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Knightsbridge Wealth

technical news

For professionals working with international clients

UK Investor Visa scheme under the spotlight

The Times recently reported that hundreds of millions of pounds of dirty money has been laundered through Britain because the 'golden visa' system for wealthy foreign investors.

Tier 1 (Investor) visas, which give British residency in return for a £2 million investment, are a potential tool for money laundering, the report says.

Since their 2008 introduction, 3,048 visas have been issued, with 60% going to rich individuals from China and Russia. More than half of the 1,173 visas issued last year went to Chinese investors. The campaign group Transparency International says that at least £3.15 billion has flowed into Britain from the visa scheme and "it is highly likely that substantial amounts of corrupt wealth stolen from China and Russia have been laundered into the UK through the Tier 1 investor visa programme".

The banking industry says it can only make limited checks on applicants and the government must carry out more scrutiny. Justine Walker, director of financial crime at BBA, the banks' trade body, said: "There are certain jurisdictions that pose challenges for banks in determining sources of funds. We would welcome any improvements to the Tier 1 visa scheme that enhance transparency and enable banks to fulfill their financial crime responsibilities."

Tackling abuse of 'golden visas' will be a test of the anti-corruption agenda being driven by the Prime Minister, who has said that Britain is "no place for dirty money" and will host a summit on corruption next year.

A Treasury assessment concluded last week that Britain's anti-money-laundering processes were inadequate. It disclosed that while hundreds of billions of corrupt funds were laundered in Britain, investigations by the National Crime Agency covered only millions.

There are no live investigations into flows of corrupt funds from China despite the authorities in Beijing running an international operation to find £82 billion in stolen funds. Britain also has limited law enforcement links with Russia, which has lost an estimated £31 billion to corruption. Nick Maxwell, of Transparency International, says that Britain should develop an asset recovery scheme with Beijing and tackle suspect funds at home by introducing "unexplained wealth orders" to require people to set out how they made their fortunes.

The Tier 1 visa attracted 153 applicants in 2009, when a £1 million stake was sufficient to qualify. The wealth limit was increased to £2 million last year and more stringent checks are being put in place.

A Home Office spokesman recently said "we have brought in a number of additional reforms to crack down on abuse of the system. This includes requiring an applicant to have a UK bank account — and therefore pass the bank's diligence checks — before they apply for a visa. Investors can no longer use loans to support the financial aspect of their application and have to be fully in control of their funds. We will also refuse a visa if we believe the funds were obtained illegally, or if the person's character, conduct or association with any other third parties giving financial backing is not conducive to the public good".

It is inevitable that the account opening and Source of Wealth requirements will make it more and more difficult to open accounts and buy investments with reputable banks. Increasingly, professional advisers will be expected to fully understand a client's source and origin of risk. Knightsbridge Wealth is experienced in collating comprehensive evidence to support an applicants' source of wealth, ensuring the best arrangements are in place for the unique needs of each client.

Attracting wealthy entrepreneurs who wish to move to the UK, to escape instability at home, remains an objective of the Home Office. However, the Global Investor Immigration Council (GIIC) has reported a drop of around 80% in applications this spring and summer, since the Chancellor raised the cost of the UK scheme in November.

Entrepreneur visa facing overhaul

The Migration Advisory Committee (MAC) published its recommendations to overhaul the Tier 1 (Entrepreneur) scheme on 29th October. At present, there are two streams to the entrepreneur route. First, the main entrepreneur route: this requires £200,000 of personal funding or £50,000 available from an approved source. The business plan is subject to a 'genuineness test' undertaken by civil servants. If approved, the applicant receives a three-year initial visa. At the extension stage the entrepreneur must demonstrate, among other things, that s/he is employing at least two full-time equivalent workers.

Almost 75% of those initially successful in being granted an entrepreneur visa do not go on to apply for extension.

Second, the graduate entrepreneur route: the individual must be a graduate from a UK university, receive endorsement from a Higher Education Institution for the proposal and is then granted a one year visa which can be, and is normally, extended for one extra year. UKTI have also run a programme under this route targeting a small number of overseas graduates with promising business ideas who are placed in UK accelerators.

