RETIREMENT LIVING IN SCOTLAND

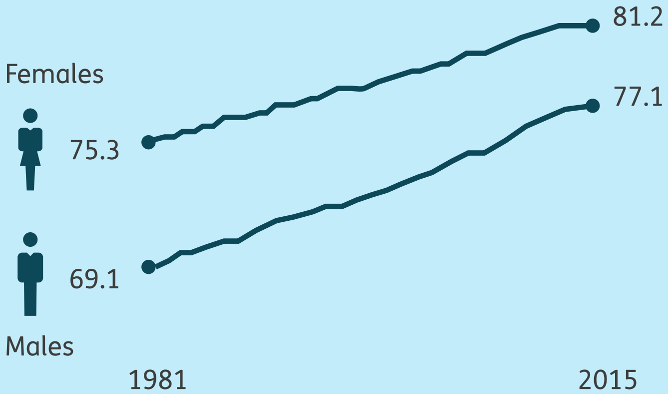
WHAT YOU NEED TO KNOW

BRODIES LLP

Retirement living in Scotland

Scotland's population of pensionable age is projected to rise from 1.05 million in 2016 to 1.32 million in 2041 according to a report from Age UK. This dramatic change in the make-up of Scotland's population presents a huge opportunity for investors and developers to service the anticipated demand for retirement housing.

Life expectancy at birth (years)



National Records of Scotland October 2017

(Source - National Records of Scotland: Life Expectancy for Scotland 2014-2016 – Key Findings).

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The housing wants and needs of those living longer is changing. Not every older person wants to move from their existing home but, for many, their existing homes are under-occupied and don't meet their current health and welfare requirements. However, this is not a case of "one size fits all". Some will be looking to downsize to a better home than their current one in terms of enhanced facilities and amenities and others will be looking to secure assisted living services for the longer term.

Whatever retirement living product they are looking for, there is currently a lack of suitable and desirable choice of accommodation.

The need for more housing options will be felt sharpest in urban locations, particularly in Scotland's main cities; Edinburgh, Glasgow and Aberdeen, as well as in well-connected towns and villages outwith the cities. In these areas, there is a real opportunity for a range of retirement living products and not just those at the top end of the market.

Retirement living in Scotland – what's different?

Retirement living in Scotland may be different from the rest of the UK but is still an attractive proposition for developers and operators looking to enter a relatively untapped market. So what is different in Scotland when it comes to structuring, buying, selling and operating retirement properties?

Structuring

A long leasehold approach is predominantly used in England and Wales, allowing operators to control use of developments by way of lease conditions and to impose a deferred management fee or event fee on assignment (transfer) of the lease interest by the occupier.

In Scotland, the preferred model for retirement operators has been to sell the freehold / ownership of individual properties to residents. This is mainly because there are restrictions on residential leases having a term exceeding 20 years and these restrictions rule out the long leasehold model. In the case of a freehold sale, operators generally retain an element of control by maintaining a presence in the development, such as a warden's flat or office, and managing the properties on behalf of the residents.

Operators in Scotland are still able to secure event fees using a freehold sale model. These can be imposed contractually on home owners by way of a title condition under a deed of conditions or a separate contractual agreement secured by way of a standard security (fixed charge) by the home owner over the freehold interest.

While freehold sale is still the preferred option in Scotland, rental may also emerge as a viable tenure alternative for retirement living operators and a more affordable proposition for occupiers. The new private residential tenancy in Scotland has the potential to be something of a 'game changer' as it offers tenants much greater security of tenure than its predecessor (the short assured tenancy). Unless the landlord can apply one of the statutory grounds to end the tenancy, the tenancy will subsist until brought to an end by the tenant, making it conceivable that a tenancy could subsist between a willing landlord and tenant for a considerable period - even beyond 20 years.

Another option for retirement operators in Scotland is shared ownership. One of the principal benefits of this type of model is the retention of control by the retirement operator. They will have a stake in the property which will give them the right to enforce title conditions. It also gives residents the comfort of knowing that the operator has a vested interest in the development to maintain it and make it attractive to future buyers and occupiers.

By **2040**, nearly 1 in 4 people in the UK will be aged 65 or over.

