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## Introduction and overview

### A tax on land transactions

- 1.1 Stamp duty land tax (SDLT) is charged on transactions the subject-matter of which is land situated in the United Kingdom. Tax is charged as a percentage of the purchase price. Unlike its predecessor, stamp duty, SDLT is a directly enforceable tax which is payable by the purchaser. The SDLT legislation is primarily contained in the Finance Act 2003 (FA 2003) as amended.<sup>1</sup> The general rule is that SDLT applies to land transactions entered into after 1 December 2003, although this is subject to detailed transitional provisions which are discussed in Chapter 10 below.
- 1.2 Tax is chargeable on transactions involving residential property where the consideration exceeds £120,000 and on those involving commercial or mixed-use property where the consideration exceeds £150,000. The initial rate is 1 per cent of the chargeable consideration and this increases to a maximum rate of 4 per cent where the chargeable consideration exceeds £500,000.<sup>2</sup> For example, on a straightforward house purchase for £750,000, SDLT of £30,000 will be payable by the purchaser. There is a separate and rather complicated regime for rental leases; this is summarised at paragraph 1.19 below and is the subject of Chapter 6.
- 1.3 As the name suggests, SDLT replaced stamp duty on land transactions. Like its predecessor, SDLT is charged primarily on sales of land as a percentage of the purchase price and must be paid before the transaction can be registered with the Land Registry (or the Scottish or Northern Irish equivalents). The increase in the nil-rate band for commercial property to £150,000 and for residential property to £120,000 is the only change in the rate of tax which has been made since SDLT was introduced. Nevertheless, despite these similarities SDLT is not a modernisation of stamp duty on land transactions but rather a new tax in its own right.
- 1.4 SDLT differs fundamentally from stamp duty in two ways. First, the charge to tax is founded on an entirely new set of concepts. Stamp duty<sup>3</sup> was charged

1 At the time of writing, primarily by the Finance Acts 2004 and 2005.

2 The rates of tax are set out in the Table of rates of tax at p. xxxv above.

3 *Ad valorem* stamp duty, as opposed to the £5 fixed duty which was payable on transfers otherwise than on sale.

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on documents which gave effect to a ‘conveyance or transfer on sale’. SDLT is charged on the ‘acquisition’ of a ‘chargeable interest’ in land whether or not there is any document giving effect to the transaction. The charge to tax is discussed in outline at paragraph 1.16 below and in detail in Chapter 2. Secondly, SDLT is a directly enforceable tax accompanied by an extremely onerous compliance regime. The purchaser<sup>4</sup> is liable to pay the tax whether or not he plans to register the land transaction. A self-assessment return must be made to HM Revenue and Customs (HMRC) within thirty days of the transaction, accompanied by a payment of any tax, or the taxpayer becomes liable to a penalty. The compliance regime is discussed in outline at paragraph 1.33 below and in detail in Chapter 9.

- 1.5 Accordingly, SDLT is a new tax founded on fresh concepts and enforced through a rigorous new compliance regime based on self-assessment. The inclusion of the term ‘stamp duty’ in the name of the new tax indicates its origins and the sort of transactions to which it applies. However, the term ‘stamp duty’ is not only strictly incorrect, because SDLT contains no requirement to stamp any documents, but also misleading insofar as it suggests that the basis of SDLT remains essentially the same as that of stamp duty.

### The importance of SDLT

- 1.6 Stamp duty on land and buildings currently raises in the region of £6 billion of revenue.<sup>5</sup> While nowadays new taxes are introduced under the guise of making the tax system fairer, the purpose of every tax is to raise additional revenue for the state. SDLT is no different: it was introduced to raise more money than stamp duty on equivalent land transactions. This has huge practical importance because it underlies every provision of the tax. The substantive provisions of SDLT as enacted in FA 2003 were designed to close down what HMRC saw as stamp duty loopholes that were being exploited by tax planners and thereby increase revenue. Most of the subsequent changes have been made with a view to preventing what HMRC has perceived to be opportunities for tax avoidance. The procedural provisions and especially the self-assessment regime are designed to ensure that the new tax is not only directly enforceable but also collected with maximum efficiency.
- 1.7 The rise in importance of stamp duties, caused by the increases in rates in the decade prior to 2000, has been a tax phenomenon during the last few years.