MAC noted that applications had increased markedly in recent years. In 2014, 5,488 visas were issued under the entrepreneur route, together with 564 to graduate entrepreneurs. 5,168 dependant visas were also issued. There is now an average of two dependants for every main applicant – the highest ratio across all economic visa routes.

The MAC believes, essentially, that the graduate entrepreneur scheme works well - it has limited numbers and attracts high quality people. However, it suggests major reform of the Tier 1(Entrepreneur) route that, they believe, has a history of low quality projects that contribute little or nothing to UK plc.

Most professional advisers working in this arena are aware that this route is often selected as the cheapest and easiest way of obtaining residency, rather than applicants wishing to show genuine entrepreneurial flair and a commitment to build a successful business. We have always believed that this area will be under the microscope and many applications will not survive the test of an independent assessment.

The Committee noted that, in examining those in the UK with an Entrepreneur Visa, some established innovative businesses. At the other end, it noted that migrants do not appear to engage in much business activity at all, using it as a low cost alternative to the Tier 1 (Investor) route.

As we predicted, the MAC suggests major reform of this route. They recommend that industry experts, through an expert panel, rather than civil servants, should assess business plans. The assessment might cover viability, scalability and innovation potential, as well as the skills and aptitude of the individual to execute their business plan. It suggests better monitoring of business progress during the initial three-year period.

The decision to extend might be widened from a consideration of jobs created to also include factors such as turnover or having secured further investment.

It concludes that applications will be much more selective, with a rigorous process to evidence wealth creation. Inevitably, this will lead to a significant fall in accepted applications.

Global property bubbles emerging

Our strategic partner, UBS, issued an October report on global house prices. It underlines the fact that when inexpensive financing is combined with a positive long-term economic outlook, property prices eventually uncouple from the real economy. In some of the world's leading financial centres, prices are now fundamentally unjustified and the risk of a bubble has risen sharply.

In London, average house prices have soared by almost 40% since January 2013, making it one of the most expensive cities in the world based on price-to-income levels. London's real estate market is now totally decoupled from the rest of the country where, in real terms, prices are still 18% below the previous peak in 2007. London is up 6%.

The increase is understandable given continued foreign demand, as so much of the world remains unstable. Domestic buyers have helped too as government schemes such as 'help to buy' has stoked demand.

However, continued foreign demand is likely to be tamed, through adjustments to Stamp Duty Land Tax

(SDLT). Buying a £2m property in May 2010 (when the previous coalition came to power) would have cost £100,000; buying at the same value now would cost £153,750.

The Chancellor has also been making a clear statement that he wants residential transactions to take place between people – not companies, especially not offshore companies. The introduction of the Annual Tax on Enveloped Properties (ATED) and related legislation confirms this drive.

Finally, there is an indication of a desire to level the playing field between different groups of residential buyers. This has been most obviously expressed by the removal of non-resident investors' exemption from Capital Gains Tax, which came into effect in April this year.

UBS advise caution in the London market. It also concludes that a price correction seems imminent in Hong Kong and that Singapore is sensitive to unexpected economic shocks.

Is there a city it notes as undervalued? Yes. Chicago.

Property remains the biggest single asset most people hold and purchase is not always an investment decision – it is often one for personal reasons. Whatever the reason, it is clear that buyers require the highest quality of advice when selecting and researching property. Knightsbridge Wealth works with a range of property professionals to ensure clients are able to make the right choice, regardless of market conditions.

Commercial property offering good value

One area that is looking more attractive is commercial property. Rental growth in the UK has returned, according to Legal & General Investment Management.

A reduction in yields is now being superseded by rental growth as the main driver of commercial property capital growth. Commercial property prices have risen nearly 20% since the start of 2014 and market yields have fallen. Yields are now consistent with the level they would see them at once central bank interest rates have normalised and without the expectation of above average rental growth. This puts the focus of return generation on yield and rental growth.

In LGIM's view. "Commercial property rents are rising, buoyed by stronger tenant demand and a shrinking supply of space. This is taking over from yield compression as the key source of capital growth. Recently, there has been a progressive improvement in the volume of space being leased by companies. While this has not permeated the whole market equally, with the retail property sector lagging on a relative basis, there has been a significant improvement in overall demand."

