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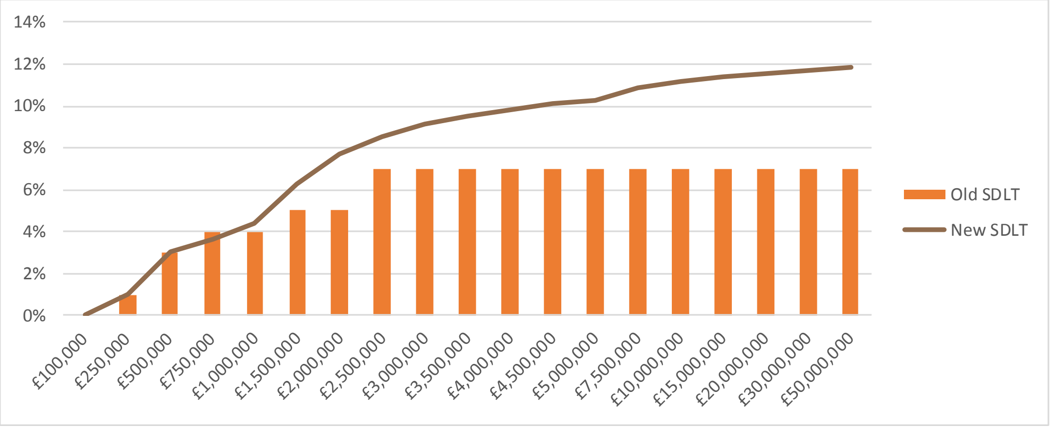
A Comparison of Global Property Costs
After the Recent Tax Reform in the United Kingdom

Introduction

Following on from the last Soane Speaks article titled 'Chinese and Indian Wealth Demographics – The Movement of Capital into UK Luxury Residential Property', Soane concluded with their belief that London is, and for the foreseeable future will continue to be, the most attractive destination for UHNWIs seeking to preserve their wealth through luxury residential property. Nonetheless, on Wednesday 3rd December 2014 George Osborne, Chancellor of the Exchequer, in his Autumn Statement unexpectedly ended the 'Slab Structure' for Stamp Duty Land Tax (SDLT) with immediate effect and replaced it with a more progressive regime. According to the Chancellor, this new system, which is structured in the same way as income tax, will mean that there are no 'cliff edges' and thus no significant increases in SDLT for home purchasers paying merely £1 over a threshold. Instead, purchasers will be subject to smooth and gradual rises that will apply solely to the portion of price that comes over each band. The Head of Policy at RICS further comments suggesting that "These changes reduce distortion and ensure those at the top end of the market contribute fairly, while those at the bottom will be given wider availability to get on the ladder, cutting out 'dead zones' in the market".

