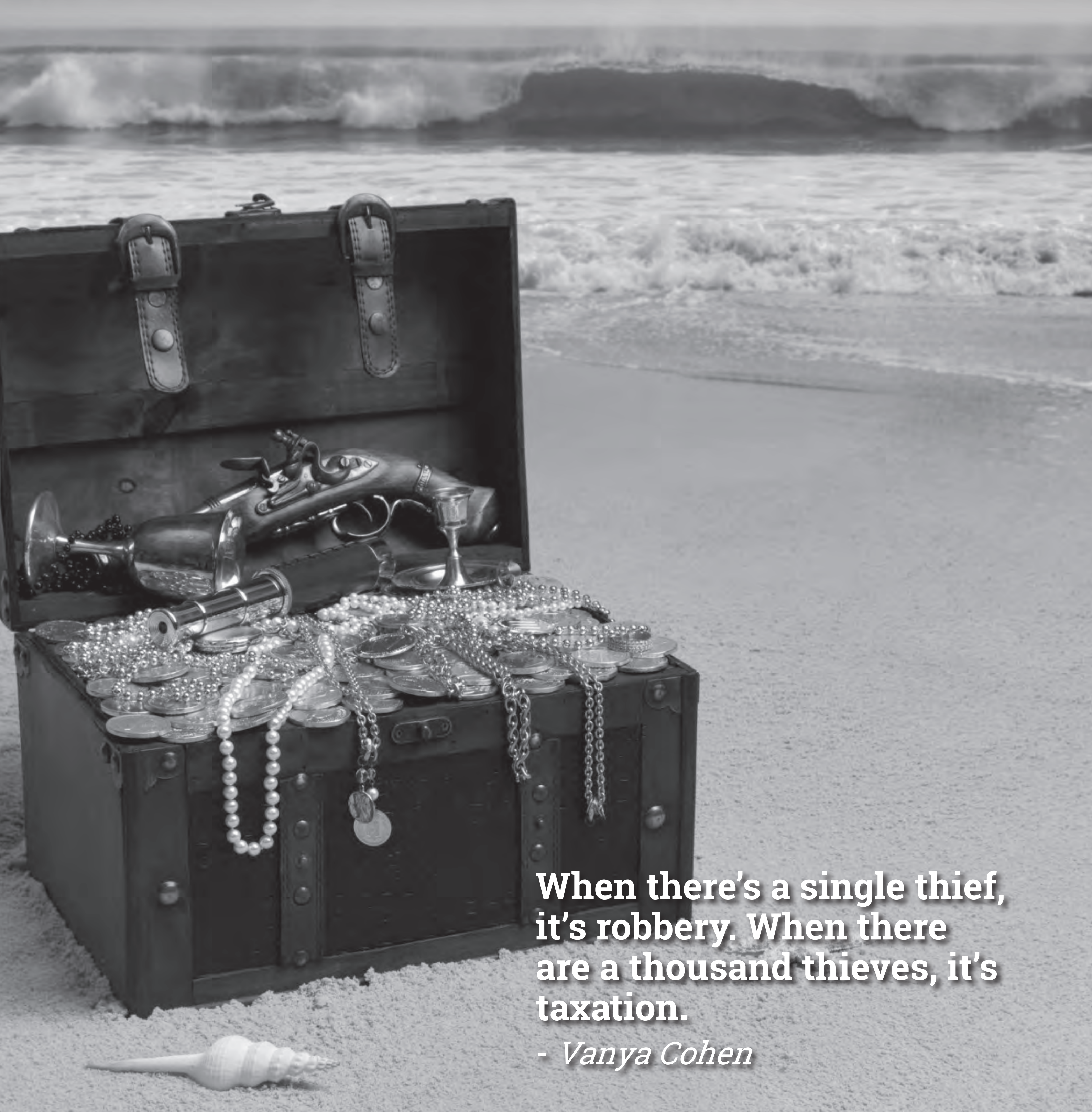
The Schmidt Tax Report

Tax, Money & Property

October 2016



When there's a single thief, it's robbery. When there are a thousand thieves, it's taxation.

- *Vanya Cohen*

The Schmidt Tax Report

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Tax

News

Making Tax Digital slammed

Government plans to make tax digital (MTD) by forcing all businesses with a turnover of more than £10,000 a year to update tax on a quarterly basis has been criticized by business groups and accountants. The latest attack has come from consultants Lamont Pridmore which estimates that 2.6 million small businesses will face an average bill of £1,250 to move to MTD as a result of increased accountancy fees and software costs. The Treasury Select Committee chairman Andrew Tyrie has warned Philip Hammond that not enough time has been allowed for consultation.

Things going well for HMRC

HMRC has had a good month:

- It won its tenth successive case against tax-avoidance schemes promoted by NT Advisors. The Court of Appeal has ruled that NT Advisors' latest scheme consists of a series of circular payments designed purely to generate tax deductions with no genuine commercial purpose. No tax relief is therefore due. NT Advisors is the firm that came up with the very creative (but unsuccessful) Working Wheels scheme, whereby participants claimed to be second-hand car dealers.

- It announced that it carried out raids on 761 properties last year, an increase of 28% on the year before. The continued rise comes as HMRC is under ongoing pressure to increase the number of successful prosecutions for tax evasion and has been granted extra resources to enable it to pursue more cases.

- It seized assets worth £42.6m from 1,592 business last year in order to settle tax debts, an increase of 145% on the previous year.

- It is now targeting 1,181 different types of tax-planning schemes for the issuing of accelerated payment notices (APNs), although there have been a number of successful legal challenges, including a number of judicial reviews. An APN is a demand for upfront payment of disputed tax within 90 days where HMRC suspects an avoidance scheme, prior to a formal hearing. The tax must be paid without appeal.

R & D claims up

The amount of money received by companies for research and development last year rose by 38% on the previous year. Since R & D tax credits were launched in 2000, the Government has provided almost £14bn in tax relief with small and medium-sized enterprises (SMEs) taking the lion's share: 39,360 different claims compared to 9,030 for large companies.

Non-doms pay more tax

Pinsent Masons has issued a report showing that non-doms pay ten times more tax than the average taxpayer pays and suggests that a combination of recent tax policy and Brexit may result in a very substantial loss to the Exchequer. Fiona Fernie, head of tax investigations at the firm, said: "Non-doms make a highly valuable contribution to the

UK economy and any substantial exodus could have serious long-term impacts. Many are highly successful entrepreneurs and in the business sector meaning they establish or invest in UK-based companies, thereby creating thousands of jobs." The total tax take from nom-doms last year was £6.57bn.

In a separate communication, Paul Johnson, director of the Institute for Fiscal Studies, said that, post Brexit, tax revenues would be hit by the departure of a relatively small number of City workers. "If we lose even a relatively small fraction of people from the City of London following Brexit – which seems at least feasible – that will have a big impact on the tax take and the rest of us will have to make up that tax they are currently paying," he said. He pointed out that the income tax system relies heavily on richer taxpayers, with over a quarter of revenues coming from the richest 1% of income taxpayers.

Clients sue Ingenious Media

Investors in Ingenious Media film schemes that HMRC has determined as tax avoidance are suing the company. In court cases, some of the Ingenious Media tax schemes were considered avoidance; others weren't. The group was responsible for funding several blockbusters, including *Avatar, Life of Pi* and *The Girl with the Pearl Earring.*

Smartphone scheme a bad idea

The self-employed workers' trade body IPSE, the Federation of Small Businesses and other groups have criticised a government plan for self-employed workers and buy-to-let investors, as well as micro-entrepreneurs including Airbnb landlords and Uber drivers, to pay tax in advance using their smartphones. HMRC intends to launch a voluntary pay-as-you-go digital tax system, designed as a budgeting tool to help businesses, landlords and the self-employed avoid the shock of big tax bills. Critics feel that it could prompt people whose income is uncertain to make advance tax payments at the wrong time and ruin their cash flow.

Post-it note experiment

HMRC has been attaching handwritten Post-it notes to letters urging taxpayers to get in touch. The tactic is an attempt to push taxpayers who are caught up in avoidance schemes into paying up. Notes say things like: "Please give me a call, if you would like to discuss…" and are signed with a first name and a phone number.

Editor's Notes

And the little one said, "Roll over!"

In the same way that one of the golden rules of property investment is 'delay, delay, delay', so one of the golden rules of all tax planning is 'delay, delay, delay'. Why? Postponing a tax liability offers many advantages, not least the hope that the tax position may improve before tax eventually has to be paid. For example, new, more favourable legislation may be passed or your own circumstances may mean a lower liability.

One of the most useful ways of delaying a capital gains tax (CGT) liability is to take advantage of rollover relief. You can claim rollover relief when the proceeds from the disposal of an asset are reinvested in another, replacement asset. Both assets have to be used for the purposes of a trade that is carried on by the taxpayer. Relief is given by treating the first asset as having been disposed of for nil gain/nil loss. As a result, the base cost of the replacement asset is treated as reduced by the chargeable gain deferred. The portion of the proceeds that are retained remains taxable.

To qualify for the relief you must buy the new assets within three years of selling or disposing of the old ones (or up to one year before), and your business must be trading when you sell the old assets and buy the new ones, and you must use the old and new assets in your business. You can claim relief on a wide range of assets, including land and buildings, fixed plant or machinery, ships, aircraft, hovercrafts and – although I feel this is unlikely for any reader of *The Schmidt Tax Report*, but one never knows – satellites, space stations and spacecraft! You may also (if you aren't trading through a company) be able to roll over gains from goodwill, agricultural quotas and even fish quotas.

As rollover relief is not without its complications, it is well worth consulting with a professional tax adviser prior to taking any action. One final tip: keep tight records. If you get into a row with HMRC, it will help if you have plenty of evidence to back up your claim.

R & D scams

The extremely intelligent and efficient MD of an SME in which I am a fairly major investor telephoned the other day to tell me that he was about to submit an R & D claim that should, after paying the specialist adviser's fees, result in a £120,000 refund. What I wanted to say was, "Are you an idiot?" Instead, I asked to see the claim and also the agreement with the advisers. I was not surprised to discover that the submission to HMRC was vague and shabby or that the so-called specialist tax firm was charging a thumping 30% of any tax credit received. It transpired that the MD had been talked into making the submission on the basis that it wouldn't take much time and wouldn't cost anything. If you have had a similar approach, I would strongly recommend rejecting it. The firms offering this sort of deal are – to say the least – flaky. They work on a numbers game. Of a percentage of claims put in, a certain number will be accepted. To put it into perspective, most reputable tax firms will offer the same service for between 7.5 and 15%. PwC charges 12.5%, for example. It is true that many companies do not claim all the R & D credits to which they are entitled. Eligible R & D must be "seeking to achieve an advance in science or technology". It must also be "subject to scientific or technological uncertainty" and "conducted in a systematic and thorough fashion". These conditions are often easier to meet than it may at first appear. Moreover, the R & D tax credits available to SMEs are well worth having. The super-deduction available has been 230% since 1st April 2015 with the cashback available to loss-making SMEs now 33.35% of the qualifying expenditure. The rise in the rate of relief for SMEs means that the cash value of claims for tax-paying companies is £26 for every £100 of R & D spend from April 2015 (based on

a 20% tax rate) and £33.35 for companies with losses.

