

Budget 2016 - Increase in SDLT for commercial transactions over £1m

In his March 2016 Budget, Chancellor George Osborne announced radical changes to Stamp Duty Land Tax on commercial property* in the UK.

Stamp Duty Land Tax Reforms

Chancellor George Osborne announced a radical overhaul of the way in which Stamp Duty Land Tax ("**SDLT**") will be charged on purchases of commercial property in the UK. The changes took effect almost immediately i.e. on or after 17 March 2016.

Where a commercial land transaction has exchanged but not completed before 17 March 2016, the purchaser will normally have the choice whether to pay SDLT under the old or the new regime, under transitional provisions. As will be seen below, the effect of the rate changes are that SDLT will be higher under the new regime where the purchase price exceeds £1.05m so it will only make sense to elect into the new regime where the purchase price is below £1.05m. Conversely, anyone who has entered into a contract pre-17 March for purchase of commercial property over £1.05m but has not completed or substantially performed that contract pre-17 March will need to take extreme care to ensure that contract benefits from the lower rates under the old regime: for instance, variations and assignments of that contract post-17 March could lose grandfathering. Future transactions pursuant to unexercised options or pre-emption rights pre-17 March are not grandfathered and are then subject to the new rates. It would be sensible to review historic uncompleted contracts/transactions and take appropriate advice on the application of the grandfathering rules.

The Chancellor's announcement included three principal significant reforms to Stamp Duty Land Tax on commercial property transactions:

First significant reform: SDLT on "purchase price" or "premium" paid for commercial property transactions

The "slab" system of calculation of SDLT on any purchase price or premium paid for commercial property (under which, if the total purchase price given exceeded a rate threshold even by just £1, the whole amount would be charged at the higher rate, and not just the excess), is replaced with a "slice" system (as is already used for calculation of SDLT on any purchase price or premium paid for residential property) so that the higher rate will only apply to the amount over the relevant threshold. New rates of SDLT on commercial property have been introduced at the same time.

**Broadly, "commercial property" for SDLT purposes is any property which is not "residential property" or is a mix of "residential and non-residential property". The definitions are complex. Obviously offices and retail are "commercial property". However, a freehold or long leasehold in six or more separate dwellings which are the subject of a single transaction would also be "commercial property". In addition, buildings used for certain communal residential purposes (e.g. children's homes, care homes, hospitals or hospices, prisons, halls of residence for students in higher education, hotels or inns) are also deemed to be "commercial property" for SDLT purposes.*

The new rates and thresholds for commercial property are as follows:

Property value band	SDLT rate under new rules
£0 - £150,000	0%
£150,001 - £250,000	2%
£250,001 +	5%

The following table compares the effect of the changes for some example freehold or premium lease transactions and shows that above £10m, the effect of the changes will be that SDLT will have increased by nearly 25%.

Example Property (total chargeable consideration given)	Tax paid under the old rules	Tax paid under the new rules (on or after 17 March 2016)	Change in amount of tax paid	Percentage increase/decrease in tax (vs under the old rules)
£150,000	No stamp duty	No stamp duty	No stamp duty	No change
£500,001	£20,000	£14,500	£5,500 reduction	27.5% decrease
£1,050,000	£42,000	£42,000	No change	No change
£2,000,000	£80,000	£89,500	£9,500 increase	11.88% increase
£10,000,000	£400,000	£489,500	£89,500 increase	22.38% increase
£50,000,000	£2,000,000	£2,489,500	£489,500 increase	24.48% increase
£100,000,000	£4,000,000	£4,989,500	£989,500 increase	24.74% increase

Second significant reform: SDLT on rent paid for commercial lease transactions

In addition to these changes to the system of calculation of SDLT on any premium paid upon grant of a commercial property lease, the Chancellor has also announced a change to the way SDLT is calculated on rent paid under such a lease; to the extent the NPV of the rent is above £5 million a new 2% rate band has been introduced.

The new rates bands and thresholds for rent paid under a commercial lease are:

Net present value of rent	Rate
£0 - £150,000	0%
£150,001 - £5,000,000	1%
£5,000,000 +	2%

The following table compares the effect of the changes for some example leasehold transactions. **These examples assume a flat rent throughout the first 5 years of the lease and a term of 10 years, but different scenarios would give rise to different calculations.**

Example Property total VAT inclusive annual rent	NPV (assuming 10 year term, and a flat rent)	Tax paid on rental element under the old rules	Tax paid on rental element under the new rules (on or after 17 March 2016)	Change in amount of tax paid on rental element	Percentage increase/decrease in tax (vs under the old rules)
£500,000	£4,158,302	£40,083	£40,083	No change	No change
£600,000	£4,989,963	£48,939	£48,399	No change	No change
£700,000	£5,821,623	£56,716	£64,932	£8,216 increase	14.48% increase
£1,000,000	£8,316,605	£81,666	£114,832	£33,166 increase	40.61% increase
£5,000,000	£41,583,026	£414,330	£780,160	£365,830 increase	88.29% increase

Third significant reform: '£1,000 Rule' will no longer apply

Before 17 March 2016, where the relevant rent on a lease was more than £1,000, purchasers could not benefit from the 0% threshold on any premium paid for the grant of the lease.

From 17 March 2016 if the relevant rent (not the NPV) is £1,000 or more, purchasers will be able to benefit from the 0% threshold for both the premium and rental elements of a leasehold transaction.

Updated SDLT Calculator

HMRC have updated their online calculator for SDLT showing the applicable rates / calculations under the old and new rules: <https://www.tax.service.gov.uk/calculate-stamp-duty-land-tax/#/intro>

Special situations

- Leases granted before 17 March 2016 but which continue after a fixed term ending on or after 17 March 2016 should normally continue to be calculated under the old regime (provided the continuation does not amount to or involve a variation of the lease);
- Leases entered into before 17 March 2016 for an indefinite term should normally continue to be calculated under the old regime;
- A successive linked lease granted on or after 17 March 2016 where the original lease was granted prior to 17 March 2016 should normally be calculated under the old regime;
- SDLT on variable or uncertain rent in relation to a lease granted prior to 17 March 2016 which becomes certain or known after that date should normally be calculated under the old regime;
- New leases granted during a period of holding over on or after 17 March 2016 should normally be calculated under the new regime.
- Where a lease is varied, on or after 17 March 2016, to increase rent in the first 5 years of its term the consequent SDLT charge should be calculated under the new regime.

Given the complexities of the rules, every transaction should be checked on a case by case basis.

Other specific computational rules are applicable where:

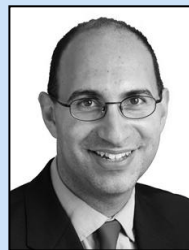
- Transactions(s) under the new regime are 'linked' with transaction(s) which occurred before 17 March 2016;
- A backdated lease is granted to a tenant holding over;
- Additional SDLT is due upon the grant of a lease on or after 17 March 2016, and that lease was substantially performed before 17 March 2016.

The changes set out in this Alert do not apply to "residential property". The SDLT system applicable to residential property is complex and subject to entirely different rules (for which, see:

http://www.cliffordchance.com/briefings/2014/12/autumn_state_ment2014realestatetax-.html and http://www.cliffordchance.com/briefings/2016/01/autumn_state_ment2015-higherratesofsdltfo.html).

The changes also only apply to land in England, Wales and Northern Ireland. Scotland has a different system known as "Land and Buildings Transaction Tax ("LBTT") and is thus not subject to the above rules.

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