Many clients are unaware of the options available in the commercial property sphere and, as pressure builds on residential property valuations, this asset class should, increasingly, form a part of an international client's investment portfolio.

Tax Changes to Buy-to-Let investments

Various changes have been announced in relation to Buy-to-Let (BTL) investments. Tax relief is being reduced on BTL mortgage interest. In future, BTL mortgage interest will only qualify for tax relief at the lower, basic rate of income tax (20%, rather than the higher rates of 40% and 45%). This change is being introduced from 2017 and will be fully implemented by April 2020. The next election is due in May 2020.

This is a significant change in tax status for those with a rental property, although the staged introduction between 2017 and 2020 will help landlords plan their investment strategy. Those planning a BTL investment will factor the new rules into their calculations, which could lead to lower pricing.

There will be a temptation for some landlords to raise rental levels – but their ability to achieve this will be constrained by rental market affordability and competition between landlords to minimise voids.

The government has also signalled its support for maximising the use of property by increasing the rent-a-room relief from £4,250 to £7,500 from April 2016.

The existing 'wear-and-tear allowance', which provided a standard 10% allowance against income on BTL properties, is to be replaced with a new relief that allows residential landlords to deduct the actual costs of replacing furnishings.

While not welcomed by landlords, this reform is unlikely to lead to a significant change in investor behaviour on its own. Added to the wider restriction of setting mortgage interest costs against tax, this will add pressure to some landlords with high loans.

Increase in Inheritance Tax (IHT) nil-rate band

The new reform increases the nil-rate band for IHT from £325,000 to £500,000 per person (£1m for married couples/civil partners). Any unused nil-rate band is transferable to a surviving spouse/civil partner.

There will be a tapered withdrawal of the additional nil-rate band for estates with a net value of more than £2m at a rate of £1 for every £2 over this threshold.

This expansion of the nil-rate band has the potential to drive house prices higher, although any impact is likely to be minimal.

The reality is that from 2017, a primary residence valued at up to £1m can be passed on to children tax free, and there is at least some relief on properties up to £2m. As a result, and despite the measure to protect downsizers, some older people may be persuaded to tie up more capital in their homes for longer – increasing demand for housing and reducing supply, liquidity already reduced by SDLT (Stamp Duty Land Tax).

Changes to non-dom legislation

When George Osborne delivered his first Conservative Budget on 8th July 2015, many people expected the Chancellor to announce some changes to the non-domicile regime. However, few anticipated that the core principle would change so dramatically.

Changes will be subject to detailed consultation and will take effect in April 2017. This gives individuals time to restructure their affairs and Knightsbridge Wealth specializes in advising international clients – either non-resident, or UK-resident, non-domiciled.

But changes will be significant. Osborne said "From now on, those who have been living in the UK for 15 of the last 20 years will pay the same tax as everyone else".

From 1914 to around 2010, anyone living in the UK, but domiciled abroad, paid no UK income or capital gains tax on their wealth — as long as they held it offshore. That made it about as tax competitive as a place can be — and it made the UK an attractive place for the international community to live.

Since the financial crisis, the non-doms have had to pay annual remittance charges to hang on to their right to pay tax only on what they bring into the UK (currently up to £90,000 a year).

It isn't immediately obvious how we move from where we are now to a system whereby non-doms pay the same tax as the rest of the population. They were hugely incentivised them to come here — and stay here.

From April 2017 anybody who has been resident in the UK for more than 15 of the past 20 tax years, will be deemed to be domiciled in the UK for tax purposes. In addition, individuals who are born in the UK to parents who are domiciled here will no longer be able to claim non-domicile status whilst they are resident in the UK.

An additional reform which will impact on this group is that from April 2017 all UK residential property held by a non-dom, whether directly or indirectly, including UK residential property held by offshore companies, offshore trust and company structures and non-UK partnerships, will be subject to UK inheritance tax. This change is likely to lead to non-doms considering the best structure in which to hold their properties.

Contact us

If you require further information about our services and how we can assist your clients, then please call us on the number below, or send us an email about how and when we can contact you.

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