

# UK Commercial Real Estate



# Knight Frank Private Office Commercial

## Access to the Best of Knight Frank's Expertise, Global Connectivity & Deal Flow

The Knight Frank Private Office Commercial team provide clients with a personalised, high quality service which is overseen by a dedicated relationship manager. The team provide strategic advice to investors and major real estate stakeholders on both the acquisition and disposal of assets. We assist you through your complete commercial real estate journey across various global locations and sectors.

We provide investors with targeted investment opportunities across the real estate risk spectrum.

Our global team of experts, supported by our dedicated research department, offer you the guidance that you need throughout the full life cycle of property ownership.

The Knight Frank Private Office Commercial team have produced this guide to answer underlying fundamental points raised by clients from across the globe to navigate their way through the UK buying process and to demonstrate how Knight Frank can be of assistance every step of the way.

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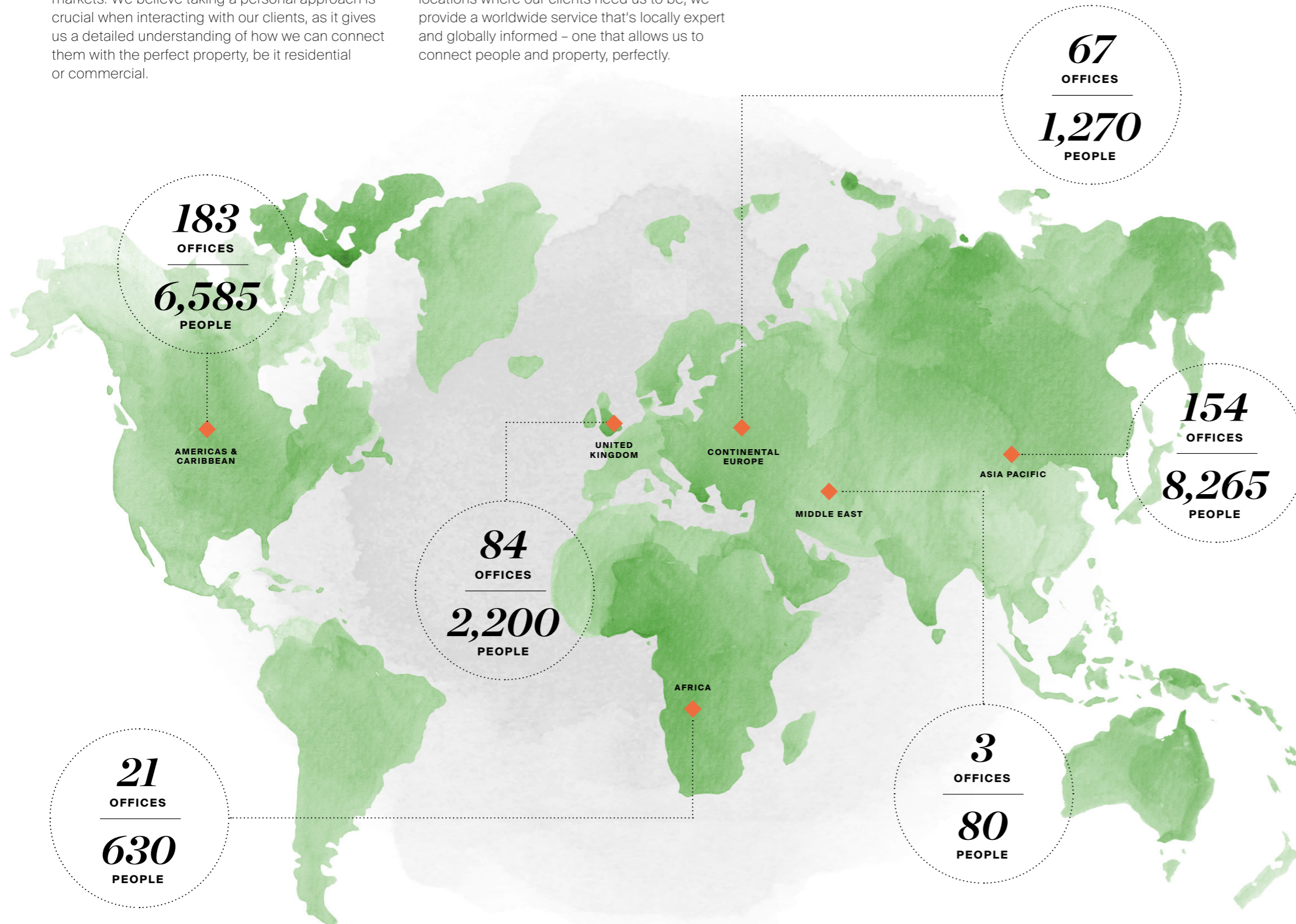
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# Locally Expert, Globally Connected

