

IRISH/UK PROPERTY BULLETIN



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01. EDITORIAL

Welcome to the 7th issue of the Morgan McManus Irish/UK Property Bulletin. Those of you unfamiliar with our service can learn more about us by visiting our Website at www.morganmcmamus.com. We have offices in Northern Ireland and the Republic of Ireland and also provide legal services in England/Wales. This publication is being delivered to Accountants and Financial Advisors, Banks, Mortgage Advisors, Property Investment Companies and Private Investors. We hope to give you an insight into the information you will need to ensure that you have adequate legal protection when investing in property, whether that property is in Northern Ireland, the Republic of Ireland or in England/Wales. As we practice in all three jurisdictions we are ideally placed to provide a comprehensive comparative analysis – and that is important, particularly where it is your first venture into international property investment.

We know that you will find the Articles in this issue of interest. We have concentrated on Pension Investment. If you are resident

in Northern Ireland/UK the word on every investor's lips is SIPPs. If you are resident in the Republic of Ireland, then perhaps it's SSAPs. Approaching "A-Day" in April 2006 there will be much interest in investing in residential property in the UK as investors seek to buy residential property in anticipation of capital appreciation. There is no doubt that this interest will be even more intense in the East London area where the Olympic Games will be based – the Thames Gateway/Stratford area. Add to that the fact that interest rates in the UK may drop in the short-term and you have a very good recipe for a revived property market in the UK. The smart property investor should always get in when the market is at a low ebb and there was never a better time than now – particularly with all the incentives which are available!

In the next issue we will cover the subject of the Olympic Games Announcement and what it will mean for investors in London.

We are delighted that Ciaran Lonergan, Private Banking Manager with Bank of Ireland

has written for us an Article on Pension Structures for Investment in Property. We know that this will be of invaluable assistance to those of our subscribers in ROI who are taking a serious look at investing in property through Pension Trusts.

As well as providing legal advice to the Private Investor, we also act for Investment Companies and can provide very competitive terms, particularly where we are acting for a number of purchasers in a common property, e.g. a number of apartments in the one block. Further details of our ROI service are available from Fergal McManus at our Clones office (e-mail fmcmanus@morganmcmamus.ie) and of our Northern Ireland/UK services from Seymour Major of our Enniskillen office (e-mail smajor@morganmcmamus.co.uk). (See telephone contact details at end of this Bulletin).

BRIAN MORGAN
EDITOR

PENSION STRUCTURES

02. Pension Structures For Investment In Property.

Ciaran Lonergan Private Banking Manager with Bank of Ireland Private Banking, Republic of Ireland, outlines the various pension structures in Ireland through which an individual can purchase investment property.

There has always been a very strong bond between Irish people and property, and the appetite for property investing has continued unabated over the last number of years, with Irish people investing billions of Euro in properties at home and internationally.

Property has always featured as an asset used in pension funding, albeit on an indirect basis, with unit linked pension property funds, where investors bought units in a fund which owned numerous individual high street properties. More recently, following significant changes in retirement options in the 1999 and 2000 Finance Acts, we saw the development of Pension Mortgages, where a property is purchased and the capital sum borrowed, ultimately repaid out of a pension fund.

The Finance Act 2004 brought about well documented changes in pensions legislation – an ability to borrow within an occupational pension scheme which combines a seemingly irresistible trilogy of Tax Relief, Gearing and Property. In this article, I will outline three of the main methods of direct property investment involving pension funds, namely;

Pension Backed Mortgages

Small Self Administered Pension Schemes (SSAPs)
Syndicated Geared Property Funds

Pension Backed Mortgage

The structure of this arrangement consists of:

1. A personal "interest only" loan, and
2. An Executive Pension Plan, from which the borrowing will be repaid in one bullet at retirement.

The property is purchased personally by you and you borrow the required funds in a personal capacity. You pay interest only to the lender, leaving the capital outstanding until you retire. In the case of a commercial loan, the interest payments can be fully offset against the rental income. Since no capital repaid, interest is maximised and thus the offset against rental income is maximised.

