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BANK OF MUM AND DAD
A LEGAL GUIDE

BANK OF MUM AND DAD A LEGAL GUIDE

*A simple guide to the legalities
of your financial support*

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OUR EXPERIENCE, CONFIRMED BY THE RESEARCH WE CARRIED OUT WITH THE LONDON SCHOOL OF ECONOMICS, HAS SHOWN JUST HOW COMMON IT IS FOR YOUNG PEOPLE, AND PARTICULARLY FIRST TIME BUYERS, TO RECEIVE A FINANCIAL LEG UP FROM PARENTS OR OTHER FAMILY MEMBERS TO HELP WITH A HOUSE PURCHASE.

With the need to provide constantly increasing deposits, the Bank of Mum and Dad is busier than ever, and now the UK's sixth largest lender. Helping family onto the property ladder can be a legal minefield and protecting family assets in the face of unexpected life events is incredibly important. But what are the legal ramifications of your help?

We don't have all the answers so turned to our partner and specialists in Property Law, **Wellers Hedleys**, to provide some useful guidance.



Richard Cunningham,
experienced solicitor and Head of Surrey Operations for Wellers Hedleys.

I've lost count of the number of times someone has contacted me to discuss their property and used the word "straightforward" to describe it. In reality, it is rarely the case that property matters are without complications but it can be easy to miss the subtle details which transform a "straightforward" transaction into something a little more challenging.

With the younger generations still struggling to keep up with the pace of increasing property prices in the face of low interest rates and stagnant wages, it is still common practice for buyers to receive financial assistance from loved ones to help them with their move. The question will then arise as to how the benefactor's interest is protected if the

assistance being provided is not to be treated as a gift or, in the case of assistance being given to a couple, to be treated as a gift only to one of them.

It never ceases to amaze me how a simple idea becomes increasingly complicated and clients can quickly become entangled in a web of unforeseen consequences. In the same way, missing an important detail can cause loss, stress and upheaval in future which could easily have been avoided with a bit more knowledge of the legal implications.

To help you navigate your way through the legalities, we've outlined what you may want to consider when helping your child financially.

WAYS TO PROVIDE FINANCIAL ASSISTANCE



A GIFT

This is the most common way that parents tend to help their children towards a deposit or other costs, and by far the simplest in terms of legalities.

Gifts can be made formally or informally but, given the size of the sums likely to be involved and the fact that such arrangements could be scrutinised by HMRC or other third parties in the future, it is always best to document gifts and to keep such paperwork in a safe place or with your solicitor.

Possibly one of the greatest concerns for those gifting capital is who might end up with money in the future and there are a number of mechanisms including preparing a **Living Together Agreement** (see page 7) or a prenuptial agreement and having a valid up to date Will that could be used to help ensure it stays in the hands of the intended beneficiary.



A LOAN

If you plan to give a loan, you'll need to make sure that everyone is on the same page when it comes to paying back the money and consider how the funds will be protected.

– Loan agreement

Even within a family, or possibly especially within a family, it is wise to ensure that the terms of a loan are clear. From the outset it's important that all parties understand that the loan is not a gift, even if it might become one at a later date. The terms of the loan can be set out in a Loan Agreement. This would cover aspects including the length of time before the loan is meant to be repaid, a specified repayment date, the amount of any repayments, what would happen in the event of a default and any other terms agreed between the parties.

– Declaration of Trust

Where your contribution will be used to fund a joint purchase, are both purchasers contributing equally to the cost of the purchase and the running costs of the property? If not, you should consider a Declaration of Trust - a legally binding document which records the financial arrangements between joint owners of a property and anyone else who may have a financial interest in the property. This will help to protect any unequal shares, document who will be responsible for the monthly expenses and to record how much each party would receive should the property be sold in the event of the relationship failing.

We agreed it was a loan but didn't put anything in writing.

– **Charge against property**

Registering a charge against the property turns an unsecured loan into a secured loan and will mean that, in the worst case scenario, a sale of the property can be forced in order to repay the debt. Often such an agreement will require the property owner's mortgage lender's consent.

