



Deconstructing the Discounted Gift Trust



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Where content includes case studies or examples these are for illustration purposes and are not recommending a specific course of action.

Past performance is not a reliable indicator of future performance. The value of an investment can go down as well as up and your client may get back less than they've paid in.

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Learning objectives

By the end of this session, you will be able to:

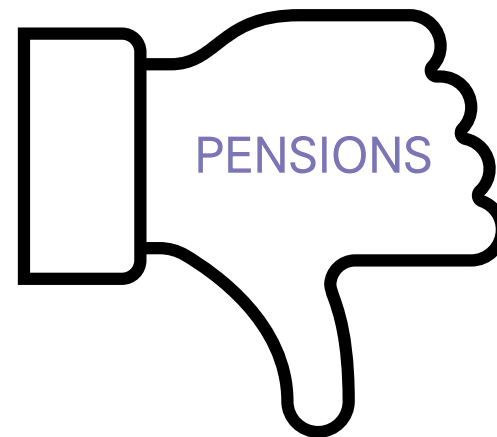
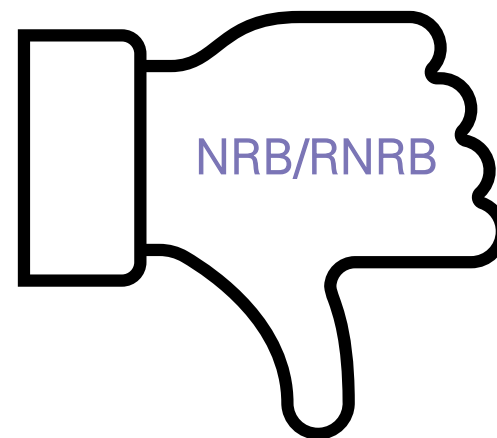
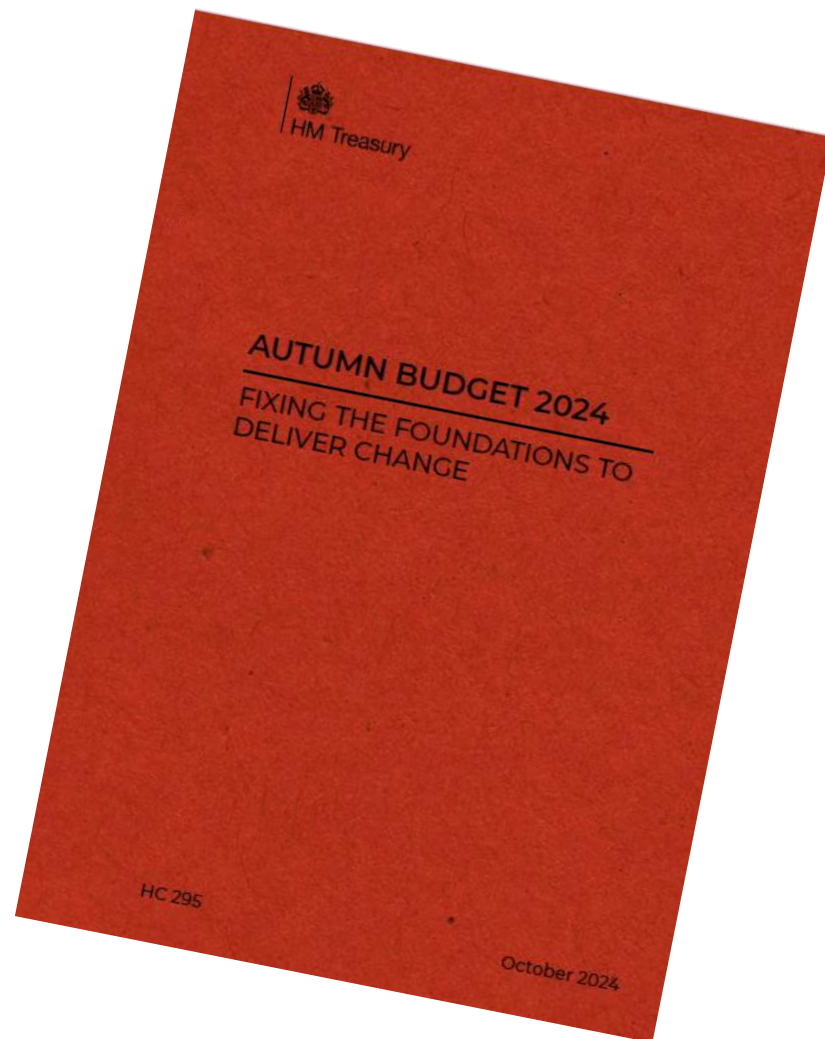
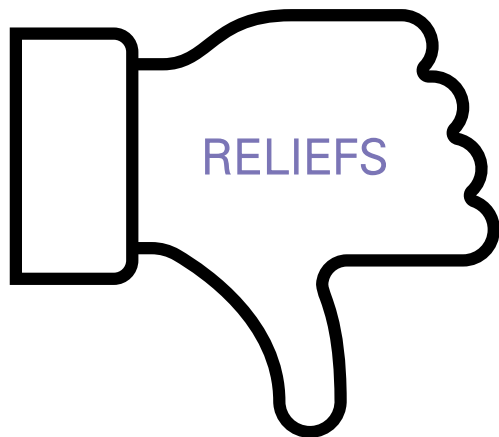
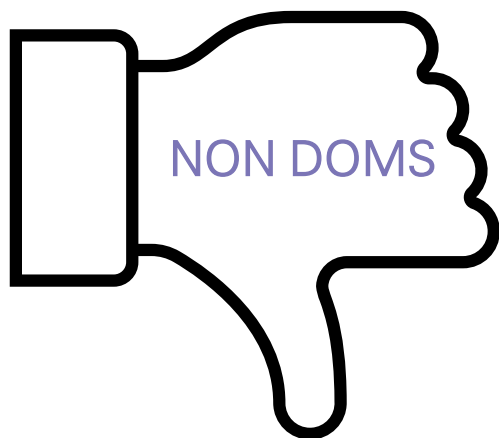
Explain how a discounted gift trust is structured and how they are set up

