Gifting the family home

Inheritance tax and trusts



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Meg Saksida considers options for reducing inheritance tax

Key Points

What is the issue?

The question practitioners are often asked by the older generation, is: ‘How can I reduce my death estate with the value of my family home?’ In most estates, this and cash are the largest assets in the estate.

What does it mean to me?

Gifting the family home without moving out of the home will almost certainly invoke the reservation of benefit provisions unless the donor pays a market rent for the home. A better solution may be to give a share of the home, and genuinely share the home with the donees.

What can I take away?

With the culture of families living further and further away from each other, children and grandchildren struggling financially and desperate to get on the property ladder, rising house prices and soaring university fees, by gifting a share of the family home where two generations can live together, tax, social and emotional benefits can be had by all.

The British press has been full of headlines on inheritance tax this year, targeting in particular the baby boomer generation who have fortuitously increased their estates over their lifetime, largely as a result of the rise in value of the family home. In 1960, when this generation were starting out their adult lives, the average cost of a house in London was £2,189. In the first quarter of 2019, it was £212,614 (*source: Nationwide*).

IHT receipts totalled £5.2bn in 2017/ 18, and this came from 4.2% of estates in the UK (*source: Office for National Statistics*). The Office for National Statistics expects this to increase in the longer term, due in part, to the freezing of the nil rate band. The question practitioners are often asked by the older generation, is: ‘How can I reduce my death estate with the value of my family home?’ In most estates, this and cash are the largest assets in the estate.

Gift with reservation of benefit

The words that fall upon most practitioners' lips in response are the 'Gift with Reservation of Benefit' rules (GWROB). This is because most potential family home donors don't want to move out of their home or give away any of the benefits of owning it; they just want the value of the home out of their estates.

Usually, if a donor gives an asset away to another individual, it will be a potentially exempt transfer (PET), and as long as the donor survives seven years, it will fall out of the donor's death estate for IHT purposes. The beneficiaries of the donor's estate therefore save IHT at a maximum of 40% as a result of the gift.

The reservation of benefit anti-avoidance rules were introduced in FA 1986. They ensure that a donor must genuinely give away all the rewards and benefits of an asset if it is to be excluded from their estate. If the asset is given away but the donor continues to derive benefit from the asset, the asset will still form a part of the deceased estate at the date of death.

For capital gains tax purposes, this is not a good situation, as the gift will have been a disposal for CGT irrespective of the IHT treatment. The house will be in the IHT death estate at market value at the date of the death, but when the donee sells the home, the cost for CGT will be the value of the asset at the earlier date of the gift. In times of rising home prices, there could be quite a disparity between these two figures.

Further, if the donor releases the reservation sometime after the initial gift (say they move into a nursing home) and the home genuinely becomes gifted to the donee, there is a second 'deemed potentially exempt transfer' at this date. This second PET is not able to use any annual exemptions to reduce its value, but will not be in the estate of the donor at death.

Residence nil rate band

For deaths after 6 April 2017, the legislation went some way to prevent the need to give away the family home by the introduction of the residence nil rate band (RNRB). The RNRB is available in the death estate where a residence which had at some time been the main residence of the deceased is left to their lineal descendants, either through the will or through intestacy. For 2018/ 19 the RNRB is £125,000 per individual, rising to £150,000 in 2019/ 20. The deceased may have the benefit of a previously deceased spouse's allowance too if not used at their death,

so a maximum of £250,000 for 2018/ 19 may be available. The issue however, is of the 4.2% of estates referred to above that were liable to IHT, some 40% of these were valued at over £2m in 2015/ 16. The RNRB is abated for estates over £2m, so for nearly half of the estates due to pay IHT, the additional band will not significantly help.

Does the reservation of benefit need to be enforceable?

Can the family home ever be given away while the donor stays living in the home? In the very old case of *AG v Seccombe* [1911] 2 KB 688, it was held that in order to invoke the operation of the reservation of benefit provisions, any reservation of benefit by the donor must be enforceable. This case applied the 'ejusdem generis' interpretation rule to the phrase 'any benefit by contract or otherwise' to make the definition appear that it only refers to benefits that are enforceable by the donor. Applying this to the family home, it could follow that if the donor cannot enforce the benefit retained, the reservation is not invoked. Although there is no definitive legislation or case law to prevent this, it is unlikely that HMRC would be satisfied that any gift with reservation of benefit would only be taxable if enforceable.

However, there is hope, as the legislation includes one or two exceptions where all or part of the value of the home may be able to be given away without invoking the reservation of benefit rules.

Exceptions from the anti-avoidance legislation

Market rent

The first possibility is for the donor to pay a market rent for the property. This can be paid in money or money's worth, but it will need to be a genuine full commercial rental value and be kept up to date by appropriate market rent reviews on a regular basis. The rental contract should also be made as a proper legal obligation, and not a casual promise to pay.

There are two potential issues to contemplate when considering recommending to the donor to pay a market rent for the family home. The first, is that if the donor needs to pay a market rent for the property, the recipient (usually the child of the donor) will need to declare this income and pay income tax on the net profit made on the rental property business. The recipient may not want to receive property

income (for example, if they are using the disregarded income scheme as they are non-UK resident, or if they require a certain low level of income to be eligible to state benefits or the income may invoke the high income benefit charge). The other issue is the assimilation by the donor of the concept that they now need to pay to rent for an asset which they might consider remains ‘theirs’ despite the gift.

Gifting only a share of the land

Another possible solution is for the donor and the donee to jointly live in the family home after the disposition. The two parties would not need to live together full time but there does need to be some element of shared living, which could be limited to different sections of the dwelling, or different times.

Where the donor only gifts a share of the land, for example half of, or a floor or wing or other percentage of the family home, the reservation of benefit provisions will not apply. This is because under FA 1986 s 102B (a later amendment to the original legislation), the rules don’t apply to transfers of a share of an interest in land if both the donor and donee occupy the land together, and the donor does not receive any benefit (other than a negligible one) that is provided by the donee in some way connected to the gift.

If the parent donor and the child donee (for example) live jointly in the home after the gift then the child can’t make up for the gift by, for example, buying all the groceries or paying all the utility bills. In this case, the donor would receive a benefit from the asset he had given away and continue to be in a reservation of benefit situation. They will need to strictly split all bills fairly.

A de minimis benefit

Only having a de minimis interest in the property post gift would also allow the donor to be outside the reservation of benefit provisions; but there is no way that a donor can continue to live in the house full time and be in any way de minimis. A de minimis retention of benefit would be using the house for domestic purposes, such as a visit to the donee for babysitting or watering the plants while they were away or going to stay for short periods.

HMRC consider staying with the donees in the house is acceptable for up to three weeks of the year, but staying in the house alone would only be acceptable for up to two weeks a year. If there was no option but to move into the house post gift, such

as a situation where the parent became ill or post operation needed short term care, this would not be considered a reservation of benefit but would instead be considered under the de minimis umbrella.

Summary

Gifting the family home without moving out of the home will almost certainly invoke the reservation of benefit provisions unless the donor pays a market rent for the home. A better solution may be to give a share of the home, and genuinely share the home with the donees.

The baby boomer generation are currently holding large high value family homes which they don’t require the space in, and according to Dame Esther Rantzen DBE, founder of ChildLine and The Silver Line, are suffering from loneliness: ‘Loneliness has become an epidemic in the UK…’

With the culture of families living further and further away from each other, children and grandchildren are struggling financially and desperate to get on the property ladder, while facing rising house prices and soaring university fees. By gifting a share of the family home where two generations can live together, tax, social and emotional benefits can be had by all.