

Dealing with Usufructs / Bare Dominium Rights in Property Transactions

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INTRODUCTION

This article explores the nature of a usufruct and how it affects the sale of the property to which it relates.

WHAT ARE BARE DOMINIUM AND USUFRUCTUARY RIGHTS?

It is a little-known fact that Ownership in property can be divided into two rights:

1. Bare dominium rights; and
2. Usufructuary rights.

The division of these rights are used in various ways. They can be used as an estate planning tool or as a tax planning tool.

WHAT IS A USUFRUCT?

A usufruct over immovable property is a personal real right registered in favour of a third party (known as the usufructuary) so that the usufructuary may benefit from the occupation, use or fruits of that property. Ownership is however retained by the registered owner of the property (who is known as the bare dominium owner).

An example of a usufruct is where a husband bequeaths a residential property to his children upon his death in his Will, but stipulates that his wife enjoys a usufruct until her death. In this way he ensures that his wife has the occupation, use and enjoyment of the property for her lifetime.

It is therefore a personal right granted in favour of the usufructuary for a limited time. Upon the death of the usufructuary, the usufruct will lapse and the entire property will revert to the registered owner/s or heirs.

WHAT ARE THE RIGHTS AND OBLIGATIONS OF THE USUFRUCTUARY?

As a general proposition, the rights in respect of a usufruct are akin to that of a tenant under a lease agreement, to enjoy the property and all benefits that come with it. The holder of the usufruct is responsible to maintain the property in its current state, fair wear and tear excepted. The usufructuary may also be obliged to make payment of the rates levied by the Council in respect of the property as well as all services (water, electricity and other municipal levies) rendered to the property, unless agreed to the contrary with the owner. The holder of a usufruct is entitled to enter into certain agreements with third parties, such as lease agreements, and receive the rental income, provided that the period of the agreement does not extend beyond the lifetime of the usufructuary or the period for which the usufruct has been granted.

The bare dominium owner remains responsible for insuring the property.

HOW DOES THE USUFRUCT IMPACT TRANSFER?

The owner's rights to deal with the property are limited by the usufruct. If, as an example, the usufruct is created in terms of a Will, transfer of the property concerned is then registered in the names of the heirs to whom ownership has been bequeathed, and the rights of the usufructuary are included as a condition in the title deed.

It is possible for the bare dominium owner/s and the usufructuary holder to sell the property. In such a case, the usufructuary must pass transfer together with the bare dominium owner and must be included with the seller on the agreement of sale, power of attorney to pass transfer and deed of transfer. Upon registration of transfer, the trust and the individual are both entitled to their respective share of the proceeds of sale based on the SARS valuation of the respective rights and must each account to SARS for CGT on this basis.

Whilst unusual, the property can be sold subject to the usufruct remaining after transfer, or, with the consent of the usufructuary, free of the usufruct. The property therefore can remain encumbered by the usufruct after transfer of the property which means that the usufructuary has rights of use and enjoyment to the property, even to the exclusion of the new owner.

If the property has been transferred to the new owner subject to the usufruct, the property cannot be bonded without the usufruct holder's written consent. Banks will not consent to the registration of any bond over the property without the usufruct holder signing a waiver of preference in favour of such Bank.

The right in and to the usufruct cannot be ceded or transferred to anyone else other than the bare dominium owner. The bare dominium owner cannot transfer the property free of the usufruct without the usufruct's consent and participation in the process.

USUFRUCTS AND TAX PLANNING

The division of property rights into bare dominium and usufructuary rights is sometimes used in order to effectively transfer a property to a trust and as part of a tax planning exercise. The bare dominium rights are valued using the tax tables from SARS and are sold via an agreement of sale to an established Trust. The usufructuary rights are retained by the individual owner.

Depending on the age of the individual owner, the bare dominium rights are usually much lower in value than the usufructuary rights. As an example, the total property value could be R1 200 000.00. The bare dominium rights valued at R400 000.00 and the usufructuary rights valued at R800 000.00. The bare dominium rights are sold and transfer duty is paid on the value of R200 000.00. The nett result after transfer is a title deed where the trust owns the bare dominium and the individual has a title deed condition where the usufructuary rights are retained by the individual.

The usufructuary rights are bequeathed to the trust and on the death of the individual, the trust receives the usufructuary rights and thus has full ownership rights.

If the trust and the individual elect to sell the property before the death of the individual, the sale agreement must refer to the trust as the seller of the bare dominium rights and the individual must be referred to as the seller of the usufructuary rights. Both must sign the sale agreement and both must sign the transfer documents (in their respective capacities).

The comment above with regards to CGT applies in this instance as well. Note that there are tax consequences to the above and legal and tax advice must be taken.

HOW IS A USUFRUCT VALUED?

While a usufruct cannot be sold or ceded, the renunciation (or abandonment) of it by the usufructuary will increase the value of the property as a whole, as it is no longer encumbered by the usufruct.

The value of a usufruct over a property is essentially calculated with reference to the life expectancy of the usufructuary or the term of the usufruct (whichever is shorter), the fair value of the Property and the annual value of the right of enjoyment of the Property (the annual yield).

If the Usufruct has been granted for the remainder of the usufructuary's life, a table known as "the life expectancy table" is used to determine the value of the usufruct. The present value is R1 per annum for life capitalised at 12% over the expectation of life of males and females of various ages. The value of the usufruct will depreciate with each passing year until such time as the usufruct lapses and the bare dominium holder becomes owner of the whole property.

Transfer duty may be payable as a result of the renunciation of the usufruct in favour of the owner/s of the property. The duty is payable due to the fact that the value of the property has been increased due to the full ownership of the property having been restored.

CONCLUSION

The tax consequences of a usufruct in a property transaction can be quite complex, and advice should be sought before a usufruct is created and when dealing with it in any potential transfer of property.



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