

PRIVATE CLIENT DEPARTMENT

DECLARATION OF TRUST FACT SHEET

Dean Wilson LLP Solicitors

Ridgeland House, 165 Dyke Road, Brighton, BN3 1TL **01273 249 200**

1. Introduction

The object of this document is to help you understand what Declarations of Trust are, what effect they have and how they may apply to you.

A Declaration of Trust is a document which generally applies to co-owned properties and records how the property was funded, who is responsible for the ongoing liabilities and how sale and other situations may be addressed.

Under English law, those holding legal title of property (the name of the owner on the registration documents) may not be the same as the people holding the beneficial (the financial) interest. This often occurs when two people buy a property together and contribute unequal shares towards the deposit or pay different amounts off of the mortgage.

Where this happens, owners generally want to ensure that their share of the property reflects their contributions.

Whilst the legal title controls whose name is on the registration documents (frequently called the Deeds), most people are interested in who actually owns the property and it is the beneficial interests which are more relevant to co-owners.

2. Co-ownership of property

There are two mechanisms for the co-ownership of property:

- Joint tenancy (as beneficial Joint Tenants) – where the owners together own the entire property in equal shares. Here, if one owner dies their share passes to the other(s) automatically, irrespective of the provisions in the deceased's Will (survivorship).
- Tenancy in Common (as beneficial tenants in common) – where each owner holds a separable right or interest in the property.

The legal title to property is always held as Joint Tenants, which is generally of little interest to owners of property and is usually only relevant for the lawyers.

The beneficial interest in the property matters more to co-owners. For the purposes of this fact sheet in connection with Declarations of Trust, we only consider ownership as Tenants in Common

3. Tenancy in Common

Where joint owners of property hold the beneficial interest as tenants in common, in the absence of a specific declaration, they will be deemed to hold the property in equal shares.

A Declaration of Trust is a form of specific agreement which determines, potentially in addition to other matters, how the shares of property are to be held. This applies in several situations and not only controls how the capital from the property may be shared but also dictates how the income is to be distributed. In particular, where property is owned jointly and there is rental income, it may be necessary to provide HMRC (Her Majesty's Revenue and Customs) with evidence of the ownership when apportioning income between co-owners.

Historically, it was most common to specify a percentage ownership for co-owners but very frequently, more complex mechanisms are required to ensure the position is fair.

Some specific examples follow

4. Partners buying property with deposit from parents

This is a fairly common situation in today's property market. Often one set of parents is providing the deposit, by loan or by gift, to their child for them and their partner to buy a property.

In this situation, parents normally want to ensure that the deposit is protected against unexpected issues; such as a breakdown in the relationship. Sometimes, where the deposit is a loan rather than a gift, the parents will want to own a share of the property themselves or hold a charge for the value of the loan.

Most commonly, where the deposit is a gift, we advise on the Inheritance Tax consequences that may arise (as the gift from parents becomes a Potentially Exempt Transfer) and can prepare Deeds of Gift to avoid any future arguments over the payment being a loan rather than a gift.

We suggest that the Declaration of Trust would be expressed to return the deposit (either as a fixed sum or as a proportion of the sale price of the property) to the co-owner who provided it and thereafter everything is split in accordance with the proportion of intended mortgage repayments. We also address the situation where the property value falls or increases and suggest the relative risks to the parties.

A simple percentage split between co-owners may not cover the situation where the property is sold before the mortgage is repaid which could leave one partner receiving a large proportion of the deposit from the other partner's parents – typically this is not intended.

5. One party paying the deposit and the other paying the mortgage

This is a common situation with subsequent families/relationships, perhaps where one party has come to the purchase with a significant deposit but less income with the other offering income but little capital.

Here, a simple percentage split might be equitable once the mortgage has been fully paid but we also advise on the position before-hand. Where there is a joint mortgage, but an agreement between the purchasers for it to be paid by one person, there is a risk to the other. Mortgagors (the purchasers) are almost universally 'jointly and severally' liable. An agreement between parties for only one person to pay is not binding against the mortgage company and it is important that each is advised on their relative risks.

