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London calling

IAIN JOHNS CONSIDERS IF TRUST STRUCTURES AND OFFSHORE COMPANIES ARE STILL A VALID MEANS FOR HOLDING UK PROPERTY

In recent years, there has been an increasing trend for cross-border investment in residential property. This movement of capital is most notable in cities that offer a world-class lifestyle and education options, in addition to providing excellent investment opportunities, all of which are key considerations for multi-generational families.

The UK, and London in particular, has traditionally been considered a safe haven for property investment, due to a transparent market, political and physical stability, the clear rule of law, an independent judiciary, the benefits of foreign currency exchange for international investors, and world-renowned schools and universities.

However, in recent UK Budgets, there have been notable changes relating to property taxes and international investment vehicles. These changes have led to a recurring and fundamental question among investors: are offshore companies and trusts still a valid means for holding UK property?

A PRAGMATIC APPROACH

A series of well-publicised budgetary measures have been introduced to minimise the benefits of using offshore structures. Such measures include an extension of the existing annual tax on enveloped dwellings (ATED) regime, higher rates of stamp duty on property purchases made by offshore companies, and proposals to extend the scope of capital gains tax (CGT).

Understandably, foreign investors are increasingly asking which holding structure is appropriate for them: an offshore trust, offshore company or direct ownership?

There has been a move away from the common, 'default' position of using an offshore company (with or without a trust) towards a much more pragmatic approach,

with investors, in conjunction with their tax and legal advisors, assessing their circumstances and objectives and weighing up their options in much greater detail.

Some older investors, for instance, are more concerned with inheritance tax (IHT). For them, a company structure might be most appropriate. If the investor is younger, then the IHT benefits of such a structure are less relevant, and a trust might be more attractive.

PRACTICAL CONSIDERATIONS

Research shows that the main motivation for overseas buyers in purchasing London new-build properties is investment (65 per cent), and a third of investors purchase property for their children's future, with tertiary education as the key decision-making factor.[1]

Therefore, there are also a number of practical considerations for investors.

If the investor or their family intends (at least temporarily) to occupy the UK property, then, depending on their circumstances, a visa may be required to work, study or otherwise reside in the UK. It can take weeks to process application forms for the purposes of satisfying residency criteria, while investor visas, for example, can require significant additional investment and administration.

Meanwhile, if the asset in question is an investment property to be let commercially, then the investor will need to consider the appointment of a managing agent and the terms of the tenancy, including such fundamentals as determining the rent and length of the lease.

There will inevitably be maintenance, security and insurance requirements too. If a property manager is required, then careful thought must be given as to how that arrangement will be managed within the parameters of a holding structure.

On the taxation side, there are also a number of practical considerations. If the property is let, filings, including income tax and ATED returns, will need to be attended to as well.

Where a trustee can be appointed as manager of all financial and practical aspects of a structure, this can be a real benefit. It is something that is demanded more and more as part of a holistic private family office service.

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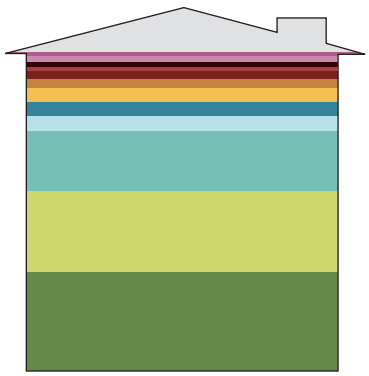
TABLE 1

NEW-BUILD CENTRAL LONDON PROPERTY: BUYERS' NATIONALITIES IN 2012



UK	27%
SINGAPORE	23%
HONG KONG	16%
CHINA	5%
MALAYSIA	4%
RUSSIAN FEDERATION	3%
TURKEY	3%
NIGERIA	2%
INDIA	2%
SAUDI ARABIA	1%
UNITED ARAB EMIRATES	1%
UKRAINE	1%
OTHER	12%

CULTURAL APPROACH TO INVESTMENT

It is also important to review cultural attitudes to property investment, as this can affect the appropriate holding structure.

Reviewing the London domestic property market in 2012, 42 per cent of purchasers were from foreign countries, with Europeans accounting for 13 per cent of sales, Asians 10 per cent and Russians nearly 5 per cent.[2]

However, when we look at new-build sales, the purchaser demographic changes significantly (see Table 1). In 2012, overseas investors invested GBP2.2 billion in the central London new-build market. Asian buyers accounted for 48 per cent of new-build purchases, with significant investment from Singapore (23 per cent) and Hong Kong (16 per cent).[3]

This is reflective of cultural attitudes towards investment in real estate, as buying property off-plan (i.e. buying a property before the structure is built) is a feature of the property market in Asia. Interestingly, high-net-worth individuals (HNWIs) in Asia Pacific (excluding Japan) invested 3.8 per cent more in real estate (24.6 per cent) than the rest of the world (an average of 20.8 per cent).[4]

As Asia Pacific is expected to become the world's largest HNWI wealth market by 2015,[5] it is imperative that trustees understand differing cultural attitudes towards various structures. For example, Asian investors may feel less comfortable with structures that limit their control. Mainland Chinese investors, meanwhile, culturally tend to think in terms of dynasties and perpetual ownership – leading one to logically align that tendency to the use of trusts. However, education surrounding the use of trusts in this geographic region remains at a preliminary stage.

There are also important differences in HNWIs' perceptions of their financial needs in emerging, versus mature, markets. HNWIs in the emerging markets of Latin America, the Middle East and Africa, and Asia Pacific (excluding Japan) have higher rates of business ownership, greater consideration for extended family in wealth planning, and higher allocations to real estate and alternative investments, including foreign exchange. As a result, 41.3 per cent of HNWIs in emerging markets describe their wealth management needs as complex, compared to only 18 per cent in developed markets.[6]

UNDERSTANDING AND PLANNING

The choice of investment vehicle or holding structure is key for non-UK nationals who want to invest in UK real estate. Offshore companies and trusts are still a valid means for holding UK property as long as advisors understand the short- and long-term objectives of private clients and their families, as well as their different cultural approaches to investment.

1 Knight Frank, *International Residential Investment in London 2013*
2 *Ibid*
3 *Ibid*
4 Capgemini and RBC Wealth Management, *The Asia-Pacific Wealth Report 2013*
5 Capgemini and RBC Wealth Management, *The World Wealth Report 2013*
6 *Ibid*

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