Describe the initial and ongoing IHT implications of setting up a DGT

Explain how the chargeable event regime applies to investment bonds held in DGTs

Identify clients who could benefit from using a discounted gift trust as part of their IHT planning strategy

The Budget and IHT



IHT planning hasn't changed



Access



Control

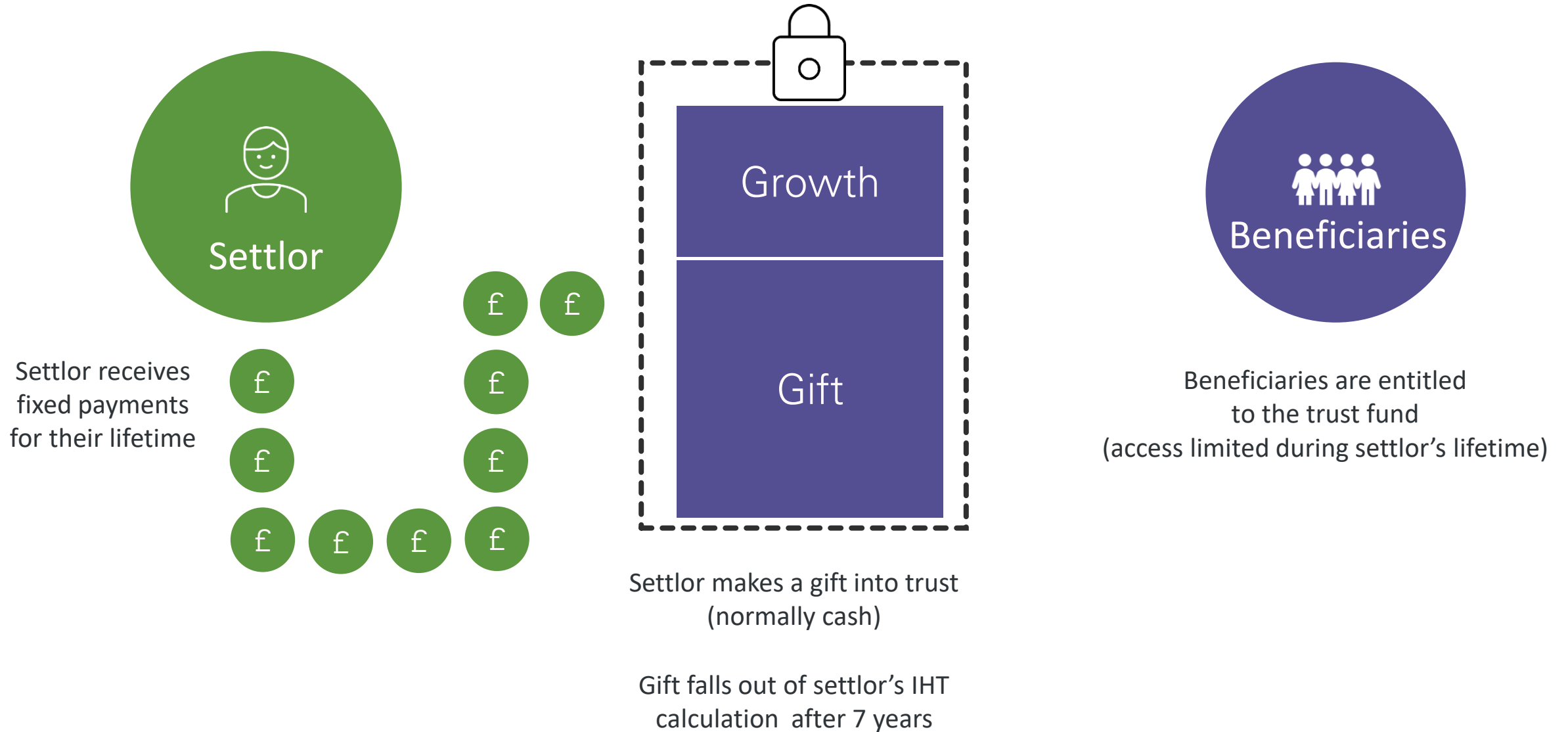


Tax



What is a discounted gift trust?

What is a DGT?



Case study - Alice



Alice, a widow, is aged 74 and in good health. Her late husband, Alan, died aged 68 leaving all his assets to Alice

She has a dependant's pension from her late husband and a state pension but this is insufficient to meet her expenditure.

Alice supplements her income from her late husband's drawdown pot and her other investments.

Alice is concerned about Inheritance tax and wants to take action now to mitigate the impact of this.

Alice has two sons who are both higher rate taxpayers.

Case study - Alice



Main residence
£875,000



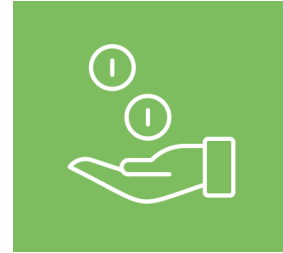
Cash
£50,000



ISAs
£100,000



Dependant's Drawdown
£480,000



State pension £11,500 p.a.
DB pension £ 8,000 p.a.



Expenditure £37,500 p.a.

Shortfall £18,000 p.a./£1,500 p.m.

£480,000 into a DGT to cover
income shortfall!

Alice's IHT position

		2025/26	2027/28
Net Estate (after liabilities)	House	£875,000	£875,000
	Bank	£50,000	£50,000
	ISAs	£100,000	£100,000
Add settled property			£480,000
Add back lifetime gifts < 7 years			
Less exemptions			
Less reliefs			
Less Nil Rate Bands	Main NRB	£650,000	£650,000
	RNRB	£350,000	£350,000
Taxable Estate		£25,000	£505,000
IHT due @ 40%		£10,000	£202,000



Absolute or discretionary?