At Knight Frank, we build long-term relationships, allowing us to provide personalised, clear and considered advice on all areas of property in all key markets. We believe taking a personal approach is crucial when interacting with our clients, as it gives us a detailed understanding of how we can connect them with the perfect property, be it residential or commercial.

Founded in 1896 and headquartered in London, we have more than 500 offices across 60 territories and more than 19,000 people. We operate in locations where our clients need us to be, we provide a worldwide service that's locally expert and globally informed – one that allows us to connect people and property, perfectly.



## AMERICAS & CARIBBEAN

### 13 Territories

– Argentina, Brazil, Canada, Chile, Colombia, Costa Rica, Mexico, Peru, Puerto Rico, Caribbean (3), USA

## AFRICA

### 10 Territories

– Botswana, Kenya, Malawi, Nigeria, Rwanda, South Africa, Tanzania, Uganda, Zambia, Zimbabwe

## CONTINENTAL EUROPE

### 17 Territories

– Austria, Belgium, Cyprus, Czech Republic, France, Germany, Hungary, Ireland, Italy, Monaco, Netherlands, Poland, Portugal, Romania, Russia, Spain, Switzerland

## UNITED KINGDOM

### 3 Territories

– England, Scotland, Wales

## MIDDLE EAST

### 2 Territories

– Kingdom of Saudi Arabia, United Arab Emirates

## ASIA PACIFIC

### 15 Territories

– Australia, Cambodia, China, Fiji, Hong Kong, India, Indonesia, Japan, Malaysia, New Zealand, Philippines, Singapore, South Korea, Taiwan, Thailand

## Why should Private Investors & Family Offices invest in UK Commercial Real Estate?

In the global real estate marketplace, private investors and family offices already have a strong presence and are becoming an increasingly important force, with almost a third of Knight Frank UK Commercial Real Estate transactions last year, involving Knight Frank.

In fact, this research shows that 21 per cent of all private wealth is held in real estate investments of some kind, excluding primary residences and second homes, whilst 78 per cent of Ultra High Net Worth Individuals (UHNWIs), have mixed residential and commercial portfolios.

The number of UHNWIs (\$30M+ in net assets), is increasing, meaning that we can expect to see more investment into global commercial real estate in the future. In fact, the UHNWI population is forecast to grow 22% over the next five years.

There are some clear themes that has led to the popularity of commercial real estate as an investment category for private clients:

**Risk Mitigation** – Real estate allows investors to diversify at both a portfolio and geographical level. It also provides the ability to tailor investment decisions in terms of location, sector and tenant components, as well as provide regular income and an underlying asset.

**Control** – Real estate, with its direct ownership, diversity of lot sizes and choice of asset management approaches is attractive to those not wanting to pass decision making to third parties, or be constrained by close-end fund models.

**Currency Diversification** – Although exchange returns are not generally a direct driver for property investment, currency movements and capital controls have, in some instances, been a trigger for investors looking to capitalise.

**New Choices** – The emergence, growth and establishment of sectors including urban logistics, convenience retail, leisure and specialist operating assets, such as student housing, hotels and care homes allow private clients to diversify and fine tune their business plan personally.