Table 1. Difference between old and new stamp duty by purchase price



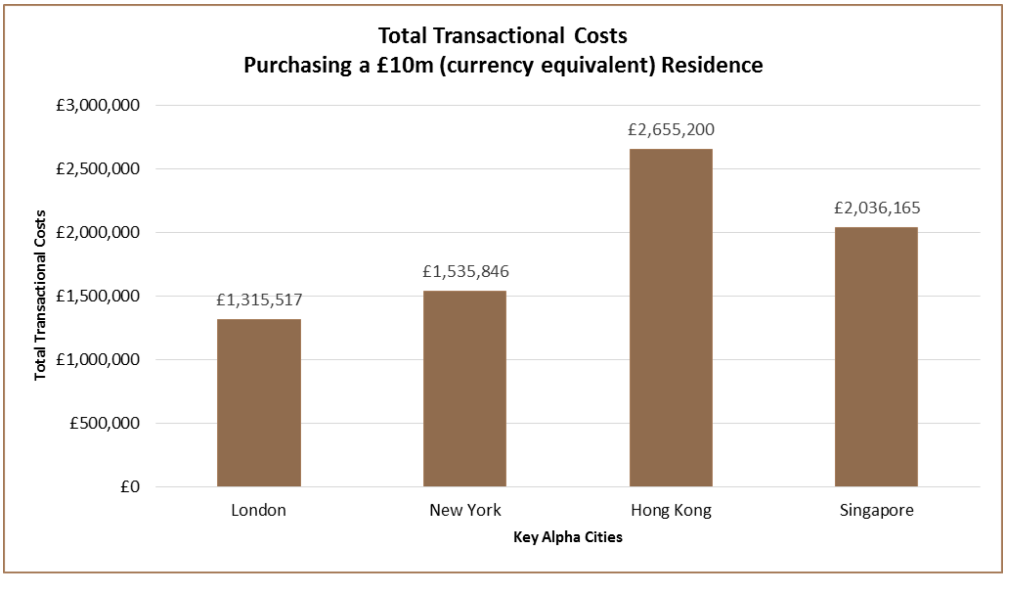
While the Chancellor's statement that "this move will benefit 98% of home buyers" may be true, the structural change only benefits those purchasing a property worth less than £937,500. Despite the belief that merely 2% of home purchasers will be worse off as a result of this reform, when you consider that the number of transactions over £1m within London is approximately one in ten, the reform does not negatively affect 2%, but remarkably more like 10% for those purchasing in the capital.

With a significant proportion of UHNWIs looking to preserve their wealth through luxury residential property, which by the purchasers' very nature characteristically retain capital values in excess of the £937,500 breakeven point, how does the recent reform in SDLT affect the desirability of one, if not the most attractive global city, London? A seemingly obvious question arises, as a result of the recent SDLT reform; do other Alpha cities such as New York, Hong Kong and Singapore now supersede London as the most sought after residential location, presenting better value for UHNWIs when comparing the total transactional costs of purchasing and owning luxury residential property?

London vs. New York?

At the prime end of the London residential market and within the highly prestigious country estates such as Wentworth and St George's Hill, where property transactions frequently exceed £10m, the effects of the SDLT reform are particularly acute and buyers will feel the pain as the Chancellor intended. For purchases at £10m, previous SDLT thresholds required the buyer to pay 7%, however under the new rates purchasers will now be paying 11.14%, an additional £413,750 in tax compared to before. For the buyer of a £20m prime London residence, this equates to a substantial uplift of £913,750 in duty. New York, undoubtedly one of the wealthiest residential markets in the USA, commands more dollars per square foot than any other state. Nevertheless, when compared against London, New York has significantly lower prices per square foot across the prime market and far lower purchasing taxes. Such purchasing taxes include the New York State 'Mansion Tax', a 1% 'cliff edge' tax, as per the previous SDLT structure, on residential transactions above $1,000,000. The catch, however, is that New York boasts the highest Governmental ownership tax out of the three other comparable Alpha cities, London, Hong Kong and Singapore. According to the Candy GPS Report, the total Government ownership tax over a 5 year period on a £10m (approx. $15.7m US dollars) residence in prime New York is approximately 5.75% of the property's capital value. This is compared to London's 0.07%, Hong Kong's 1.15% and Singapore's 0.49% estimated total Governmental ownership tax over a 5 year period. When it comes to disposing of the asset, New York encompasses an approximate agency fee of 6%, a substantial increase on the variable 1% to 2% seen within London, Hong Kong and Singapore. Purchasers of properties in New York with capital value of £10m (currency equivalent) rarely act without representation, and therefore the use of buying agents is customary. However, unlike London, the buying agency fees are not paid by the purchaser but the vendor and on top of their own listing (selling) agency fees. Consequently, the total costs of selling a luxury £10m currency equivalent residence in New York is 8.01% and mainly attributable to the seller's real estate transfer tax, attorney fees and the substantial agency fee. While the costs associated with purchasing luxury residential property within New York seem inexpensive on a global level, the total transactional costs (purchasing, retaining for five years and disposing) on a £10m currency equivalent residence are 15.36% of the property's capital value, and therefore marginally more expensive than London. Despite possessing the lowest purchasing costs out of the three comparable Alpha cities, when analysing the total transactional costs involved with a £10m currency equivalent luxury residence, suddenly New York does not look such an attractive destination to preserve individual wealth and a location that does not present more value than London. One must also take into account that New York's Governmental ownership tax accounts for a significant percentage of its total transactional costs. Therefore, it can be said that if a property is retained for more than five years, the economical gap in the total transactional costs between New York and London becomes even greater. Furthermore, due to global positioning and the associated time zone, New York, unalike London, lacks the simplicity in travelling East and West, a prerequisite for many international UHNWIs.