The capital repayment is accumulated within the Pension Plan. The Company can contribute to the Pension Plan and such contributions are fully tax deductible by the Company as a trading expense. In addition, the company contributions are not treated as a Benefit-in-Kind (BIK) in your hands. At retirement, you can take up to 25% of the Pension Fund in the form of a tax-free lump sum and use such to repay the borrowing. If this is insufficient, you can access further cash from the Pension Fund, but subject to marginal rate tax.

The end result is that:

- You personally own the property unencumbered,
- The Company has effectively paid for the capital cost of the property, with no tax cost to you, and
- Interest paid by you is fully off settable against rental income during the loan period.

Advantages of Pension Backed Mortgages

- Allows you to own a property personally, from the outset.
- Tax relief is received on interest paid, tax on rental income minimised or removed altogether.
- Contributions towards capital repayment receive tax relief (pension contributions).
- Capital repayments grow tax free before bullet payment is made to the lender.
- Property can be used as leverage for future acquisitions.

- Sale of the property invokes a CGT charge of 20% of the gain on the transaction.

Disadvantages of Pension Backed Mortgages

- Capital balance outstanding does not fall over the term of the loan.
- The pension fund aims to repay the loan outstanding based on assumed levels of pension fund growth. There is no guarantee that the fund will grow at a sufficient rate to meet the repayment.
- Pension backed mortgages are reliant on the tax legislation and current tax rates. Future changes in tax legislation could impact on the pension mortgage.

Small Self Administered Pension Schemes (SSAPs)

A Small Self Administered Pension Scheme (SSAP) is an occupational pension scheme mainly used by Company Directors. One of the attractions of a SSAP is the direct control that trustees can exercise over the investment policy of the scheme. They can invest directly in stocks and shares, deposits, directly in property etc. The range of investments is generally much greater than available in life assurance company unitised funds. The Finance Act 2004 allows SSAP's to borrow as part of their investment strategy. SSAP's have investment restrictions attaching to them and there are additional Revenue requirements associated with establishing and reporting on a SSAP. Specific restrictions surround the area of property investment and can be summarised as follows;

- The vendor must be at 'arms length' from the scheme and the employer, including its directors and associated companies.
- The property cannot be disposed of, or let to, the employer, including its directors and associated companies.

PENSION STRUCTURES

- A transaction that involves the scheme trustees directly in the acquisition and development of property with a view to its disposal will not qualify for tax exemption.
- Acquisition of property for personal use is not permitted.

Where a property is purchased by a SSAP, it is important to remember that it is the Trustees of the SSAP which arrange the borrowing and legally own the property. Rent received from a property within a SSAP is tax free, and contributions to the SSAP are also tax relievable. The rent and contributions are used to repay the debt, which must be cleared within 15 years or selected retirement age, whichever occurs first. There is a facility to retain the property in an Approved Retirement Fund post retirement, and to ultimately pass the value of the property to the next generation in a tax efficient manner. There are constraints on how much you can invest through a pension scheme, most notably those related to salary. In broad terms you cannot generate a pension fund that would provide you with a pension at retirement of more than 2/3rds your final salary. Any more and you could be "over – funded" which can cause complications where there is a property involved. The effect of gearing can enhance returns so care needs to be taken to ensure overall funding limits are not exceeded.

Advantages of a Small Self Administered Pension Scheme (SSAP)

- Company contributions to a SSAP receive tax relief, and are not taxable as income in the hands of the individual (i.e. no BIK).
- Rent received into a pension fund does not incur tax.
- Contributions, when invested within the scheme, grow tax free.
- If a property is sold prior to retirement, the proceeds are exempt from tax within the pension scheme.
- It is possible to retain a property post retirement, within a tax exempt structure, i.e. an Approved Retirement Fund.

Disadvantages of a Small Self Administered Pension Scheme (SSAP)

- Additional set-up and reporting requirements compared to standard executive pension contracts.
- Property investments must be on a totally 'arms length' basis.
- Property cannot be let to the scheme's employer.
- Personal use and development of property prohibited.
- Property will need to be sold in the event of death before retirement.
- Whilst fund growth and inflows to the pension scheme are free of tax, once a tax free lump sum of 25% of the overall fund is taken at retirement, any subsequent withdrawals from the scheme are subject to marginal rate tax.
- Surplus Capital Allowances not utilised where a Scheme purchases a property.
- It is not possible to leverage off an existing property or any other assets (inside or outside of the Scheme) when purchasing other properties.