## Who can own property in the United Kingdom?

*Property can be owned by any individuals or legal entities with legal capacity. There are no restrictions on the foreign ownership of property in the United Kingdom.*

*Once purchased, all property and their registered owners must register the new ownership with HM Land Registry.*

### Tenure – Types of Property Ownership

#### **FREEHOLD**

The main basis of ownership for commercial property across the UK\* is Freehold.

As the owner of a freehold interest in property:

- You own both the property and the land on which the property stands into perpetuity.
- You are responsible for its maintenance and repair if it is not let to tenant(s) on a fully repairing and insuring (FRI) lease.
- You can do what you wish within the property as long as this is in accordance with the legal and planning requirements.

\*The Scottish equivalent of Freehold is called Heritable Interest.

#### **LEASEHOLD**

This type of interest entitles you to ownership of a property for a fixed period of time, upon which ownership of the property will return to the freeholder when the lease comes to an end. This is most common in London but is becoming increasingly common across the UK.

- Unlike freehold property, you will not own the ground upon which the property stands, you will however have exclusive rights to the property for the length of the interest.
- The terms of the lease will be contained within a document called the 'head lease'. This outlines the rights and obligations of each party (generally referred to as the lessor and lessee).
- The length of leasehold interests do vary and typically can range from 25 years to 999 years.
- The length of the lease can be extended by agreement between the lessor and lessee at an agreed cost or in accordance with current legislation, however the lessor is not obliged to extend.
- All leasehold properties will be subject to a ground rent payable to the lessor. Typical ground rents can vary from £1 if collected (otherwise known as peppercorn), to a fixed amount per year or a percentage typically of current passing rent of the occupational tenant(s) but this can also be a percentage of the estimated rental value (ERV).
- Once the term of the long leasehold interest element expires, the lessee forfeits their exclusive rights to the property and these are transferred back to the lessor.

# How is UK Commercial Real Estate Classified?

*The Town and Country Planning (Use Classes) Order 1987 (as amended) puts uses of land and buildings into various categories known as 'Use Classes'. It is generally the case that you will need planning permission to change from one use class to another, although there are some exceptions where the legislation does allow some changes between uses. As of 1st September 2020, a new Use Class Order came into effect.*

**This list outlines the types of uses within asset classes and their corresponding land use code:**

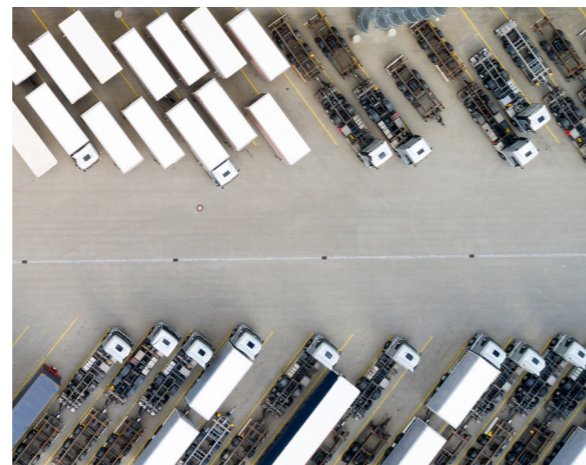
## Class B

### **B2** GENERAL INDUSTRIAL

Use for industrial process other than one falling within class E (g) (previously class B1) (excluding incineration purposes, chemical treatment or landfill or hazardous waste).

### **B8** STORAGE OR DISTRIBUTION

This class includes open air storage.



## Class C

### **C1** HOTELS

Hotels, boarding and guest houses where no significant element of care is provided (excludes hostels).

### **C2** RESIDENTIAL INSTITUTIONS

Residential care homes, hospitals, nursing homes, boarding schools, residential colleges and training centres.

### **C2A** SECURE RESIDENTIAL INSTITUTION

Use for a provision of secure residential accommodation, including use as a prison, young offenders institution, detention centre, secure training centre, custody centre, short term holding centre, secure hospital, secure local authority accommodation or use as a military barracks.

