Game *CHANGER*

Julian Hayden suggests a new approach to overseas investment in UK property

Events, such as Brexit and changes to UK taxation, have unsettled the UK's residential and commercial property markets.

Sterling's fall post-Brexit brings obvious opportunities for overseas investors, and the core attractions of London as a cultural centre, and the UK generally as a secure place for investment, remain.

Overseas clients who do wish to invest in, or buy and occupy, property should now be reviewing how such purchases are structured to fit their needs for succession planning and asset protection.

COMMERCIAL, NOT RESIDENTIAL?

Recent tax changes include higher rates of stamp duty land tax (SDLT) for purchases of residential property through companies, and for any second-home buyers, including non-residents. Perhaps more important is the proposed exposure of residential property to inheritance tax (IHT), despite structured ownership.

Overseas investors will still be able to protect all other UK assets from IHT, and some investors may be attracted to commercial property by its lower rates of SDLT. In addition, price compression caused by SDLT changes may be a golden opportunity to move devalued properties into different structures at a low tax cost.

OFFSHORE COMPANIES

Offshore companies remain attractive in certain circumstances. For all asset classes other than residential, full protection from capital gains tax (CGT) and IHT is still available. A company can be used to manage the rates of tax on rental income and enjoy relief for interest payments, but personal-ownership rules are changing. Company ownership allows the sale and purchase of shares outside CGT and mitigates SDLT. A company-owned residential property can be let exclusively to a third party on commercial terms and not be subject to annual tax on enveloped dwellings (ATED).

Offshore companies can still be used for the acquisition of commercial or mixed-use properties where residential property is commercially let, or for UK land trading.

MINDSET CHANGES – LEND TO BUY

An overseas purchaser might consider lending to buy, not simply buying. Trustees, instead of buying a property for a UK beneficiary and allowing rent-free occupation, might instead form an offshore company that lends to the beneficiary to buy personally. Alternatively, a non-domiciled, non-resident individual might form an offshore company that lends to a UK family member, who in turn buys a property.

MULTIPLE INVESTORS AND PARTNERSHIPS

Recent changes may encourage a shift towards multiple investors. Rather than a wealthy investor owning multiple special purpose vehicles, each with its own property, investors might form a holding company for all the properties exempt from the stamp-duty hike.

Partnerships are corporates for tax purposes but not for ATED; like trusts, they can last forever, avoiding probate issues. Both are efficient structures for long-term ownership and flexible for clients' needs. There should be no reservation of benefit and the general partner can keep voting control, leaving the other partners with economic interests, but no vote.

PROPERTY FUNDS

Investment funds offer tax benefits not available to individual investors, as such funds are exempt from non-resident CGT and 'look through' IHT. They are unaffected by current reductions in mortgage interest relief and benefit from low non-residential rates of SDLT for buildings of six or more properties. Closed-end vehicles should have few liquidity issues currently affecting some open-end funds.

Some investors may prefer to hold property-backed units with borrowing facilities, rather than direct ownership of bricks and mortar.

> 'Recent changes may encourage a shift towards multiple investors, who might form a holding company'

RENT AND OCCUPY RATHER THAN OWN AND OCCUPY

Prospective owner-occupiers may now prefer to rent. They could hold property investments in the form of shares or units, or they might ask a fund to buy their chosen property, having invested into the fund in exchange for units – then renting the property from the fund. The individual pays rent but receives indirect rental income from the units.

A Jersey property unit trust could hold such properties through a Jersey subsidiary. This structure would offer the pooling of properties, rental income and an eventual capital return, compared with the traditional model, whereby an investor buys a property, improves it and sells it on at a gain, but with minimal rental yield.

Investors wanting a residential portfolio could unitise it without an ATED charge and avoid IHT, the fear of which might otherwise precipitate 'fire sales' by direct owners. Funds might also appeal to occupiers currently paying ATED who will be exposed under the new IHT rules, and who could transfer in their property in exchange for a commercial lease and income-producing units possibly carrying premium value.

After Brexit, despite uncertainties and tax changes, the attractions of London and the UK remain. There are new opportunities for owning, investing and renting, especially for overseas investors with strong currencies. The need for good succession planning and proper asset protection persist, but the game has changed.

FURTHER READING

Turn to page 83 to read Mark Biddlecombe's explanation of reforms to UK non-domiciled status and the opportunities and challenges it brings for trust companies and their clients.

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