<sup>4</sup> A term of art for SDLT purposes the meaning of which is discussed at paragraph 2.34 below.

<sup>5</sup> For the year 2002–3, the last full year of stamp duty, stamp duty on land transactions raised almost £5 billion. In the year 2003–4, during which SDLT was introduced, stamp duties on land transactions raised £4.982 billion and stamp taxes as a whole £7.545 billion. For the year 2004–5, the intake for stamp taxes as a whole, of which SDLT forms the majority, rose sharply to £8.966 billion. Although no figure is yet available for SDLT, the increase in overall stamp duties revenue suggests that the introduction of SDLT has increased revenue by approximately £1 billion.

In 1990, stamp duties as a whole, including stamp duties on shares and other assets, raised only £1.7 billion.<sup>6</sup> This was less than capital gains tax, which in 1990 raised £1.9 billion, and little more than inheritance tax, which then raised £1.3 billion. By 2002, stamp duties as a whole were raising some £7.5 billion of which around £4 billion was raised on sales of land and buildings, and for 2004/5 the figure is now £8.966 billion. In contrast, capital gains tax raised only £2.279 billion in 2004/5 and inheritance tax £2.922 billion. Accordingly, SDLT on sales of land raises more than inheritance tax and capital gains tax combined.

### The inadequacy of stamp duty

- 1.8 The purpose of introducing SDLT was to raise more money from land transactions in a similar way to stamp duty without increasing the rate of tax. The early indications are that it has succeeded. In order to understand how SDLT is to achieve this, it is necessary to understand the limitations<sup>7</sup> of stamp duty. The biggest problem faced by HMRC in trying to enforce stamp duty was that it was not directly enforceable. Although documents were not admissible in evidence or at the Land Registry unless properly stamped,<sup>8</sup> HMRC could not directly assess any person for the duty. Even if a document had been submitted for stamping, the taxpayer was not required to pay the correct amount of duty but could withdraw the document if HMRC wanted additional duty.<sup>9</sup>
- 1.9 The stamp duty legislation was last consolidated in the Stamp Act 1891 and is scattered throughout subsequent Finance Acts.<sup>10</sup> The increases in rates brought stamp duty to the fore and created a surge in tax planning work. Unsurprisingly, the legislation proved to be hopelessly outdated and inadequate for such an important source of revenue. Not only was the legislation difficult to follow, but it was often possible for taxpayers to reduce the stamp duty charge, or even avoid having to pay it at all, through the use of careful planning.
- 1.10 Some planning techniques were blocked by piecemeal anti-avoidance legislation. One example was the provisions enacted in the Finance Act 2000<sup>11</sup> which prevented taxpayers transferring land into a connected company so that the shares in that company could then be sold with stamp duty payable at 0.5 per cent on the shares rather than at 4 per cent on the land. That such simple planning

6 The source for all the figures in this paragraph (except for the amount of stamp duty raised on land transactions) is HMRC's table showing 'Net Receipts of Former Inland Revenue Taxes'. The table gives no figure for stamp duty raised on land transactions, only a figure for stamp duties as a whole including stamp duty and stamp duty reserve tax levied on shares.

7 Of course, HMRC viewed stamp duty's limitations as shortcomings and, conversely, taxpayers saw them as advantages.

8 Section 14 SA 1891. 9 Albeit such withdrawal would be subject to a £300 penalty.

10 Although there was a partial consolidation of stamp duty in Sch.13 FA 1999.

11 Sections 119 and 120 FA 2000.

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was effective into the twenty-first century says everything about how far behind the times stamp duty was lagging. It was generally agreed that stamp duty was long overdue for fundamental reform.

