Pros and cons of buying property through a family trust

A family trust offers individuals an alternative to purchasing the property in their own name, however, this comes with its own set of pros and cons, according to Adrian Goslett, regional director and CEO of Re/Max of Southern Africa. While purchasing through a trust offers more security than purchasing through a bank, there are other tax implications that could cause this to be a less desirable option for some buyers.

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There are several ways to purchase a home through a family trust. For example, one could apply for home finance through the trust, or, if there is enough capital readily available in the trust, buyers could loan this amount from their family trust instead of through a financial institution. This would then be considered a cash offer and, depending on how the trust is managed, is likely to result in lower interest charges than one would receive on a traditional home loan.

Depends on buyer’s circumstances

In terms of deciding whether this would be a good option, Goslett explains that it all depends on the buyer’s unique circumstances. “If, for example, the buyer has his or her own business, then it is safer to purchase the home in the trust’s name rather than have it registered in his or her own name. In this scenario, if the business were to run into financial problems, the home cannot be liquidated as it is not seen to be part of the owner’s assets,” Goslett explains.

In addition to this, buying the home through a trust means that estate and transfer duty as well as capital gains tax can be avoided upon the owner’s death. “A trust is often used to protect the assets and ensure that the appointed beneficiaries, which are more often than not the trust founder’s children, get the benefit of using the assets if something happens to the trust founder. If the home is registered to the trust, then the home will not form a part of the deceased estate and will not be used in the calculation of estate duty. The beneficiaries of the trust simply inherit the home without incurring any additional costs as long as it remains within the trust,” says Goslett.

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Maximising rental profits

However, if the buyer is purchasing the home as a source of rental income, then Goslett suggests that it is possibly better to finance the home through a bank rather than a trust in order to maximise profits. Any income received by a trust is taxed at the highest tax bracket at around 45% and will incur capital gains tax (CGT) on any capital profit that it makes. To minimise this, the trust can distribute the rental profits to its beneficiaries who will then be taxed on this income according to their personal income brackets. However, no deductions will then apply as the usual non-capital expenses that can be used to offset against an individual’s rental income are all billed through the trust and not through the individual.

“Those who are considering forming a trust should ideally consult with a professional financial adviser before they proceed. While a trust can be a highly effective vehicle to manage assets, it will not suit everybody's needs. A financial adviser will be able to explain all the implications and assess whether it is the right route based on the individual’s criteria,” Goslett concludes.