Syndicated Geared Property Funds

In this type of arrangement, the Syndicate promoters source and purchase a significant "Trophy" type building and endeavour to obtain top class tenants with strong covenants. The promoters will look for a number of investors to invest an equity contribution in the particular property. The promoters then arrange borrowing for the balance of the purchase price. These transactions are structured in a way which involves the individual making a contribution to a pension scheme. These funds in turn are used as the equity contribution. The contribution to the pension fund is fully tax relievable. In general the rent received from tenants is used to repay the debt. The property would be sold after a period of 7-10 years, with returns based on capital appreciation of the property on the back of rent reviews. As the transaction is "wrapped" within a pension fund, the proceeds of the sale are tax free in the fund and can be used to invest in other funds such as traditional managed or cash funds to retirement.

Advantages of a Syndicated Geared Property Fund

- Tax relievable access to trophy buildings.
- Returns are tax exempt within the pension fund structure.
- Promoters borrow on non-recourse basis for individual.
- Gearing has potential to enhance returns.

Disadvantages of a Syndicated Geared Property Fund

- Gearing could accentuate losses in the event of a property falling in value.
- Due to the long term nature of the investment, Syndicated Geared Property Funds are generally unsuitable for those aged over 53.
- On death prior to retirement, there may be a need to sell the share of the property at an inopportune time.

Summary

Recent changes in legislation have increased the popularity of linking property investments with pension funds. Whether it is buying a property as an asset of your pension fund (assisted by gearing) or buying a property personally with the intention of repaying the loan on retirement, more choice is now available.

For Company Directors in particular, these new investment structures can be particularly attractive. It is however important to stress that in any headlong dash to buy property, wrapping a poor property in a tax efficient structure will not turn such property into a good investment. The fundamentals of property investment still apply.

Whatever way you go about such an investment, it is critical to get professional advice so as to ensure that the structure will be fully compliant and appropriate to your particular requirements.

Ciaran Lonergan
Private Banking Manager
Email: ciaran.lonergan@pb.boi.ie



RESIDENTIAL PROPERTY UK



**BRIAN
MORGAN**

03. UK Residential Property How Big A Boost Will SIPPs Be To The Property Market?

In the April 05 issue of the Bulletin Brain Morgan suggested that there could be more interest in investment in residential property in the United Kingdom after the 6th April 2006 when individuals who hold SIPPs would be entitled to invest also in residential property.

Research carried out by Paragon Mortgages has shown that over half of Buy To Let investors in the UK would want to place residential property into a SIPP after April 6 next year, when the rules change to allow this.