Table 2&3. Comparing the Total Transactional Costs of Purchasing a £10m Residence



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Sales Price	£10,000,000

London		
Stamp Duty	11.14%	£1,113,750
Gross Legal Fees	0.25%	£25,000
Ca.Total Cost of Purchase	11.39%	£1,138,750
Appx. Government Ownership Tax over 5 years*	0.07%	£6,767
Gross Legal Fees	0.20%	£20,000
Agency Fees	1.50%	£150,000
Ca.Total Cost of Sale	1.70%	£170,000
Approx.Total Transactional Costs	**13.16%**	**£1,315,517**
*Westminster Council Tax - Band H (£1,353 p.a)		

New York		
Approximate Currency Equivalent	**£1.00 - $1.57**	**$15,700,000**
NYC Mansion Tax	1.00%	$157,000
Gross Attorney Fees (Inc. Title Assurance)	0.60%	$94,200
Ca.Total Cost of Purchase	1.60%	$251,200
Appx. Government Ownership Tax over 5 years*	5.75%	$902,294
Seller's Real Estate Transfer Tax	1.80%	$282,600
Gross Attorney Fees	0.20%	$31,400
Total Agency Fees (Buying Agency Fees paid by vendor)	6.00%	$942,000
Managing Agents Closing Fees	N/A	$1,784
Ca.Total Cost of Sale	8.01%	$1,257,784
Approx.Total Transactional Costs	**15.36%**	**$2,411,278**
	GBP	**£1,535,846**
*Est. New York City Real Estate Tax ($180,458 p.a)		

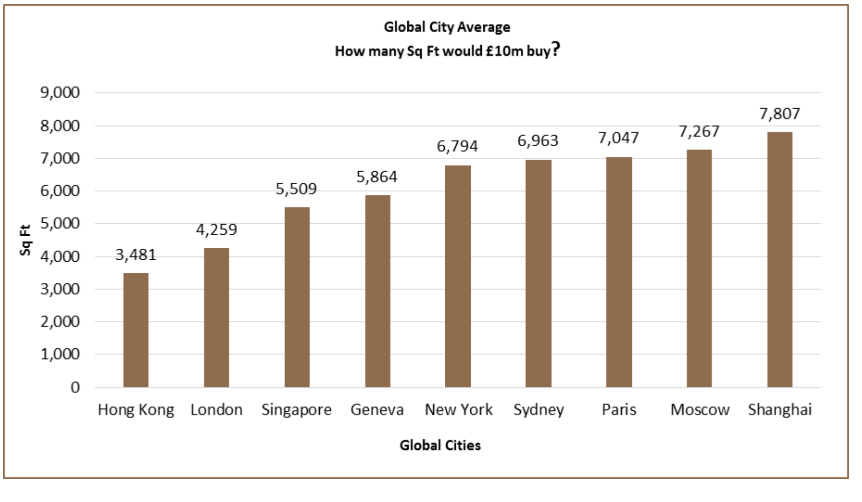
Hong Kong		
Approximate Currency Equivalent	**£1.00 - $12.14**	**$121,400,000**
Stamp Duty	8.50%	$10,319,000
Gross Legal Fees	0.20%	$242,800
Additional Stamp Duty for Foreign Buyers	15.00%	$18,210,000
Ca.Total Cost of Purchase	23.70%	$28,771,800
Appx. Government Ownership Tax over 5 years*	1.15%	$1,398,528
Gross Legal Fees	0.20%	$242,800
Agency Fee (Purchaser and Vendor)	1.50%	$1,821,000
Ca.Total Cost of Sale	1.70%	$2,063,800
Approx.Total Transactional Costs	**26.55%**	**$32,234,128**
	GBP	**£2,655,200**
*Est. Hong Kong Residential Property Tax ($279,705 p.a)		