A rare enough taxpayer victory

Pity poor Mr Bayliss, a retired teacher who inherited, quote, a lot of money in the 1990s and – on the advice of his accountant and another specialist – used something called the Pendulum Long arrangement to save a rather juicy six-figure sum of tax. Perhaps not surprisingly (the scheme involved a very dubious loss of £539,000) HMRC decided to investigate in 2007 and the case was finally settled – in the taxpayer's favour – this year. Still, nine years of HMRC breathing down your neck is no joke! The Revenue accused Mr Bayliss of fraud and negligence. He denied both, pointing out that he took specialist advice from a reputable professional whom he repeatedly asked to reassure him that the scheme was legal. The First-tier Tribunal agreed with him. So, a victory. And good news for other taxpayers who have been wrongly accused by HMRC. But, as I say, pity Mr Bayliss for having to go through so much, especially as he kept offering to pay the disputed amount of tax and only objected to the penalties and interest.

An end to all taxation?

A huge fuss is being made in the business media about how blockchain is the biggest digital development since the Internet. The technology – which allows anything of value to be traded securely through a tamperproof log of events – is what allows digital currencies, such as Bitcoin, to exist. However, blockchains have many other applications such as, to offer just one example, the ability to create a permanent, public, transparent ledger system for compiling data on sales, storing rights data and tracking digital use and payments to content creators. To offer another example, in the banking and insurance sector, blockchains could be used to strengthen and streamline compliance checks on customers and reduce the risk of fraud.

Basically, a blockchain is a type of database that takes data and places it in a block. Each block is then 'chained' to the next block, using a cryptographic signature. This allows blockchains to be used like a ledger, which can be shared and the information within it corroborated by anyone with the appropriate permissions. Any change to the data cascades down to all the other copies, making any nefarious scheme a tricky proposition.

The UK Government's chief scientist, Sir Mark Walport, says that blockchains should completely redefine the relationship between government and citizen in terms of taxation, data sharing, transparency and trust. He makes the case for integrating the technology into the state's daily apparatus: "Ledgers have been at the heart of commerce since ancient times… Now, for the first time algorithms enable the collaborative creation of digital distributed ledgers with properties and capabilities that go far beyond traditional paper based ledgers."

Opinions differ on how the new technology will affect taxation. On one hand, some experts feel it will enable the Government to tighten its hold on a substantial percentage of all financial transactions and thus ensure that it gets its share of any tax due. On the other hand, a specialist blockchain publication called *Coin Express* suggests that:

The advent of Bitcoin and blockchain technology has made government taxation obsolete, given how difficult cryptocurrency can be to identify and trace. With the rise of Bitcoin and other cryptocurrencies based on blockchain technology, state power to tax income is slipping, and may at some point become a thing of the past entirely. While all Bitcoin transactions are public and viewable by anyone, the ownership or control over wallets and addresses are not. Simply use different addresses, and financial investigation is effectively obfuscated from a superficial investigation.

Whoever is right, there can be no doubt that blockchain technology is here to stay and we all need to understand what it is and how it will affect our businesses and lives – for better or for worse.

Ask The Experts

Q. Since the death of my father earlier this year, I have spent many weeks sorting out my mother's finances, finding help for her (gardeners etc.), organising medical treatment for her (including many hours of driving taking her back and forth to appointments), finding a new house for her, the sale of the family house, the purchase of the new one, organising for work to be done on the new one, etc., etc. Those weeks/months have significantly delayed development of the initial product of my own start-up company, so have not only taken much time but also had a significant financial impact. My mother would like to compensate me financially for the time I spend on her behalf. Normally I would say no, as I've been helping family, but the amount of time/effort involved is so significant that I am now wondering how such financial compensation could be organised. If just done as a gift, there is a high probability that there would be inheritance tax (IHT) consequences later on given my mother's age. Can you advise on alternatives, please, ideally covering both the effort so far (maybe 3 months of my time), with an on-going element too (estimated at 2 days per week for the next few months at least)? (I don't mean to sound heartless, but if the launch of my company's first product continues to be delayed, continuing with no income is going to become a problem in the not too distant future).

J. H., via email

A. Let us assume you are correct and a gift to you would be liable to IHT at 40%. It is unlikely that a deed of variation would do anything to improve the position, since a gift made in your father's name would just reduce the IHT nil rate band available to your mother.

Three ideas do spring to mind.

First, if your financial position is as bad as you suggest then perhaps you will only be a basic rate taxpayer in 2016/17. In which case, if you actually charged your mother for your services, the income would be taxed at 20% in your hands but would save 40% IHT on her death, so this would be tax efficient. (Depending on how much you charged and

whether you treated this as a trade, there could be National Insurance contributions as well as tax, but even if this were added it would still be cheaper than paying the IHT.) If you treated the money as trading income you would then be able to claim relief for your mileage, telephone costs, use of your home, etc. which would reduce the tax payable.

Second, does your mother have more income than she needs for her living costs each year? If so, then any amounts she gives you can be treated as regular gifts out of income. If she establishes a pattern of giving and the gifts do not cause her to eat into capital to fund her own living costs, they will not count as gifts for IHT purposes and will not be taxable on you.

Third, get your mother to invest in your start-up company. While this won't provide any direct income for you, an investment in a trading business is always good IHT planning as the shares should qualify for 'business property' relief when she dies so there will be no IHT on the amount invested. This would indirectly help you financially through helping your business and the capital injection may permit you to take a salary from the business.

Finally, do bear in mind that if your mother makes a gift to you now and she does die within seven years the IHT payable will not be any greater than if she had held on to the money and passed it to you in her will. So there is no disadvantage to making a gift now and there is always the possibility that she will survive for seven years, in which case IHT will have been saved.

Q. A further question from J. H.

All of those options make sense.

One question regarding the third suggestion – that of my mother investing in my company to use BPR. At present, although the Ltd company exists, it is dormant, so no corporation tax returns etc. to complete. Would an investment into the company (presumably by purchase of shares) change the dormant status, whether the company were to pay the money to me as salary, or whether the company uses it to pay expenses (whilst still not trading in the sense that there are no sales etc. going on)?

J. H., via email

A. If the company were just to receive the investment but do nothing with it so that its balance sheet showed, for example, share capital of £10,000 and cash of £10,000, it would still be considered dormant as there would be no income or expenditure.

However, if the money were used to fund expenses then the company would no longer be dormant: it would need to do accounts showing those expenses and file tax returns to establish the loss for the year, which would be carried forward for offset against future profits once the company was generating income.

Divorcing? Don't Cut The Taxman In On A Share

Life is so complicated these days that couples going through the traumatic experience of ending their marriage haven't just got practical and emotional issues to deal with: they also have financial problems, and in particular problems with our old friend HMRC, who is never backward in coming forward where there are assets to be divided up and, perhaps, a share of those assets to seize.

So we thought it would be useful to provide a handy guide to ways of leaving the taxman out of the distribution and, more generally, a guide for the divorcing or newly divorced as to what they should be doing to make their situation as tax efficient as possible.

The race before the end of the tax year

This is definitely an example of how our tax system doesn't look like it was made up on purpose. The chances are that wealthier couples will be holding on to assets which are within the scope of CGT. Such assets include investment properties, second homes which aren't the main residence of the couple (who can only have one main residence between them), shares in companies, interests in businesses and other similar investments. And this is where the practical problem comes in.

The problem arises because these assets are likely to be owned jointly or, if they aren't, there is at least likely to be some transferring of CGTable assets between the soon-to-be ex-spouses, as part of the financial settlement. The usual rule for transfers of assets between spouses, of course, is that there's no CGT on them. Technically, assets are treated as transferred at what is effectively their original cost on purchase, so that no taxable gain arises. However, this treatment has got to come to an end at some point, if the marriage is finished. The thing is, this point comes sooner than many people suspect.

CGT-free inter-spouse transfers stop not when the decree absolute of divorce is made but on the date, sometimes very much earlier, when the couple separate.

And this brings us on to a quirk of the rules. If one peers through the thick surrounding undergrowth of the Taxation of Chargeable Gains Act, one sees that CGT-free inter-spouse transfers happen during the tax year in which they are living together, i.e. in which they have not yet separated. So, practically speaking, one has to take the date of separation and then work through to the following 6th April, which is the date on which such tax-free transfers can no longer take place.

An extreme example can be used to illustrate the effects of this legislative quirk.

Janet and John are a couple who have been getting increasingly on each other's nerves for a period of years now, and the flaming rows are becoming increasingly incandescent. Unknown to Janet, John has already prepared a bolt-hole, in the form of a flat in town, which he's acquired and furnished to move into if life with Janet finally becomes 100% intolerable.

On 5th April comes the last and most

violent of the arguments between the couple. John says to Janet: "That's it! I'm off! and I'm not coming back – ever… you understand?"

Janet listens as the front door slams. It's half past eleven at night on the 5th April.

Next door, Darby and Joan are also having a terminal row. Darby hasn't thought ahead as John has, and so, although he feels suffocated living in the same house as Joan, has nowhere to go at 11.30 at night. So, although the argument is taking place (by coincidence) at exactly the same time as Janet and John's next door, Darby has to content himself with sleeping on the sofa and packing his things the next morning to stay in a hotel.

Those who've been through the tax trauma of divorce (to say nothing of all the other traumas) will recognise that there is a fundamental, and quite arbitrary, difference between the tax situation facing these two couples. Both have a jointly held buy-to-let property portfolio, which is a substantial source of income for them, and which they acquired, mostly, some years previously. So there is a big capital gain 'inherent' in these portfolios.

The difference between the couples, essentially, is that Janet and John can't share out the properties, moving them from John's ownership to Janet's or vice versa, with the shelter of the CGT-free inter-spouse transfer rule. This is because a new tax year has started, and it is one in which the couple were at no time living together as husband and wife – because John moved out half an hour before midnight on 5th April.

Darby and Joan, on the other hand, have virtually a whole year to arrange their inter-spouse transfers, because they were living together, even if only for a few hours, at the beginning of the tax year. You see the problem?

CGT planning on divorce

Of course, we're not suggesting that couples should carefully time their flaming rows to ensure that these happen early in the tax year, and therefore give them maximum time for asset transfers! But things often aren't as clear-cut as what we've described, with the door slamming behind a departing spouse who never comes back. Very often, dare we say it, the 'final' departure turns into no more than a temporary estrangement? Often, too, there can be some lack of clarity about when the actual separation took place.

The law doesn't give us very much guidance at all on this, merely stating that the cohabitation of a married couple ends when they separate in such circumstances as that separation is likely to be permanent.

So, while tax obviously isn't going to be uppermost in the minds of those who are in a highly emotional state, separating couples who are able to be more dispassionate and rational in the way they go about things will find a potentially major benefit in setting the formal date of their separation at the beginning of the tax year. If life isn't absolutely intolerable under the same roof, the potential tax advantages of being sensible in this respect are obvious.

The matrimonial home

The couple's main residence, if it has been such throughout their period of ownership, is of course an exception to the above situation where asset transfers after the year of separation give rise to tax problems. A person's main residence is exempt from CGT. So, whether the house is made over by one of the spouses to the other or the house is sold in order to provide money for each to buy new homes, there shouldn't be an issue – providing things are dealt with on a timely basis.

