

Dwelling House Exemption

Capital Acquisitions Tax Manual Part 24

This document should be read in conjunction with section 86 of the Capital Acquisitions Tax Consolidation Act 2003.

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1 Introduction

There is an exemption from Capital Acquisitions Tax (CAT) where an individual living in a residential property (dwelling house) bequeaths the property to a successor who:

- has lived there for a specified period before the inheritance;
- will continue to live there for a specified period after the inheritance; and
- has no beneficial interest in any other residential property at certain specified dates.

Since 25 December 2016, the exemption no longer applies to gifts of dwelling houses unless the gift is made to a dependent relative of the donor.

2 Legislation

The relevant provisions are contained in section 86 of the Capital Acquisitions Tax Consolidation Act (CATCA) 2003, which has undergone many changes since the relief was first introduced by Finance Act 1991. Finance Act 2000 (section 151) significantly expanded the scope of the relief by turning it into a full exemption and extending it to gifts of dwelling houses and to all recipients. Finance Act 2016 (section 52) then significantly restricted the relief, particularly in relation to the ability to make tax-exempt gifts of dwelling houses and, in relation to inheritances, by restricting the exemption to the principal private residence of a disponer. Finance Act 2019 (section 64) ensured that the exemption would operate as intended in relation to the restriction on having a beneficial interest in any other residential property.

Subsection (1) defines a “dwelling house” as a building or part of a building which is suitable for use as a dwelling and includes grounds (curtilage) surrounding that building of up to an acre in area. The meaning of “successor” takes its meaning from the definition in section 2 CATCA 2003 (i.e. a person who takes an inheritance) but is further defined in subsection (1) to include a person (‘remainderman’) who has inherited due to the early termination of a life interest under section 32(2). Subsection (9) defines a “dependent relative”.

3 Qualifying conditions

In summary, a dwelling house qualifies for the exemption where:

- it was occupied as the only or main residence of a disponer at the date of his or her death (except in the case of a gift or an inheritance taken by a dependent relative);

- it was occupied by a successor as his or her only or main residence for the three years immediately preceding the date of the inheritance or, where the dwelling house for which the exemption is claimed replaced another dwelling house as the successor's only or main residence, the combined period of occupation was at least three years falling within the four years preceding the date of the inheritance;
- a successor does not have a beneficial interest in any other dwelling house at the date of the inheritance (whatever way such an interest was acquired);
- a successor does not acquire a beneficial interest in any other dwelling house from the same disponent at any time after the date of the inheritance and up to and including the valuation date of that inheritance; and
- it is transferred by way of an inheritance, except in the case of a gift to a dependent relative, or such a gift that becomes an inheritance when a disponent dies within two years of making the gift (section 3(1)).

These conditions are described in detail in sections 3.1 to 3.3 below.

3.1 Only or main residence of disponent

A dwelling house must be the only or main residence of a disponent at the date of his or her death (section 86(2)(a)). This requirement effectively means that a disponent can only bequeath a single qualifying house.

The disponent is not explicitly required to have lived in the dwelling house for a specified period before his or her death (but see section 3.2 below).

The word 'residence' is not defined and therefore has its normal meaning. This is a dwelling in which a person habitually lives as his or her home. Therefore, actual physical occupation of a dwelling house is necessary before it can be accepted that it is or was the person's residence.

The words 'only' and 'main' also have their normal meaning. Where a person owns just one residence then this is where the person habitually lives as an owner-occupier. Where a person has more than one residence, the 'main' residence will be the one in which the person habitually lives for the majority of his or her time. Only one residence can be the only or main residence at any time; i.e. the principal private residence.

In the case of a gift or an inheritance of a dwelling house taken by a dependent relative, the dwelling house is not required to have been the only or main residence of the disponent.

An exception to the residency requirement is made where a disponent is absent from his or her only or main residence because of physical or mental ill health at the date

of death; for example, if the person has moved into a nursing home. In this situation, the disponent is deemed to have lived in the dwelling house at that time (section 86(3)).