CASE STUDY:

WE AGREED IT WAS A LOAN BUT DIDN'T PUT ANYTHING IN WRITING

1. Tom is buying a property and is getting some money from his mum to help fund this.
2. Tom and his mum are required by his mortgage lender to document that the money being provided by Tom's mum is a gift.
3. Tom and his mum view the requirement of his mortgage lender as a formality but agree between themselves that Tom's mum is providing a loan. However, they don't make a formal Loan Agreement and Tom agrees to pay back the money as and when he can.
4. Tom defaults on his mortgage and the mortgage lender takes possession of the property.
5. The property is sold by Tom's mortgage lender and as there was no formal agreement made regarding the loan, his mum is not entitled to any repayment whatsoever.
6. To make a bad situation worse, Tom's mum dies within seven years of him purchasing the property and Inheritance Tax must now be paid on the money she 'gifted' to him. On a sum of £50,000, tax of up to £20,000 could be payable.

WAYS TO PROVIDE FINANCIAL SUPPORT



JOINT OWNERSHIP

Another way to help your child onto the property ladder is through joint ownership. If going down this route you may want to consider the tax implications of Stamp Duty and Capital Gains.

- **Stamp Duty Land Tax (SDLT)**

Registering as a co-owner of a property can be a good solution but there can be serious tax implications, which are now exacerbated by the higher rate of SDLT that applies to those who are named owners of more than one property. Avoiding this can be tricky as even if you rearrange the ownership of your existing assets, as SDLT will take into account property registered in the name of any spouse or civil partner, as well as that registered in your name.

Even setting up a trust arrangement, whereby the property is held by the named owners, but an interest is reserved in favour of the benefactor, is not a clear cut solution and HMRC will look beyond the legal ownership when making its assessment. Some suggest registering a charge against a property in the same way that any mortgage loan would be secured, but if the property is already subject to a mortgage this would require that lender's consent and there

is also the question of how to record the agreed terms; when will repayment be made? Will it be by instalment or single lump sum? Will interest be charged? What happens if something goes wrong?

- **Capital Gains Tax (CGT)**

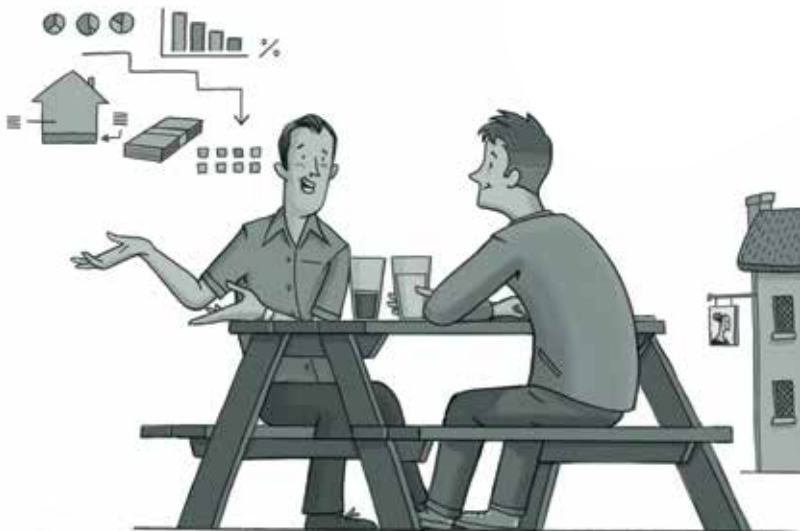
If you're directly involved in purchasing a property with your child and you already have your own home, it will be construed as an investment on your part. As such it will be subject to tax when it is sold. The rate of CGT for residential property is currently 18% if your overall annual income is below £50,000 and 28% if your overall annual income is above the £50,000 threshold. The annual allowance for capital gains is £12,000 for an individual or £6,000 for a trust during the 2019/20 tax year. Married couples can combine their allowances for jointly owned assets.

As a part owner of a second property you'll pay the proportion of the growth in value between buying and selling, attributable to your share of the property. However estate agent fees, legal fees and SDLT are considered allowable costs that can be deducted from the exposure to CGT.