Singapore		
Approximate Currency Equivalent	**£1.00 - $2.06**	**$20,600,000**
Stamp Duty	2.97%	$612,600
Gross Legal Fees	0.20%	$41,200
Additional Stamp Duty for Foreign Buyers	15.00%	$3,090,000
Ca.Total Cost of Purchase	18.17%	$3,743,800
Appx. Government Ownership Tax over 5 years*	0.49%	$100,500
Gross Legal Fees	0.20%	$41,200
Agency Fees	1.50%	$309,000
Ca.Total Cost of Sale	1.70%	$350,200
Approx.Total Transactional Costs	**20.36%**	**$4,194,500**
	GBP	**£2,036,165**
*Est. Singapore Residential Property Tax ($20,100 p.a)		

London vs. Hong Kong?

The estimated total transactional cost for an international buyer over a five year period on a £10m currency equivalent residence in New York is more expensive than that of London, however considerably more economical than Hong Kong. As evident within the above tables, this is due to entirely different transactional costs. Since 1997, Hong Kong has risen to become a key global financial centre. During this time, occupier demand and purchaser confidence has increased, which as a consequence has created a substantial price growth. This growth has been seen across all sectors, however most noteworthy within ultra-prime residential property, which due to limited stock, is highly sought after among UHNWIs. As a result of increasing demand, prices have surged, propelled by a combination of stringent government regulations on development, low interest rates and currency stability, while the supply of land, which is regulated by the government, continues to diminish. In an effort to curb soaring residential property prices, a number of measures have been introduced, such as a 15% 'flip tax' on residences resold within six months, and Buyer's Stamp Duty (BSD), which imposes a 15% tax for international purchasers on top of the more traditional SDLT rates. It is of significant importance to note that the amount of square footage a buyer is able to purchase for their money in Hong Kong is significantly less than that of London, New York and Singapore. According to CNBC, the currency equivalent of £10m ($121,400,000 HK currency equivalent) purchases 3,481 square feet of luxury residence, as opposed to 4,259 square feet in London (22% increase), 5,509 square feet within Singapore (58% increase) and a substantial 6,794 square feet (95% increase) in New York.

Table 4. Global City Average: How many Sq Ft would £10m buy?



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Despite the fact that purchasers of a £10m luxury residence in Hong Kong will pay 8.5% in traditional SDLT, or £263,750 less than they would if the property was situated within London, the costs of purchasing are estimated to be 23.7%, as opposed to 11.39% in London. Nonetheless, this is almost entirely attributable to the 15% additional SDLT for international buyers of residential property. Furthermore, the approximate total transactional costs of purchasing a £10m currency equivalent luxury residential property in Hong Kong is estimated to be 26.5% of the property value, compared to London's 13.2%, New York's 15.4% and Singapore's 20.4%. Hong Kong, and to some degree Singapore, illustrates the eye watering heights that some Asia Pacific markets have reached and why Hong Kong is considered to be the most expensive city for residential property investment.

London vs. Singapore?

Singapore, an additional Asian Alpha city, has observed exceptional growth of ca.115% since 2005 on residential property, while super-prime residential prices have seen an increase of approximately 232%. Due to the substantial economic expansion within South East Asia, together with naturally restricted land situated within a minuscule state, limited stock has led to significant price increases. According to Savills, Singapore has the largest percentage of millionaire households in the world (16% of residences worth more than £1m currency equivalent and above), combined with one of the highest home ownership rates. These two factors provide some further explanation to why Singapore's prime residential market has such limited stock and additionally why luxury residential property prices have been subject to momentous growth. In spite of paying a relatively cheap SDLT rate (2.97%) when compared to London and Hong Kong, Singapore, in an effort to cool the escalating residential market while in turn increasing available stock levels, has also introduced a 15% additional SDLT for foreign purchasers of residential property. As a result, the costs of purchasing a £10m ($20,600,000 SGD) currency equivalent residential property in Singapore is approximately 18.2%. Despite both the costs of purchase and the total transactional costs associated with a £10m currency equivalent luxury residence in Singapore being considerably cheaper than that of Hong Kong, it is still some way off the value London offers even with purchasers paying £413,750 more in SDLT than pre 3rd of December.