Source: Paragon Mortgages

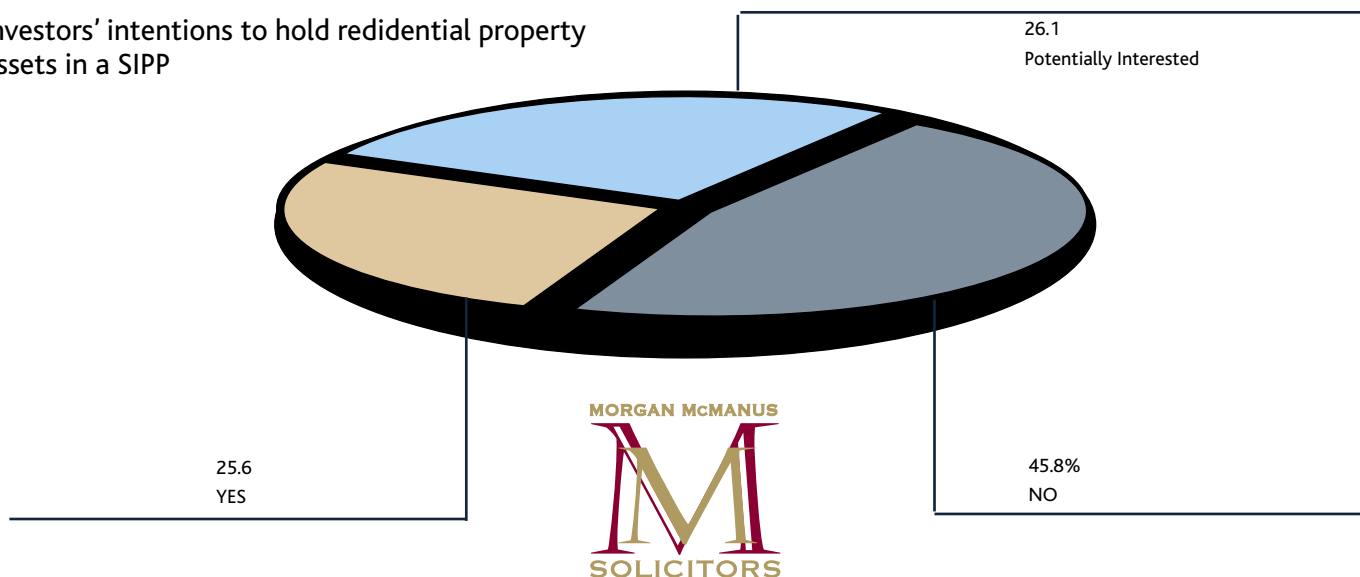
The only conclusion which one can reach is that there will be a big demand for housing to go into SIPPs and therefore a big boost to property prices. This is good news for individuals who already own residential property in the UK and those looking to purchase property in the UK in anticipation of price increases in the UK property coming up to the SIPPs deadline in April 2006.

How does this affect the R.O.I Investor?

The proposed changes in the UK allowing the SIPPs to invest in residential property will benefit both UK and R.O.I property investors who already own residential property in UK (because of capital appreciation) or planning to purchase residential property in the UK in the near future in anticipation of further capital appreciation. Furthermore, an R.O.I investor who is a Company Director could also choose to purchase this UK residential property through a similar R.O.I tax vehicle, known as Small Self Administered Pension (SSAP) and thus avail of similar type tax relief's in R.O.I which are available in the UK to UK investors through SIPPs.

Brian Morgan, Solicitor
Email: bmorgan@morganmcmamus.ie

Investors' intentions to hold residential property assets in a SIPP



SIPP SSAP

04. SIPP And SSAPs – How Do They Work?



**BRIAN
MORGAN**

Brain Morgan advises on the common structures between UK SIPP and R.O.I SSAPs

In the UK an individual can purchase property through a tax vehicle known as a "Self Invested Personal Pension" (known as a SIPP). In the Republic of Ireland, a similar facility is available to certain individuals through a tax vehicle known as a "Small Self Administered Pension" (known as a SSAP). In R.O.I it is restricted to Company Directors. There is however a lot more to it than just buying a property and writing to the taxman to tell him your new investment is part of your pension plan - and request a tax reduction!

This tax vehicle allows you to manage your own pension. It gives you far more control over your pension than before. However, this tax vehicle is a legal entity. This means that, while you will be able to 'shop' for the sort of buy-to-let (or commercial) property you want in this tax vehicle fund, and put the money into the pension fund to purchase that property, in law it will not be you that will own the property but the pension fund. And it will not be

you that buys the property, but your pension fund. The pension bank account holds the funds. You pay into this through pension contributions or rent from your property. The fund makes mortgage payments to the bank to cover the property purchase, and it also pays out fees to the SIPP/SSAP provider and to the property manager.

If, for instance, you go the commercial property route, then having bought the property via your pension fund, the company occupying the building pays rent not to you, but to your pension fund.

The pension fund pays no income tax on any profit that the rents generate. And when your pension fund (not you) sells the property there is no capital gains tax to be paid on any capital appreciation. The vital part about your SIPP/SSAP is that it can be tailored to meet your demands, and your ability to invest, and fees are highly variable too. So search for a SIPP/SSAP provider who will advise you on the appropriate property investment.

Brian Morgan, Solicitor
Email: bmorgan@morganmcmamus.ie



TRANSFER



**FERGAL
MCMANUS**

5. Transfer Of A Site To A Child - CGT And Stamp Duty Exemptions.

Fergal McManus, Solicitor and Professional Tax Advisor, advises on tax reliefs available in ROI where a parent is transferring a development site to a child.