Example 1

Theresa inherits the family home in which she has lived all her life from her father Pat. Although Pat lived in a nursing home when he died, Theresa qualifies for the dwelling house exemption because of the exception to the disponent's residence requirement in the case of ill health and the treatment of the dwelling house as Pat's principal private residence at the date of his death.

3.2 Only or main residence of successor

A successor must have lived in a dwelling house as his or her only or main residence for the three years **immediately** preceding the date of the inheritance. Combined with the requirement for a disponent to have lived in the dwelling house as his or her only or main residence at the date of death, this means that, in effect, the disponent and successor will have lived together in the house for some or all of that 3-year period.

As happens with a disponent, a successor who is absent from his or her principal private residence because of physical or mental ill health is treated as having lived in the dwelling house during the period of absence.

While a disponent can bequeath only a single qualifying dwelling house, this dwelling house can be inherited by more than one successor, each of whom may qualify for the exemption on his or her particular share of the inherited dwelling house, provided that each successor has lived in that dwelling house for at least three years before the date of the inheritance.

Example 2

Emma and her brother Paul jointly inherit a house from their grandmother. They both lived in the house with their grandmother over a period of three years and three months prior to the date of the inheritance. However, while Paul lived in the house for this full period, Emma spent six months on holiday in Australia during this period. While Paul qualifies for the dwelling house exemption on his share of the house, Emma does not qualify for the exemption as she did not occupy the house as her only or main residence for a period of three years immediately prior to the date of the inheritance.

Where the dwelling house for which the exemption is claimed replaces another dwelling house within the 3-year prior occupation period, the occupation requirement will be satisfied provided that the combined period of occupation of both properties comprises at least 3 years out of the 4 years immediately preceding the date of the inheritance. For the occupation of a property to count towards the

required 3-year period, any property which has been replaced by the dwelling house for which the exemption is claimed must have been owned by a disponent.

Example 3

In May 2018 Jack sold his house in which he had lived with his daughter Deirdre for the previous 10 years. He bought a new house in November 2018 and lived there with Deirdre from then until his death in March 2020. Deirdre qualified for the dwelling house exemption when she inherited the house on the basis that she occupied both it and the previous house as her only or main residence for the period of 3 years and 5 months immediately preceding the date of the inheritance.

The dwelling house is not required to be the only or main residence of the disponent in the case of gifts or inheritances taken by dependent relatives. Therefore, there is no requirement for the disponent and his or her dependent relative to have lived together in the house for any length of time preceding the gift or inheritance. However, the dependent relative must have occupied the house for the required 3-year period, as is the case with any other successor.

3.3 Limit on number of dwelling houses in which a successor can have an interest

A successor is not entitled to the exemption for an inherited dwelling house if he or she has a beneficial interest in another dwelling house at certain specified dates. Such an interest includes both full ownership and lesser interests. A part share in another dwelling house, however small the share, makes a successor ineligible for the exemption. This restriction applies in relation to dwelling houses situated either in the State or abroad. The same restriction applies to a dependent relative who receives a gift of a dwelling house.

The examples in this section of the manual assume that the other qualifying conditions for the exemption have been satisfied.

3.3.1 Interests transferred to discretionary trusts

An anti-avoidance provision (section 86(2A))¹ treats a successor as having a beneficial interest in another dwelling house where the successor himself or herself has transferred an interest in the dwelling house into a discretionary trust of which he or she is a beneficiary. However, this restriction does not apply where such an interest is transferred by a person other than such a successor.

3.3.2 Interests held at date of inheritance

¹ Introduced by Finance Act 2018 (section 52).

The exemption does not apply where a successor has a beneficial interest in another dwelling house at the date of the inheritance of the potentially exempt dwelling house (section 86(4A)(a)(i)). This is usually the date of death. This would most commonly happen where the successor already has a beneficial interest in another dwelling house not acquired from the inheritance in question.

Example 4

John inherits the family home from his father. At the date of the inheritance he co-owns a holiday home with his three brothers. John does not qualify for the exemption as he had a beneficial interest in another dwelling house at the date of the inheritance.