- 1.11 In April 2002, the government announced a consultation exercise to reform stamp duty on land and buildings. The three aims were stated to be fairness, modernisation and to facilitate e-conveyancing. This consultation exercise was abruptly terminated in January 2003 leaving those who participated in the consultation in no doubt that, so far as HMRC was concerned, clamping down on perceived avoidance was the dominant motive for change. In HMRC's view, fairness requires the prevention of what they perceive to be tax avoidance because it is unfair for well-advised taxpayers to avoid paying tax through good planning, as this puts an unfair share of the tax burden onto everyone else. It is against this background that the SDLT regime was enacted in the Finance Act 2003.

### The SDLT regime

- 1.12 The SDLT regime is a comprehensive code contained primarily in the Finance Act 2003. The legislation is written, or so it is claimed, in plain English. Unfortunately, while the wording of the legislation may be readily understandable, finding the statutory provisions which apply to any particular land transaction is a more difficult exercise because the relevant provisions are scattered throughout the part of the Finance Act 2003 which deals with SDLT and the Schedules to it. Moreover, the FA 2003 has now been amended by the 2004 and 2005 Finance Acts together with numerous statutory instruments.
- 1.13 The SDLT code is an entirely new tax with a new charging mechanism. In theory, there should be no need to refer back to stamp duty. Unfortunately, in practice this is unrealistic because, even though the SDLT charge is fundamentally different, the new legislation is derived and often copied directly from the old stamp duty provisions. Accordingly, what a particular SDLT provision is trying to achieve often cannot be properly understood without referring back to the old stamp duty position. In particular, large parts of the SDLT regime, including almost all of the main changes from stamp duty,<sup>12</sup> are designed to stop the sort of planning that was being used for stamp duty. As the tax matures the need to refer back to stamp duty will progressively diminish.
- 1.14 However, in practice the most important change introduced by the SDLT regime is not substantive but procedural. The introduction of the new self-assessment regime means that SDLT is directly enforceable and the taxpayer must both file a return and pay the tax within thirty days or incur a penalty. Whereas before it was possible to take a more relaxed attitude to stamp duty, it is now absolutely imperative that SDLT is properly complied with.

<sup>12</sup> With the important exception of the tax charge on rental leases which is simply designed to raise more cash.

- 1.15 The remainder of this chapter contains an overview of the substantive and procedural provisions of the SDLT regime. The aim is to provide an outline of the structure of the tax and to highlight the major changes in comparison with stamp duty. Each area of the SDLT regime is then discussed separately in more detail in the chapters which follow.

## Overview of the charge to SDLT and other substantive provisions

### **The basis of charge: the acquisition of a chargeable interest in land**

- 1.16 SDLT is charged on 'land transactions'. A land transaction means the 'acquisition' of a 'chargeable interest' in land situated in the UK. The meaning of chargeable interest is defined widely to include any estate or interest in or right over land; it includes any equitable interest in land but expressly not a licence or a lender's charge. Unlike stamp duty, SDLT is chargeable irrespective of whether there is any instrument effecting the transaction. It is similarly irrelevant whether or not the parties are present in the UK at any time. The charge to SDLT is discussed in detail in Chapter 2 below.

### **Tax is charged as a percentage of the chargeable consideration**

- 1.17 Tax is charged on a percentage of the 'chargeable consideration' given for the transaction. The principle is the same as it was for stamp duty. However, the meaning of chargeable consideration is defined very widely and includes consideration in money's worth. No discount is made if the consideration is only payable on a contingency, although an adjustment can be made if the consideration subsequently turns out not to be paid. An assumption of debt by the purchaser expressly counts as chargeable consideration as it did under stamp duty. The rule that a transfer of land to a connected company is deemed to take place at market value is also retained in order to prevent avoidance through land being transferred into a special purpose company which could then be sold on to a purchaser with stamp duty payable at only 0.5 per cent on the share sale. The rules for identifying and valuing the chargeable consideration are explained in detail in Chapter 4 below.

### **Rates of tax**

- 1.18 The rates of tax are as set out at the start of this book.<sup>13</sup> They follow the old stamp duty rates and increase in stages as the chargeable consideration increases. There is a new distinction between residential and non-residential property, although as yet the only differences are the increased nil-rate bands for residential property of £120,000 and non-residential property of £150,000. Surprisingly, for a supposedly modern tax, there is no tapering of the rate increases. Instead, the rate is simply increased when the consideration reaches a particular figure, a crude technique aptly described as the 'slab system'. The real

<sup>13</sup> See p. xxv above.