Up until 6th December 2000, a transfer of a building site by a parent to a child gave rise to a Capital Gains Tax charge for the parent and Stamp Duty for the child. Despite the fact that no money changed hands, the Revenue Commissioners deemed that the transaction took place at market value and assessed tax accordingly. Up until the 6th December 2000, these tax liabilities would not arise if the property passed to the child on the death of a parent. The Government felt that this position encouraged parents to postpone the transfer of a building site to a child so an exemption was introduced to overcome this perceived resistance..

Capital Gains Tax

The parent will not be obliged to pay Capital Gains Tax provided the following applies:-

1. The market value of the site at the time of transfer does not exceed £254,000.
2. The Transfer must be from a parent to a child of that parent
3. The Transfer must be for the purpose of enabling the child to construct a dwelling house on the land which would be occupied by the child as his/her only or main residence.



4. There is a claw back provision that provides that the exemption will be withdrawn if the child subsequently disposes of the land, otherwise than to his or her spouse and at the time of the disposal the land does not contain a dwelling house which was:-

1. Constructed by the child since he or she acquired the land
2. Has been occupied with the child as his or her only main residence for a period of three years. Should the claw back occur, the Capital Gains Tax liability effectively becomes the liability of the child. It should be noted that the Capital Gains Tax exemption is a once in a lifetime relief and a parent cannot repeat the process of give a site to the same child again in the future and hope to avail of the exemption.

Stamp Duty

From the child's view point they would ordinarily be liable to Stamp Duty on the market value of the site. To obtain the Stamp Duty exemption contained in Section 83 of the Stamp Duty Consolidation Act the following conditions must be fulfilled:-

- a) The market value of the site at the date of transfer cannot exceed £254,000.
- b) The transfer must be of the entire beneficial interest in the site.
- c) The transfer must be from a parent to a child of that parent. The purpose of the transfer must be to enable the child build his or her only or main residence on the site.
- d) The transfer is the first and only qualifying transfer to that child.
- e) The Deed must contain the statement certifying that the above conditions are met.

One anomaly is that the Stamp Duty exemption

does not contain a claw back provision so therefore there are no circumstances on which the stamp duty exemption can be lost or withdrawn.

Sons/Daughters-in-law

It should be noted that in order to avail of the exemption under Capital Gains Tax and Stamp Duty the Deed of Transfer must be to the child only and that the exemption cannot be obtained if the transfer is made jointly to a child and his or her spouse. A simple tax planning mechanism to get around this is to transfer the site into the child's sole name initially and then the child can subsequently transfer the site into the joint names of his or her spouse without triggering a clawback. The transfer of a family home between spouses does not give rise to further Capital Gains Tax or Stamp Duty liabilities due to the benign tax treatment of such transactions between spouses. It should be noted that this tax planning arrangement would not work in respect of partners or engaged couples.

While this tax planning opportunity has been in existence for some years at this stage, it could be said that the exemptions are not being utilised to their full capacity as they are not commonly known among members of the public. Once again, it proves the wisdom of always seeking professional advice at the earliest possible stage of considering any transaction.

Fergal McManus,
Solicitor and Professional Tax Advisor.
Email: fmcmanus@morganmcmamus.ie

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MORGAN MCMANUS SOLICITORS

OFFICES AT

ENNISKILLEN

12 PAGET LANE,
ENNISKILLEN,
COUNTY FERMANAGH. BT74 7HT
TELEPHONE 028 6632 0102
FACSIMILE 028 6632 2232

CLONES

LAW CHAMBERS,
THE DIAMOND,
CLONES,
COUNTY MONAGHAN
TELEPHONE 047 51011
FROM NORTHERN IRELAND - 00353 47 51011
FACSIMILE 047 51679
FROM NORTHERN IRELAND - 00353 47 51679

NEWTOWNBUTLER

THURSDAY EVENINGS
MAIN STREET,
NEWTOWNBUTLER,
COUNTY FERMANAGH. BT92 6JT

EMAIL US

NORTHERN IRELAND LAW@MORGANMCMANUS.CO.UK
REPUBLIC OF IRELAND LAW@MORGANMCMANUS.IE