,000 this would also increase the SDLT payable to £35,600, an effective rate of 6.2% and an increase of £27,050.

If you were to proceed with option 3, John's tax free cash sum would rise by £129,613 as the disposal would be on the uprated value and this increases the value of the pension fund. The income tax that would have been payable under the equivalent of John's pension at current income tax rates would be at least £45,488. Therefore, under option 3 it would be better for the pension scheme to hold the property under change of use as the tax savings would be at least £9,888. In addition, you would have a lower capital gains tax disposal in the Company once the property has been developed and sold on.

Taxable Property Regulations

It would be heedless not to raise the question on whether obtaining a change of use certificate would give rise to a challenge that the pension scheme is undertaking a disposal of residential property. This is a very important issue and failure to get this right would mean a tax penalty on the pension scheme of at least 40% of the value of the property.

The Finance Act 2006 defines residential property as a building that is used or suitable for use as a dwelling, or is **in the process of being constructed or adapted for such use**. Under this aspect of the legislation, this could trigger the disposal as residential property for SDLT purposes.

Pension scheme rules concerning residential property define residential property differently. A residential property is defined as a building that is used or suitable for use as a dwelling, any land consisting of, or forming part of, the grounds of such a building which is used or intended for use for a purpose connected with the enjoyment of the building. "Building" includes a structure, and a part of a building. On this basis, whilst the disposal of the property with change of use consent may give rise to SDLT at residential rates, it does not therefore mean that a residential property is being disposed of and as such it could be considered that for pension scheme rule purposes the property remains as a commercial property. You could therefore argue with HMRC that this disposal with change of use falls under the commercial rules and not residential for SDLT purposes.

I realise that this is a very technical area, but it is important that this area of pension practice is clear to you both. Clearly, there is a substantive tax difference under residential and commercial rules.

Funding the property transfer

The pension scheme can lend one of your property companies 50% of its value to fund the property purchase. It cannot receive a premium in respect of the conversion of work to residential property, unless that disposal takes place prior to an NHBC being issued.

Loans from a pension scheme to the business must be repaid at the latest with one year's interest at the end of year one and capital repayment at the end of year two. Therefore, based on a property value of £285,000 the business must repay this at the rate of £57,000 p.a. i.e. in five equal instalments.

If this property is to be bought and held by either company, then the repayment of the loan can be made from you crediting the director's loan account of the relevant company each year for £57,000 and transferring this same amount to the pension scheme, or John giving up part of his tax free cash sum to set off the loan to be repaid to the pension scheme.

My guidance would be to use the sale proceeds from your property in Richmond to meet future loan repayments to the pension scheme in 2 years' time. In the intervening two years, I would invest the capital payment due in a fixed term fund until that payment falls due. To reduce your capital gains tax in the Company, I would make a pension contribution to the maximum amounts and also charge a meaningful rate of interest to the Company for the loan.

I do consider that the change of use certificate does not necessarily warrant that the disposal is of a residential nature, given how the rules of the pension scheme are constructed. I would also recommend that Nikki Spoor also gives her advice on this matter.

Kind regards

Gavin McCloskey
For Pension Practitioner .Com

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Yours sincerely

Gavin McCloskey
For Pension Practitioner .Com

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