



IN THIS ISSUE... Pages 1, 2 & 3 **Tax relief on a disposal of your home – do you qualify?**

Pages 3 & 4 **Risk and Registration**

Note from the editor



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Welcome to this, my first edition as editor of this newsletter. It never ceases to amaze me how quickly time passes and it will not be long until I have completed my first year with landtax.

Our team of consultants continues to grow and I would like to introduce Lizzie King who joins us this month.

Since our last newsletter we have had Alastair Darling's third budget and experienced an emergency budget under the coalition government on

22nd June. For our budget reports go to www.landtax.co.uk/resources

This newsletter will explore the availability of Principal Private Residence relief in respect of the sale of a property which is, or has been, your residence.

We then continue the risk theme of previous newsletters with a view from a property lawyer's perspective, for which I would like to thank Iain Davis of Henmans LLP.

Tax relief on a disposal of your home – do you qualify?

Melanie Maycroft

It is generally known that there is a relief available for Capital Gains Tax (CGT) on the disposal of your main residence. However, there tends to be a misconception that this relief results in the sale of a private residence being entirely free of CGT. In reality, the relief available is much more complex than this.

The first point to be considered is what qualifies for the relief. The relief is generally known as Principal Private Residence relief. However, the word 'principal' does not appear in any of the legislation relating to the relief. The legislation actually refers to a relief which is available to an individual in respect of disposals of a whole or part of a dwelling house. The property must be the only or main residence of that individual, together with land for

occupation and enjoyment of that individual as the garden or grounds of the residence up to the permitted area. I therefore refer to the relief throughout this article as 'Only or Main Residence' (OMR) relief.

The relief is also extended to trustees where the property qualifying in all other respects is the only or main residence of a person entitled to occupy it under the terms of the trust and to personal representatives of a deceased person. The property must be occupied both before and after the death by a beneficiary entitled to a beneficial interest in 75% or more of the property. However, it is important to note that OMR relief will, in almost all cases, not be available where the base cost of the property is reduced by holdover relief in respect of an earlier transfer.

Bits and pieces...

Offshore funds with reporting status

Under new offshore fund regulations which came into force on 1 December 2009, investment in funds classified as 'reporting funds' will result in a requirement for investors to report income of the fund on their tax return and therefore pay tax, regardless of whether the income has been distributed from the fund.

There is no definition of a 'dwelling house' in the legislation. The Courts have taken a fairly broad view on what can constitute a dwelling house, which can generally be considered to be in line with the dictionary definition. However, it is useful to point out that the concept is

...Continued on page 2

not confined to bricks and mortar, caravans and chalets could qualify, if they are stationary and provide all of the services which one would expect in a dwelling.

The case of *Green v IT Commrs* (1982) ruled that unused or seldom used parts of one house should not be apportioned, and relief disallowed, if there was no evidence that any part of the house was not the taxpayer's residence. It would seem, based on this case, that highly exceptional and unusual facts would be required to lead to such an apportionment, such as the blocking of internal access between certain parts of the house. In line with this decision extensions, wings, annexes etc would generally be relievable where it is clear there is a single household with internal communication.

In *Batey v Wakefield* (1981) it was decided that 'residence' includes not only the main building but also any other buildings that are occupied for the purpose of the main residence e.g. shed, staff bungalow etc. Many cases have followed questioning whether a separate property on an estate could be covered by the relief, most of which went in favour of the taxpayer until

Bits and pieces...

Furnished holiday letting

Tax breaks for Furnished Holiday Lettings were due to be withdrawn from April 2010, as reported in previous newsletters. However, for the time being, the proposed changes have been postponed. It remains to be seen whether the proposed changes will be revived following the general election.

Lewis v Lady Rook (1990). The successful argument of HMRC in *Lewis v Rook* was that one must look at the curtilage of the main house to decide whether a secondary building is part of the dwelling house. Of course, in itself the argument as to what is the curtilage may be a subjective one.

It is important to be aware that a conversion of the entire property to non-domestic use prior to a sale could result in no OMR relief being available. The provisions which allow for changes in the property occupied as the residence during the period of ownership all rest on the fact that the property remains a dwelling house based on a strict reading of the legislation.