The exemption also does not apply where a successor acquires an **immediate** beneficial interest in another dwelling house on the death of a disponent without having to wait for the assets in the disponent's estate to be ascertained following a grant of probate (in the case of a will) or letters of administration (in the case of intestacy). This can happen in several ways, which are set out in the following three paragraphs.

With the **joint tenancy** form of co-ownership of property, the death of a joint tenant results in the automatic passing on death of the deceased tenant's share in a property to the other joint tenant(s). This is known as passing by survivorship. In contrast, with a tenancy-in-common form of co-ownership, a deceased tenant's share of property passes under the rules of a will or intestacy. (see examples 5 and 14 below).

A '**donatio mortis causa**' is a gift made in contemplation of death and is conditional on the death of the donor. On the death of the donor title to a gifted dwelling house automatically passes to a successor on the date of death. Similarly, with a dwelling house that has been gifted subject to a **power of revocation** by a donor. When the donor dies, without having exercised the power of revocation, the dwelling house automatically passes to a successor on the date of death. (see example 8 below).

Where a person holds a **life-interest** (or other limited interest) in a dwelling house, the interest in the dwelling house automatically passes to a successor who is the 'remainderman' on the death of the life-tenant. (see example 9 below).

Example 5

Carmel inherits her aunt's home. She also co-owns another dwelling house as a joint tenant with her aunt. As survivor under this joint tenancy, Carmel acquires an immediate beneficial interest in this dwelling house on the death of her aunt. As a result, she does not qualify for the dwelling house exemption for her aunt's home as she has an interest in another dwelling house at the date of the inheritance. The beneficial interest in both dwelling houses is acquired on the date of the inheritance.

3.3.3 Period between date of inheritance and valuation date

The condition limiting the number of dwelling houses in which a successor can have a beneficial interest was amended by Finance Act 2019 (section 64) following a High Court judgement on 25 September 2018² (see section 3.3.4 below). Before this amendment, Revenue applied the 'test' for interests held in other dwelling houses at the date of inheritance only. However, the High Court judgement focussed on the reality of the process by which beneficiaries actually acquire interests in the property in a deceased person's estate. Following a death and the grant of probate or letters of administration, personal representatives administer an estate by using available assets to pay expenses, debts and liabilities and then distributing the net assets to beneficiaries. So, depending on how solvent an estate turns out to be, intended beneficiaries may not actually receive their expected beneficial interest in a dwelling house.

The result of the Finance Act 2019 amendment is that Revenue can now apply the 'test' for interests held in other dwelling houses throughout the period from the date of inheritance to the valuation date for the inheritance (section 86(4A)(a)(ii)). However, for dates after the date of inheritance, the 'test' takes account only of interests acquired from the same disponent from whom the potentially exempt dwelling house is acquired.

The valuation date is typically later than the date of the inheritance (date of death) and is, in most cases, the date of the grant of probate. At this date, the net assets that are available for distribution to beneficiaries will have been ascertained.

The change from a point in time 'test' (date of inheritance) to a period of time 'test' (ending on the valuation date) has no impact on the calculation of the CAT liability or the pay and file requirements. The date of the inheritance is still the date that determines the Group thresholds and applicable tax rate. The valuation date is still the date by reference to which the date that tax is payable, and a return is due, is determined. See section 5.4 below in relation to the extended date from which interest on late payment accrues in certain circumstances.

Example 6

Liam's mother died in January 2020. Her will contained a specific bequest of the family home to Liam. He also hopes to inherit a rental house as part of the residue of the estate. At the date of the inheritance, Liam does not have a beneficial interest in any dwelling house. Probate is granted on 10 March 2021 (valuation date) and the net assets of the estate are sufficient for the personal representatives to pass the beneficial interest in both houses to Liam. Because he inherits both

² **Leanne Deane v the Revenue Commissioners** [2018] IEHC 519.

houses from the same disponer on the valuation date for the inheritance, he is not entitled to the dwelling house exemption for the family home.

Example 7

Simon is bequeathed the family home under his father's will. He has no beneficial interest in any other dwelling house at the date of the inheritance. Prior to the grant of probate in respect of his father's estate, Simon inherits another dwelling house on the cessation of a life interest. The disponer in relation to this life interest is Simon's grandfather. Simon will qualify for the dwelling house exemption on the family home as he does not have a beneficial interest in another dwelling house from the same disponer at the valuation date of the dwelling house on which the exemption may be claimed.