Sometimes, though, such is not the case. Very often, in fact, what happens is that one of the spouses moves out (and possibly moves in with someone else) without the home being sold, and without any formal divorce proceedings being started. Sometimes, indeed, this situation can last for a period of some years, with the departed spouse continuing to own a joint interest in the ex-matrimonial home.

This does become a problem once this period of absence has gone on beyond a certain length of time. The rule is that if a property which has been your main residence ceases to be such your last eighteen months of ownership are treated as still exempt by a kind of statutory concession. Do watch out for this point: the period used to be three years, and has recently been halved to this much shorter period. Effectively, after the departing spouse has been away for eighteen months, a portion of the gain on any ultimate sale of the house becomes taxable, and this becomes a greater proportion the longer the situation goes on.

So the obvious practical point, if it can be brought about, is to secure a disposal of the departing spouse's share in the property before the eighteen months are up. (If you go over the eighteen months by a short period only, it may be that you would only make a small gain within your available CGT annual exemption of about £11,000.) If there is going to be any kind of divvying up, for example the remaining spouse getting a 100% interest in the house in exchange for their transferring an investment asset, say, to the departing spouse, it's best to get on and get this sorted, for this reason. Alternatively, the person staying put may have a new partner who is able to buy out the departing individual. If so, better sooner rather than later.

Divvying up jointly held assets

In some cases, you will have a neat situation where assets, such as investment properties, are all held jointly between the two individuals. If a fair and equal split can practically be arranged, it can be very advantageous from the CGT point of view (CGT is the main tax enemy of divorce) for spouse A to take a 100% interest in half of the properties and spouse B a 100% interest in the other half. This is what is known as an exchange of joint interests, and there are reliefs from both CGT and stamp duty land tax (SDLT) for such transfers.

Where the amounts being received by each ex-spouse are not equal and there is a balancing payment, this payment gives rise to tax.

Also, bear in mind that this relief doesn't apply to the main home. That is, you can't

roll over the gain on a property if what one of the spouses is getting in return is an increased entitlement to the home.

With SDLT, there's also potentially a nasty trap where the properties are mortgaged. If a spouse takes over sole liability on a mortgage which previously was joint that could be treated as consideration given for the exchange of interests over and above the handing over of other property interests. Where there is consideration in the form of debt in this way, SDLT can apply.

Although the rules are the usual obscure muddle, it does look as though, if you have a sensible bank or building society that will refinance on the strength of the new ownership, without the previous loans actually being taken over as such, you may be able to wriggle out of this SDLT problem. This is a little bit beyond the scope of a practical advice-giving article such as this, however!

Valuing the joint wealth

How do you value the jointly held assets, particularly if they are what is known as 'pregnant with gain'? This is a thorny subject, and one on which the lawyers seem to have made up their minds in a way which accountants find more than a little baffling.

To focus on the issue by taking an example: let's say Adam and Eve are getting divorced, and Adam owns an investment property worth £1 million, which he paid £500,000 for a few years ago. If he ever sold it, he would be facing a tax charge based on 28% (it's a residential property) of the £500,000 gain (i.e., ignoring annual exemptions, £140,000). If he had to turn the asset into cash, he would end up with only £860,000 rather than the £1 million that the property was actually worth.

This is where the lawyers may be landing someone in Adam's position with what accountants would regard as an unfair advantage, because the rule seems to be (and we're not experts here) that you take the net of tax value of assets held, such that Adam only needs to account for receiving value of £860,000, not £1 million, if the divorce settlement is that he takes the whole property away with him, in return for Eve being allowed to keep something else. Accountants would say that you should only take account of this tax liability if the charge was likely to arise in practice in the foreseeable future. However, subject to correction by matrimonial lawyers, it does seem to us that this is the way the matrimonial estate should be valued.

Income: A clean break?

Moving on (at last) from CGT, there's sometimes a question as to whether the couple should bring about a clean break, if they practically can or whether the wealthier or the higher-earning spouse should pay over regular maintenance to the other. Income tax suggests that a clean break is generally better, because the spouse with higher income no longer gets tax relief for paying maintenance to the other spouse, to look after that spouse and, perhaps also, the children. These payments used to secure relief but this was done away with many years ago now.
So it makes obvious sense, from the income tax planning point of view, for income-producing assets to be transferred to the spouse once and for all so that the income becomes hers (let's be honest: it's usually the husband paying maintenance to the wife).

Sometimes, though, it's not practicable for an asset simply to be transferred over, root and branch, in this way. Take the example of the couple whose main or sole income-producing asset is the family business. Let's say the husband will continue to run this business after the divorce, but that the needs of the ex-wife and children dictate that a share of the profits should continue to be paid to them.

The wrong way to bring this about is to have a maintenance order where the husband receives income from the family company and pays it over in a non-taxable, and non-tax-relievable, form to the spouse.

A much better way of doing it, if it can be agreed, is for – preferably non-voting – shares in the business that give rise to an entitlement to receiving a dividend to be made over to the wife or to a trust for the wife, so that the dividends become the wife's income rather than passing through the husband's income tax computation on the way. This can result in a major saving in terms of using the wife's lower tax rates.

Inheritance tax

Finally, remember that divorce is likely to make a substantial difference to your ultimate IHT exposure, and therefore planning. Unlike the situation with CGT, IHT goes by decree absolute: a bequest to a surviving spouse is normally 100% exempt from IHT, and remains so all the time the marriage still continues. This leaves aside, of course, a question of whether the spouse will want to continue to have their ex as the main beneficiary of their will!

Once the divorce has gone through, though, what could be termed the IHT 'safety net' has been removed. Assuming both individuals remain unmarried, as is most often the case these days, the old basis of planning, under which the entire estate was exempt because it was left to a surviving spouse, is no longer available. Where a married couple have the most customary form of will, the so-called mirror will, under which the estate goes to the other, there is no tax on first death because this bequest is IHT exempt. The surviving spouse then hopefully has a period of years over which he or she can downsize and make gifts to the younger generation.

In the typical example of a couple who divorce and find other partners, whom they don't marry, this situation is replaced by one in which the estate could be radically depleted on the death of the individual, so that the surviving partner has much less to live on than they would have done. The planning implication of this is almost too obvious to state: if you're going to be sharing your life with someone on a permanent basis in any event, you may as well go through a legal form of marriage, whatever your religious views. This at least will have the effect of fixing the IHT-planning safety net back in place. You can vary a person's will after their death in order to make the situation more tax efficient, but we don't know of any legal system under which you can marry them posthumously!

Saving SDLT Through LLPs (With Apologies For The Acronyms)

First of all, rather than irritatingly assuming prior knowledge as so many acronym users do, let's explain exactly what we mean by the above title. SDLT is stamp duty land tax, a tax that replaced the older stamp duty back in 2003, where the subject matter is property (land and buildings). In Scotland, this has recently been replaced by LBTT, or the land and buildings transaction tax, but basically all the rules, as far as this article is concerned, seem to be the same with LBTT as they were for SDLT. LLPs are, of course, limited-liability partnerships.

Let's consider two specific situations where using an LLP could save you bucket loads of SDLT:

• Where you want to give a property, or an interest in a property, to a family member, and there is a mortgage secured on the property; or
• Where you want to transfer the property to a company you own.

Fortunately, in a lot of situations, there's no SDLT on gifts of property. However, where you transfer a property subject to a mortgage, the transferee is treated for SDLT as having 'paid' the amount of the mortgage. So if you 'gave' a property worth £1 million that had a £400,000 mortgage secured on it to your son, your son would have to pay SDLT as if he had bought the property from you for £400,000. However, note that you can achieve much the same commercial result by forming an LLP in which you and your son are the two members. The property can be introduced to the LLP by you as capital, but at a lesser value. Even though there is a mortgage on the property, special rules applying to LLPs (and partnerships generally, indeed) mean that the existence of this mortgage is disregarded and, because you and your son are 'connected' within the meaning of these special rules, there is no SDLT to pay. Your son can then effectively enjoy as many of the benefits of ownership of the property, via his LLP membership, as you choose to give him.

Sometimes, also, you want to transfer a property to a limited company. There may be either commercial or tax-based reasons for doing this, but the normal rule is that the transfer of a property to a limited company gives rise to SDLT at the market value of the property. Even if you transfer the property in at an under value for accounting purposes, the rule with company transferees is that they pay SDLT on the market value.

This is not necessarily (with the emphasis on the word 'necessarily') the case where you introduce a property into an LLP in which the company is another member. Depending on what rights the company has to income, you can use the formulae which apply under the special rule regime we've mentioned to reduce or even completely eliminate the SDLT that would otherwise have applied. Depending on other circumstances, you can then bring about the situation where the company receives a share of the income from the property (assuming it's let at a rent) and thus you enjoy the more favourable tax regime for net rents that limited companies enjoy. The objection could be raised, in some cases, that it simply isn't possible to transfer a property with a mortgage on it to an LLP. It may be, of course, that the same objection will apply to the father transferring a mortgage property to his son, if the son's income isn't sufficient for the mortgage company to be happy in changing the loan over into his name.

However, we understand from the lawyers that it is possible to transfer the beneficial interest in a property to the LLP without transferring the legal interest, and that this is in no way prejudicial to the lender's interest. The beneficial interest can be transferred by a deed, prepared by a solicitor, stating that the legal owner is now only holding the property as bare trustee for the LLP. This has all the same effects for tax purposes as transferring the property, legal interest and all, to the LLP.

Funding From Your Pension?

There are times when people in businesses of any kind, including investment businesses, chafe at the amount of funds they have 'locked up' and inaccessible in their pension schemes. But there are situations where you can unlock your pension scheme funds.

In situation one, it may be that you are running a business through a limited company and that company has need of working capital. (It may need that working capital because you've drawn too much money from the company, but that's another issue.) If your pension scheme is what is known as an SSAS (small self-administered scheme), it can loan its funds to the company to make up such a working capital deficit. The terms of the loan are quite strict in law, and must allow for a commercial interest to be paid, and for the loan itself to be paid off over no more than a five-year period. However, the ability to use the funds may well make these commercial constraints justifiable.

If your pension scheme isn't a company SSAS but another type of scheme, like a personal pension, it is usually possible to transfer the personal pension into a newly formed SSAS so as to bring it within these rules.

A second way of potentially 'unlocking' funds in a pension is for that pension scheme to acquire an asset from you. There is, perhaps surprisingly, no bar against pension schemes transacting in assets with their own members, providing the transaction is at the market value of the property. There is, however, of course, a restriction in what the pension scheme can invest in. The big restriction likely to apply here is residential property.

If, though, you have a commercial property investment or, indeed, you have a commercial property from which you are carrying on some kind of trade (or your company is), there is nothing stopping the pension fund from buying this, and your thereby turning the pension fund cash into cash in your own bank account, which you can then do what you like with. Bear in mind, of course, that the sale of the asset to the pension fund may give rise to CGT. Bear in mind also, though, that this tax may be something you can reduce by way of a counterbalancing contribution into the pension scheme itself. The possibilities are endless!

The Business Column

Starting a new business

It's been a long time now since I last dealt with tax issues arising on starting a new business and, with the current headlong pace of change in the tax rules, it's probably high time I looked at it again. Many of the considerations won't have changed, of course, but some will, and the worst thing you can do is act on out-of-date information.