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reason why there is no tapering is that the government would need to increase the rates in order to achieve the same yield. If transactions are 'linked', within the meaning of s.108 FA 2003, then the chargeable consideration is aggregated for the purposes of determining the rate of tax. Section 108 is a re-enactment of the old stamp duty 'series of transactions' rule,<sup>14</sup> although once again the wording of the legislation is more widely drafted. The rules for calculating the tax liability are discussed in Chapter 4 below.

### Rental leases

- 1.19 The new rules for taxing the rent payable on a lease are not only one of the most important changes brought about by SDLT but also one of the two most complicated and controversial.<sup>15</sup> The old stamp duty rule that leases were charged on a percentage of the average annual rent has been scrapped and replaced with the rule that leases are charged according to the full value of the future rental stream at the time of grant, known as the 'net present value'. The net present value of a lease is calculated using a statutory formula which applies a discount rate to reduce the value of future rents. Tax is then charged at the rate of 1 per cent on the net present value to the extent that the net present value exceeds the relevant nil-rate band: £120,000 where the property is residential and £150,000 where the property is commercial or mixed use. Accordingly, the tax burden on the grant of rental leases remains much less onerous than on both freehold sales and leases granted at a premium. Nevertheless, the charge is very high in comparison to the old stamp duty position. A further problem is that both the rules for calculating the tax charge and the ongoing compliance regime in relation to leases are disproportionate in their complexity to the amount of tax at stake. The charge to SDLT on leases is the subject of Chapter 6 below.

### Special rules for particular transactions

- 1.20 The Finance Act 2003 contains a number of special provisions dealing with how the charge to SDLT is to apply to certain types of transaction. The most important rule is that both a contract for the sale of land which requires a separate completion (typically, the sale of a freehold or the assignment of a lease) and an agreement for lease are now chargeable, under s.44 and para.12A<sup>16</sup> Sch.17A FA 2003 respectively, on the earlier of completion (settlement in Scotland) or 'substantial performance'. This is to prevent parties from resting on contract in order to avoid paying tax. Substantial performance occurs as soon as either party obtains what he bargained for: when the purchaser either takes possession of the land (or becomes entitled to receive the rents and profits) or the vendor receives either the purchase price (other than a deposit) or the first payment of

14 Which had to be applied when certifying that the transaction did not form part of a larger transactions or series of transactions under para.6 Sch.13 FA 1999.

15 The other contender is the SDLT partnerships regime as described in Chapter 7 below.

16 This paragraph does not apply in Scotland – see paragraph 6.77 below.

rent. The rule for determining when tax becomes payable on the sale of freehold and leasehold land and the concept of substantial performance are discussed in more detail at paragraph 2.37 onwards below. The rule for determining when tax becomes payable on the grant of a lease is discussed further at paragraphs 2.42 and 6.74 below.