It may happen that a successor will initially be entitled to the dwelling house exemption where he or she does not have an interest in another dwelling house at the date of the inheritance of the dwelling house for which the exemption may be claimed. However, the successor may subsequently acquire such an interest from the same disponer and, therefore, cease to be entitled to the exemption. See section 5.4 below in relation to the extended date from which interest on late payment accrues in such circumstances.

Example 8

In June 2019 Megan's grandfather had given her a gift of the house in which they both lived but had made the gift subject to a power of revocation. He died in March 2020 without revoking the gift. Megan, therefore, acquired the beneficial interest in the house on the death of her grandfather. She intends to continue owning and living in the house for the required 6-year post-death period and claims the dwelling house exemption. However, when administering the estate, the personal representatives discover the existence of another house in France owned by Megan's grandfather that she will inherit under his will. As a result, the exemption for the family home will cease when she acquires the beneficial interest in this other house.

It may also happen that a successor becomes ineligible for the exemption because of a beneficial interest acquired in another dwelling house even though he or she has not yet acquired a beneficial interest in the potentially exempt dwelling house.

Example 9

Cian (as remainderman) inherits a house, in which his father had a life interest, on the death of his father. He, therefore, acquires the beneficial interest in this house at the date of inheritance. He is due to inherit the family home in which he has lived for several years with his father under his father's will whenever the personal representatives are in a position to distribute the assets in the estate. However, because of the interest acquired in the other dwelling house, he will not be entitled

to the exemption on the subsequent acquisition of the family home on the valuation date of the inheritance.

3.3.4 'Deane' case

The 'Deane' case³ concerned a successor who inherited two dwelling houses from the same disponer. Revenue refused the dwelling house exemption on the basis that the successor, as part of the same inheritance, became beneficially entitled to both dwelling houses at the same time at the date of the inheritance. The dwelling houses were not bequeathed by a specific legacy but formed part of the residue of the estate. The High Court held that the successor did not have a beneficial interest in either of the dwelling houses at the date of the inheritance on the basis that a successor cannot become beneficially entitled to property which forms part of the residue of an estate until the property available for distribution has been ascertained. Depending on the debts payable out of an estate, the available assets may turn out to be insufficient to fulfil the terms of a will and to actually transfer an interest in dwelling houses to the intended successors.

The judgement effectively meant that the exemption could only be refused where a successor already had an interest in another dwelling house at the date of the inheritance. Revenue did not appeal the judgement and started to operate the exemption in accordance with the effect of the judgement pending a legislative amendment to section 86.⁴ The effect of the judgement on Revenue's operation of the qualifying condition relating to the limit on the number of dwelling houses in which a successor could have an interest is set out below.

1 Position before 25 September 2018

Before 25 September 2018 (date of 'Deane' judgement), Revenue refused the exemption where a successor already had an interest in another dwelling house at the date of the inheritance or inherited an interest in more than one dwelling house from the disponer, whether by way of a specific legacy or from the residue of an estate.

2. Position between 25 September 2018 and 18 December 2019

On or after 25 September 2018, Revenue distinguished between whether any other dwelling house(s) (i.e. other than the potentially exempt dwelling house) were inherited by way of a specific legacy or from the residue of an estate and allowed the exemption in a residue situation.

³ **Leanne Deane v the Revenue Commissioners** [2018] IEHC 519.

⁴ Finance Act 2019 (section 64).

Taxpayers who paid inheritance tax in respect of a dwelling house which, based on the 'Deane' judgement, would have qualified for the exemption could claim a refund. However, such refunds are subject to the usual 4-year time limit on refund claims. Inheritance tax liabilities that were already settled by agreement with Revenue are final and conclusive and cannot be re-visited.