A limited company or not?

Many people don't even raise this question in their minds. They take it for granted that, if you're starting a new business, you need to form a limited company to run that business through. Such is not, of course, the case.

In earlier additions of this magazine, indeed, readers could be forgiven for drawing the conclusion that we thought the only really sensible structure for a business was the LLP structure. Certainly LLPs ticked all the boxes, if they had limited companies as partners, and almost the only argument against an LLP structure of this sort was the fact that it was more complex and, therefore (even if marginally), more expensive to run.

This is, in fact, arguably the biggest change in the whole area of the subject of this article since I last addressed it. With the Finance Act 2014 came a raft of restrictions which made life much more difficult for the LLP or partnership with company partner, and these are arguably now more of a specialist concern (even though, in my view, this is ultimately going to be the best structure still, in many cases) and one which those in the very early stages of running a business probably don't need to bother their pretty heads about just yet.

But the basic question of "Should I be a limited company or not?" is still very much a live one, no matter what the size of business.

Without rehearsing all of the tax and other considerations in full, which would take over the whole of this article, and is in any event summed up in my book *The Entrepreneur's Tax Guide*, it might be more useful, here, to state the case for and against companies in the form of a rebuttable presumption.

The presumption is that a brand-new start-up business does not need the additional formality and cost of a limited company unless either:

- limited liability is a must; or
- profits are likely to be very substantial even in the early periods.

Limited liability

Limited liability is, indeed, a must in a number of business situations that are either substantial in size or risky in character. Subject to the ability of those who have suffered loss to sue individuals if those individuals are directly to blame, what limited liability does is provide protection for your personal assets held outside the business. In the worst-case scenario, a big claim, or the unprofitable running of the business, can result in that business's insolvency: but it is the company which goes bust and not you personally.

Hitting the ground running

The other situation in which you would almost certainly want a limited company from the word go would be if you were anticipating substantial profits even in the first period or periods of the business. Quite simply, companies pay a lower rate of tax on substantial profits (which, if accruing directly to individuals, would result in those individuals' income exceeding about £42,000 a year) and it is too late to put the business into a company after those substantial profits have arisen.

Of course, the additional complexity and red tape requirements of a limited company aren't the only reasons why I've set up the above rebuttable presumption. Companies also have the disadvantage of cocooning any start-up losses within the company itself, rather than allowing them to be used to relieve directly against your other income as an individual. If those losses are simply carried forward to the next period, and the company never makes a profit, you could end up ultimately with no tax relief for those losses at all.

Also, a company tends to abrogate to itself all of the value of the business, whether it is 'goodwill' or other intangible assets, such as know-how and computer software. If a company becomes the owner of these intangible assets, you can no longer use them as a tax-efficient way of getting profits out of the business.

Keep the intangible assets separate

Let me explain what I mean by this. Taking the relatively straightforward example of computer software to illustrate the point, let's say that Pete is a gifted software engineer who has started up a computer business. If he is one of the kneejerk boys and simply runs the business through the company, going to work every day in the company's business and writing the software, the natural presumption (which HMRC will no doubt insist on) is that the company owns the rights to that software.

If, on the other hand, the business is run as an unincorporated partnership, or as an LLP, the software rights, which may become very valuable if they mean the business can make profits, will be treated as actually or effectively owned by the individuals.

Personal ownership of an asset in these circumstances can be invaluable in tax-planning terms, because of the ability, at some subsequent point, to sell that asset back into the business, probably at advantageous rates of CGT or even none, and then use the amount which the business owes you as a method of drawing cash out of the business tax-free. (This is a highly potted summary of the way this particular form of tax-efficient profit extraction works, but apply to me for more detail!)

The 'kitchen table' business

My next remarks are really addressed to those who are starting in business in a small way, perhaps from home and using

assets which you already own.

What's often overlooked by people in this situation is that they can claim tax relief for bringing these pre-owned assets into the business. You may, for example, use a desk, filing cabinet and computer equipment that previously you'd owned for non-business use. What the tax rules enable you to do is notionally bring these into the business and treat them as having been acquired by the business at their current value. So expenditure you may have incurred some time ago, and on which you never anticipated securing tax relief at the time, can now be claimed on the basis that it is being applied for business purposes.

The same principle applies to your car, motorbike, van or other vehicle. If this is utilised in the business, even if only partially, it can be brought into the business at value and capital allowances claimed, subject to a suitable disallowance of a proportion of those capital allowances to take account of the ongoing private use of the vehicle.

Those running small start-up businesses also tend to need to change the way they think about administration, particularly financial administration. Whereas, in your private existence, you weren't interested in assembling large rolls of receipts, etc. recording your expenditure, as a business this is very important 'skill' to learn. Think of that £20 taxi fare, going to see a prospective client or customer, as equivalent to an £8 note: because this is the value of the tax relief you may well be able to claim if you make sure you get a receipt from the driver. And, of course, that's only one example of how careful record keeping is worth solid cash to you.

Even if the business itself doesn't make a profit, or doesn't make a profit straight away, these expenses can give rise to a start-up tax loss that you may well be able to use as the basis of a reclaim of tax paid on your other income. (Note, incidentally, that this is an area in which the non-limited company structure scores very significantly over the limited company, as I've already commented above.)

The tax formalities

If you're going to be paying somebody a wage, you'll need to start up a payroll. Here's another area where recent changes have made life much more difficult for the start-up and small business. We now have what's known as Real Time Information, which is basically a requirement to keep HMRC up to date online with everything you do in the way of paying employees as you do it. Anyone who has a payroll to operate, in my view, would do well at least to consider using an outside payroll bureau. These companies will tend to charge comparatively modest amounts, and in return will take over all of your onerous obligations, not just in respect of Real Time Information but also in respect of things like workplace pensions, statutory sick pay and the whole tangled mess of red tape that suffocates so many small businesses.

Of course, if the only people who work for your business are your and your spouse, you could decide to sidestep the whole palaver of setting up a payroll, and instead take money out of the company in the form of dividends. If it's a partnership, indeed, any amounts you take out of the business are outside the scope of the payroll requirements in any event.

VAT

The other irritating tax nuisance, of course, is value-added tax, or VAT. Do I need to register? If I don't need to register yet, when will I need to?

These questions come up all the time, and another one which start-up businesses don't ask so often, which arguably they should, is: "If I don't have to register, is there an advantage in registering voluntarily?"

Well, the simple answer is that you have to register once your turnover has gone over the registration threshold, of £83,000. If you've taken over a business from someone else as a going concern, you have to take into account their turnover as well as your own in deciding whether you've breached the compulsory registration threshold.

If your turnover is less than this, at least in the initial period, you may nevertheless decide to register for VAT voluntarily. Why? The benefit of VAT registration is, simply, that you are able to reclaim the VAT on expenses you incur.

In some businesses this isn't going to be much of an incentive, because they won't be incurring a substantial amount of VAT. Other businesses, though, particularly those that deal in goods or necessitate substantial capital expenditure (e.g. on computer equipment) will want to get this VAT back as soon as possible and will want to register for VAT in order to do so. If the customers of your business are themselves VAT-registered, or if your particular type of turnover is 'zero rated' (e.g. selling food or constructing new houses) then there's no downside, commercially, in registering sooner than you need to. Your customers/clients will be indifferent as to whether you are VAT registered or not, because it won't make you any more expensive from their point of view.

Don't overlook the fact, also, that VAT you've incurred prior to registering can also be reclaimed, providing you still have the invoice for the expenditure, and providing it happened sufficiently recently. The rule is, basically, that any goods (generally physical objects) you bought before registering but still own on the date you register for VAT can be made the subject of an effectively retrospective reclaim of the VAT – on production of the relevant invoice. This is known as 'pre-registration input VAT' and the overall time limit is four years from when the asset was purchased. For services, the rule is that services supplied within the six months prior to registration can be made the subject of a pre-registration input VAT claim.

In fact, you can even claim 'pre-incorporation input VAT' if you decide to run the business through a limited company and the VATable expenditure was incurred prior to the company even existing.

Finally under the VAT heading, if you're a small start up it's likely that you'll be eligible for the VAT special rates scheme, under which different types of business can elect to pay over less than the full 20% VAT rate on their sales, in return for agreeing not to reclaim VAT on their purchases. In many

cases, where VAT on purchases is small or non-existent, this can give you a worthwhile annual saving in VAT.

Larger start ups

If you're going to be paying somebody a Moving up the food chain a bit, I'd like to consider two specific situations which are likely to be of immense importance, in terms of their ultimate tax liabilities, to those whose circumstances fit the situations I will be describing.

These are, first, the situation where a person who is already in business, perhaps in a substantial way of business, decides to diversify into a new line of trade etc. and, second, the situation where the highly beneficial tax reliefs given by the Enterprise Investment Scheme (EIS) are available.

Let's take diversification first. Again, here there's a 'natural' or 'unplanned' situation and the contrary situation where tax planning has been considered.

The unplanned situation, if you are running a successful company and decide to open up a new line of trade, is to open up that line within the existing company. This certainly has the advantage of administrative simplicity, because you don't need to set up a separate set of books. However, there are two major potential disadvantages with doing it this way, or conversely you could say there were two major advantages of setting up the new trade in its own new entity or special purpose vehicle (SPV). You could, for example, much more easily bring about a separate, and personal, ownership of any valuable assets which arise in the new business. If, instead of running it in X limited (your current company), you formed A LLP (of which the company may be a member, in order to help finance the new business with initial capital) you could specifically provide that the capital assets of the new business belonged to you as an individual, be they goodwill or any other intangible assets like trademarks or computer software. This takes me back to the principle I mentioned earlier about keeping valuable intangible assets out of the net of company ownership. Second, putting a new business in these circumstances into an LLP potentially enables you to claim tax relief as an individual if there are start-up losses. If you've been paying higher rates of income tax in any of the last three years, this could result in a very welcome tax refund cheque. Of course, you would still get tax relief for start-up losses if you set up the business within X limited, by offsetting them against that company's current profits; however, that is your only option in those circumstances, and the rate of relief you would get within X limited could be significantly lower.

The Enterprise Investment Scheme

Well, I haven't got much room, at the conclusion of an article about business start-ups, for spreading myself about EIS, so let's just concentrate on the essentials. You should be seriously looking at EIS if the answer to either of the following questions is 'yes':

- Are there a number of people who are acquiring equity in the business and are unconnected?
- Have you personally realised a substantial capital gain (or are you expecting to realise one very shortly); and is the business one which requires capitalising with a reasonably substantial amount of money?

It is important to realise that an EIS company isn't a special kind of company in itself. It is simply a company whose activities happen to qualify for the generous tax reliefs I will come on to describe. Any stand-alone (not subsidiary) company formed to carry on a trade that is not on the 'excluded' list qualifies prima facie for EIS reliefs. The excluded activities are largely those which involve heavy investment in land (because the Government feels that these are too 'safe'!) and things like providing legal or accountancy services or dealing in shares or commodities. The land exclusion rules out things like hotels, nursing homes and farming. If you're lucky enough not to fall within one of the exclusions, though, you can apply for the company to be treated as one which is eligible for EIS, by filling in the relevant form *EIS1* and sending it to HMRC.

