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Real Estate Tax Checklist

What should be on your radar?

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Introduction

Since our last briefing, there have been a number of important tax developments which affect the real estate sector, including various measures and consultations that were announced in the Spring Budget and on April's Tax Administration and Maintenance Day. Several of these relate to real estate funds and stem from the government's ongoing review of the UK fund landscape, such as the publication of a consultation on the possible introduction of a new form of onshore contractual fund. However, there have also been important tax developments on a "bricks and mortar" level, such as the introduction of full expensing for qualifying capital expenditure until March 2026.

With so much going on, it can be difficult to stay on top of things. This briefing provides a checklist of the key tax issues that those in the real estate sector should be aware of (including potentially significant future developments) and sets out the actions that you should now be undertaking in preparation.

How we can help

As one of the largest teams of tax lawyers in the City, we advise on all tax issues relating to real estate. We are currently advising clients on the matters identified in this briefing, and, through our membership of industry bodies and government working parties, are also involved in many of the new developments referred to here.

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Real Estate Vehicle Tax

Tax development	Introduction	What does this mean for the real estate sector?
Government consults on introduction of unauthorised onshore contractual fund	The government has published a consultation document on the possible introduction of a new fund type, the "Reserved Investor Fund (Contractual Scheme)" (RIF). The RIF would be transparent for tax on income and not subject to tax on gains, with transfers of its units being free from stamp taxes. The basic position is that investors would only be subject to gains tax when they dispose of their units, but the government is concerned that this could lead to loss of tax from non-residents and so is proposing potentially restricting the situations where the basic position would apply. The eligibility criteria for RIF status would include that it is both a "collective investment scheme" and an "authorised investment fund" (AIF) for regulatory purposes, and that it either (i) is not closely held, (ii) is only closely held due to the presence of certain institutional investors, or (iii) meets requirements to be widely marketed and made available to certain categories of investors.	A potential new UK fund is an exciting development. As the RIF will be unauthorised (although its manager will be subject to the AIF regulations), it should be flexible and easy to use. This, combined with the generous tax treatment being proposed, should make it attractive for investors in UK real estate. However, it will be important that in its (understandable) desire to address loss to the Exchequer, the Government does not add undue complexity which is not present in rival offshore structures (such as the JPUT) to ensure that the attractiveness of the RIF is not undermined. Under the proposals the RIF would be available to professional investors, as well as those who invest at least £1m (or have already invested in it). The consultation closed on 9 June 2023.
New Luxembourg/UK double tax treaty – timing update	On 7 June 2022, the UK and Luxembourg signed a new double tax treaty (DTT). The new DTT makes some significant changes to the tax treatment of UK property holding vehicles owned by Luxembourg residents. For more detail please see our last briefing. If Luxembourg had ratified the treaty before the end of 2022, it would have come into force during 2023. However, that did not happen, so the key changes will not come into force until sometime in 2024 at the earliest.	The delay in ratification has given real estate investors more time to consider the impact on their current and future structures of the changes made by the new treaty. Disposals of UK property holding vehicles by Luxembourg residents in 2023 are still likely to be able to benefit from protection under the DTT against UK non-resident capital gains tax.
Proposed amendments to the QAHC Regime	The government has announced measures that refine and expand its proposals to amend the QAHC regime (which we discussed in our last briefing). Included in the raft of measures are proposals to facilitate access to the regime for corporate funds and for fund structures that use multiple vehicles (such as parallel funds). For more information, please see our Budget briefing.	The proposals should enhance the attractiveness of the QAHC regime. QAHCs holding overseas real estate have significant tax benefits due to the simplicity and breadth of the exemptions of tax on profits and gains from such property. Although these exemptions do not apply in relation to UK real estate, the availability of other UK tax benefits, such as an exemption from having to withhold tax on interest, make it a useful part of the toolkit when structuring the holding of such real estate.