### **C3** DWELLING HOUSES

This class is formed of 3 parts:

- C3 (a) covers use by a single person or a family.
- C3 (b): up to six people living together as a single household and receiving care.
- C3 (c) allows for groups of people (up to six) living together as a single household.

### **C4** HOUSES IN MULTIPLE OCCUPATION (HMO)

Small shared houses occupied by between three and six unrelated individuals, as their only or main residence, who share basic amenities such as a kitchen or bathroom.



## Class E Commercial, Business & Service

Class E broadly covers uses previously defined in the revoked Classes A1 / 2 / 3, B1, D1 (a-b) and 'indoor sport' from D2 (e):

- E (a)** Display or retail sale of goods, other than hot food
- E (b)** Sale of food and drink for consumption (mostly) on the premises
- E (c)** Provision of:
  - E (c) (i) Financial services,
  - E (c) (ii) Professional services (other than health or medical services), or
  - E (c) (iii) Other appropriate services in a commercial, business or service locality
- E (d)** Indoor sport, recreation or fitness (not involving motorised vehicles or firearms)
- E (e)** Provision of medical or health services (except the use of premises attached to the residence of the consultant or practitioner)
- E (f)** Creche, day nursery or day centre (not including a residential use)
- E (g)** Uses which can be carried out in a residential area without detriment to its amenity:
  - E (g) (i) Offices to carry out any operational or administrative functions,
  - E (g) (ii) Research and development of products or processes
  - E (g) (iii) Industrial processes



## Class F Local Community and Learning

In two main parts, Class F covers uses previously defined in the revoked classes D1, 'outdoor sport', 'swimming pools' and 'skating rinks' from D2 (e), as well as newly defined local community uses.

### F1 LEARNING AND NON-RESIDENTIAL INSTITUTIONS

Use (not including residential use) defined in 7 parts:

- F1 (a) Provision of education
- F1 (b) Display of works of art (otherwise than for sale or hire)
- F1 (c) Museums
- F1 (d) Public libraries or public reading rooms
- F1 (e) Public halls or exhibition halls
- F1 (f) Public worship or religious instruction (or in connection with such use)
- F1 (g) Law courts

### F2 LOCAL COMMUNITY

Use as defined in 4 parts:

- F2 (a) Shops (mostly) selling essential goods, including food, where the shop's premises do not exceed 280 square metres and there is no other such facility within 1000 metres
- F2 (b) Halls or meeting places for the principal use of the local community
- F2 (c) Areas or places for outdoor sport or recreation (not involving motorised vehicles or firearms)
- F2 (d) Indoor or outdoor swimming pools or skating rinks

### SUI GENERIS

Certain uses do not fall within any use class and are considered 'sui generis'. Such uses include: betting offices/shops, pay day loan shops, theatres, larger houses in multiple occupation, hostels providing no significant element of care, scrap yards. Petrol filling stations and shops selling and /or displaying motor vehicles.



**If you have or are acquiring a property that would benefit from a change of use, Knight Frank's in-house planning team would be delighted to advise and assist in securing this for you.**

## Changes to the Use Classes Order

Use	Use Class up to 31st August 2020	Use Class from 1st September 2020
Shop ≤ 280 sqm mostly selling essential goods, including food and at least 1km from another similar shop	<b>A1</b>	<b>F.2</b>
Shop	<b>A1</b>	<b>E</b>
Financial and professional services	<b>A2</b>	<b>E</b>
Café or restaurant	<b>A3</b>	<b>E</b>
Pub or drinking establishment	<b>A4</b>	<b>SUI GENERIS</b>
Hot food takeaways	<b>A5</b>	<b>SUI GENERIS</b>
Offices (Other than a use within Class A2)	<b>B1a</b>	<b>E</b>
Research and development of products or processes	<b>B1b</b>	<b>E</b>
Industrial processes (Uses can be carried out in a residential area without detriment to its amenity)	<b>B1c</b>	<b>E</b>
Industrial	<b>B2</b>	<b>B2</b>
Storage or distribution	<b>B8</b>	<b>B8</b>