CASE STUDY:

WE DIDN'T REALISE THE IMPLICATIONS ON SDLT

1. Mr and Mrs Hall wish to help their daughter purchase her first home.
2. Their daughter intends to purchase a property with her partner.
3. Mr and Mrs Hall are wary of their daughter's partner so wish to be named as joint owners of the property as they believe this will ensure it cannot be sold or re-mortgaged without their consent.
4. As Mr and Mrs Hall own their own property, their daughter will now have to pay SDLT at the higher rate. On a purchase of £250,000 an additional £7,500 of tax would be payable.
5. Despite the arrangement, Mr and Mrs Hall's daughter and her partner are both legal owners and are able to sell or remortgage the property without Mr and Mrs Hall's consent. This is because two or more property owners can deal with the property without the consent of any other named owners.



STAMP DUTY LAND TAX



STAMP DUTY LAND TAX (SDLT) AND THE BANK OF MUM AND DAD

In recent years the Government has introduced a higher rate of SDLT to property sales where the buyer already owns a property.

How could the higher rates affect you?
If you're helping your child onto the property ladder, this may have a big impact on the amount of SDLT charged. If, at the end of the day on which the purchase is completed, any of the purchasers will own more than one property, the higher rates will apply.

The Government has gone to great lengths to ensure that the new SDLT rules cannot be circumvented easily. Firstly, the rules specify that if the property is being purchased jointly by more than one individual, the higher rates will apply if any one of the purchasers would be subject

to the higher rates in their own right. Secondly, if any spouse or civil partner of any one of the purchasers would be subject to the higher rates then higher rates will apply, even if that spouse or civil partner is not named as a purchaser.

What are the “higher rates”?
When buying a property, SDLT rates apply to the amount of the purchase property price that falls within each band, rather than applying a flat rate to the entire purchase price. So, for example, on a property worth £300,000 the tax calculation would be:

£125,000 at 0%
£125,000 at 2%
£50,000 at 5%
Total tax = £5,000

However, if the property is being bought by anyone who already owns a home, the higher rates will apply. This will add an additional amount of tax equal to 3% of the total purchase price. Whereas the standard rate of SDLT is nil on the first £125,000 of the purchase price, there is no such “nil rate band” for the higher rates.

STAMP DUTY LAND TAX BANDS

STANDARD RATES

Purchase Price	Standard Rates
Up to £125,000	0%
£125,001 - £250,000	2%
£250,001 - £925,000	5%
£925,001 - £1.5m	10%
over £1.5m	12%



HIGHER RATES

Purchase Price	Higher Rates*
Up to £125,000	3%
£125,001 - £250,000	5%
£250,001 - £925,000	8%
£925,001 - £1.5m	13%
over £1.5m	15%



* Higher rates (from April 2016)

With the higher tax rate applying on a property worth £300,000 the tax calculation would be:

£125,000 at 3%

£125,000 at 5%

£50,000 at 8%

Total tax = £14,000

Quite an increase!

Are there exemptions if the property being purchased will replace a main residence?

Thankfully, yes! There is an exemption to allow for the scenario in which the owner of more than one property is selling their main residence and buying a property to replace it. Where the sale and purchase complete simultaneously, the higher rates will not apply. However, should the transactions not complete on the same day, there is a time limit of three years in which both transactions must complete if the exemption is to apply. If the purchase completes before the sale, the higher rates will apply but the purchaser can recover the additional tax paid on the completion of the sale, provided this takes place within the time limit.

There is also an exemption if the purchaser will own more than two properties but only due to the fact that they have inherited an interest of less than 50% in another property. In this case the higher rates will not apply.

PARTNERS, FRIENDS AND TENANTS



Are you helping your child to purchase a home together with a friend or partner, or will they rent a room to a tenant? What else do you need to consider?

– Living Together Agreement

If you're helping a child who's unmarried but buying with a partner, they should consider a cohabitation agreement otherwise known as a Living Together Agreement (LTA). This can be necessary whether you're gifting, loaning or acting as a guarantor and is the perfect opportunity for you all to discuss and record any third-party contribution made towards the purchase of the property and how it will be dealt with in the event of a breakdown in the relationship.

