

Dwelling House Exemption

Capital Acquisitions Tax Part 24

This document should be read in conjunction with section 86
CATCA 2003

Document last updated December 2018

Table of Contents

24.1.	Introduction	2
24.2.	Legislation	2
24.3.	Qualifying conditions	3
24.3.1.	Only or main residence	3
24.3.2.	Prior occupation by the successor	4
24.3.3.	Limit on number of dwelling houses in which the successor has an interest	5
24.3.4.	Gifts to dependent relatives	7
24.4.	Withdrawal of exemption	8
24.5.	Compliance	10

24.1. 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 of time before the inheritance,
- will continue to live there for a specified period of time after the inheritance, and
- has no beneficial interest in any other residential property at the date of the inheritance.

The exemption also applies to residential properties that are gifted to dependent relatives of a donor; i.e. individuals who are incapacitated to such an extent that they are unable to maintain themselves by earning an income from working or who are aged 65 or over.

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. When this restriction was introduced, there were no special arrangements made 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 (see example 1 below). In addition, in the case of an inheritance, the exemption now applies only to the principal private residence of a disponent.

Example 1

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 once James's required 3-year period of occupation had expired. James sold an apartment in which he had previously been living in March 2014 and has been living in the dwelling house owned by his mother since then. The changes to the exemption from 25 December 2016 mean that James will not qualify for the exemption if the dwelling house in question were to be gifted to him in March 2019 as was originally intended because he is not a dependant relative of his mother.

24.2. 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 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) 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 disponent.

A “dwelling house” is defined as a building or part of a building which is suitable for use as a dwelling and includes grounds 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 section 86(1) to include a person who has inherited due to the early termination of a life interest under section 32(2). Section 86(9) defines “dependent relative”.

24.3. Qualifying conditions

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

- it was occupied as the only or main residence of a disponent 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;
- it is the only dwelling house in which a successor has a beneficial interest at the date of the inheritance; and
- it is transferred by way of an inheritance, except in the case of-
 - a gift of a dwelling house to a dependent relative, or
 - a gift to a dependent relative 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 24.3.1 to 24.3.4 below.

24.3.1. Only or main residence

A dwelling house must be the only or main residence of the disponent at the date of his or her death (section 86(2)(a)). The disponent is not explicitly required to have lived in the dwelling house for a specified period of time before his or her death (but see section 24.3.2 below).

The word ‘residence’ is not defined and therefore has its normal meaning. This is a dwelling in which a person habitually lives and is his or her home. It follows

that 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 multiple residences, 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 one time; i.e. the principal private residence.

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)). (see example 2 below).

Example 2

Theresa inherits the family home in which she has lived all of her life from her father Pat. Theresa has no interest in any other dwelling houses and the house is the only residence of her father. Pat was residing in a nursing home when he died. Theresa qualifies for the dwelling house exemption because Pat was absent from his only residence at the date of his death because of ill health and, therefore, the dwelling house is considered to be his principal private residence at the date of his death.

The requirement for a dwelling house to have been a disponent's principal private residence effectively means that each disponent can only bequeath a single qualifying house. This house can, however, be left to multiple successors who may each qualify for the exemption on their particular share of the inherited house, provided that each of them has lived in that house for at least three years before the date of the inheritance.

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.

24.3.2. Prior occupation by the 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 (see example 3 below). 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 the dwelling house is not required to be the only or main residence of the disponent in the case of gifts or inheritances of houses taken by dependent relatives, there is no requirement that the disponent and his or her dependent relative will 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 with any other successor.

Example 3

Emma inherits a house from her grandmother in which she lived with her grandmother for three years and three months prior to the date of the inheritance except for a period of six months spent travelling in Australia. She does not qualify for the dwelling house exemption as she was not resident in the house as her only or main residence for a period of three years prior to the date of the inheritance.

Where the dwelling house for which the exemption is claimed replaced another dwelling house within the 3-year prior occupation period, then this requirement will be met 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. Any property which has been replaced by the dwelling house for which the exemption is claimed must have been owned by the disponent for the occupation of that property to count towards the required 3 years.

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 at that time.

24.3.3. Limit on number of dwelling houses in which the successor has an interest

A successor cannot claim the dwelling house exemption if he or she has an interest in another dwelling house at the date of an inheritance (or the date of a gift to a dependent relative). Such an interest includes both full ownership and lesser interests and applies to dwelling houses situated either in the State or abroad. Even a part share in another dwelling house, however small the share, makes a successor ineligible for the exemption. This is the position where the successor already owned or had an interest in another dwelling before the date of the inheritance (see example 4 below) and **may** be the position if the interest is acquired as part of the same inheritance.

Under an anti-avoidance provision¹, a successor is treated as having an interest in another dwelling house at the date of an inheritance, where the successor has transferred an interest in the dwelling house into a discretionary trust of which he or she is a beneficiary before the date of the inheritance. However, where a

¹ New subsection (2A) introduced by section 52 Finance Act 2018

person, other than a beneficiary of a discretionary trust, places a dwelling house in the trust, the beneficiary is not treated as having an interest in the dwelling house for the purposes of the dwelling house exemption.