If the company qualifies then anyone subscribing for shares in the company who, together with connected persons, has no more than 30% of the equity can claim the following reliefs:

- 30% income tax relief for the amount of the investment, so that an investment of £10,000 is equivalent to paying tax of £3,000; and
- complete exemption from CGT if the shares are sold after at least three years.

If everything goes wrong with the business, and the shares become of negligible value, the shareholder can claim loss relief against his other income, even though this is really a capital loss and not an income loss.

Even those who, together with their associates, have more than 30% of the shares qualify for what is potentially a very useful tax relief. This is the ability to offset the expenditure on the new shares against any capital gains that they have made over a given period. It's important to remember that this CGT 'deferral' relief is available even if you own 100% of the company. It just has to qualify under EIS because its trade doesn't include an 'excluded activity'.

It's likely, if EIS applies, that all my other cavils about whether to set up your new business as a company will be overwhelmed by the advantages of being able to claim EIS relief, so that the company option is the clear winner.

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The Offshore Column

HMRC launches new disclosure facility

HMRC has launched its Worldwide Disclosure Facility (WDF). It offers taxpayers a last chance to declare previously undisclosed offshore income and assets prior to the adoption of the Common Reporting Standard (CRS). The facility is available to anyone who wishes to disclose a UK tax liability that relates wholly or partly to an offshore issue, such as:

- income arising from a source in a territory outside the UK;
- assets situated or held in a territory outside the UK;
- activities carried on wholly or mainly in a territory outside the UK; and
- anything having effect as if it were income, assets or activities of the kind described.

The disclosure facility is also available in respect of funds connected to unpaid or omitted UK tax not included above that have been transferred to a territory outside the UK or are owned in one.

Interestingly, this new facility does not offer favourable terms. Anyone taking advantage of it will have to pay the outstanding tax, interest and penalties according to legislation in force at the time the tax arises. They may also still be liable to criminal prosecution.

You may well ask why anyone would wish to take advantage of the WDF. Although it has a minimum penalty of 30%, it is described by HMRC as a "final chance to come forward" before much harder sanctions are introduced in September 2018. After that, tax evaders will pay up to three times the tax evaded, if the proposals currently under consultation are adopted.

HMRC receives more offshore data

Details of hundreds of thousands of offshore accounts were passed to HMRC during September, as a result of recent tax information agreements. At this stage, it is only the Crown Dependencies and Overseas Territories that have handed over information, but HMRC still hopes to raise up to £300 million from this data alone. The information received includes details of bank and investment management accounts, hedge funds, private equity funds, offshore trusts and certain insurance policies. The information relating to non-domiciles – people living in Britain whose permanent home or domicile is abroad – will initially be strictly limited. HMRC inspectors are expected to work their way through the records using software programs that can identify and match information from various different sources. It is anticipated that it could take at least six months before the taxman begins to contact suspected evaders. To date, HMRC claims to have raised £2.4 billion from offshore evasion initiatives and is currently pursuing criminal investigations against more than 90 individuals for offshore offences.

Trust issues

Unless one is willing to break the law, it is now almost impossible for anyone who is British domiciled to establish an offshore trust and still maintain British residence. Or, perhaps, it would be truer to say that for anyone who is UK domiciled *and* UK resident there is no purpose to establishing an offshore trust since it will be considered UK resident for UK tax purposes.

But if you are not UK domiciled, or if members of your immediate family are not UK domiciled or if, perhaps more likely, you become non-resident in the future (or have already become non-resident) then establishing a trust is the perfect way of ring-fencing wealth and shielding if from divorce and litigation as well as political and economic upheaval. It is also the ideal method for passing it on, intact, to future generations. There are also, of course, tax advantages.

By establishing a trust in an offshore financial centre it is often possible to substantially reduce and even eliminate tax charges that would otherwise have to be paid by the trustees on any income or capital gains. The reason for this is that most jurisdictions assess liability to tax on the basis of the residence of the taxpayer. So a UK established trust (with UK trustees) would expect to pay income tax at between 20 and 45% and CGT at 20 or 28%. Of course, if the trust is located in, say, the British Virgin Islands or New Zealand then the trustees will be under no legal obligation to pay any sort of British tax. Trusts also offer an opportunity to reduce or avoid IHT. However, this only really works providing the settlor and the beneficiaries involved no longer reside (or plan to reside at any point in the near future) in the UK after any trust has been established. If a beneficiary of a trust still lives in the UK then establishing a trust overseas is unlikely to bring any tax benefit.

So, what criteria should you bear in mind when choosing a suitable jurisdiction in which to establish your trust? Given how the offshore world has been changing, I would suggest you consider the following factors:

- *Whether you want the trust to be governed by civil law* or common law. Much of the world operates under either civil or common law. Civil law countries traditionally did not recognize trusts but in recent years countries such as Switzerland, Panama and the Netherlands Antilles have seen the error of their ways (or rather the commercial opportunities) and now offer trusts. Nevertheless, many financial advisers feel that from a legal perspective it is better to form your trust in a common law jurisdiction. Essentially, this means any country that was formerly part of the British Empire.
- *Credibility.* You want your trust to be established in a country with a good reputation, excellent international relations and plenty of double tax

agreements. Otherwise, you may find that it is impossible to operate in the future. Countries that do not comply with international tax standards are likely to be penalised.

- *Efficiency.* Some countries are more dynamic than others. Naming no names, there can be a tendency in the smaller, sunnier offshore jurisdictions to take a relaxed view to administration and even office hours. Choose a location where you can rely on the government and the service providers to adhere to the highest possible standards of efficiency.
- *Communications.* You will want to be able to talk to the trustees so a suitable time zone and good telephone links will be important. Although you may not visit the trustee very often, good flight connections will also mean a reliable courier service.
- *Level of influence.* If you are from the UK, you may not want your trust to be established anywhere that can be leaned on by the UK tax authorities or Government. If you are American, the same will be true regarding any country that the US may exert unfair influence over.

My own personal list would include Bermuda, Ghana, the British Virgin Islands, India and New Zealand. I would rule out Hong Kong on the basis that I don't trust China not to interfere in its internal affairs. And, if I had to choose just one country, I think it would probably be New Zealand. The big advantage of New Zealand is it is a completely independent country that doesn't have close connections with either the EU or the US. It is not an offshore haven but a normal, high-tax jurisdiction. It has plenty of double taxation agreements and plenty of exchange information agreements. It taxes its trusts on the residence status of the settlor as opposed to the residence of the trustees. So if neither the settlor nor the beneficiary is a resident of New Zealand, the trust is not liable to any tax except on New Zealand-source income. Moreover, there is no CGT or IHT in New Zealand. As an aside, New Zealand offers quite a high degree of confidentiality. It is a well-regulated, highly efficient jurisdiction. Moreover, it is a lovely place to go and visit.

Country-by-country reporting update

As regular readers will be aware, the UK Government is committed to implementing the OECD recommendations on country-by-country reporting (CCR). Now, HMRC has announced that CCR will include partnerships, including reverse hybrid partnerships. As CCR only affects companies with revenue of over €750m, you may feel that this is irrelevant. However, many experts have suggested that over time CCR principles will be applied to smaller and smaller organisations.

Non-dom news

By 20th October 2016, all responses must be in to HMRC's latest consultation regarding proposed changes to the taxation of non-UK-domiciled individuals. Basically, the Government has it in for long-term non-doms! It is already agreed that they will have to pay UK tax on their worldwide income, while those born in the UK and with a UK domicile of origin will no longer be able to claim non-dom status for tax purposes while they are living in the UK, even if they have subsequently left the UK and acquired a domicile of choice in another country. Moreover, non-doms that have been tax resident in the UK in 15 out of the last 20 years will become deemed UK domiciled for all tax purposes. Another rule which is going to affect a lot of non-doms is the fact that those who are deemed to be domiciled in the UK after 6th April 2017 will only be able to rebase foreign assets providing they have previously paid the remittance basis charge in any year before April 2017. UK trusts set up by non-doms prior to their becoming UK domiciled will enjoy only limited protections. Returning non-doms will not benefit from asset rebasing or relief for mixed fund bank accounts.

Your Own Personal Charity

More and more people are catching on to the fact that they can tap into the very generous tax reliefs available to charities without simply donating their money to Oxfam or the like. Subject to jumping through the relevant bureaucratic hoops, you can form your own trust for charitable purposes that, in practical terms, is one which you can dictate to, as far as the good causes it supports are concerned, thus keeping a measure of control with the overall proviso that the money must only be applied for commercial purposes.

You can also put assets directly into your own personal charitable trust.

And the tax advantages of charities?

Well, for a start, anything you donate to the charitable trust, even though it's your own trust, is eligible for 'gift aid' relief. That is, it is a deduction from your income for higher-rate tax purposes, and enables the trust to reclaim tax at the basic rate. To take an example, supposing your income for a year is £150,000 and in that year you decide to transfer £100,000 from your savings to your charitable trust. This effectively reduces the income on which you will be paying higher-rate tax to none at all, because, first you're only liable at the higher rates on total income of over about £42,000 and, second, the £100,000 donation is 'grossed up' at 20%, making it £125,000 (£100,000 is 80% of £125,000).

The charitable trust, on its side, can then reclaim the £25,000 (in our example) supplementing the value of the gift so as to make it worth £125,000 rather than £100,000.

But the tax breaks don't stop there. The trust itself is also exempt from all tax on income from investments. Furthermore, if it puts the money into investment assets which are within the scope of CGT (or if it receives such an asset from you) the trust is exempt from CGT on any future disposal of that property. So you have, here, an amount of value building up entirely tax-free where, if you had retained it in your ownership in order to keep control, it would have been within the scope of substantial taxation.

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Money

Income At Any Price

Traditionally, investors seeking income had three options. They could leave their money in a bank or other financial institution and earn interest. They could lend their money to a government or business – in other words purchase bonds – and be paid for doing so. Or, and this was by far the most lucrative option, they could invest in the stock market and hope to receive dividends.

The problem is that, nowadays, none of these traditional investment strategies is bringing much in the way of a return. Bank interest rates are so low that they might almost be said to be negative. In fact, they are negative. Bonds are looking incredibly expensive, especially as many of the countries and companies issuing them have serious underlying financial problems. There is most potential, probably, in the stock market but, despite what investment managers would have you believe, it is very difficult to pick long-term, high-yield securities. As it happens, dividend growth for FTSE companies has been good in recent years. However, no one, given the general political and economic uncertainty, expects it to last. Anyway, some of that dividend growth is really driven by currency.

Driven by a need for income, many investors chose residential property (and still continue to do so). This was a good option until recent tax changes in the UK that make buy-to-let investments substantially less attractive.

So, what should you do if you want passive income? Here are three options.

• Consider less conventional property. One possibility, for example, could be to invest in health service property. I am talking about GPs' surgeries, care homes, retirement housing and even private hospitals. Typically, such properties are let for long periods of time, often to the NHS or a similar government or non-government organisation. Another good niche could be student accommodation, especially as the weak pound may bring more foreign students into the UK to study. There is at least one advantage to English being the most popular business language in the world.

• Start, or buy your own, income-generating business. I have been long tempted by the idea of buying or starting a caravan park. Not very glamorous, I know. But they are surprisingly popular both as holiday destinations and as long-term residences.