3. Position after 18 December 2019

Finance Act 2019 (section 64) amended section 86 in relation to the limit on the number of dwelling houses in which a successor could have an interest by replacing paragraph (2)(c) with a new subsection (4A). This amendment came into effect on 18 December 2019.⁵

The effect of the amendment is that the 'test' for beneficial interests held in any other dwelling houses is now applied both at the date of the inheritance (usually the date of death) and then throughout the period up to the valuation date for the inheritance. This ensures that all dwelling houses that are inherited as part of the same inheritance/estate are taken into account in determining whether a successor has an interest in another dwelling house. See section 3.3.3 above.

4 Gifts to dependent relatives

A gift of a dwelling house (including a gift that becomes an inheritance as a result of the donor dying within two years of making the gift – section 3(1)) can qualify for the dwelling house exemption only if it is made to a dependent relative of the donor.

"Relative" is defined as a lineal ancestor, lineal descendant, brother, sister, uncle, aunt, niece or nephew of the donor or the spouse or civil partner of the donor. A "dependent relative" is defined as a relative who is permanently and totally incapacitated due to mental or physical infirmity from maintaining himself or herself or who is aged 65 years or over at the date of the inheritance. Maintain in this context means to support oneself by earning an income from working. Total incapacity therefore means that an individual is not capable of earning a living from any kind of work. Also, the incapacity must be permanent; i.e. there must be no prospect of the individual recovering or of the condition improving to the extent that the individual would become capable of maintaining himself or herself.

Incapacity in this context has quite a high threshold. A person who is visually impaired may qualify as permanently incapacitated but not necessarily as totally incapacitated or incapable of maintaining himself or herself by working.

⁵ Finance Act 2019 was enacted on 18 December 2019.

Relatives who are not incapacitated can still qualify for the exemption if they are aged 65 or over.

Example 10

Anthony is gifted a dwelling house by his brother Tom. Anthony has lived in the house for the previous five years and has no interest in another dwelling house. At the date of the gift he is 68. He qualifies for the exemption as he is a dependent relative of Tom due to his age. Had Anthony been 64 at the date of the gift, he would not have qualified for the exemption.

The restriction on the allowability of gifts only to dependent relatives took effect on 25 December 2016. When this restriction was introduced (Finance Act 2016, section 52) there were no transitional arrangements put in place to retain the exemption for people who may have acquired a dwelling house for another person to live in less than three years before 25 December 2016 with the intention of gifting the house to that person three years later.

Example 11

Margaret purchased a dwelling house in February 2016 with the intention of gifting the house to her son James and availing of the dwelling house exemption when his required 3-year period of occupation had expired. James sold his own house in March 2014 and began living in his mother's house. However, as a result of the changes to the exemption from 25 December 2016, James does not qualify for the exemption if his mother's house was gifted to him in March 2019, as was originally intended, because he is not a dependant relative of his mother.

5 Withdrawal of exemption

Where a dwelling house ceases to be exempt, tax is chargeable as if it had not qualified for the exemption. The dwelling house must then be taken into account under the aggregation rules when computing tax on later gifts or inheritances within the same group threshold.

5.1 Sale or disposal

A dwelling house ceases to be exempt where, within the period of six years beginning on the date of the inheritance, it is sold or otherwise disposed of (whether fully or partly).

However, a sale or disposal does not result in the cessation of the exemption where:

- it happens after the death of the successor;
- the successor was aged 65 or older at the date of the inheritance of the dwelling house; or

- the full proceeds from a sale are used by the successor to purchase a replacement dwelling house, which then becomes the successor's only or main residence. If less than the full proceeds are used to purchase the replacement dwelling house there is a clawback of the exemption in proportion to the amount of the proceeds not used.

Example 12

Robert inherited a dwelling house from his sister three years ago which qualified for the dwelling house exemption. The dwelling house, which was valued at €350,000 at the time of the inheritance, was sold by him eight months ago for €400,000. He purchased a replacement dwelling house for €320,000 leaving an amount of €80,000, a fifth of the sale proceeds, not used to purchase the replacement property. The exemption is therefore clawed back in relation to one-fifth of the value of the original inheritance. The inheritance tax payable by Robert is calculated as follows (it is assumed that Robert has already fully utilised the Group B threshold):

| | |
|--------------------------------------|---|
| Taxable value | $€350,000 \times (\frac{€80,000}{€400,000})$ = €70,000 |
| Remaining Group B tax-free threshold | = nil |
| CAT @ 33% | = €23,100 |

The sales proceeds are not required to be re-invested completely in the purchase price of the replacement house. Necessary expenses associated with the purchase, such as stamp duty and legal costs, are treated as a legitimate part of the re-investment. However, expenses associated with the sale of the dwelling house that qualified for the exemption are not treated as a legitimate part of the re-investment.

