



ROSE
Financial Planning

THE UK'S FIRST 'INHERITANCE MORTGAGE' ARRIVES – BUT WE ALREADY USE IT IN SPAIN!

Now here's confirmation of just why you need sensible financial planning in Spain!

In recent months I have written on numerous occasions about the benefits of using long term 'Interest Only' mortgages for many reasons and, in particular to avoid unnecessary exposure to Inheritance Tax (IHT). How strange then that this week the Kent Building Society has launched a new 'Inter-Generational Mortgage' to counter the rising number of estates in the UK that are exposed to IHT.

This article will be in 2 parts to enable me the space to explore this matter. So make sure you pick up the next issue!

Part 1

First I need to explore the background to why the Kent Building Society has developed the product and launched it at this time.

The Inland Revenue (IR) announced some numbers a few weeks ago that should make all home owners sit up and pay attention to the changing face of IHT exposure. The tax was launched many, many moons ago to make the rich, renowned for their ability to mitigate other taxes, pay their fair share into the country's Treasury's coffers. It remains a tax on the estate value on death. But the IR have announced that there has been a 72% increase in 5 years of estate numbers paying this tax, and this is purely as a result of rising property values. That is not the 'rich' per se, at least not in the traditional sense, but 'middle class' property owners who have failed to plan to mitigate the tax!

And there's worse to come. This year 2006/7, the IR estimates that a further 22% growth in the number is expected. And, if property prices continual to spiral versus only a limited increase in the IHT tax allowance, then it will rise further still.

The Halifax has suggested an increase in the allowance from £285,000 to £435,000 to reflect the gap between the rise in property values over the last 10 years. Of course that is not going to happen!

IHT has always been described as a 'voluntary tax' because it can so easily be avoided by estate planning i.e. protection of assets by gifting them to children and grandchildren or the use of trusts.

But using a mortgage has long been accepted as a simple and very easy product to use so, whilst the Kent Building might be the first to package or brand it, the news for them is that good financial planners have been using the ploy for years.

And the same applies in Spain! At Rose FS, we consider that every single property should have a mortgage taken out at the purchase point as that is the most efficient time to do it! Logical really!

But a 'remortgage' (releasing funds after the purchase) can still be arranged relatively easily to achieve the same end.

The problem is this! Brits buying in Spain have a 'British' view of things and ideals and dreams that they believe are right for them. That translates into buying the home here outright for cash or, if they have to take a small mortgage, to look at paying it off as quickly as possible.

Take that one step further! There is an odd attitude with many that if they do not eventually pass the family home to their children debt free, then they have failed in some way! Call it pride if you wish for that is probably the case with most!

But that falls right into the hands of the IR in the UK and the Spanish hacienda here! You are exposing your estate and hence, your surviving spouse and end beneficiaries to a tax that can be so easily avoided legitimately! Do you really, really want to pay the Tax Man even more than you have already done? Remember that your estate has invariably been built from funds that have already been taxed! So you are allowing him to tax you again?

Or more to the point, because you will not be here, to tax your children! A point to note here. IHT has to be paid to the tax authorities BEFORE the estate can be taken over by the family. It cannot be used to raise a mortgage until the tax has been paid. So how will they find the money to pay the tax? Use valuable savings or mortgage another property of their own? All a little bit silly really, isn't it?

Make sure you read next week's issue to conclude the argument in favour of long term 'interest Only' mortgages for sensible estate planning, BUT also just why it suits every single property purchase transaction whether you are buying short term, long term, for investment purposes only, for retirement, and whether you are a tax Resident or a Non resident.

See www.rosefp.com or call 0034 677 874 948.

THE UK'S FIRST 'INHERITANCE MORTGAGE' ARRIVES – BUT WE ALREADY USE IT IN SPAIN!

Last week I gave an introduction to the timing of a new 'inter-Generational' mortgage launched by the Kent Building Society in the UK, and gave some background as to just why the lender is promoting it's use now.

If your missed the article, get the back issue of this paper or contact Rose FS for the copy.

Part 2

So, back to the theory of just why a long term 'Interest Only' works for every single property purchaser or owner.

A negative that has been used against this product is that you pay more interest over time because the debt never reduces. All rather obvious, of course. But there is one fundamental element that this argument forgets, and that is that if you have the funds to otherwise repay the mortgage debt, then save that money into other tax efficient products to build an aside capital base.

In other words what you have is a home with a mortgage on it, BUT you also have funds, protected legitimately using a variety of products, where the capital and growth is tax free and which also give you total flexibility and free access if you need it. Try getting access to capital (equity) in a home quickly, especially here in Spain!

In Spain, the benefits of using long term 'Interest Only' mortgages are even greater than in the UK. Take a look at the table below which compares the various benefits of the product in Spain and the UK.

	UK	Spain
1) IHT Mitigation	Yes	Yes
2) Interest Rate differential	Yes	Yes
3) Exchange Rate risk mitigation	No	Yes
4) Mortgage Interest Tax Relief	No	Yes
5) Transfer of mortgage on Sale	No	Yes

1) IHT Mitigation. As I have discussed already. The mortgage is taken with the children added to use the younger ages and, for some cases anyway, their income as well. Many older people rely on private or state pensions and, where these are limited, the extra earned income of the children gives access to a larger mortgage.

2) Interest Rate differential. Again, as discussed. In the UK this difference will depend upon the tax efficiency of the savings products used, for example, an ISA or equivalent. In Spain, we are looking simply at the difference between a normal Euro mortgage rate, say 4.4% today, versus the normal UK

mortgage rate, ranging from discounted deals at 5% plus all the way up to the variable rate of 6.75. Quite a margin, especially when you look at the compounded growth over a long period and add that tax efficiency element.

For example, if we assume a mortgage of say Euro 100,000 at a saving of 2% per annum over 10 years, excluding any added capital growth, we start at a saving of circa Euros 25,000. Free!

3) Exchange Rate risk mitigation. If your capital and income base (even if it is UK pension orientated) is in Sterling, then there is always the possibility that a deterioration of the foreign currency, the Euro, that you have used to purchase your Spanish home will eventually cost you extra money.

This is a subject that should be discussed at much greater length than I have time for now, but needless to say that a risk exists that should, at least, be recognised as such. That being so, the use of a long term mortgage (i.e. using someone else's capital rather than yours) reduces your own investment and hence, the risk to the exchange moving against you. If you would normally buy for cash think again and retain your own capital in Sterling, invested tax efficiently, of course.

4) Mortgage Interest tax relief. If you adopt Spanish Tax residency and you have a mortgage, the interest on the mortgage acquired to purchase your home can be offset any income tax payable. Note that this does not apply for remortgages i.e. where you release capital for general purposes. It may apply though where you release equity to produce an income in retirement.

This used to apply in the UK under the MIRAS system, but no longer.

5) Transfer of mortgage on Sale. Simply put, the long term 'interest only' mortgage can be as attractive for the eventual purchaser of your property if you sell up. The Spanish system refers to this transfer as a 'subrogation', and an extra benefit to the recipient is that it helps to eliminate the normal 2% mortgage tax payable on a purchase.

So, even if you are buying as an investor for a relatively short period of time as opposed to using long term 'interest only' for IHT and estate planning, the product still offers certain benefits with no downside.

To summarise then. Every single property purchase in Spain really has to have an 'interest only' mortgage on it and, where this is for a retirement home especially, with consideration given to the eventual inheritors by using our Spanish Euro equivalent of the 'inter-generational' mortgage.

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