• Get involved with peer-to-peer (P2P) lending. This is where you lend direct (or almost direct – it is through online website) to individuals. Caution is required as the concept is still quite new and one can't be certain what the long-term returns will be, especially if the country dips into recession. Still, many of the P2P websites suggest that anything from 4 to 5% a year is possible. Lord Turner has predicted that: "The losses which will emerge from peer-to-peer lending over the next 5 to 10 years will make bankers look like lending geniuses." Maybe. On the other hand, many banks and investment managers are piling into the market. Blackrock purchased nearly £13 million worth of shares in Funding Circle, for example. And Liberum, the investment bank, says that it expects P2P lenders to enjoy a return of about 6% a year.

Whither Wine?

The research company Euromonitor International has reported that the amount of wine being consumed here in the UK fell by nearly 4% over the last five years. It anticipates further falls during the next five years. One of the reasons for this has, of course, been the collapse of sterling. However, there is good news. Although the price of wine is set to rise as a weak pound pushes up the price of all imports, it has to be remembered that wine works at as very low margins. If you buy a typical bottle of wine from, say, Marks & Spencer costing £8, about 50% of that is going to the Government. Of the remaining £4, some £3 goes to purchasing the wine from overseas and £1 goes to the retailer. A 20% fall in sterling will not, therefore, result in a 20% increase in wine prices. My guess is that the £8 bottle of wine may cost around 60p to 80p more. Hardly, therefore, a deal breaker when it comes to ordinary drinking wines. It will have a slightly larger effect on more expensive wines but – again – I don't think disastrous.

My bigger fear, as an enthusiastic oenophile, is that UK wine merchants will struggle to compete with European and other buyers when it comes to negotiating with the smaller artisan wine producers. With uncertain demand, I am concerned that many British wine merchants will stop importing the finest but not necessarily the most popular wines. For my own part, I took advantage of the strength of sterling in recent years to stock up. So I feel that for a few years at least any hike in prices will have minimum effect on my cellar.

On Your Bike

I've just saved more or less £400 on a £1,000 bike. How? I've taken advantage of the Government's Cycle to Work scheme. The way the scheme works is this. First your employer purchases a bike on your behalf, before renting it to you under a hire agreement. Your monthly payments are then deducted under a so-called salary sacrifice agreement which is interest-free and allows you to spread the cost over between 12 and 18 months. The higher your tax bracket, the bigger the saving. For example, on a £1,000 bike the net cost is £588. In theory, incidentally, you don't have to limit yourself to a £1,000 bike. If your employer takes out its own consumer credit licence, there is no upper limit to the value of the bike purchased.

At the end of the term, incidentally, the bike technically belongs to the employer. However, the employer is committed to sell the bike, at the end of the hire period, to the employee for market value. If they promise to do this, incidentally, they could lose their tax benefits. A scheme well worth peddling.

Gold (Again)

Given the low levels of interest available (see above) the fact that gold is a non-income-producing investment does not, in the current environment, necessarily matter. Those in favour of gold as an investment always point out that it has a low correlation with equities and bonds and is a useful way to store wealth. So when the bond yields are virtually negative and currency markets are volatile, gold does, in some ways, continue to be an attractive investment. This year has, of course, seen spectacular increases in the price of gold. At this juncture it has gone up by about a quarter. In certain circumstances, one can see it going up even further. For example, if the dollar falls (as I believe it would if Trump were elected president), I don't think it is unreasonable to believe that many investors will turn to gold. On the other hand, if the Federal Reserve increases borrowing costs then that could soften the gold price.

I have read recently that a number of advisers believe that buying gold mining shares is a mistake because, ultimately, their price will be linked to the stock market rather than to the price of gold. There is some truth in this, and yet, equally, for reasons covered in previous issues of Schmidt, gold mining shares often represent a fantastic opportunity. The gold miners of today are much more sophisticated and technologically savvy than the gold miners of yore.

It is tempting, of course, to purchase actual bullion but, unless you think you are going to end up fleeing somewhere, I would recommend against it. Instead, the obvious choice is almost certainly a gold exchange-traded fund (ETF). An exchange-traded security will track the gold price and is physically backed, meaning it owns some gold instead of using derivatives to follow an index. I often think that the iShares physical gold ETF is one of the best options.

Rope For Old Money

According to the Office for National Statistics, over the next quarter of a century the number of households headed by someone over the age of 65 will rise by 155,000 a year and will account for three-quarters of all growth in households. This age group, if they are lucky, tends to be asset rich and cash poor. That is to say a high percentage of them own property but have relatively low incomes. Moreover, as they get older, they feel a natural desire to divest themselves of properties that are often too large or unsuitable in some other respect and move into smaller, lower-cost, more convenient homes. One of the biggest areas of growth for those in property development has been the provision of specialist retirement housing. This tends to divide into two categories. There is the sheltered housing model. This is where a developer builds a number of apartments and houses each with their own kitchens and bathrooms and then provides communal areas and a range of services. The idea is that its inhabitants can remain more or less independent but that they have support there when they need it. The second category is that of assisted living. This serves those who are less independent and require 24-hour support. They are still relatively independent but the management company keeps a regular eye on them. The service charges for sheltered housing are relatively light – usually £2,000 to £3,000 a year. However, the service charges for assisted living could be as much as £10,000 a year.

So far, so good. You can pick up a brand-new house in a retirement village for between £200,000 and £300,000. But there is, however, a serious catch. A political lobby group called Carlex has recently published a report that indicates the values of some retirement homes have plummeted. For example, Risingholme Court, developed by one of the biggest players in the market, McCarthy & Stone, which is located in Heathfield, East Sussex, has dropped in value. One property, purchased there in 2007 for £231,950, was sold in 2014 for £130,000. Another home fetched £140,000 when sold last year, representing a loss of £148,462 over eight years. Moreover, many developers seek to make a share of any sale price. This can be anything from 1 to 30%. Pretty tough if you have already seen the value of your property halve!

The moral? If you are thinking of buying a retirement property for yourself, read the small print closely and consider the long-term investment value. If you are looking for a business idea then this market certainly has room for some ethical players who come up with a business model that generates profit without causing undue expense to its customers.

Small Is Beautiful

When King Carol II fled Romania in 1940 in a hail of Nazi bullets, it was the sale of his rare and prized stamp collection that helped him finance his future. Seguin Bailie, racing driver and entrepreneur, secretly amassed a stellar stamp collection that broke auction records after his death. More recently, 'Bond King' Bill Gross of Pinco quadrupled his investment with a $10 million sale of British stamps in 2010.

Every few weeks I receive an emotive email from Keith Heddle, managing director of Stanley Gibbons Investment, imploring me to consider investing in stamps. His core message is always the same: since the crash of 2008, investors and wealth managers have been on the hunt for options to spread risk and provide returns from a wider range of asset classes. Art, classic cars, fine wine, coins and rare stamps have all come under the spotlight as diversification options. The reasons these prestige collectibles have remained largely secure, profitable and continue to grow in value is because they are generally uncorrelated with any mainstream market and unaffected by trends and market whimsy.
His investment arguments can be summarised as:

- Supply and demand economics. Rare stamps, coins and books have always had a special place in the affection of collectors. Now, a record of steady growth and capital appreciation is attracting investors seeking new investment options.
- Their potential is further fuelled by increased demand from a growing global middle class, particularly in the emerging economies, and a finite supply of investment grade stamps and coins.
- Key determinants of future value and capital appreciation include rarity, condition, quality, marketability, price and authenticity.
- Stamps, coins and books are a way of diversifying your portfolio to protect and grow your capital. They are also heritage assets, each with their own story to tell.
- Rare tangible assets are not volatile but driven by the basic dynamics of supply and demand economics.
- The worldwide market for stamps is estimated at £6 billion a year with eBay in the US alone selling approximately $6 billion of collectibles annually. The rare coin market is estimated to be between five and ten times that size.

Other benefits include no management or valuation fees, relatively inexpensive entry level investments, structured exit options to help you liquidate your portfolio and realise your return and – if you buy through Stanley Gibbons – free storage and insurance.
It is certainly true that the various indices (the GB250 Rare Stamp Index, the China 200 Index, the GB200 Rare Coin Index and the Rare Book Index) show steady growth over the last 20 years. Moreover, between 2007 and 2011, when most markets were crashing, they continued to rise. In the last 14 years, for example, the GB250 Rare Stamp Index has grown around 300%. It is also true that Stanley Gibbons Investments makes it very easy to buy into this market and offers all sorts of guarantees regarding the amount of growth you will enjoy.

For my own part, when it comes to any alternative investment, I'd rather educate myself and make my own buying decisions. Nevertheless, I have to say that every time I hear from Mr Heddle I am tempted to send him some money. If you are interested in learning more, visit www.stanleygibbons.com/invest.

All Change For Uk Non-Doms

In August, the Government released a further consultation on the proposed changes to the taxation of those non-UK domiciliaries (non-doms) who will become deemed domiciled in the UK under the new '15 out of 20 years' rule, as announced in the 2015 summer Budget. New provisions will also prevent foreign companies from being used to shelter UK residential properties from inheritance tax (IHT).

As is often the case with consultation papers, however, it is clear that the Treasury still has much work to do in refining the required legislation before it comes into force next April. The key points appear to be:

- The reforms will become effective from the beginning of the 2017/18 tax year.
- The rules determining whether an individual is deemed UK domiciled will not be changed significantly from those in the original announcement.
- New rules will prevent those non-doms who have not become deemed domiciled from gaining an advantage with regard to IHT by holding UK residential properties via overseas companies.
- Although the Government has confirmed that there is a rationale for encouraging those who own UK residential properties via offshore companies and other structures to 'de-envelop' (i.e. extract) those assets, it does not intend to offer any relief against tax charges which may be triggered as a consequence of doing so. Individuals who have opted to own UK residential properties via this route may therefore wish to consider unwinding such ownership sooner rather than later.
- There will be two transitional provisions for non-doms who become deemed domiciled under the new rules and these are intended to make the transition to being taxed on a worldwide basis easier to manage. One deals with the rebasing of the value of offshore assets for capital gains tax (CGT) purposes, while the other allows the separation of 'mixed funds', which comprise both clean capital and foreign income and/or gains into their component parts.

Both of the transitional rules apply only to those non-doms whose domicile of origin is outside the UK, so will affect only those to whom the proposed 15 out of 20 years rule applies. This is the new provision under which a non-dom becomes deemed domiciled in the

UK for the purpose of all taxes on 6th April 2017 if they have already been UK resident for 15 years at that point or at the beginning of their 16th tax year of residence if they have not.

Notably no such transitional reliefs are on offer to non-doms born in the UK who also have a UK domicile of origin. Such individuals will simply become UK deemed domiciled if they are UK resident during 2017/18 or any subsequent tax year.

Rebasing

One surprising aspect to the 2016 Budget proposal was contained in the accompanying documentation to the effect that there would be a transitional relief for the rebasing of overseas assets. This would allow non-doms affected by the new deemed domicile rule to rebase the values of their non-UK assets to their 5th April 2017 value for the purposes of CGT. This would clearly limit the taxable gain on a rebased asset to any increase its value since that date, even if the proceeds were subsequently remitted to the UK, meaning that any capital gain prior to the 2017/18 tax year would be treated as clean capital.