Control



Beneficiaries fixed at outset

Beneficiaries can access at age 18*

Trust fund is in beneficiaries' estate

Unlimited - no immediate tax charge

Classes of potential beneficiaries

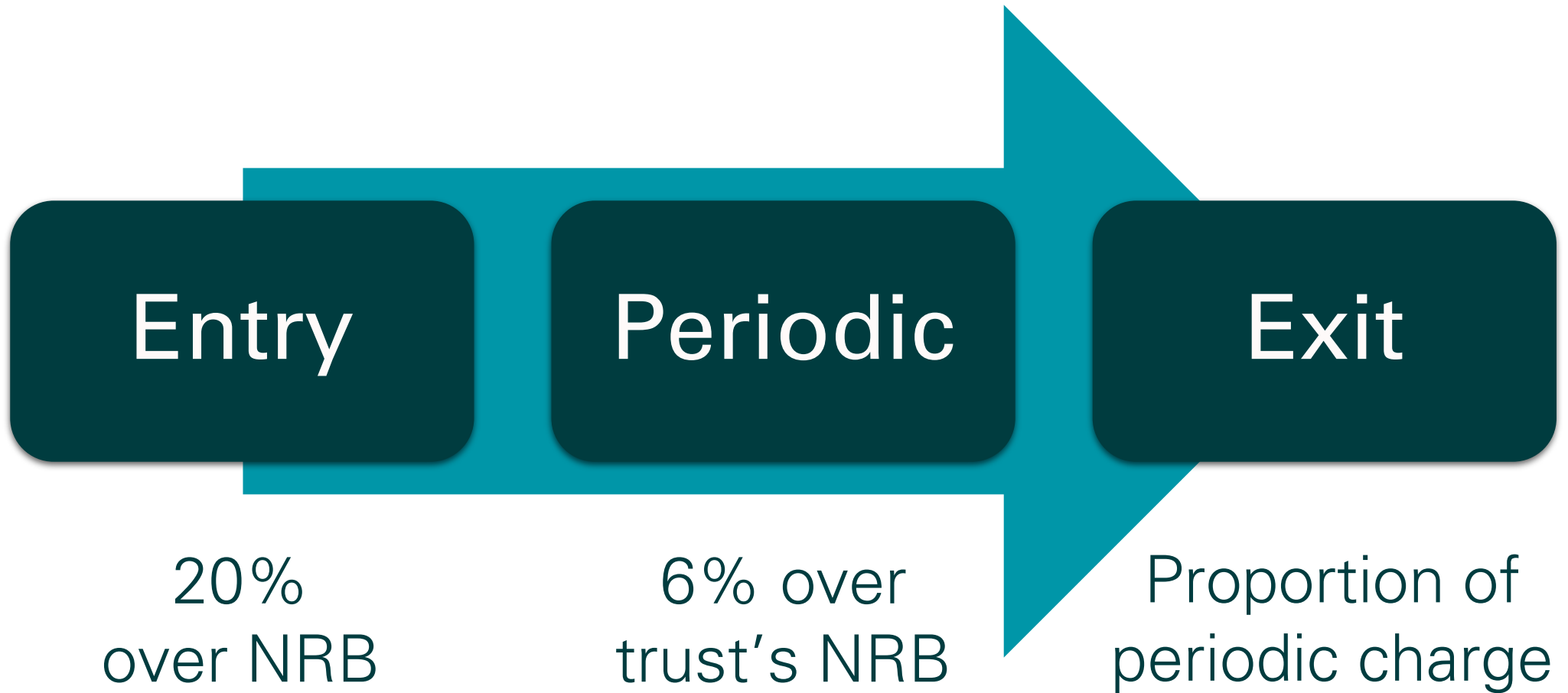
Trustees have control over distribution

Not in beneficiaries' estate

CLTs over NRB incur entry charge

*Limited access with DGT during settlor's lifetime

Relevant property regime and DGTs





What happens if the beneficiary
dies before the settlor?



The discount

The discount (broadly!)

- Tom is gifting £100,000 and needs £4,000 p.a.
- Underwriters assess life expectancy to be 10 yrs
- Retained Rights – $10 \times £4,000 = £40,000$
- Discount - $£40,000 / £100,000 = 40\%$
- Transfer of Value (gift) = £60,000



Underwriting options

Tele-underwriting

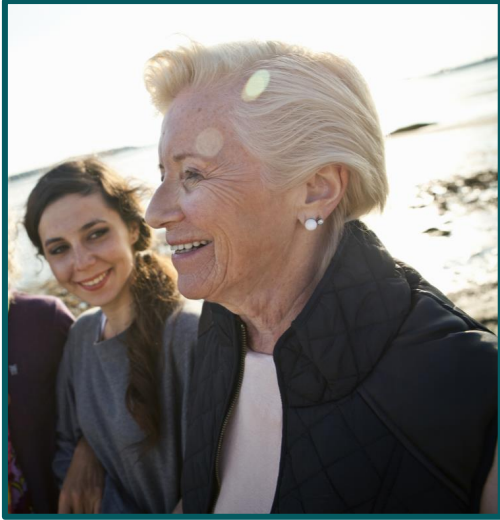
Full
GP Report

No underwriting
(nil discount)



Is a discounted gift trust
unsuitable if no discount is given?

Alice's discount



Discounted Gift Trust - Discount Estimator tool

built by M&G

Investment amount ?	£ 480000	
Tax basis ?	<input type="radio"/> Onshore <input checked="" type="radio"/> Offshore	
Regular withdrawal amount ?	£ 1500	Withdrawals frequency ? Monthly
No of settlors ?	1 Settlor	
Settlor 1 age next birthday ?	75	

[Reset to defaults](#) [View results](#)

Discount results

Estimated discount %	33.03%
Estimated gift	£321,500



Is ongoing advice charge taken
into account when calculating the
discount?