5.2 Occupation as only or main residence

A dwelling house ceases to be exempt where, within the period of six years beginning on the date of the inheritance, a successor ceases to occupy it as his or her only or main residence. However, a cessation of occupation of the dwelling house does not result in the cessation of the exemption where a successor –

- has died;
- was aged 65 or older at the date of the inheritance of the dwelling house;
- was required to live elsewhere because of his or her physical or mental infirmity, where this is certified by a doctor; or
- was required by his or her employer to live elsewhere (whether in the State or abroad) to perform the duties of his or her employment.

Example 13

Edel inherited a dwelling house from her mother four years ago for which she qualified for the dwelling house exemption. She is an engineer and has been informed by her employer that she is to be transferred to the Dubai office for a year. The dwelling house exemption will not be clawed back as Edel's temporary absence within the required six-year period post inheritance is as a result of an instruction from her employer, provided that the property remains her only or main residence for the remainder of the six-year period on her return from Dubai.

Where a person who was at least 55 years of age received a gift or inheritance of a dwelling house before 25 December 2016 and satisfied the other qualifying conditions for the exemption at that time, there is no clawback of the exemption as a result of the age threshold being increased to 65 after that date. Such people have no requirement to live in the house for the following six years, provided the gift or inheritance was received before 25 December 2016.

5.3 Beneficial interest acquired in another dwelling house

It may happen that a successor will initially be entitled to the dwelling house exemption where he or she does not have an interest in another dwelling house at the date of the inheritance of the dwelling house for which the exemption may be claimed but may subsequently acquire such an interest from the same disponent and, therefore, cease to be entitled to the exemption (section 86(4A)(b)). Where this happens, an inheritance tax liability arises as if the exemption had never applied. See example 8 above.

However, the acquisition of a beneficial interest in another dwelling house from a disponent other than the disponent of the dwelling house for which the exemption can be claimed has no effect on entitlement to the exemption.

5.4 Interest on late payment

To cater for situations where the valuation date for a dwelling house for which the exemption may be claimed has already passed when the subsequent 'clawback' event happens, the date from which interest on late payment accrues is extended. The extended date is the valuation date for the inheritance of the subsequent interest in the other dwelling house.

Example 14

Andrew inherits a half-share in a dwelling house in which he was a joint tenant with his brother. As this interest was inherited immediately on the death of his brother, the date of the inheritance and the valuation date in respect of this benefit are the same. Andrew did not hold a beneficial interest in any other dwelling house on this date and satisfied the other conditions for the exemption. However, his brother

also bequeathed him a holiday home in the residue of his estate, on the acquisition of which Andrew will cease to qualify for the exemption. Inheritance tax will then be payable on his previously exempt inheritance and interest will accrue from the valuation date for the inheritance of the holiday home instead of from the valuation date for the inheritance of the jointly owned dwelling house.

6 Compliance

The exemption should be claimed on the IT38 return form by a successor or dependent relative as part of the normal self-assessment process. However, Revenue may decide to examine the validity of any claim as part of its normal compliance programme. This may involve the person being required to provide evidence and supporting documentation to prove that he or she qualifies for the exemption. Such supporting documentation could include, for example:

- documents as evidence of living at a particular address;
- a disclaimer of a benefit under a will or intestacy under section 12 CATCA 2003;
- a copy of the will;
- a doctor's letter stating the nature and extent of an individual's incapacity;
- proof of residing in a nursing home;
- a letter from the successor's employer;
- documents relating to the sale of a dwelling house and purchase of a replacement dwelling house.

The following material is either exempt from or not required to be published under the Freedom of Information Act 2014.

[...]