It should be noted that merely rebasing an asset's value for CGT purposes to its 5th April 2017 value does not guarantee that no tax liability would be due on the remittance of the sale proceeds, since if it had been purchased using foreign income or gains a tax charge may still arise to the extent that the sale proceeds comprise such income and gains. Nevertheless, depending on individual taxpayers' circumstances, these historic income and gains may be covered by existing transitional provisions introduced back in April 2008. Even if such reliefs do not apply, it may be possible to remit only the non-taxable gain element of the proceeds using the existing mixed fund rules; alternatively, for assets disposed of in 2017/18, the proposed unmixing relief may be applicable.

As noted previously, rebasing will only be available to those non-doms becoming deemed domiciled under the new 15 of 20 years test in April 2017. However, only those who have paid the remittance basis charge in at least one tax year from 2008/09 to 2016/17 will be entitled to it, so it may actually be worthwhile for them to pay the remittance basis charge in the current tax year in order to qualify for the relief if they have not done so previously.

This gives rise to a somewhat anomalous situation, in that for an individual who has the misfortune to become deemed domiciled after 2017/18 and then disposes of an asset, their entire gain will be subject to CGT, whereas someone who becomes deemed domiciled during 2017/18 can dispose of an asset on 6th April 2017 and remit the entire proceeds tax-free. Clearly the former could liquidate the asset (or could already have done so before the measures were announced) prior to becoming deemed domiciled, but this would prevent the proceeds being remitted without incurring a CGT charge on them.

Rebasing can be asset-specific, which appears to create the potential to opt to rebase some but not other assets that are held, for example where some have appreciated in value but others show a loss; although the consultation paper is silent on the question of how this will work, it seems likely that the taxpayer will need to make an election via their tax return.

Perhaps unsurprisingly, rebasing is only applicable for those overseas assets which are held directly rather than via offshore corporate structures, even though UK-resident shareholders in such entities may be subject to 'look through' for tax purposes and thus no UK tax advantage is conferred by that route.

Rebasing is restricted to assets which are foreign on 5th April 2017 and were also foreign on 8th July 2015 (the date of the Budget in which the measures were announced) so may be unsuitable for assets which are currently in the UK even if they could be moved offshore before the end of 2016/17.

The treatment of 'mixed funds'

Mixed funds are assets (such as bank accounts or holdings in investment funds) which comprise both the original capital invested and subsequent income and gains arising on that capital. Under the current rules, any remission of capital from such a fund to the UK is deemed to be the taxable element (i.e. overseas income and gains) first before any of the original (clean, non-taxable) capital. From 6th April 2017, tax will become due on an arising basis, but pre-April 2017 capital cannot be remitted to the UK without first paying tax on those overseas income and gains within it.

The transitional relief in this instance will be a one-time (i.e. during 2017/18 only) facility for non-doms with a domicile of origin outside the UK to separate mixed funds within overseas accounts into their constituent parts, so that clean capital, offshore gains and offshore income can each be transferred to separate accounts. The proceeds of each can then be treated as clean capital and remitted to the UK in any order and at any time.

It should be evident that in order for this even to be possible it will be essential for the individual concerned to have a complete record of all prior transactions on the account in order to identify the relevant values. Clearly, there will also be some instances in which even if that data is available the cost of carrying out the analysis will be uneconomical in the context of the potential tax to be saved.

Unlike the rebasing rules, the unmixing facility will be available to all non-doms with a domicile of origin outside the UK, so is not limited to those who will become deemed domiciled (for income and CGT purposes) in 2017/18 under the new 15 out of 20 years test.

However, the fact that the relief is limited in time to 2017/18 only is arguably discriminative against those who will only become deemed domiciled after 5th April 2018. Even if they do elect to use the unmixing relief in 2017/18, they will then need to maintain the segregation of those accounts until such time as they start to be taxed on an arising basis.

What is interesting about this relief is that it applies to all individuals with a non-UK domicile of origin, irrespective of when they became UK resident (in fact they need not even be UK resident in 2017/18). Since the purpose of the relief is presumably to allow those who are about to become taxable on an arising basis to be able to access funds to spend in the UK without incurring historic tax on them, this seems a little wider in scope than strictly necessary.

It is also unfortunate that it does not cover assets owned via offshore companies and trusts rather than just applying to individuals, given that these are often transparent from a tax perspective for UK resident shareholders and which may have been established in the past based on the then prevailing legislation.

At the time of writing, the indications are very much that the legislation is to be introduced in 2017, but with some anomalies still evident, it is not clear whether the apparent inconsistencies and elements of unfairness will be amended, delayed or survive to Royal Assent as currently scheduled.

In a future edition we will also consider the implications of the reforms for non-resident trusts and the proposals affecting the IHT treatment of UK residential property for non-doms.

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Property

Tax-Free Property Gains

There are two ways in which the gains/profits from property are taxed. If you develop, buy and sell property professionally or receive an income from a property then in most instances you will be liable for income tax. In the current tax year, the first £11,000 of your profit will be tax-free, thanks to your personal allowance. The next £32,000 is taxed at 20%, the next £57,000 is taxed at 40% and the next £22,000 is taxed at 60%. Sixty per cent? Yes, because you lose your personal allowance when the income goes over £100,000. However, if you have an income of between £122,001 and £150,000, the tax rate is 40%, although anything above £150,000 is taxed at 45%. There are three different levels of capital gains tax (CGT), 10, 20 and 28% – the last figure being applicable to residential property.

Property investors are, therefore, basically working to see that the rate of tax they pay is as close as possible to 10%. Achieving 10% (and even 20%) is not easy. But, paradoxically, it is extremely easy to achieve 0%. How? By taking advantage of private residence relief.

The legal name for a person's main residence is his or her 'principal private residence', or PPR. In a nutshell, you won't have to pay CGT when you sell or dispose of your home if all of the following apply:

- You have one home and you have lived in it as your main home for all the time you have owned it.
- You haven't let part of it out (although this doesn't include having a single lodger).
- You haven't used part of it for business only.
- The grounds, including all buildings, are less than 5,000 square metres (just over an acre) in total.
- You didn't buy it just to make a gain.

Married couples and civil partners can only count one property as their main home at any one time.

During times when property prices are rising, it has not been unusual for those with a growing family and/or a growing income to trade up properties taking advantage of PPR on every sale to build wealth. Indeed, it could be said that PPR is responsible for all those tedious dinner party conversations about how much each guest's home increased in value since they purchased it. If all those property bores thought they would be paying between 28 and 60% on their gains the topic would almost certainly be tax not profit.

One of my less glamorous journalistic commissions is to answer the property tax queries in a well-known national UK newspaper largely read by older, wealthier citizens. I thought it would be interesting to analyse the number of PPR-related questions I have received over the last 36 months. I wasn't surprised to discover that readers seemed twice as interested in claiming PPR now than they did in 2013. True, it is a rather small sample size (three years ago I was receiving, on average, seven PPR enquiries a month, whereas at the moment it is closer to 15) but I still think that it is meaningful. It suggests to me that the idea of putting all one's wealth into one's home and selling it for a profit, safe in the knowledge that there will be

no tax to pay, is becoming increasingly popular amongst a group that would otherwise have relied on different forms of investment income.

Let me offer you just one real-life example from my postbag. A retired publishing director owned a £1 million house in London together with about £1 million worth of mixed investments. Five years ago, he sold his home and cashed in his investments in order to purchase a suburban house in need of renovation with a large garden. The house cost him £1.25 million and he spent £500,000 improving it. So a total investment of £1.75m. During the first year of his ownership, he was able to sell a garage and part of his garden to a developer for £200,000. Last year, despite the softening market, he was still able to get £2 million for the main house and what remained of its grounds. So, over five years he has made a £450,000 return on a cash investment of £500,000. Interestingly, during the five years, he dipped into his capital to support his living costs. He felt justified in doing so because he knew he would be making a substantial capital gain with no tax to pay. He is renting now while he waits for London property prices to fall. Next time around he plans to buy a large property and convert it into two luxury flats, living in one and renting out the other.

(Incidentally, it is possible to claim partial residents' relief if your property has been your main residence for a period of time but not for the whole time you owned it. In this case the amount of relief you can claim is determined by dividing the periods when the property was classed as your PPR by the total periods of ownership. For example, if you owned a property for 10 years, but for the first 7 years you let it out, you will be entitled to 3/10ths partial residence relief.)

HMRC does not offer any guidance as to how long you need to live in a property before you can claim that it has been your PPR. However, the longer you have lived there the less chance there is that the relief will be denied. Certainly, you should consider a minimum period of at least 12 months. There are a number of other things you can do to ensure that the relief is not denied. These include:

- Make sure that all the utility and other bills are in your own name. Moreover, have them addressed to the property and not to some other address.
- Make sure that the council tax bills, TV licence and so forth are also in your own name and sent to that address.
- Register the address as your voting address on the electoral register.
- Be able to demonstrate that you furnished the property either with delivery receipts or by some other means.
- Have all your bank statements sent to the property address.
- Have your driving licence and other official documents sent to the property address.
- Keep a selection of personal photographs of you and your family members (as well as friends) taken while you were living at the address.

Basically, it is important that you can show the taxman that the property was genuinely your main home.

What the taxman is considering, incidentally, is your intention when buying and moving into the property. Even if subsequent events result in your changing your mind, it doesn't necessarily matter. However, it is important to remember that CGT exemption can be denied. In particular:

The main exemptions shall not apply in relation to a gain if the acquisition of, or if the interest in, the dwelling house or the part of the dwelling house was made wholly or partly for the purpose of realising a gain from the disposal of it, and shall not apply in relation to a gain so far as 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.

HMRC isn't interested in catching out people who have improved a property for their own use, but tax officers are looking for a number of different situations. To begin with they are concerned about what may best be termed quasi-property development, that is to say someone who purchases a rundown house, does it up and then sells it in a short period of time. They are also looking for tenants who get the opportunity to buy a freehold from their landlord and then sell it straight on. However, with due care and attention, it is certainly possible to avoid making any of these mistakes.
You may have read in previous issues of The Schmidt Tax Report about the switch from the old 36-month rule to the new 18-month rule in relation to PPR. Up until the 5th April 2014, if a house had been your main residence, the last three years of ownership were always treated as though you lived there for the purpose of working out the number of PPR years in the capital gains calculation. This was true even if you actually didn't live there in those last three years. However, since the 6th April 2014, things have changed. If a property has at some time been your main residence, then the last 18 months are now only treated as though you lived there. Incidentally, you should always discuss with your accountant the advantages of advising HMRC that you wish to elect for a particular property to be your main residence.

While I am on the subject of CGT and property ownership, I just want to remind readers that, regardless of whether a property is your main residence, it is possible to obtain tax relief on any capital gains made in the first 12 months of property ownership.

The relief arises because many investors find themselves in a situation where they bought a property but they are unable to occupy it immediately. This may be because the property is being built or altered or redecorated or because they are still living in their old home until they sell it.

If you can't move into a property immediately after you have purchased it, it is possible to claim something called the '12-month relief'. This means that the first year of ownership will be exempt from any CGT. This is regardless of whether you currently have another property that is your main residence. However, in order to take advantage of this relief, you must occupy the property within 12 months of the purchase. And a condition of the relief is that after moving in you stay in the property long enough for it to become your qualifying main residence.