- 1.21 The rules on sub-sales contained in s.45 FA 2003<sup>17</sup> follow on from s.44. The general rule is now that both the original sale and the sub-sale will be chargeable to tax unless the original sale is not substantially performed except as part of the sub-sale. Relief is given to the extent that substantial performance or completion of the sub-sale contract is deemed not to complete the original sale. The practical effect of this is that sub-sale relief is only available when the original purchaser does not take possession of the property and pays nothing more than a deposit until after the sub-sale has taken place. Sub-sale relief thus remains potentially available to land speculators and to those who, for whatever reason, buy a site comprising additional land to that which they wish to retain and sell off the remainder. The rule for sub-sales under s.45 is discussed further in Chapter 3 at paragraph 3.2 onwards.
- 1.22 Options are the subject of a special rule contained in s.46 FA 2003 designed to ensure that the grant of an option is always chargeable to SDLT. Exchanges are treated under s.47 FA 2003 as two separate sales of the properties being exchanged; it is no longer possible to structure an exchange as a single sale of the more valuable property. The transfer of an interest in possession in a trust where the underlying assets include land is also within the charge to SDLT. The tax treatment of options, exchanges and trusts is discussed further in Chapter 3.
- 1.23 The purchase of land by a partnership from an unrelated third party is chargeable to SDLT in the normal way. A special charging regime applies to levy a charge to SDLT where land is transferred either by a partner to a partnership or from a partnership to a partner and also where there is a transfer of a partnership interest and the assets of the partnership include land. The charging regime for partnerships is extremely complicated, and how it applies is the subject of much uncertainty and debate. It is contained in Sch.15 FA 2003 and is the subject-matter of Chapter 7 below. In summary, the position is as follows. First, where land is transferred to a partnership by a partner, whether an existing partner or an incoming one, then tax is charged on the market value of the share in the land which he is treated as giving away (i.e. on the market value of the land less the share in it treated as retained by the transferor-partner) through his interest in the partnership. Secondly, where land is transferred from a partnership to a partner, then tax is charged on the market value of the land which the transferee-partner is treated as acquiring (i.e. on the market value of the land less the share in it treated as owned by the partner prior to the

<sup>17</sup> See now also s.45A and para.12B Sch.17A FA 2003.



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transfer through his partnership interest). In addition, a charge arises on any actual consideration given in either of the two situations outlined above; this charge is on the inverse proportion to the charge on the market value of the land. Thirdly, where an interest in a partnership is transferred for consideration, then the person who acquires a partnership share or an increased partnership share is chargeable on the proportion of the market value of the land owned by the partnership which corresponds to the increase in his partnership share.

### Exemptions and reliefs

- 1.24 The exemptions and reliefs for SDLT are based on those which applied to stamp duty. Disadvantaged areas relief no longer applies to commercial property from 17 March 2005 and is now of minimal importance. Group relief, reconstruction and acquisition reliefs apply to SDLT in a similar way as they did under stamp duty. However, the conditions for their application have been tightened up and each is now subject to a three-year clawback in order to try and prevent them from being exploited by tax planners.
- 1.25 There is no longer a fixed £5 duty for transactions otherwise than on sale, and transactions which are not made for chargeable consideration are now simply exempt from SDLT under Sch.3 FA 2003. The reliefs which have been introduced by SDLT are mostly targeted reliefs aimed at specialised types of transaction. For example, the reliefs in s.58A and Sch.6A FA 2003, which include a relief for purchases made in part-exchange by housebuilders, compensate for the abolition of resting on contract and the much more limited sub-sale relief in the specific situations to which Sch.6A applies. The exemptions and reliefs from SDLT are the subject of Chapter 5 below.

### Commencement, transitional provisions and abolition of stamp duty

- 1.26 The general rule is that, from 1 December 2003, all land transactions are subject to SDLT. Stamp duty is abolished on land transactions but continues to be chargeable on shares.<sup>18</sup> Stamp duty also continues to apply to the transfer of an interest in a partnership; this is discussed further at paragraph 7.179 below. Stamp duty reserve tax also continues to be chargeable on agreements to transfer 'chargeable securities' as an alternative to stamp duty. So, on a share sale agreement, stamp duty or stamp duty reserve tax is chargeable at the rate of 0.5 per cent. On a business sale agreement, then, no stamp duty is chargeable unless the assets transferred include shares, and SDLT will only be chargeable to the extent that the consideration is attributable to UK land.
- 1.27 There is also a complicated set of transitional provisions to deal with transactions which somehow straddle 1 December 2003. In summary, where the

<sup>18</sup> More precisely, on 'stock' and 'marketable securities'.



contract for the land transaction is made after 1 December 2003 the transaction will always be subject to SDLT. Conversely, where the contract was made before 11 July 2003, the day after the FA 2003 received Royal Assent, the land transaction will not normally be subject to SDLT even if it is completed after 1 December 2003. If the contract was made after 10 July 2003 then it will normally be an SDLT transaction unless it was also completed before 1 December 2003, even if it was substantially performed before 1 December 2003. The transitional provisions and in particular the special rules for sub-sales are discussed in more detail in Chapter 10.