Generally, it is the person providing the capital who is at the greatest risk of losing money in such a transaction but proper advice and careful planning can help to minimise the risks.

6. Buy to Let properties

With let properties, especially when the rental income is to be split unequally, it may be necessary to provide a Declaration of Trust to satisfy HMRC as to the income tax position.

There may be Inheritance Tax consequences of this where the purchase price is provided by parties in unequal proportion to their holding and we would advise on the position here. This can be efficient for Income Tax by ensuring all the income is received by the party with the lowest income tax rates, but cause an Inheritance Tax liability if one owner dies within 7 years of the transfer.

7. Position on sale

Whilst selling a property together should be the same as buying it together, we have to consider the situation where a relationship has broken down between purchase and sale. A Declaration of Trust can specify exactly what mechanism the parties should use under those circumstances in order to sell the property either on the open market or for one owner to purchase the other share(s).

By having a suitable declaration in place, it can considerably reduce any arguments over how the property is sold and reduce the likelihood of someone applying to the Court – this not only speeds the process up but also reduces the risk of expensive litigation at what is, often, a stressful time.

8. Cohabitation/Marriage/civil partnership and Inheritance Act claims

A Declaration of Trust dictates the beneficial co-ownership of property and this can apply between any co-owners. However, marriage, civil partnership and claims under the Inheritance (Provision for Family and Dependants) Act can enable the Court to make Orders which override any previous agreement relating to property ownership. There is draft legislation intended to provide cohabiting partners with similar rights to divorcing couples and albeit not current legislation, co-owners may wish to consider the potential impact on their shares of property.

In financial settlement proceedings, a Court can Order the transfer of assets between the former spouses. A Declaration of Trust may serve as a useful indication of how the parties wish for the property to be held, and this may be of more use following a short marriage/civil partnership, but if it is intended that the property ownership should stand a greater chance of binding spouses in a subsequent separation then separate matrimonial advice is warranted. Our family department can advise on pre-nuptial agreements and post-nuptial agreements which are now being given increasing weight by the Courts.

Similarly, if co-owners wish to have their non-financial contributions recorded in respect of their co-ownership of property, a Living Together agreement might be beneficial. Again, our family department may discuss this with you and advise appropriately.

On death, it is possible for certain classes of people to make a claim on the deceased's estate if they have not been left with sufficient provision. These are usually spouses and children but anyone who has been financially supported by the deceased prior to death may

be able to make a claim. This can mean that co-owners, particularly where the deceased owner has been paying all the outgoings, may make a claim against each other's estates if they have not been adequately provided for.

Whilst such claims will not necessarily be successful, if they are, the Court can reappportion assets in contradiction of a Will. Where this is a possibility we can advise on how the risk of this might be reduced.

9. Your Will

Where property is held as tenants in common, each party's share passes by their Will after death. Where there is no Will, the Intestacy rules will apply and control how assets are passed – please see our separate Will Facts Sheet.

For this reason, we always recommend that clients consider their Will provisions on any change in property ownership – it may be that Inheritance Tax planning is appropriate or that Wills should be re-drafted to reflect changes in capital assets.

In particular, there is no automatic provision for the benefit of unmarried partners and it may often be appropriate for some form of lifetime interest trust to be created such that the survivor has use of the property for their lifetime.

10. In conjunction with purchase

Given the specialised nature of Declarations of Trust and their close association with Wills and Tax matters, these are undertaken by our Private Client Department.

Whilst these are undertaken separately to any property transaction, we work closely with the Residential Conveyancing department in order to ensure that documents are prepared together with any purchase and registered at the same time.

We can act for purchasers who provide instruction jointly and are in agreement but purchasers are always advised to seek their own independent legal advice on any declaration of trust to satisfy themselves as to its particular effect on them.