Use	Use Class up to 31st August 2020	Use Class from 1st September 2020
Hotels, boarding and guest houses	<b>C1</b>	<b>C1</b>
Residential institutions	<b>C2</b>	<b>C2</b>
Secure residential institutions	<b>C2a</b>	<b>C2a</b>
Dwellinghouses	<b>C3</b>	<b>C3</b>
Use of dwellinghouse by 3-6 residents as a 'house in multiple occupation'	<b>C4</b>	<b>C4</b>
Clinics, health centres, creches, day nurseries, day centre	<b>D1</b>	<b>E</b>
Schools, non-residential education and training centres, museums, public libraries, public halls, exhibition halls, places of worship, law courts	<b>D1</b>	<b>F.1</b>
Cinemas, concert halls, bingo halls and dance halls	<b>D2</b>	<b>SUI GENERIS</b>
Gymnasiums, indoor recreations or fitness (not involving motorised vehicles or firearms)	<b>D2</b>	<b>E</b>
Hall or meeting place for the principal use of the local community	<b>D2</b>	<b>F.2</b>



# The Standard Process of Purchasing Commercial Real Estate in the United Kingdom

The processes and procedures for acquiring a commercial real estate asset in England and Wales usually follows the order below:

01

## INSTRUCTING A SURVEYOR

Knight Frank can assist you throughout the entire acquisition process from initial sourcing of opportunities to completion of the transaction and beyond through a singular point of contact. When acquiring investment opportunities, we would seek to act on the buy-side, our fee for which would be 1% of the gross purchase price + VAT. This is only payable on the completion of a successful acquisition.

06

## OFFERS & NEGOTIATION

Knight Frank will assist you with the offering process should you decide to proceed with a formal proposal. We will use our analysis to recommend a suitable offer price and our market intelligence to establish the most appropriate level to start the negotiation process. We will use our relationships with other agents to your advantage throughout the process.

05

## ASSET ANALYSIS & INSPECTION

As part of the identification process, Knight Frank will provide full cash flow analysis. We will work closely with our best-in-class debt advisory team to drive geared returns. We will also provide detailed business plans incorporating leasing and investment comparable evidence to support our analysis as well as inspecting and measuring the property.

02

## MARKET INTELLIGENCE

An exclusive mandate will provide you with full access to Knight Frank Research's broad range of services including information on market trends and forecasting. At the outset, we will provide market research reports highlighting our views on where to invest in the relevant sectors.

03

## SOURCING OPPORTUNITIES

Our experienced and well-connected investment teams will source opportunities for you both on and off market. We have an extensive database of available opportunities and a stocklist of likely future sales which enables us to quickly present opportunities to suit your investment criteria.

04

## BUILDING YOUR TEAM

Knight Frank can advise you on and recommend individuals to form a professional team to support and fulfil your business plan. This can include solicitors, accountants, tax advisors, debt advisors, architects and building consultants.

09

## EXCHANGE & COMPLETION

Knight Frank will assist you and your legal advisors up until the point of exchange and completion. If required, we can provide a full purchase report prior to exchange outlining a summary of the property, legal and tax due diligence as well as any asset management recommendations. At this point, Knight Franks fee for advising on the acquisition would be payable as well as the supporting acquisition team used including solicitors and supporting services such as accountants, debt advisors and building surveyors.

08

## PROPERTY DUE DILIGENCE

Knight Frank will liaise with the assembled team undertaking the property due diligence including all building, mechanical and environmental surveys whilst keeping in close contact with the legal and tax teams working throughout the contract stage.

07

## HEADS OF TERMS

Should you be successful in having an offer accepted by a vendor, we will then help you to agree suitable Heads of Terms for the transaction. This will usually involve further negotiation with the vendor and their advisors in order to secure the most favourable transaction terms. We will liaise with your solicitors at all stages.

