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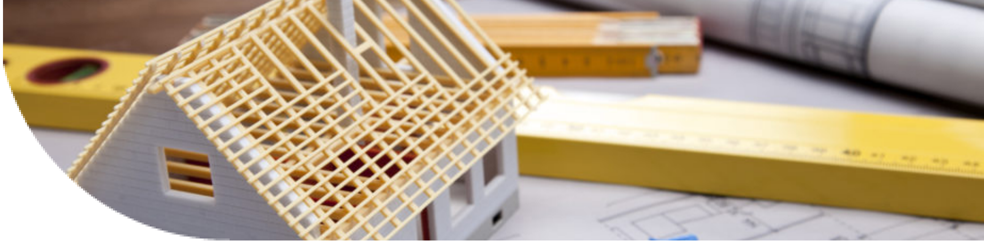

Let’s Not Dwell in the Past: an SDLT Update for Developers

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Stamp duty land tax (SDLT) has been headline news since Rishi Sunak unveiled the temporary reduction in SDLT for residential properties in July in an attempt to boost a stalled housing market.

But SDLT is rarely far from developers’ minds. Here are three SDLT areas where developers often make mistakes.

On what is SDLT payable?

Developers often forget that SDLT is not just payable on the price. The tax is payable on the “chargeable consideration”; this includes VAT, other sums paid to the seller throughout the transaction (such as legal fees) and sums paid on behalf of the seller (which could include the seller’s agents’ fees, depending on the arrangement). SDLT is also payable on future sums that could become payable, such as overage.

When is SDLT payable?

Payment is due within 14 days of the “effective date”. The effective date is usually completion, unless the contract is “substantially performed” before then e.g. by payment of a substantial part of the price or by the developer (or its contractors) taking early possession of the whole or substantially the whole of the land. According to HMRC guidance, this happens when "the purchaser obtains 'the keys to the door' and is entitled to occupy the property".

What about accessing a site for surveys? The more limited the nature of the entry (e.g. in terms of hours and area), the less likely it is to amount to substantial performance. Access to remove asbestos could easily constitute taking possession. Carrying out demolition works would definitely constitute substantial performance.

If a site is held under an option agreement, it is not possible to substantially perform the option until it has been exercised, due to options having their own separate SDLT regime.

What is a residential property?

The question of what constitutes residential property continues to confound developers, as the classification of many sites for tax purposes is not always clear cut. As such, this question is the focus of this article.

The savings for a developer can be substantial. By way of an example, on a £5m purchase of a potential development site, the SDLT payable for non-residential or mixed property is £239,500 compared with a tax bill of £663,750 for SDLT for residential property – a saving of well over £400k.

So what is residential property?

The Finance Act 2003 provides that property is residential if it is used as a dwelling or suitable for use as a dwelling or in the process of being constructed or adapted for such use. This includes the garden or grounds of a dwelling. All other property is considered by HMRC to be non-residential.

Developers have long tried to minimise their SDLT liability by demolishing buildings or disconnecting services prior to completion (so as to make the property unsuitable for use as a dwelling), but such attempts tend to fall foul of the rules around substantial performance referred to above. The courts have also differentiated between a property being "capable" for use as a dwelling and "suitable" for such use. In the Fish Homes case, also decided in April 2020, the court held that defective cladding did not render a property unsuitable.

The complexity of the law, combined with the fact that the allocation of tax rates could mean the difference between a viable and a non-viable development site, means that disputes with HMRC over the categorisation are frequent. This is despite HMRC publishing (and regularly updating) detailed guidance to assist developers and their advisors in establishing the appropriate tax rate.

And it does not stop there… The number of dwellings purchased can change the rate, and other reliefs could be available to reduce the tax liability.

Six or more separate dwellings purchased by way of a single transaction changes the rate to non-residential. Savings can also be made using multiple dwellings relief (MDR) where the consideration is averaged out across the transaction by reference to the number of dwellings. This has made the courts recently in respect of "granny" annexes, for example in the Fiander and Brower case decided in April 2020, where MDR was held to be unavailable as the annex (which had an external door but no door separating it from the main residence) could not constitute a separate dwelling.

What about undeveloped land?

As there is no dwelling, it is likely to be non-residential for SDLT purposes (but see below if it falls within the grounds of a dwelling). If a developer buys a site where construction has already started, previous uncertainty has been eased by HMRC guidance released in October 2019. New dwellings will only be considered as such when works have begun "on top of the foundations", bringing the concept of a newly constructed dwelling in line with the golden brick VAT rules. So most site preparation would not make the land residential.

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Gardens and grounds are another area where uncertainty may arise. The Hyman case in July 2019 provided that “grounds” has a wide meaning, and decided on the facts that a barn in the extensive grounds of a farmhouse near St Albans formed part of the residential property. If it had been used for a commercial purpose, it would not have been occupied with the residence.

More recently, in March 2020, the court again held in HMRC’s favour, deciding that an adjoining paddock formed part of the grounds of a dwelling as it was an appendage to the dwelling and did not have a stand-alone function. Interestingly, the court also noted that there may be circumstances where land surrounding a dwelling is so extensive that it ceases to be “grounds” (and thus non-residential). Here, three acres was not considered to be “so extensive.”

If you would like further information, please contact our Real Estate Solicitors across our Bournemouth, Southampton and London offices.

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