One final point. If you keep buying properties, doing them up and selling them, it is likely that HMRC is going to suspect you of being a property dealer or developer. My general advice would be not to move too frequently. Yes, you will get away with a move every 12 to 24 months once or twice, but a far more sensible route is to look for periods of at least four or five years between each change of address.

On Track With Hometrack

Hometrack is one of the leading property market analysts and provides data to a wide range of companies across the residential sector. Indeed, its automated valuations are used by four out of the five top UK lenders. I find the company's UK Cities House Price Index particularly useful. Basically, Hometrack analyses the price of houses in 20 cities throughout the UK. Its last report, for example, which was issued at the end of September, showed that city level house price growth was running at 8.2%… but slowing down. Year on year, London house price growth was still running at roughly 6% but the underlying rate was definitely slowing down. The 20 City Index recorded its lowest level of quarterly growth (1.9%) for six months as a seasonal lull in market activity and weaker demand post Brexit (and the March stamp duty change) reduced the upward momentum of house price growth.

The report's authors point out that it is dangerous to view London as a single housing market – the highest rates of house price growth remain in the outer London boroughs of Barking and Dagenham (16.2%) and Havering (14.6%), where average house prices are 30% lower than the London average. Affordability is running out fast in these markets, which have significantly outperformed central London for the last two years, and single-digit growth awaits in the months ahead.

Interestingly, the city housing markets with the strongest underlying rates of growth remain those that have some of the lowest prices and where the pickup in prices has been running for the shortest period. Liverpool and Glasgow have recorded the fastest growth in the last three months, where average prices of £114,000 are around half the price of the 20-city average of £239,000.

So, where does Hometrack think future growth is likely to come from? It believes that momentum is more likely to centre in cities where house prices are closer to their 2007 levels but where economic factors – low mortgage rates, low unemployment and rising wages – set the conditions for stronger price rises. Richard Donnell, Hometrack research director, believes: "As long as the economy continues to grow and interest rates remain low, cities such as Liverpool, Glasgow, Birmingham and Manchester are likely to see house prices rise." He also tips Bristol as another possible place to purchase.

As an aside, research published this week by the council of mortgage lenders showed mortgages to first-time buyers had grown in Wales by 31% and Scotland by 39% between the first and second quarter of the year. To put this into some sort of perspective, it only grew by 3% in London. The Council of Mortgage Lenders has suggested that, for the first time since 2008, first-time buyers had borrowed more in home loans than movers throughout the UK had.

Anyway I can't recommend Hometrack enough as an excellent source of free market information. You will find its website at www.hometrack.com. Incidentally, they cover other countries, including Australia.

While I am on the subject of research, I was interested to see that the property crowdfunding platform Property Partner has analysed the number of new buy-to-let properties being advertised throughout the UK. What the company found was that there has been a 15% drop in new rental properties being listed across more than 90 towns and cities in the UK. The company looked at the number of new rental properties being advertised between 1st August and 28th August and compared it to the same period in July. Some areas experienced really significant falls. For example, Hartlepool in the north-east saw rental listings down nearly 40%. Some 11 other towns experienced falls of between 26 and 30%.

Eastern Promise

In last month's Property section, we looked at the investment opportunities in the west of London. This month, I thought it would be interesting to turn to the east. Essex runs predominately to the north-east of London. It borders the counties of Suffolk and Cambridgeshire to the north, Hertfordshire to the west, Kent across the estuary of the river Thames to the south and London to the south-west. Interestingly, it only has one city: Chelmsford. It is an extremely diverse county. On the one hand, it has some extremely rural and sparsely populated areas that could almost be considered wildernesses. On the other hand, it also contains densely populated urban areas. As it currently stands there are about 1.4 million people living in Essex and this is expected to grow slowly but steadily until it reaches around 1.65 million people in around ten years.

One of the first issues for any property investor is, of course, transport. Essex is one of the most important London commuter locations. Indeed, the *Daily Telegraph* identified Basildon, Harlow, Braintree and Southend as being in the top ten most affordable London commuting locations. The existing railway infrastructure is actually remarkably good. Moreover, Crossrail should be fully open and serving Brentwood and Shenfield by 2019. The county does, however, desperately need either a new tunnel or a new bridge across the Thames. At the moment a public consultation is under way to decide on a new tunnel, to be called the Lower Thames Crossing, linking Essex and Kent. This would include a major road between the M25 and M2/A2 towards the south coast ports. Given the long waits required by anyone who wishes to cross the river at Dartford, my own bet is that the Lower Thames Crossing will go ahead. It is worth noting that the port at Thurrock is the UK's largest container port terminal and that the port of Tilbury is one of the three largest ports in the country.

As already mentioned, Chelmsford is the only city in Essex and it enjoys a particularly buoyant economy. John Lewis has a flagship store in the New Bond Street Retail and Leisure Development. It is also to be noted that it is possible to make the journey from Chelmsford into Liverpool Street in just 34 minutes. The town also has a small but rapidly expanding university (Anglia Ruskin) that currently has 6,000 students. The current average property price in Chelmsford is £300,000. During the last year, it rose by a staggering 13%. A two-bedroom flat will achieve a rent of roughly £1,000 per month and a four-bedroom house should rent for between

£1,600 and £1,800 a month. There is a shortage of available property.

Another area to look at in the region is Harlow where the current average property price is £246,000 and experienced an 18.3% annual rise over the last 12 months. Rents here are, if anything, higher than in Chelmsford.

If you are looking for an area that has not yet necessarily reached its full potential then I would suggest looking at Basildon or, possibly, Brentwood. One expert told me: "Both towns are very attractive to London commuters with the journey taking 30 and 40 minutes." Once Crossrail is in, I think Basildon and Brentwood will see demand go up even more.

Finally, I would like to commend Southend to you. Southend has been a rather neglected town over the last 40 or 50 years. The economy has been dependent on light industry and what remains of the tourist trade. However, plans are afoot to change all that. Southend Airport has been upgraded and expanded and a new airport business park is planned. A new technology campus is also on the cards. The current average property price in Southend is £240,000 and it rose by 13.5% last year. Here, a two-bedroom flat rents for between £800 and £900, somewhat less than other areas in Essex.

Whither Fintech?

In city halls all over Europe (with the exception of the UK), politicians and civil servants are weighing up their chances of getting their hands on part of London's lucrative fintech sector. Each of the contenders has different things to offer. Paris has culture, beautiful properties but a complicated and ruinously expensive tax system. Dublin already has a well-established financial services centre and is English-speaking with amazing travel connections but is suffering a severe housing shortage and, as anyone who has tried to drive through the city during the working week will tell you, it is almost impossible to get around. Logically, of course, Frankfurt could pick up quite a bit of the slack. It is cosmopolitan, has almost no crime and relatively little unemployment. There are plenty of international schools. On the other hand, it is a small city and expensive.

Probably no one city will end up gaining an enormous amount if some fintech companies abandon the UK, but rather, if things go as anticipated, it will lead to a number of new fintech hubs, of which Barcelona, in my opinion, could end up doing very well. Why? Well, it has an amazing climate, offers all the advantages of a Mediterranean lifestyle and yet has brilliant transport links for those who need to travel internationally. As a place to live (and for people involved in fintech this is surprisingly important) it has everything: food, art, fantastic architecture, culture, beaches, golf and even (if you don't mind driving to get there) skiing. It is a fairly international city, too. Indeed, according to Saville's, foreigners made up nearly one in six of all buyers last year. This was, in part, because of the golden visa offered to non-EU investors.

Certainly, Barcelona is much more affordable than Europe's other major cities. Moreover, prices are still a good fifth or more below their peak, which was in 2007. One word of caution: you will require patience. Things do not more quickly in Barcelona. Everything from restaurant service to building work takes time. Still, if you are looking for a non-UK, European property investment, Barcelona could well be a fantastic option.

Cause And Effect

Britain's Court of Appeal has made an important judgment in a professional negligence case. Its decision also has the effect of setting a new precedent, in that it changes the legal principle of causation. The case was brought by the liquidator looking after a bridging lender called Tiuta. The defendants were a firm of surveyors called De Villiers. The argument was over an £890,500 loss that Tiuta suffered when one of its refinanced loans went bad. Its argument was that De Villiers' valuation report significantly and negligently overvalued the property.

What made the case particularly complicated was that De Villiers has actually valued the property twice. First for one loan and then for refinancing that loan. Its argument was that their liability should only be for the difference between the first and second loan (some £290,000). However, the Court of Appeal found that De Villiers was, in fact, responsible for the entire loss.

As a result of this case we can expect to see much increased insurance premiums, as valuers and surveyors seek to protect themselves from future litigation.

To Flee, Or Not To Flee?

That is the question

What should commercial property investors do in a post-Brexit referendum landscape? The answer depends, of course, on how exposed you already are to the UK property market and whether you are a UK or overseas investor.

Those in the business of selling UK commercial property are at pains to emphasise that, if not exactly thriving, the market is alive and well. True, they will concede, the number of transactions has fallen dramatically and political and economic uncertainty has caused stagnation. But they will point out that if you are an overseas investor British property just became, more or less, 20% cheaper. Moreover, in dollar terms the UK real estate market is now back to pre-2004 pricing levels.

The early signs are that overseas investors are not convinced that the market has fallen to its lowest point. Immediately after the referendum many UK property funds had to suspend trading, owing to the number of investors who wished to withdraw money. Many of these funds still remain closed.

Some are also charging investors massive exit penalties if they insist on withdrawing their cash. This is, of course, because property is a relatively illiquid asset. Obviously, it takes time to select the properties to sell and, then, to sell them. Unsurprisingly the Royal Institute of Chartered Surveyors (RICS) UK commercial property market survey for the most recent quarter indicated that demand for commercial real estate had fallen sharply and predicted that the sector had much further to fall.

Meanwhile, activity has been up across the Eurozone: in German cities (take-up was plus 5% year on year, led by Munich); France (Paris plus 16%), Benelux (Brussels plus 108%, Amsterdam plus 29% and Luxemburg plus 39%); and in southern Europe (Madrid up plus 76% and Milan plus 57%).

So, suppose you are stuck with office space in the UK. What should you do with it? One area of the market has shown remarkable growth: that of flexible workspace. According to one player in this sector, the Instant Group, demand has increased by 21% in the last year. Interestingly, the greatest increase in demand is in suburban locations probably because occupiers are choosing lower rents and good transport links over the highly competitive market in city centres. The supply of flexible workspace in London has outstripped conventional office space by some margin in the last year and this trend seems set to continue in the future. Interestingly, there are now 3,300 flexible workspace centres in the UK and the cities with the fastest increase in enquiries for this type of office space over the past year have been Brighton, Bristol, Birmingham, Nottingham and Cardiff. We have written about serviced offices before so I won't waste space going over it all again. Moreover, a quick Internet search will find lots of useful information on the subject. In summary, a serviced office is fully fitted and furnished and ready for immediate occupation. It also offers a selection of business services, including reception, telephone answering, secretarial support, conference and meeting rooms as well as tech support (video conferencing, high-speed Internet access and so forth). Rent is inclusive of rates, utilities, security, cleaning, insurance and so forth. Leases, on the other hand, tend to be short. Typically between 6 and 12 months. A very good business, it would appear, to get into.

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