

chapman tripp

**Estate and Taxation
Planning Council -
Helping the kids into
houses**

Jarrold Walker, September 2021



Overview

- Setting the scene – relationship property considerations
 - Basic arrangement – gift and/or loan
 - Relevance of section 21 agreement
 - Trust overlay:
 - Place of parents’ trust
 - Use of “child” trust
 - Joint trust of borrower couple
 - Section 21 agreements and “trust busting”
 - Future possible trend – continued ownership in “parent” trust
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Relationship property issues

- PRA section 8:
 - Relationship property includes the family home whenever acquired
 - Includes all property owned immediately before the relationship, if acquired in contemplation of the relationship and for common use
 - Doesn't help that funded by way of gift, bequest or trust distribution:
 - PRA section 10 otherwise protects gifts, bequests or trust distributions
 - But not where then intermingled with relationship property (with consent)
 - And special character of family home as relationship property expressly confirmed in any event (section 10(4)) - unless the subject of a section 21 agreement
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Relationship property issues

- Setting up a trust immediately prior doesn't help (much):
 - Section 182 Family Proceedings Act
 - Potentially applies if the trust is a prenuptial settlement "made on the parties"
 - Constructive trust analysis could get claimant to same point:
 - *Lankow v Rose*, 1995
 - Four considerations:
 - Contributions, direct or indirect, to the property in question
 - Expectation of an interest therein
 - Expectation was a reasonable one
 - Trustees should reasonably expect to yield an interest
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Relationship property issues

- Section 44 / section 44C of the PRA might also apply:
 - transfer of property made in order to defeat claim or rights of person under the PRA; or
 - since the relationship began, disposal of property to a trust which has the effect of defeating a claim
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Basic arrangement

- Loan from **parents to their child**
 - Problematic if couple don't have a section 21 agreement:
 - a section 21 agreement can protect the proceeds of the loan (or gift):
 - treat it as separate property to be repaid in event of split
 - can outline detailed repayment schedule or refinancing obligation in event of split if sale of property not the obvious consequences
 - can in theory also provide for an "equity" share of the appreciation to be returned to the parent lenders
 - often in practice the loan might match the equity contribution from the other party:
 - sometimes also funded by loan from other party's parents
 - i.e. the section 21 agreed treatment is logical and fair – debt and equity both treated the same
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Basic arrangement

- Without the section 21 agreement though:
 - the parents' loan – reflected in equity in the house - is at risk of spousal claim in split
 - hard to avoid that outcome:
 - consider where party didn't contribute anything
 - hard to say that section 13 standard be met – needs “extraordinary circumstances” making equal sharing “repugnant to justice”
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Basic arrangement

- Therefore, loan from **parents to the couple** arguably better if no section 21 agreement:
 - Both parties on the hook for the debt
 - Easier to take security (although this is not common especially if bank funding)
 - But - capital appreciation in house not protected (see over):
 - parents usually philosophical about that
 - especially if contribution of families, or party / family combination, is equal (e.g. loan from one set of parents matching equity contribution from other party) – kids are getting the appreciation anyway, equally
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Basic arrangement

- Note – what about on death of a party?
 - Often not given a lot of thought given ages of the parties, but needs some consideration
 - Consider joint tenancy v tenants in common:
 - young couple with equal contribution may prefer tenants in common structure
 - consider repayment obligations in either situation in respect of parents' loan – section 21 gives greater scope for providing for this (regardless of ownership structure adopted)
 - Consider also unwind scenarios if ownership in a trust (see following) and debt from trustees to parents of deceased party
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Trust overlay

- Similar issues apply if the young couple have **a joint trust** (i.e. which buys the property)
 - Loan to the joint trust preferable (including if security required, albeit problematic if existing bank funding)
 - Other structures are possible:
 - gift or loan to child (proceeds should be separate property at that point)
 - proceeds then loaned to the joint trust
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Trust overlay

- What about where child has **an existing trust**?
 - Reasonably common - “bloodline” trusts set up for individual children while still young, assets devolved into each of these “sibling” or “child” trusts over time, as distributions flow from family business (e.g. grandparent’s business)
 - Loan (or gift) might be directed through this trust and then on-loaned to the couple
 - Consider status of that trust for relationship property purposes / section 182 purposes / developing constructive trust issues
 - Answer will depend on facts:
 - how long has the trust been in existence?
 - what has it been used for and what access has other party had to the assets in the trust, directly or indirectly?
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Trust overlay

- Generally:
 - if existing “bloodline” trust has good governance, and is not used as routine “bank” for the young couple or their joint trust, should be remote from challenge;
 - but risky - consider contribution of other party to assets in the trust, or if child of family works for business in the trust (problematic) – potential route to challenge
 - Not ideal to acquire joint home in that trust
 - use it as a conduit for financing / gifting if wanted
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Relationship property reform

- Law Commission report June 2019:
 - Thorough review and overhaul, recommended new Act
 - Reforms relevant to status of family home relevant to “Bank of M&D” arrangements – but query whether substantial change?
 - Key relevant recommendations
 - pre-acquired family home may stay separate property
 - but appreciation in value will still be joint property (presumption of equal contribution)
 - if house acquired for common use / in contemplation of relationship - still joint property (all of it)
 - if house acquired during relationship – still joint property (ditto, all of it)
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Relationship property reform

- So – any real change?
 - Not really, for young couples
 - Yes, for young person getting help on property ladder from parents – house safer from future claim as relationship property
 - But not really a change for young couples buying a home together with assistance from parents (or young person doing so in contemplation of relationship)
 - Section 21 agreement will still be needed
 - Note:
 - not surprisingly, if relationship property used to pay down debt to one party's parents, other party will be entitled to compensation
 - No roll-over relief – if house is separate property at time of commencement of relationship, but the parties subsequently sell it to upgrade when in a relationship, it *all* becomes joint property
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Continued family ownership?

- Possible future trend:
 - Are houses becoming so expensive that it is almost illusory to “loan” the value to the young couple?
 - Parents have invested / planned for future by buying children “investment” houses when they were younger
 - Advanced estate planning, in effect, by providing the houses to the children
 - If so, what is the best structure - why transfer the house at all?
 - new trust raises section 182 issues
 - therefore keep the house in the parents’ trust?
 - reconsider use of that existing bloodline trust for the child?
 - in any event - protect the house with a section 21 agreement
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Continued family ownership?

- Consider the wider family issues this structure can raise (multi-sibling scenario):
 - equity between the children – what is fair?
 - when is a Deed of Family Arrangement appropriate?
 - If a Deed of Family Arrangement or similar (charter?) is appropriate, what should it cover?
 - initial value to be made available / equalisations if houses not similar in value
 - further funding availability – interest charge? security?
 - how does it deal with change over many years?
 - and into the next generation – “per stirpes” or “per capita” approach to inter-generational asset planning?
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