What about Total Transactional Costs at sub-£10m?

This article to date has discussed transactional costs on residences entirely with capital values of £10m (currency equivalent), however it is of importance to examine whether London's superiority over the three other Alpha cities continues when purchasing residencies with capital values of £1m and £5m (currency equivalent). Our findings identified that when purchasing residences with capital values of £1m and £5m, or currency equivalent, London as a global city continues to present better value for money irrespective of the recent reforms in SDLT. Regardless of having higher costs of purchase than New York, London presents better value when comparing the estimated total transactional costs. This can also be said for the Alpha cities of Hong Kong and Singapore.

The Proposed Mansion Tax?

It may be of interest to note that through working the metrics, for most property transactions, it is far more economical to pay a one-off increase in SDLT than an annual mansion tax, which Labour indicate they still intend to press ahead with. If introduced, this would therefore require the buyer of a residence worth £10m under the proposed 2% over £2m mansion tax formula to pay £160,000 a year, plus SDLT of £700,000 under the old system. Over a period of five years this would equate to a total of £1,500,000. The recent SDLT reform however stipulates a buyer to pay £413,750 more than the £700,000 (7%), which as a result suggests the purchaser to be £386,250 better off.

There is a widespread belief that the super-rich can deal with facts and figures and react accordingly. However, like the majority of people, the super-rich feel particularly uncomfortable when it comes to uncertainty and recently this uncertainty has been connected with the proposed introduction of a mansion tax. Nevertheless, Soane feel that the subsequent introduction of a mansion tax on top of the recent SDLT reform is unlikely, despite Labour's comments, as the total transactional costs together with the ongoing annual costs on residential property to those considered wealthy would be implausibly high. This is positive news for London's luxury residential market and furthermore the highly prestigious estates of Wentworth and St George's Hill, two of the key destinations for wealthy individuals seeking a luxury residence in a sylvan setting outside the capital. In addition, harking back to 1992 when Stamp

Duty was increased from 1% to 2% on purchases over £60,000, there was a common disbelief that a buyer would have to pay double the Stamp Duty. Nevertheless, history tells us that while there has and will be a small correction at the top end of the residential market and see those properties currently marketed somewhat affected, within six to twelve months' time the initial reaction and pain felt at present will be forgotten and the increase will be considered an accepted transactional cost.

Conclusion

Top end luxury London residences are not immune from the recent reform in SDLT and buyers will feel the pain as envisioned. Analysing the total transactional costs of purchasing, holding for five years and disposing of a residence at £1m, £5m and £10m, London continues to present better value than its rival Alpha cities of New York, Hong Kong and Singapore. Irrespective of having higher SDLT rates than other Alpha cities in certain property transactions, London possesses a cheaper Government ownership tax and is not subject to the additional stamp duty for foreign investors seen within Hong Kong and Singapore. As a result, Soane Capital strongly believe that London, not only due to total transactional costs, but also its stable economy, mature residential market, strong legal system, respected institutions, preferable time zone, and as one of the global centres for financial services, will for the foreseeable future continue to be the premier destination for UHNWIs who wish to preserve their wealth through luxury residential property.

Following on from this Soane Speaks, the next issue will examine the consequences the current collapse of the Rouble has and will continue to have on Russian luxury residential property investment within London. Soane have documented in recent months a desperation from wealthy Russian individuals to withdraw their money out of Moscow in the wake of the Russian Economic Crisis.