Moving on to OMR, what an only or main residence is accepted as being, again there is no definition in the legislation and therefore we must look to the relevant case law. We must first decide what is a residence. For this purpose the Courts would refer to Viscount Cave's definition in *Levene v IRC* (1928). This was a case on whether a taxpayer was UK resident for tax purposes. However, the Courts take the view that residence has the same meaning regardless of whether looking at country of residence or residence in a particular property. This was confirmed by the OMR relief case of *Goodwin v Curtis* (1998) where the following quote of Viscount Cave in the *Levene* case was referred to:

'My Lords, the word "reside" is a familiar English word and is defined in the Oxford English Dictionary as meaning "to dwell permanently or for a considerable time, to have one's settled or usual abode, to live in or at a particular place...'

There is no minimum period of residence but the property must be physically resided in for some period. In line with the above, it is quality, not quantity, of residence that is the important factor. Essentially the relief is only available for periods when the property was the OMR with a few exceptions. I do not detail all of the exceptions here, but the main exception which is often important is that the last 36 months in respect of a property which has at any time been the OMR is always eligible for relief regardless of whether the property is the OMR in that period. This can provide

significant planning opportunities.

Where a property which partially qualifies for OMR relief has at any time been wholly or partly let to residential tenants, it will qualify for another relief known as lettings relief to a maximum of £40,000 per owner of the property.

Any part of a property used exclusively for business purposes is excluded from relief. An office which is used also for private paperwork will not cause a problem for OMR, but then the exclusive use requirement if Inheritance Tax Business Property relief is to be claimed would be lost.

Now to consider 'only or main'. A person may only have one OMR and, in the case of married couples or civil partners, they can only be one OMR for both of them although there is a view that this may be contrary to human rights law.

Where there is more than one residence, the OMR can be determined by making a written election to HMRC. The legislation provides for a two year time limit for making this election. However, there are differing views as to when this time limit begins. The HMRC view is that the two year period begins within two years of the date when the taxpayer first acquires an additional residence. It could also be argued, based on the wording of the legislation, that the two year period begins two years prior to making the election so that a later election can be made but would merely reduce the relief available. There is a case, *Griffin v Craig-Harvey* (1994) which accords with the HMRC view and therefore my advice would always be to make the election within two years of acquiring an additional residence. However, if this has been missed I would suggest that an election could be submitted and argued in line with the alternative view, particularly in light of the fact that *Griffin v Craig-Harvey* was decided based on the wording in older legislation which was consolidated into the wording in the current Capital Gains Tax Act.

Once an election has been made, it is then possible to vary the election at a later date without time limit, to apply to a period up to two years prior to the date of the variation. Guidance in HMRC's own manuals sets out a planning opportunity created through the use of an election and subsequent variation whereby it is possible to obtain OMR relief for the last 36 months of ownership of a second residence with only a loss of one week on the main home. This opportunity can be extended to further additional residences. Where an election is not made, the question as to what is the OMR is to be concluded. Where an election is not made, the question as to what is the OMR is to be concluded by self assessment subject to enquiry by

HMRC and will be a question of fact.

The legislation sets out that the permitted area of garden or grounds is half a hectare or a larger area if required for reasonable enjoyment of the dwelling house having regard to its size and character. When looking at areas larger than half a hectare it is necessary to ignore the circumstances and peculiarities of the particular individual and ask 'what would a reasonable man require for his reasonable enjoyment?'. The size and character tests recognise, for example, the common sense point that a larger house may require more extensive grounds or historic country houses may have been designed for their physical setting with larger grounds.

One final point for caution. Gains in respect of property acquired 'wholly or partly for the purpose of realising a gain from the disposal' or if 'attributable to any expenditure which was incurred after the beginning of the period of ownership and was incurred wholly or partly for the purpose of realising a gain from the disposal' are not eligible for relief regardless of whether any of the other conditions are met. An example where this may apply would be if a property was purchased for renovation and resale with the view of making a profit and the investor moved into the property merely to make matters easier whilst completing the works.

'Land for Sale: one careful owner' Risk and Registration



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We live in an uncertain age: Hung Parliaments; Double Dips; Junk Bond status; changing weather patterns; ash; the Ashes... I could go on.