Tax development	Introduction	What does this mean for the real estate sector?
Changes to the REIT regime	Following on from the change to the REIT regime made in April last year, the government has proposed a further batch of reforms. These include disapplying the need for a REIT to hold at least 3 properties, provided it holds a single commercial property worth at least £20 million, and helpfully amending the rule that can switch off the exemption from tax on gains from sale of property within three years of development. In addition, it has been proposed that the regime be amended to facilitate use of private REITs by limited partnership fund structures consisting of multiple vehicles (such as parallel funds) and that the withholding tax position on property income distributions paid to partnerships be amended to allow gross payment to the extent that the partners would be entitled to gross payment if they held their interest in the REIT directly.	The proposed changes are welcome and should enhance the attractiveness of the REIT regime. The change to the withholding tax rules on PIDs paid to partnerships is a particularly innovative step which, together with the relaxation relating to multi vehicle fund structures, should facilitate the use of private REITs by limited partnership funds. This is important because limited partnerships are a very common fund vehicle for private capital. For more information on the proposals, please see our Budget briefing.
Sovereign immunity reduction proposal dropped	The government has confirmed that it will not go ahead with plans to materially narrow the UK's sovereign immunity exemption. Under the current sovereign immunity principle, heads of state, foreign governments and governmental bodies (for example, sovereign wealth funds and public pension schemes) are exempt from UK corporation tax, income tax and capital gains tax on all UK source income and gains. However, in July 2022 the government launched a consultation to materially narrow the categories of sovereign immunity from UK taxation, proposing that the exemption would be restricted to UK source interest income.	The proposed changes would have resulted in a much wider scope of income and gains coming within the charge to UK tax for sovereign immune persons, particularly impacting the attractiveness of investments in UK real estate by sovereign immune persons. Real estate sector businesses will therefore be relieved that they will not be going ahead.
Implementation of OECD Pillar Two (global minimum corporate tax rate) from 2023	As mentioned in previous briefings, the main plank of Pillar Two is the Global antiBase Erosion rules (GloBE rules) that seek to establish a global minimum corporate tax rate of 15% for multinational enterprises (MNEs) that meet a €750m turnover threshold. There will be various exclusions, including for investment funds that are ultimate parent entities of an MNE group and pension funds (and holding vehicles used by such funds). The GloBE rules will impose top-up taxes where the effective tax rate of an MNE in a jurisdiction is below the global minimum corporate tax rate (15%). Many jurisdictions, including the UK, intend to introduce a domestic top-up tax, so that any tax arising from an under payment of tax by entities in their territory is retained by the local tax authority, as opposed to a tax authority in a parent jurisdiction. The GloBE rules will also allow source taxation (for example, withholding taxes) on certain cross-border related party payments that are subject to tax below a minimum rate of 9%.	The timetable for implementation of Pillar Two is tight, with the OECD (ambitiously) aiming for them to take effect by the end of 2023. Most jurisdictions (such as the UK and EU) have opted for a commencement date of accounting periods commencing on or after 31 December 2023, with the UTPR (undertaxed profits rule) to be implemented at a later date. As GloBE focuses on an MNE's "effective tax rate" in a jurisdiction (and not that jurisdiction's headline rate), many real estate businesses may need to carefully consider whether they may be affected by these rules.

Bricks and mortar tax

Tax development	Introduction	What does this mean for the real estate sector?
Government announces full expensing for qualifying expenditure for 3-year period	In his Spring Budget, the Chancellor announced "full expensing" of qualifying capital expenditure incurred in the next three years, with the intention of making this permanent afterwards. This means that 100% of the amount of any "main rate" capital allowance expenditure will be immediately deductible, with 50% of any "special rate" capital allowance expenditure being deductible in the first year with a deduction at 6% thereafter. The government also reconfirmed that the £1m annual investment allowance is to be made permanent.	The United Kingdom has historically been seen as much less generous than its peers in giving tax relief for capital expenditure, so this change will be welcomed by the industry. Full expensing will mean that capital investment in the UK can be made out of pre-tax profits and therefore will encourage businesses to invest in plant and machinery in the UK. Businesses will be keen that the Government maintains this policy following April 2026.
Government reconfirms creation of investment zones	In the Spring Budget the government reconfirmed the intention, first announced in the Truss government's "Mini-Budget", to create twelve "Investment Zones". Each zone is to have an £80m spending envelope which can include "special tax sites". Proposed tax reliefs include: • SDLT relief (subject to the relevant property being acquired for a qualifying purpose and used within three years); • 100% capital allowance for plant and machinery; • an enhanced structures and buildings allowance of 10% per year for 10 years for qualifying expenditure (down from 20% under the 2022 Mini-Budget); and • employer's NICs relief in respect of the first £25,000 of earnings of new employees working in tax sites for at least 60% of their time for up to three years (down from £50,270 under the 2022 Mini-Budget).	The current Chancellor, Jeremy Hunt, expressly reversed many of the measures announced in the Mini-Budget. However, the fate of investment zones was unclear. Those in the real estate sector will therefore welcome their retention, albeit on a slightly pared back basis. The tax reliefs will only be available on tax sites within investment zones. Taking up tax sites is optional – if an investment zone does not introduce a tax site, it will have more of the spending envelope available to for other forms of funding. Any tax sites must be tightly defined and located on underdeveloped land – the government can reject tax sites if they do not meet the criteria.
Changes to VAT option to tax process	From 1 February 2023, HMRC stopped issuing option to tax notification receipt letters. Option to tax notifications should be sent by email to optiontotaxnationalunit@hmrc.gov.uk, and HMRC will send an automated response containing the date when the notification was received (which taxpayers should keep for their records). HMRC will now only respond to requests for confirmation of an option to tax if (i) the effective date is likely to be over six years ago, or (ii) the request is from a person who has been appointed a Land and Property Act receiver, or an insolvency practitioner to administer the property.	It will be important that taxpayers comply with the new option to tax notification process and retain the automated response for their records. Where sellers of real estate are not able to provide evidence of their option to tax status, buyers may be put in particular difficulty if the transaction cannot be characterised as a transfer of a going concern. As a result the parties to these kinds of deals may need to agree some form of contingency should HMRC challenge the position and unearth a valid option to tax.
Construction Industry Scheme (CIS) consultation	The government has published a consultation on the CIS. It is seeking views on how to strengthen the tests for receiving or retaining gross payment status and potential easements to make the regime easier to apply, including by potentially removing payments made by landlords to tenants from the scope of the CIS altogether. The consultation closes on 20 July 2023.	For some time the government has been considering how to tackle labour fraud in construction, and so it is unsurprising that consideration is being given to strengthening the requirements surrounding gross payment status. Landlords will particularly welcome the suggestion that landlord-to-tenant payments may be brought outside the scope of CIS entirely as this will remove a common pain point when tenant inducement payments are made.

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