High Court Judgement

A High Court judgement of 25 September 2018² has implications for the way in which Revenue treats the requirement that a successor cannot have a beneficial interest in more than one dwelling house at the date of an inheritance. In this particular case, the successor inherited more than one dwelling house from the same disponent. These dwelling houses formed part of the residue of the estate. The appeal was against the disallowance of the dwelling house exemption on the basis that the successor became beneficially entitled to both dwellings at the same time as part of the same inheritance and, therefore, the qualifying condition under subsection 86(3)(b) (the relevant subsection at the time - now 86(2)(c)) was not met.

The judge held that the successor did not have a beneficial interest in either of the dwelling houses at the date of the inheritance as a successor cannot become beneficially entitled to a house which forms part of the residue of an estate until the assets available for distribution have been ascertained.

Revenue did not appeal the judgement and adopted a revised approach in distinguishing between dwelling houses inherited as a specific legacy and those inherited in the residue of an estate. Accordingly, a dwelling house forming part of the residue of an estate is not to be taken into account in determining whether a successor has an interest in another dwelling house at the date of an inheritance. The relevant factor for the purposes of the dwelling house exemption is whether a successor already had an interest in another dwelling before the date of the inheritance or whether the successor received more than one dwelling as a specific legacy in the same inheritance.

See examples 4, 5 and 6 below.

Example 4

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

Example 5

Liam inherits a specific bequest of the family home from his mother, in which he lived with her for the five years preceding her death, together with an interest in additional dwelling houses in the residue of her estate. Liam did

² Leane Deane v the Revenue Commissioners (High Court) – judgement of Ms. Justice Costello delivered 25 September 2018.

not have an interest in any other dwelling house prior to the death of his mother. He qualifies for the dwelling house exemption on the specific legacy as he does not have an interest in another dwelling house at the date of the inheritance.

Example 6

Carmel is specifically bequeathed a dwelling house from her aunt, in which she has already been living for four years. The house was her aunt's principal residence at the date of her death and at that time Carmel did not have an interest in any other house. As part of the same inheritance, her aunt also leaves a specific bequest to Carmel of a half share in a holiday cottage in Kerry. Carmel does not qualify for the dwelling house exemption as she has an interest in another dwelling house at the date of the inheritance.

Caseworkers may be asked about cases with similar circumstances to those in the High Court case referred to above where CAT has already been paid. They should take the following approach.

Settlements are final and conclusive and cannot be re-visited. Taxpayers or their agents who challenge a settlement should be advised accordingly.

Taxpayers who paid a CAT liability in respect of the inheritance of a dwelling house which, based on Revenue's revised approach following the High Court judgement, would have qualified for the exemption may apply for a refund. However, a refund should not be made where the relevant CAT return was not filed within the allowable four-year period for claiming refunds.

24.3.4. 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) 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.

Relatives who are not incapacitated can still qualify for the exemption if they are aged 65 or over. (see *example 7* below).

Example 7

Anthony is gifted a dwelling house by his brother Andrew. 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 dwelling house exemption as he is a dependent relative of the donor due to his age. Had Anthony been 64 at the date of the gift he would not have qualified for the exemption.

24.4. Withdrawal of exemption

A dwelling house ceases to be exempt where, within the period of six years beginning on the date of an inheritance -

- it is sold or otherwise disposed of by a successor, or
- a successor ceases to occupy the dwelling house as his or her only or main residence.

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

However, a sale, disposal or cessation of occupation does not result in the withdrawal of the exemption where -

- the full proceeds from a sale are re-invested in a replacement dwelling house that will then be the only or main residence of the successor. If less than the full proceeds are re-invested there is a clawback of the exemption in proportion to the amount of the proceeds not re-invested in a replacement dwelling house (see *example 8* below),
- the successor was 65 or older on the date of the inheritance,
- the successor was required to reside somewhere other than the dwelling house because of his or her physical or mental infirmity and where the infirmity is certified by a doctor, or

- the successor was required by his or her employer to live somewhere else, whether in the State or abroad, to perform the duties of his or her employment (see example 9 below).

Example 8

Robert inherited a dwelling house from his sister three years ago for which he qualified for the dwelling house exemption. The dwelling house, which was valued at €350,000 at the time of the inheritance was sold by Robert 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 re-invested in acquiring a replacement property. The dwelling house exemption is therefore clawed back in relation to one-fifth of the value of the original inheritance. The CAT payable by Robert in this instance is calculated as follows:

Taxable value	€350,000 x (€80,000/€400,000) = €70,000
Remaining Group B tax-free threshold	= nil
CAT @ 33%	= €23,100

Example 9

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 to lead a new project. The dwelling house exemption will not be clawed back in this instance as Edel's temporary absence from the dwelling house 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 the proceeds from a sale are re-invested in a replacement dwelling house, necessary expenses associated with the purchase of that replacement dwelling, such as stamp duty and legal costs, are a legitimate part of the re-investment. The full proceeds of the sale are not required to be re-invested completely in the purchase price of the replacement property; these necessary associated expenses can form part of the re-investment without triggering a clawback of the exemption. 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.

Where a person who was at least 55 years of age received a gift or inheritance of a dwelling house prior to 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 persons have no requirement to live in the house for the following six years, provided the gift or inheritance was received before 25 December 2016.

24.5. Compliance

The exemption should be claimed on the IT38 return form by a successor / 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 showing the type of inheritance; i.e. specific legacy or residue;
- 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.

[...]