

A photograph of a construction site under a clear blue sky. On the left, a modern building with a glass and white facade is partially completed. In the center and right, two large tower cranes are visible, with one in the foreground and another slightly behind it. The background shows more buildings under construction.

PROPERTY INSIGHT SPRING 2011

INSIDE Business property relief: who qualifies ■ **What a relief - a business guide to tax relief on property** ■ VAT: clawing its way back





GREETINGS FROM THE MENZIES PROPERTY TEAM

The early part of the year is always a time of renewed energy and enthusiasm in both our personal and business lives.

THIS ISSUE of Property Insight will show you some of the ways you can implement your New Year business goals, whether that be saving money on taxes, or choosing the right methods to organise your assets.

Richard Godmon, Menzies Tax Partner shares some of his expertise on inheritance tax and enlightens us on how Business Property Relief can drastically reduce any inheritance tax charges.

We hope you enjoy reading this issue of Property Insight and welcome any comments, feedback or contribution you would like to make to the publication.

Until next time,

THE MENZIES PROPERTY TEAM

property@menzies.co.uk



Many thanks go to:
Salvador Amico
Sara Davies
Richard Godmon
Lorraine Langridge
Andrew Moorcroft
Tom Govan



BUSINESS PROPERTY RELIEF: WHO QUALIFIES?

Business Property Relief (BPR) is a useful relief that is available to help individuals reduce their potential inheritance tax liability. However, care must be taken to plan ahead and ensure that the ability to claim BPR is not jeopardised.

IN ORDER to qualify to claim BPR, certain conditions and criteria need to be met. Generally, BPR is only available where an individual owns shares in an unquoted, trading company. Conversely, shares in an unquoted *investment* company will not attract BPR.

The distinction between shares in a trading company and shares in an investment company reveals a potential inheritance tax trap that many property developers are unaware of.

Menzies Tax Partner Richard Godmon says: "Shares in an investment company, whose main activity is investing in property, in order to generate rental income and capital growth in the value of the property it owns, will not qualify for BPR. Therefore there is a risk that on

the death of a shareholder, that owns shares in an investment company, inheritance tax will become payable by the deceased's estate. This liability could be avoided with a little foresight and careful planning."

Furthermore, shares held in an investment company carry further restrictions. For example, it is also not possible to avoid capital gains tax on a gift of the shares to another individual. However, this restriction would not apply to shares held in a trading company.

So with regard to any planning that can be made to avoid the tax problems associated with investment companies, it is important to consider whether the conditions can be created to change the nature of the investment company so that it can be deemed to be trading.



Inheritance tax: keep it trim and slim

Richard sheds some light on two important planning strategies that can help minimise exposure to the tax pitfalls associated with investment companies.

Trading business

As mentioned above, there are major advantages in changing the nature of the company's activity from being investment to trading. This would mean it participates in a range of qualifying trades and property development is an activity that could be used to change the fundamental nature of the company's business.

Discretionary trusts

Another possible way of reducing exposure to future inheritance tax liabilities is through the use of trusts.

There are a number of methods to potentially reduce the exposure to inheritance tax liabilities through the use of trusts. For example, it is possible to transfer properties from a property investment company into a trust without incurring any inheritance tax. Additionally, a provision in capital gains tax legislation offers relief on gifts of assets to a qualifying trust.

With the inheritance tax threshold standing £325,000, it is vitally important that advice is sought at the earliest opportunity in order to ensure that the risk of a liability arising is minimised. Contact your local Menzies adviser who will be happy to discuss strategies that will help.



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WHAT A RELIEF- A BUSINESS GUIDE TO TAX RELIEF ON PROPERTY

Are you paying too much tax? Have you considered all the allowances you could claim? In the current economic environment, it is more important than ever to ensure you are claiming all available tax reliefs.

RICHARD Godmon, Tax Partner at Menzies LLP outlines a number of reliefs, that are commonly overlooked:

1. Capital allowances for integral features

The Annual Investment Allowance applies to all expenditure on integral features incurred after 1 April 2008. Integral features are:

- Electrical systems (including lighting systems);

- Cold water systems;
- Space or water heating systems, powered systems of ventilation, air cooling or air purification, and any floor or ceiling comprised in such systems;
- Lifts, escalators and moving walkways;
- External solar shading

All integral features will qualify for capital allowances at a rate of 10% per annum.

2. Contaminated land remediation relief

What is contaminated land? This refers to any land, estate or building within the



Richard Godmon
Tax Partner



UK, which is polluted with a substance that may be damaging to the health and wellbeing of the local community and surrounding ecosystems. Any business, that has invested in a clean up operation of the land, can deduct 150% of the cost it has incurred. If a loss has been made as a result of the claim, this loss can be claimed back as a cash sum of 16% equal to the loss.

