

PROTECTING YOUR SHARE OF THE FAMILY HOME



It is common for couples to make wills leaving everything they own to the survivor of them unconditionally with further provisions to take effect on the second death, such as the survivor leaving everything to their children. A consequence of this arrangement is that the spouse or Civil Partner who dies first has no control over what happens to the assets which pass to the survivor who is free to do with them whatever they wish. If the survivor later requires nursing or residential care their assets (including those inherited) are likely to be the source of funding the fees. Further, the survivor is free to change their will in any way they choose.

If you have sufficient assets, you may be able to divide them between your surviving spouse/partner and the others you wish to benefit. If that is not possible or if it would leave the survivor inadequately provided for, one way to retain some control over the ultimate destination of your assets whilst also providing for your spouse/partner, is to create a trust in your will. This brief guide focuses on Life Interest Trusts, primarily in relation to the share belonging to the first co-owner to die of a jointly-owned property. Other types of trust can be created but may not be as tax-efficient or give the same certainty of outcome.

A Life Interest Trust is a means of protecting some part of the family wealth in the event that the surviving partner moves into residential or nursing care. It can also be used when the parties have children from earlier relationships and wish to ensure that the assets brought to the current relationship are protected for the benefit of their respective children.

What is a Life Interest Trust?

A Life Interest Trust set out as part of a will only comes into effect on death. The trust, gives one beneficiary (the Life Tenant), typically the surviving partner, the right to the 'use and benefit' of an asset for the remainder of his/her lifetime or for a defined period. The trust also provides that the asset ultimately passes to another beneficiary or group of beneficiaries (called the Remainderman or Remaindermen), typically the children of the deceased, chosen by the spouse or Civil Partner who dies first.

A Life Interest Trust provides that the Life Tenant is entitled to the income from the asset(s) held within the trust and the capital value must be preserved for the Remaindermen. The income may be the interest, dividends or rent generated. Alternatively, it may be the right to live in and enjoy a property (or the deceased's share if the Life Tenant is the co-owner).

A Life Interest Trust is most commonly used to protect the family home. A home (or your share of a jointly-owned home) is left on a Life Interest Trust so that your spouse/Civil Partner can remain living there after your death and the Remaindermen will ultimately receive your share of the property.

The survivor is permitted to occupy the property rent-free on such terms as you may wish to stipulate, these usually being an obligation to pay the outgoings, maintain the property and keep it fully insured. In short, the surviving owner continues to own their share of the property and has an exclusive right of occupation in the share within the trust.

The trust can run until the survivor's death or you can stipulate that it comes to an end sooner.

What if the Life Tenant wishes to move home?

Power can be included for the property to be sold and the sale proceeds reinvested in a replacement property which would be held on the same terms. This means the Life Tenant can move home if they wish. If this results in any surplus monies (eg, due to downsizing), the trustees and the survivor have to agree on the proportions in which the replacement property will be purchased and therefore how the surplus money should be divided.

Additional flexibility can be built in to give your trustees an overriding power to distribute capital from the trust to any of the Life Tenant or Remaindermen. This may be useful if unforeseen circumstances arise or to help avoid the need for the trust to hold liquid assets.

If the trust is used as a vehicle to hold a share of the family home little needs to change upon the first death. The Life Tenant can continue to live in the property, almost as if they were the owner of the entirety. The deceased's trustees step into the shoes of the deceased owner. The trust must be registered with HMRC's Trust Registration Service.

Inheritance Tax treatment

For married couples and Civil Partners any assets (including a share in a property) passing on the death of one to the other (either outright or in trust) are exempt from IHT at that time. On the death of the Life Tenant IHT is calculated by adding the value of the estate of the Life Tenant and the value of the trust. Any IHT payable is apportioned according to value between the estate and the trust.

For unmarried couples, Life Interest Trusts are less attractive for IHT purposes. The Life Interest mechanism might still be ideal, for example if the couple ultimately wish to protect their share of their assets for their children.

However, as there is no spouse exemption, the value of the estate on the first death not covered by the £325,000 Nil Rate Band attracts IHT at 40%. The Residence NRB is not available on the first death. This may mean IHT is payable on the first death and on the second death when the Trust and the estate of the second are added together to calculate the IHT payable.

Title to your property

If you are leaving your share of a jointly owned property to a trust, it is important to check how the title is held. Only as Tenants in Common can leave a share in a property into trust by will.

Drawbacks and limitations

There are some potential drawbacks of Life Interest Trusts and it is important to be comfortable with these if you decide to proceed.

- Trusts inevitably come with some additional administration.
- The Life Tenant may feel that they have less freedom.
- If the trust holds a share in a jointly-owned property, the survivor will not be able to take an Equity Release loan against his/her own share in that property.
- The trustees owe a duty to the Remaindermen to ensure the capital of the trust is protected.
- Problems may arise if the Life Tenant refuses to maintain the property to a reasonable standard.
- Trustees may be reluctant to invest the proceeds of sale in a replacement property a long distance away.
- If the trust only holds a property (or a share in a property), there will be no liquid funds available to cover any administrative costs which may arise.
- Life Interest trusts may not be tax efficient for unmarried couples.



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