One reassuring constant in this turbulent world is land.

Prices may go up as well as down, but we can all agree that they (or he/she – depending on your particular belief system) aren't making any more of it. Your land will always have a value, whether by dint of its location, what you use it for, the quality of its soil, or the sheer fact that someone wants it more than you.

In some ways, my fundamental role as an agricultural property lawyer is to ensure that my clients buy what they think they are buying, sell what they

think they are selling and own what they think they own. This may sound like setting the bar relatively low, but the fact remains that whether dealing with a large landed estate or a small family farm, there can often be a mismatch between reality and expectation when it comes to the full extent of actual land ownership.

It always helps to have a clear plan of what you own and what you occupy (and I will come back to what you means later). Better still if this plan is actually on paper, simply comparing this with your title deeds in a leisurely moment will save you both time and money in the long run. Finding out that your land ownership isn't quite what you expect during a deal can be fatal.

About 30% of land in England and Wales remains unregistered. The Land Registry have tried introducing new triggers (compulsory registration on changes in trustees for example), but the time is fast approaching when they

will have to resort to more extreme measures to achieve their previously stated (but not recently re-stated) aim of complete registration by 2012.

Bits and pieces...

Correction of VAT return errors

Where the net value of errors does not exceed the greater of £10,000 or 1% of turnover (to a maximum of £50,000) it is possible to adjust for errors on the next VAT return. However, the new penalty regime now in effect means that without detailed disclosure of errors significant penalties could arise where the errors have arisen because reasonable care has not been taken or there has been a deliberate inaccuracy.

The obvious advantage of registering your land is the state's guarantee of your title. This doesn't mean to say that mistakes don't happen. It isn't entirely unknown for the same field to be

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registered in the names of two entirely separate owners. For the most part however the Land Registry is a very efficient and sensible outfit that will work helpfully with your solicitor to complete voluntary registrations in a timely and effective way.

Once registered the title to your land should be safe from marauding squatters and other interlopers trying to take what's rightfully yours. Somewhat illogically a squatter only has to show 10 years adverse possession to claim ownership of registered land (compared to 12 years for unregistered land), but the registered land owner will be armed with his trusty land registry title which will go a long way to guaranteeing success in any future battle.

Land registration does also mean that, along with the intrusions of Google Earth, people can, if they choose to, check who owns a particular piece of land and how much they paid for it. The thin end of the wedge? Well, at the risk of mixing my metaphors, you can't have your cake and eat it. Once land is registered there is a nice neat red line on a title plan that shows you (and no-one else) are the owner. In future you

will always be alerted by the land registry if some third party is trying to claim ownership of it, or rights over it, or turn it into a village green, or otherwise despoil your title to it.

The joy of registration, and the secret behind it, is that there is a central repository of knowledge that will always be in place (notwithstanding how many of its branches the Land Registry chooses to close). Come fire or flood or other misadventure that may befall your precious unregistered deeds (your crown jewels, if you will), once registered you can sleep easy in the knowledge that even if your solicitor's or banker's strong room suffers from rising damp (or rising floodwaters), it matters not.

As a parting shot (and I appreciate that this is a *cri de coeur* that's been heard before from these pages) please remember to be very clear as to who you are when you come to consider what land you own. Do you mean you, or your trustees, or your partners (limited or otherwise), or your company, or even your spouse. If you know the answer to this (not always easy) question, is it documented, and if so is it documented properly?

If any of your land is let, is there a written tenancy in place? If not could the oral tenant assign onto a company and live on forever? Do you check who pays the rent: is it the tenant or A.N.Other? If the tenancy is written, has it expired and is it actually dated?

If you have office lets or other commercial tenancies, are you punctilious about renewing them; are they contracted out of the Landlord and Tenant Act 1954? It's terribly easy to do, but even easier not to bother. You may save on a solicitor's fee, but repent at leisure when you want to re-take possession at the end of the term.

It is probably fair to say that most lawyers, and particularly agricultural property lawyers, are risk averse. Not only by training and general disposition, but by experience. Land may seem permanent, real and fixed, but experience tells us that the title to it may not always be so.

your feedback...

We would like to know if there are any particular issues which are important to you and that you feel we should cover. Please do get in touch...

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