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Inheritance tax and trusts | Personal tax

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Lynne Thompson explains the tax and benefit considerations of transferring the family home to qualify for means-tested local authority funding

Key Points

What is the issue?

Many people are looking to transfer assets in order to qualify for means-tested local authority funding

What does it mean for me?

Tax advisers may be asked about this and need to explain why it may not work and the tax implications of the exercise

What can I take away?

Be aware of the deprivation of assets rule and have a general idea about state benefit entitlement for elderly and vulnerable clients

As care home fees rise, it is natural that people want to prevent their assets, usually their home, being used to pay for long-term care. People about to enter this new phase of their life may need to seek the services of a tax adviser to find out how to avoid selling up.

One strategy is to transfer the property to their children, which can be risky, the most obvious being relationship breakdown.

It is also possible that the children may themselves need to claim means-tested benefits or become bankrupt, or they may divorce and the house would be taken into consideration when splitting assets.

Tax implications

The transfer is a gift with reservation of benefit for inheritance tax. This is unlikely to be an issue because the intention was not inheritance tax planning.

However, capital gains tax could be an issue. Principal private residence (PPR) relief would cover the first transfer. But on subsequent sale the gain is not covered by the PPR exemption.
These issues can be avoided by using a trust where no person has absolute entitlement to the property but family members and the parent are included in the class of beneficiaries. The parent could even be a trustee. This gets around the issue of family rifts and any financial problems of the children and, as long as a beneficiary of the trust occupies the property, PPR relief continues to be available (see *Sansom v Peay* [1976] 1 WLR 1073). The biggest problem with these transactions is that the exercise could be pointless.

A local authority that arranges residential care for a service user is required to carry out a financial assessment using the National Assistance (Assessment of Resources) Regulations 1992. Reg 25 states: ‘A resident may be treated as possessing actual capital of which he has deprived himself for the purpose of decreasing the amount that he may be liable to pay for his accommodation.’

What counts as deprivation?

The following examples of deprivation are given in the Department of Health’s *Charging for Residential Accommodation Guide* (CRAG), used by local authorities:

- a lump sum payment has been made to someone else (for example, as a gift);
- substantial expenditure has been incurred (for example, an expensive holiday);
- the title deeds of a property have been transferred to someone else;
- money has been put into a trust which cannot be revoked;

- money has been converted into another form which would fall to be disregarded (such as personal possessions);
- capital has been reduced by living extravagantly; and
- capital has been used to purchase an investment bond with life insurance.

The intention is important in each of these cases.

How does the local authority decide and how far can it go back?

It is the responsibility of the local authority to prove deprivation of assets, which tends to turn on the timing of the disposal. The longer the period between the disposal and entering accommodation, the less likely it is that avoiding charge was the motive.

One urban myth is that, after six months, the local authority runs out of time to prove deliberate deprivation. This is incorrect; there is no limit. The local authority must simply prove that deprivation was the key motive for the transfer.

Liability of the recipient for the fees

If the transfer was within six months of the resident permanently entering the care home, the Health and Social Security Act 1983 s 21 allows the local authority to transfer some of the liability for the care home fees to the recipient.

Outside this period, the local authority can still treat the resident as still owning the capital, but cannot hold the recipient as liable.

The key to the whole exercise is intention. So if a tax adviser is asked about this it is vital to understand both the anti-avoidance provisions and the tax implications. The adviser must also be aware that, if a client is clear in their reasons for seeking to transfer assets, any advice may be used as evidence of their intentions. In *London Borough of Brent v Kane and Others* [2014] EWHC 4564 (Ch) the local authority provided residential care for both parents. The property had previously been transferred to both sons. The local authority sought to recover the sums it maintained it was owed and disclosure of the files of the firm that acted for the family. The longstanding exception to the rule that legal advice is privileged is where it has been obtained for an iniquitous purpose. The local authority obtained the files and the outcome of the recovery proceedings is due soon.

Although a tax adviser's engagement letter would be for tax advice, it is common to discuss other financial matters at meetings with their business clients. So it is not surprising that private client tax advisers are being asked about care home planning and other financial issues concerning older and vulnerable clients.

It is helpful therefore for a private client tax adviser to familiarise themselves with these and other financial issues relevant to older clients, in particular state benefit entitlement.

PPR relief changes

Bernard Critchley discussed ('On the move', *Tax Adviser*, September 2014) changes in FA 2014 that reduced the final period of deemed occupation of a property from 36 to 18 months. An exception from this was long-term residents in a care home. So those who fund their care from renting their own property will retain the original 36 months of deemed occupation.

There was also an exception for disabled people.

The definition of disabled in FA 2005 Sch 1A includes a person in receipt of:

- attendance allowance;
- disability living allowance by virtue of entitlement to the care component at the higher or middle rate; and
- personal independence payments by virtue of the daily living component.

Someone in sheltered accommodation or moving in with relatives therefore remains entitled to the final 36 months of deemed occupation if they qualify as disabled.

This definition also applies for trusts for vulnerable beneficiaries. So knowledge of benefit entitlement in both of these circumstances is useful. However, the three benefits cover the same thing. All that differs is who can claim.

Attendance allowance (AA) is claimed by individuals over 65.

Disability living allowance (DLA) was previously claimed by people under 65 and most claimants will keep their DLA. Only those aged 16 or under will now claim DLA.

Personal independence payments (PIPs) are claimed by people aged 17–64.

These benefits are available to individuals needing help or supervision with their personal care or need. They need not be receiving the help or supervision, but they must need it.

Personal care includes:

- preparing or eating food;
- washing, bathing and using the toilet;
- dressing and undressing;
- reading and communicating;
- managing medicines or treatments;
- making decisions about money; and
- engaging with other people.

A person requires help if it takes them substantially longer to perform an activity than it would for someone without a disability. Someone may need supervision if they require another person, such as a warden in sheltered accommodation, to check on them several times a day. They may need help to get up if they fall or may need someone to remind them to eat or manage their medication.

If a person has changed their living arrangement – perhaps they have moved in with relatives or into warden-assisted accommodation – it would suggest that they cannot manage independently and need help or supervision. In this case, they may be able to claim one of the three benefits. These benefits continue to be payable if a person is self-funding in residential care. However, if care is paid by the local authority the benefits cease.

Carer’s allowance

When an award is made of AA, DLA at the middle or upper rate, or PIPs at the standard or enhanced rate, anyone caring for that person can claim carer’s allowance as long as they are not receiving some other benefits, are in full-time education or earning, after certain deductions, over £100 a week. Salary and self-employed profits count as earnings, but dividends do not.

There is nothing in the legislation to prevent someone who is claiming carer's allowance being paid by the service user; neither is there anything in the regulations to prevent the allowance being paid to relatives. So someone who uses their DLA, AA or PIPs to pay for help could ask the carer to claim an allowance too. Surprisingly, there is nothing in the legislation to prevent the allowance being paid to care home employees, as long as they meet the criteria. So tax advisers with clients that are care homes could offer valuable advice. Claire Johnson explained ('A question of capacity', *Tax Adviser*, November 2014) what needs to be done if a client loses capacity and the tax adviser's role if they accept the role of attorney.

The Court of Protection will expect an attorney or deputy to claim all benefits to which a person is entitled. So it is important when accepting that role to be aware of state benefits entitlement. A professional attorney is expected to show a higher level of knowledge than a lay person.

Correct identification of benefits for older and vulnerable clients can also mean that, if a tax adviser is asked to comment on or help with the transfer of assets into the name of a relative or into a trust, they can not only give advice on the regulations governing deprivation of assets but can also offer an alternative way to finance residential care.