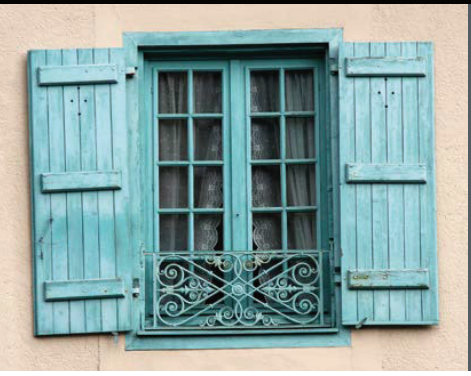

Understanding CGT on overseas property sales

Important factors UK residents need to be aware of to minimise tax liabilities.

Selling an overseas property can have unexpected implications for capital gains tax (CGT) liabilities for UK residents.

Whether a property is in Spain or New England, it's worth considering these potential issues well in advance of a disposal to minimise CGT payments in the UK.

A common error UK residents often make is failing to report the profits made from selling any foreign-based property.

Many are either unaware of the requirement to report the disposal to HMRC, or don't think it's important to do so because they wrongly assume they are only liable to pay tax in the country where the property is located.

While it's true that primary taxation rights are generally with the country where the property is physically situated, a gain remains reportable in the UK for anyone filing on a worldwide basis, which is most people. Credit may be given for overseas taxes against the UK liability, but it's possible a margin of CGT will be payable in the UK if the overseas tax rate is lower than the UK CGT rates on residential property of 18% and 28%.

Double taxation challenges

Even if the gain is less than the CGT annual exemption and no UK tax is due, the sale remains reportable in the UK if the proceeds exceed the 'proceeds reporting level' – equivalent to four times the annual exemption, so £49,200 this year.

Fortunately, the UK has double taxation treaties with many countries and therefore it's usually possible to claim credits in the UK for the taxes paid in the country where the property is situated.

However, a complicating factor is that every country has its own way of calculating profits on property sales that can lead to mismatches with the UK approach.

For example, the US has two methods of charging gains depending on whether it is 'short term' or long term', with the long-term top rate being less than the UK's 28%, possibly leading to a margin due in the UK.

There are also varying approaches to the value allowed as the base cost (the starting point) for gains around the world. Other countries may also have differing rules on what may be allowable as a deduction and, in particular, main residence relief is likely to be different. This means a property gain could be exempt overseas but chargeable in the UK, or vice versa.

Exchange rate impact

The impact of foreign exchange rates on a property sale is another area to be aware of, as transactions are usually made in foreign currency but UK reporting is in sterling.

For the purposes of calculating CGT on gains, HMRC takes whatever is paid in foreign currency on the day of purchase and converts it into sterling at that time, and the same when the property is sold.

Also, fluctuating foreign exchange rates can lead to currency gains or losses with implications for CGT. Hypothetically, if you bought and sold an overseas property for the same amount in US dollars there would no currency gain in the US but you would almost inevitably end up with a currency loss or gain in sterling.

Timing is critical

Getting the timing of a sale right can make a huge difference to tax liabilities, particularly if the seller will receive principle private residence (PPR) relief against CGT in the UK.

This can be claimed on the disposal of an overseas dwelling house providing the individual was resident in that country, or spent at least 90 nights in the property during the tax year.

Where a dwelling house has been an individual's only or main residence for part of the time they owned it, only a proportion of the gain is CGT-exempt. Clearly, these factors need to be taken into account when planning a disposal.

The timing of a sale also impacts on how 'split year' rules on CGT are applied for individuals who leave or return to the UK part of the way through the tax year the property sale is made in. Under split rules, CGT only applies to gains arising in the part of the year where the resident is designated as being in the UK for tax purposes.

These rules are very complicated and while they can help mitigate tax, there are many potential traps for the unwary.

Getting advice

Given the split rules issues and the wider range of complications with CGT in general, it's absolutely essential to get good advice when you're looking to sell an overseas property.

Shipleys is a member of an AGN, a global association of independent accounting and advisory business, enabling us to offer clients support and expertise relating to the country where their property is based.

If you would like to know more about how we can help with the CGT on overseas property sales, please speak with your Shipleys contact or contact one of our tax specialists.