Media Q&A

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Can we use our tax-free lumpsum to build a modular home in our back garden?

With back-garden modular homes set to be exempt from planning rules soon, my wife and I, who will retire soon, are considering using some of our pension tax-free lump sums to build a modular home. Not only could this serve as a granny flat into the future but we could earn tax-free income from the modular home in our retirement under the rent-a-room scheme. This would help supplement our pension income, which will be relatively modest. Is there anything we should be aware of that could affect our pensions?

It's important that you and your wife carefully plan your retirement. A key part of retirement planning is knowing how much retirement income you will have – and managing that income so that your expenses are covered and that you both enjoy as comfortable a standard of living as possible in your latter years.

While you mention that your pensions will be relatively modest, you don't mention how much of a pension tax-free lump sum you and your wife expect to receive. Under current Irish Revenue rules, you can typically take up to 25pc of your pension as a tax-free lump sum – up to a maximum of €200,000 over your lifetime. While a pension tax-free lump sum might initially seem like a large amount of money, it's important to be careful how you use it.

People often underestimate the amount of money they need to have saved up for retirement, as well as the amount they will spend at that stage of their lives. If you spend too much of your tax-free lump sum early in retirement, you could regret this in later years. So before exploring the use of your lump sum to fund the construction of a modular home, consider setting aside a certain amount of it to fund your lifestyle in retirement and to address other financial priorities - such as having adequate private health insurance, keeping enough money for nursing home care, and leaving an inheritance.

If at that stage, you feel you have enough left to fund the construction of a modular home, you could consider doing so – but wait until all the necessary legislation is in place to exempt these units from

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planning permission requirements first. While the Government plans to allow free-standing modular or cabin-style homes of up to 45 square metres to be built in back gardens without formal planning permission, these plans are in their early days. A proposal to grant planning permission exemptions for these modular homes was brought to the Cabinet last April.

The Government intends to expand the rent-a-room scheme to cover modular homes, possibly in the upcoming Budget. If modular homes are included in the rent-a-room scheme, homeowners who rent out these units will be able to earn up to €14,000 a year in tax-free rental income (assuming the current tax-free limits allowed under the rent-a-room scheme remain the same), as long as the terms and conditions of the rent-a-room scheme are met. It's important to be aware that if you earn more than €14,000 (or whatever the rent-a-room annual tax-free limit is at the time) from renting out your modular home in a calendar year, the full amount becomes taxable, not just the excess. Note too that Revenue recently confirmed that homeowners who build modular homes in their back garden will be liable to pay a separate Local Property Tax on that home.

It would be important to fully understand the costs of building a modular home, how easy or difficult it might be to secure tenants and rental income, and any obligations you might have towards those tenants. Any rental income earned from your modular home will provide ongoing financial support, which is great, but be sure to consider any ongoing expenses associated with the property - such as maintenance, insurance and tax. This will help you to determine whether that level of rental income is sufficient to support you in your retirement. There could be periods of time when your property may not be able to be rented out and this needs to be borne in mind too.

It's important not to do anything that will hamper your retirement plans or undermine your financial security and independence. So, the best place to start is to sit down with a Financial Broker who will look at all the options available to you and work with you to implement a strategy that best suits your retirement needs.

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