– Tenancy Agreement

If your child intends to allow another person (e.g. a partner or friend) to live at the property, a Tenancy Agreement can be a good idea. They may also want to consider a LTA to set out the responsibilities and rights of each party. This will make it clear who owns what (not just the house) and also sets the expectations for meeting the costs of living and, importantly, what would happen if the relationship were to end.

PARTNERS, FRIENDS AND TENANTS



It's always wise to give thought to how any relationship may evolve in the future. Does the agreement anticipate marriage, separation and even remarriage? Does it provide for the arrival of children? If not, it might well need revisiting. Following a divorce, should one of the parties decide to remarry, any agreement may cease to be binding and so one should consider the need for a pre-nuptial or post-nuptial agreement to deal with such eventualities.

CASE STUDY:

WE DIDN'T THINK A TENANCY AGREEMENT WAS NECESSARY

1. Mr and Mrs Lloyd are helping their daughter purchase a property. Their daughter's partner will be living there but won't be named as an owner of the property.
2. No documentation is drawn-up to formalise the arrangements.
3. Mr and Mrs Lloyd's daughter later decides to separate from her partner but he refuses to leave the property.
4. As no Tenancy Agreement was prepared at the outset, the property cannot now be sold without the partner's co-operation. The partner is able to hold Mr and Mrs Lloyd and their daughter to ransom as they cannot sell the property while he remains there.

WHAT ABOUT A WILL?

However you decide to help, it's highly likely that both you and your offspring will need to update your Will. It's always worth considering the implications on your estate when buying and selling property or assisting someone else to do so. If the sum being provided constitutes an early inheritance does this need to be taken into account in the Will to ensure fairness in respect of any other children?

Please be aware that none of the information provided should be taken as legal advice. Each situation needs to be examined by a legal professional in detail to determine the best legal advice before proceeding.

WE'RE HERE TO HELP

We're sure you'll agree there's a lot to consider when helping a child onto the property ladder. Along with our partners, **Wellers Hedleys**, we're here to help. If you'd like to find out more why not give us a call on **03300 244595**.

FURTHER READING

Earlier this year, and in conjunction with the London School of Economics, we published our report, '**The Bank of Mum and Dad: how it really works**'. This report reveals the results of an extensive academic study into how families approach parental help when buying a property.

We also produced a guide '**How to run the Bank of Mum and Dad**', which outlines some of the key issues that parents and adult children need to consider when it comes to providing or receiving family financial help, and '**A Conversation Guide**' to help family members through those difficult discussions when it comes to financial support.



The guides and report can be downloaded from our website:
familybuildingsociety.co.uk/bomad

OTHER HELP

FAMILY BUILDING SOCIETY

The Bank of Mum and Dad: how it really works
familybuildingsociety.co.uk/bomad

Generational Divide
familybuildingsociety.co.uk/generational-divide

Family Mortgage
familybuildingsociety.co.uk/Family-Mortgage

ADVICE AND CHARITIES

Citizens Advice citizensadvice.org.uk

The Money Advice Service moneyadviceservice.org.uk

National Debtline nationaldebtline.org

BROKERS AND INDEPENDENT FINANCIAL ADVISERS

British Insurance Brokers' Association biba.org.uk

Unbiased.co.uk unbiased.co.uk

Vouchedfor.co.uk vouchedfor.co.uk

FINANCE

Financial Ombudsman Service financial-ombudsman.org.uk

Moneyfacts moneyfacts.co.uk

PROPERTY

Association of Residential Letting Agents arla.co.uk

Deposit Protection Scheme depositprotection.com

Help to Buy helptobuy.org.uk

The Letting Protection Service Northern Ireland
lettingprotectionni.com

The Letting Protection Service Scotland
lettingprotectionscotland.com

National Association of Estate Agents naea.co.uk

National Approved Letting Scheme (NALS)
nalscheme.co.uk

New-homes new-homes.co.uk

Ombudsman Services ombudsman-services.org

Onthemarket onthemarket.com

The Property Ombudsman tpos.co.uk
reallymoving.com reallymoving.com

Rightmove rightmove.co.uk

Royal Institution of Chartered Surveyors rics.org

Self Build Portal selfbuildportal.org.uk

Shelter shelter.org.uk

UK Association of Letting Agents ukala.org.uk

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FOR MORE INFORMATION CONTACT OUR
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