### Overview of the SDLT compliance regime

- 1.28 The fundamental limitation in the old stamp duty regime was that duty was not directly enforceable. Conversely, the most important change introduced by SDLT is to make the tax not only directly enforceable on the purchaser but also the subject of an onerous self-assessment regime. The purchaser must now make a return and pay any tax within thirty days of a 'notifiable transaction'. The return must be in a prescribed form and sent to a central unit in Netherton. A transaction may be notifiable even though there is no tax to pay and a taxpayer who fails to make a return will be liable to a penalty.
- 1.29 There is a very complicated set of rules to decide whether a transaction is notifiable.<sup>19</sup> Transactions which would be chargeable but for any of the reliefs, for example group relief, will normally be notifiable. Where there is no chargeable consideration then the transaction will not be notifiable. However, where the transaction is not notifiable, the taxpayer must still self-certify that the provisions of SDLT have been complied with before a transaction can be registered with the Land Registry (or the Scottish or Northern Irish equivalents). Where a return has been made a certificate will be issued by HMRC.
- 1.30 Once the return has been made, HMRC has nine months in which to raise an enquiry. However, this is subject to the rule that HMRC may make a discovery assessment at a later date in certain circumstances, principally when it was not provided with all the relevant facts in the original return. The old stamp duty adjudication procedure has been abolished and there is now no procedure for requiring HMRC to give rulings either before or after a transaction. However, HMRC may agree to give a pre-transaction ruling in a particular case,<sup>20</sup> and in any event they have only nine months in which to raise an enquiry. If an enquiry is made HMRC may issue a further assessment. Should the taxpayer wish to appeal against an assessment then, the appeal will now be heard by the General or Special Commissioners rather than by the High Court or the Court of Session.

<sup>19</sup> Discussed in detail in Chapter 8.

<sup>20</sup> Following Code of Practice 10.

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- 1.31 The new regime also contains the usual provisions for HMRC to charge interest where tax is paid late and penalties where returns are not made in time or the compliance provisions are not otherwise satisfied. HMRC also has wide-ranging information-gathering powers modelled on those for direct taxes contained in the Taxes Management Act 1970. Taxpayers are under a duty to keep the records relating to a land transactions for at least six years. The time limit for making assessments is extended to up to a maximum of twenty-one years where tax has not been paid owing to negligence or fraud on the part of the taxpayer and six years if HMRC were not provided with the relevant information on the return.

### Summary of the substantive changes introduced by SDLT

- 1.32 The main substantive changes introduced by SDLT in comparison to stamp duty include the following:
- (1) The mandatory nature of the charge.
  - (2) The different nature of the charge: SDLT is a charge on land transactions, however they take effect, whereas stamp duty was a charge on instruments.
  - (3) The abolition of the rule that contracts for the sale of freehold and leasehold land are only chargeable on conveyance and its replacement with the rule that contracts are chargeable on the earlier of completion or 'substantial performance'.
  - (4) The restriction of sub-sale relief to situations where the original contract of sale is not substantially performed (except as part of the substantial performance or completion of the sub-sale).
  - (5) The introduction of a new formula for leases at a rent designed to charge the full value of the rental stream at the time of grant (the 'net present value') at the rate of 1 per cent.
  - (6) The tightening up of the anti-avoidance rules in order to prevent the exploitation of reliefs including the extension of the group relief claw-back to three years and the introduction of similar provisions for the reconstruction, acquisition and charities reliefs.
  - (7) The introduction of new reliefs targeted at specific transactions.
  - (8) The abolition of the £5 fixed duty.
  - (9) The increase in the nil-rate band to £150,000 for commercial and mixed-use property and to £120,000 for residential property.
  - (10) The new rules for valuing contingent and deferred consideration.
  - (11) The abolition of the ability to structure an exchange as a single sale of the more valuable land.
  - (12) The replacement of the stamp duty 'series of transactions' rule with the wider concept of 'linked transactions'.
  - (13) On a business sale no stamp duty is chargeable (unless the assets of the business include shares) and SDLT is only chargeable to the extent that the consideration is attributable to land.