3. Flat conversion allowances

These are designed to give landlords relief for the conversion of underused space above shops and other commercial premises into premises available for residential use. Where available, the allowance gives 100% relief for any capital expenditure incurred in the conversion of the property.

4. Business Premises Renovation Allowance (BPPRA)

The BPPRA provides a 100% initial capital allowance for qualifying costs on the conversion or renovation of unused commercial property. The BPPRA scheme encourages people or companies to convert or renovate their derelict or unused commercial properties by giving them immediate, full tax relief on the capital spending.

However be warned, you have about a year left to make the most of this scheme, as it expires on 11 April 2012. We will be running a full feature about this in next issue of Property Insight– so get renovating!

5. Capital gains on lease terminations

Payments from a tenant to a landlord for early termination of a lease are taxed as a capital gain in the hands of the landlord. In some cases, there may be opportunities to structure the transaction in a way that minimizes the tax impact. Please contact your local Menzies adviser for further details.

6. Options to Tax – 20 Year Revocation

From 1 August 2009 it became possible to revoke options to tax made when the facility was first introduced 20 years ago. This will be of interest to those taxpayers wishing to make their property more attractive to tenants in general and those with existing partly exempt/non-business tenants.

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VAT: CLAWING ITS WAY BACK

The current economic climate has created a challenging environment for property developers selling residential properties. As a result, the depressed housing market is seeing a sharp rise in the number of properties that are being let out for a short period of time before they are sold.

LETTING a residential property is an exempt supply for VAT purposes, rather than a zero-rated (VAT at 0%) supply. This means that no VAT is charged on your supply, however VAT incurred in respect of an exempt supply is not recoverable.

In contrast, the sale of a new build residential property is zero-rated, which subject to the normal VAT rules allows you to claim back the VAT incurred.

Short-term letting may seem the right short-term solution for developers, but it is important to bear in mind that it can cause HMRC to claw back of the VAT already recovered.

On the plus side if the VAT which relates to exempt supplies is small enough to fall within the de minimis limits of £7,500 per year, then no VAT has to be paid back to HMRC.

Long-term solution to short-term lets

HMRC has published guidance which confirms

that if a property developer has been unable to sell a new residential property to an unconnected third party, they can make a sale of the property to a connected company.

This connected company can then rent out the property. Consequently, it is this company which will make exempt supplies of residential letting and will be unable to recover the VAT. However, the property developer can still recover the VAT incurred in the construction cost.

Structuring the transaction in this way ensures that you still fulfil the necessary conditions to recover all of the VAT incurred on the construction costs.

It is also important to consider other tax implications of structuring a transactions in this way.

If you would like more information on how to minimise your exposure and potential VAT cost please contact a member of the Menzies property team.

Build your business from the ground up with the team that knows about property

The Menzies property team acts for over 500 property and construction clients, including developers, investors and sub-contractors. And as one of the largest independent accountancy firms in the South East, it also has an extensive network of associated professionals who can assist in specialist areas such as law, surveying and valuations.

The firm's focus on the property and construction sector has enabled it to develop a comprehensive suite of business and tax related services. In addition to audit and accounts preparation, Menzies can help with corporate tax, VAT planning and financing. The diagram below shows the range of Menzies compliance, tax and advisory services.



If you would like help with tax matters or any other issues relating to property business and investments, please contact your local Menzies property specialist or email the property team at property@menzies.co.uk

Blackwater Valley

Victoria House
50-58 Victoria Road
Farnborough
Hampshire GU14 7PG

+44 (0)1252 541244

Heathrow

Heathrow Business Centre
65 High Street
Egham
Surrey TW20 9EY

+44 (0)1784 497100

Kingston upon Thames

3rd Floor, Kings House
12-42 Wood Street
Kingston upon Thames
Surrey KT1 1TG

+44 (0)20 8974 7500

Leatherhead

Ashcombe House
5 The Crescent
Leatherhead
Surrey

+44 (0)1372 360130

London

7-12 Tavistock Square
Lynton House
London
WC1H 9LT

+44 (0)20 7387 5868

Solent

Wentworth House
4400 Parkway
Whiteley
Hampshire PO15 7FJ

+44 (0)1489 566700

Woking

1st Floor, Midas House
62 Goldsworth Road
Woking
Surrey GU21 6LQ

+44 (0)1483 755000

www.menzies.co.uk

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