# What are the costs associated with purchasing Commercial Real Estate?

## Stamp Duty Land Tax (SDLT)

SDLT is payable on all property transactions, except where the purchase price is under the minimum threshold. SDLT is an incremental tax, therefore a higher level of tax is applicable as the price of the property increases.

The table below denotes the brackets applicable for SDLT and an example also below outlines its structure delimiting the tax payable for a property worth £5,000,000. SDLT will be payable within 14 days after the 'performance' of the transaction, which is usually completion.

Property or lease premium or transfer value	SDLT Rate
Up to £150,000	<b>Zero</b>
The next £100,000 (the portion from £150,001 to £250,000)	<b>2%</b>
The remaining amount (the portion above £250,000)	<b>5%</b>

**Example:** If you buy a commercial property for £5,000,000, the SDLT applicable for the transaction can be calculated as follows:

0% on the first £150,000	<b>£0</b>
2% on the next £100,000	<b>£2,000</b>
5% on the final £4,750,000	<b>£237,500</b>
<b>Total SDLT payable</b>	<b>£239,500</b>

\*The rates above (correct as at 1st March 2020) denote SDLT applicable for commercial and mixed-use property in England and Northern Ireland and are provided for general information only. You must obtain professional or specialist advice in respect of stamp duty land tax from your property lawyers, accountants or other financial or tax advisers. [The rates and brackets when purchasing residential property differ, for clarification on residential SDLT, please contact the Knight Frank Residential Team.]

Land & Buildings Tax (LBTT) if situated in Scotland and Land Transaction Tax (LTT) if situated in Wales apply and this document does not cover the rates. Anyone contemplating purchasing a Scottish or a Welsh property should ensure they take appropriate advice on the position.

# Property Tax in the United Kingdom

## Value-Added Tax (VAT)

If a property has been elected for VAT, this will be charged in addition to the purchase price of the property at a rate of 20%. Property is usually elected for VAT when substantial refurbishment or redevelopment works have been undertaken or are planned, as the VAT on the expenses can be recovered. If a building is elected for VAT, a landlord will be required to charge VAT on rents payable to the occupational tenants.

The majority of commercial property transactions will be outside the scope of VAT and constitute a Transfer Of a Going Concern (TOGC). This is applicable if the property is tenanted, or is subject to an agreement for lease, even if the prospective tenant(s) are not yet in occupation. If the transaction constitutes a TOGC, then no VAT is chargeable by the seller, but a condition on the sale is that the purchaser is required to opt to tax.

## Income Tax

Income Tax is payable on rental income received by investors from commercial real estate, at the appropriate marginal rates i.e. up to 45% of net rental income regardless of an individual's UK residence status.

This level of Income Tax can be reduced if any deductible expenses exist. The main two deductions are capital allowances or interest on a loan taken out to purchase the property.

## Corporation Tax

From 6th April 2020, overseas buyers in receipt of income from UK commercial property investment will also be subject to Corporation Tax on that income (instead of Income Tax) at the main rate of 19%.

## Inheritance tax (IHT)

UK IHT applies to UK assets which are directly owned, regardless of the residence or domicile status of the owner. IHT is chargeable on death at 40% in relation to assets held at death.

## Other considerations

A purchaser must review the capital allowances position and consider if it is possible for the vendor and the purchaser to jointly elect to fix the portion of the purchase price to be allocated to fixtures qualifying for capital allowances.

## Capital Gains Tax

As of April 2019, all Capital Gains Tax exemptions for non-resident landlords (foreign investors) of UK property have been removed, including for foreign companies, individuals and Jersey Property Unit Trusts (JPUTs). In addition to this, profits derived by non-residents, levied on value uplifts from April 2019 on the disposals of companies, JPUTs, and other vehicles including Real Estate Investment Trusts (REITs) and funds will be taxed, as long as 75% of the gross value comes from UK property.