One in four (25 per cent) over 60s would be interested in buying a retirement property – equating to 3.5 million people across UK nationally.*

*(*source - Age UK January 2017)*

Planning

Similar to England, retirement properties do not inhabit their own use class in Scotland. Planning authorities in Scotland treat retirement living developments as residential developments, although some have been willing to adopt different approaches in dealing with issues specific to retirement homes.

The vast majority of planning authorities in Scotland will seek to restrict occupancy of retirement living developments to over 55s by entering into a Section 75 agreement (equivalent to a Section 106 agreement in England). During this process, applicants are often able to negotiate non-payment of education contributions and reduced transport contributions on the basis that the occupants, by definition, cannot be of school age and are less likely to own cars.

Planning authorities will also often identify retirement living as an area of identified housing need. In such instances, where a proposed retirement living development has been short of the requisite number of affordable housing units, authorities have been willing to accept 'off-site' affordable housing contributions in lieu of 'on-site' provision. This often makes smaller, more constrained sites more attractive to retirement living developers as such sites would be less viable to standard private residential developers.

Taxation matters

Land and Buildings Transaction Tax (LBTT)

LBTT, the Scottish equivalent of Stamp Duty Land Tax (SDLT), is charged according to progressive rate bands, with different rates and bands applying to residential and non-residential properties.

LBTT will arise at different stages in the development of a retirement scheme. It will be payable on the purchase of development sites at the non-residential rates which have a top rate band of 4.5%. It will also be payable on the purchase of a completed retirement unit at the residential rates with the top rate being 12.5%.

The purchase of six or more individual retirement dwellings in a single transaction will be treated as non-residential property and subject to the lower non-residential rates.

Multiple dwellings relief ("MDR") may also be available against bulk purchases of two or more units, further reducing the LBTT cost.

As with SDLT, there is an additional 3% LBTT payable (the additional dwelling supplement or "ADS") on the purchase of certain dwellings. However, the LBTT ADS rules can be more favourable for bulk purchases of six or more retirement units than the equivalent SDLT 3% charge.

If a retirement scheme is let to a management company, who will then sublet to the tenant occupiers, then the lease to the management company will be treated as a commercial lease and subject to LBTT. Leases to residential occupiers will not be subject to LBTT.

VAT

For developers and funders, it is essential that retirement schemes are properly structured to maximise VAT recovery on project costs.

Where VAT costs do arise, these can be recovered by making a zero-rated supply of the scheme, either by disposing of it or leasing the scheme under a long lease of not less than 20 years. There are a number of technical conditions around making a zero rated supply that need to be looked at in each instance. Zero rated supplies of retirement schemes should be carefully planned to ensure that the structuring does not give rise to an unnecessary LBTT charge and meets the ongoing commercial objectives of the parties involved.

Direct lets to retirement occupiers are exempt from VAT.

Operating

As well as planning conditions such as age limit restrictions, operators often use title conditions to maintain the status of a retirement development. These title conditions are known as core burdens.

Unlike ordinary title conditions which can generally be varied or discharged by a majority of proprietors, core burdens cannot be totally discharged by proprietors - they can only be varied by a two thirds majority of the proprietors.

This added protection applies to conditions regulating the use, maintenance, reinstatement or management of a facility or service which makes the development particularly suitable for occupation for elderly people. Importantly, the proprietors cannot change any age restriction included in the title to their home without first applying to the Lands Tribunal for Scotland.

Title conditions are sometimes coupled with management agreements to allow retirement operators to manage the properties and recover service charges and event fees.

With a well-publicised lack of suitable retirement accommodation in Scotland, the Scottish Government has acknowledged the need to address the shortage of housing for older people by opening up existing shared equity schemes to people over the age of 60. With the prospect of increased financial assistance becoming available coupled with the high number of individuals able to self-finance their choice of retirement housing from the sale of existing homes, there is a real opportunity for developers and investors to plug the gap and take advantage of the growing demand.

Driven by the ambitions of our clients

Brodies is at the forefront of advising on property transactions in Scotland. We have the experience and the expertise to advise on all aspects of a scheme from planning to site assembly, construction, funding, leasing, managing and sale, as well as tax planning.

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