For individuals, the top rate of Capital Gains Tax is currently 28%.

Despite this, there are exemptions for overseas institutional investors such as pension and sovereign wealth funds. Vehicles such as REITs that already enjoy exemptions from Capital Gains Tax will continue to do so. However, the gains on the sale of shares in 'property rich' vehicles (where 75% of assets are UK real estate) will be taxed.

Anti-forestalling provisions have already taken effect to prevent non-residents structuring or restructuring to avoid this tax change.

The information above (correct as at 1st March 2020) is provided for general information only. It is not definitive nor is it intended to amount to advice on which you should rely. You must obtain professional or specialist advice from your property lawyers, accountants or other financial advisers on tax issues before taking, or refraining from, any action on the basis of the content above.

## How can Knight Frank Service & Implement the Business plan to drive performance?

Once a property has been acquired, Knight Frank can still be of assistance through the full life cycle of property ownership, ensuring the business plan

is seamlessly executed in order to drive performance and maximise your returns. A sample of some of our key relevant services are listed below.

### Debt Advisory

Our debt advisory team enables you to access the right financing options aligned with your strategic plans. The team works and maintains relationships with different types of lenders across all sub-sectors of real estate providing development and investment finance advice.

### Property Asset Management

The team manage every aspect of a property or portfolio across all sectors, so our clients have 'no noise'. The team keep tenants happy and engaged to minimise risk of lease breaks, whilst also driving value through strategic asset management.

### Project & Building Consultancy

The team provide building surveying and cost consultancy services. The team help form and implement asset business plans, turning buildings into real assets. The team can also provide detailed development consultancy advice for major refurbishment or redevelopment projects.

### Business Rates

As one of the leading specialist teams in the business rates sector, the Knight Frank Business Rates team offer a full rates management service which will ensure that any costly rates overhead is mitigated at every stage.

### Commercial Agency

The team provide landlords with expert advice with regards to the leasing and disposal of commercial properties. The team have an in-depth knowledge of all the UK's major sub-markets and a substantial track record to prove it.

### Lease Advisory

Our lease advisory team provides a full range of services including lease extensions, rent reviews, lease renewals and head lease re-gears. The team will unlock latent value and drive rental performance through strategic lease advisory.

### Valuation & Advisory

The team value real estate for a range of purposes and clients. Our market-leading capital markets, leasing and research teams operate at the coalface to help make our valuations real-time.

### Investment Disposal

Once a business plan has been completed, our award winning capital markets team have an unrivalled track record of maximising outperformance in the international sales area.

## What are the methods of disposal of UK Commercial Real Estate?

*The Private Office Commercial Team, supported by the Global Capital Markets Network are on hand to guide you through the best process, giving you the highest chance of disposal. The following provides an overview on the different methods.*

### Formal Tender

- Sealed bids.
- Vendor can state they are under no obligation to accept the highest bid.
- Transparent process.
- No opportunity to amend/increase their offer after submitting.

### Informal Tender

- Best offers or 'Bids'.
- Used typically when there is good interest to bring negotiations to a conclusion.
- The process is not legally binding upon either party.

### Auction

- Property to be offered for auction subject to a reserve price.
- When the gavel falls, if you are the top bidder at or above the reserve price you will have acquired the property.
- Competition drives the sale price, therefore achieving market value.

### Private Treaty

- Parties free to negotiate without commitment in the open market.
- Advantages include flexibility with both parties able to negotiate without obligation whilst maintaining an element of confidentiality.

# Knight Frank Research & Intelligence Lab

Knight Frank benefits from a dedicated research team producing over 500 specific reports each year covering all aspects of the commercial, residential and specialist property markets across the globe.

The Intelligence Lab is home to Knight Frank's cutting edge, data-led research which helps understand important trends across the global property market and provides access to reports such as *Active Capital* and *The Wealth Report*.

**The Intelligence Lab can be accessed at  
[knightfrank.co.uk/research](https://knightfrank.co.uk/research)**

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