Should you try to maximise the discount?

Discounted Gift Trust - Discount Estimator tool

built by M&G

Investment amount ?

£ 480000

Tax basis ?

Onshore Offshore

Regular withdrawal amount ?

£ 2400

Withdrawals frequency ?

Monthly

No of settlors ?

1 Settlor

Settlor 1 age next birthday ?

75

Reset to defaults

View results

Discount results

Estimated discount %	51.68%
Estimated gift	£231,950

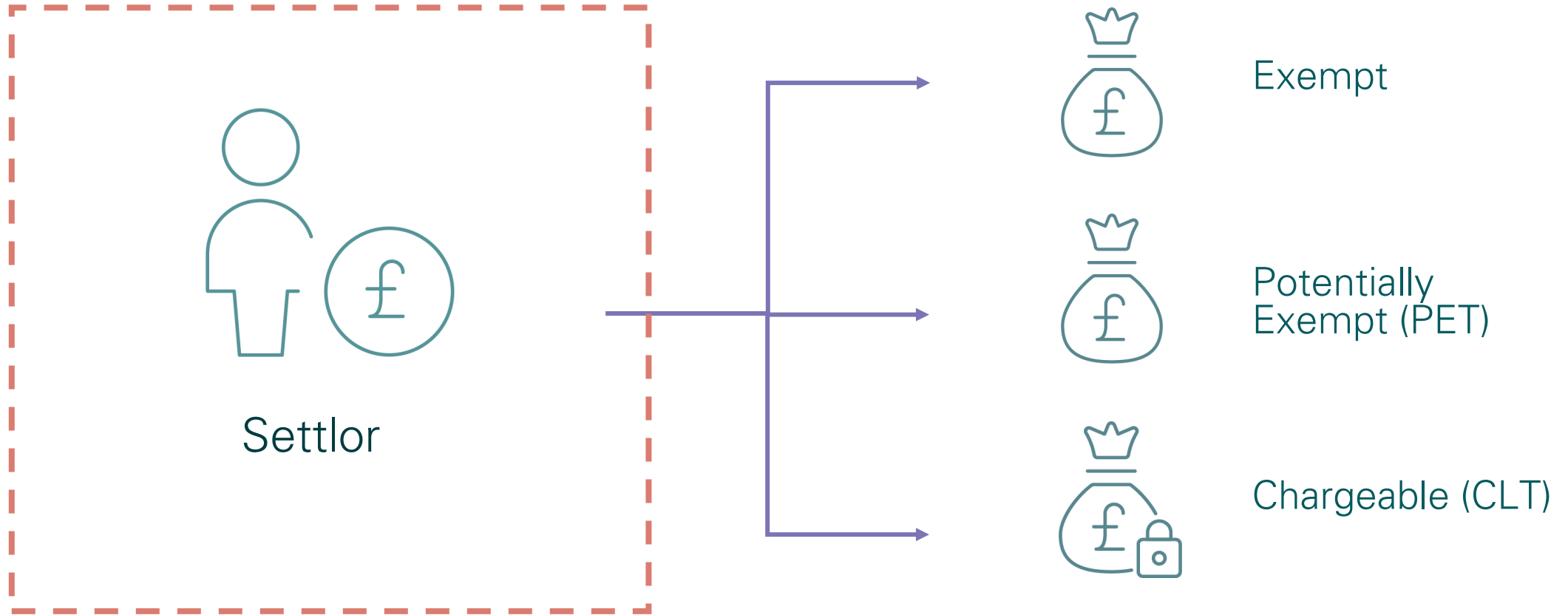
Should you try to maximise the discount?

	DGT with £1,500 p.m. withdrawal		DGT with £2,400 p.m. withdrawal	
7 years after setting up the DGT	£0 in estate		£75,600 in estate	
	£0 in estate		£162,000 in estate	



Can the settlor give away the
withdrawals if they no longer
want them?

IHT treatment of gifts



Normal expenditure out of income?

IHTM14250 - Lifetime transfers: conditions for normal out of income exemption: out of income

The second condition ([IHTM14231](#)) for exemption is that the transferor should have made the gift out of their income. So a gift of capital assets such as jewellery or securities does not qualify unless it was specifically purchased by the donor from income with the intention of making the gift.

Income is not defined in the IHTA84 but should be determined for each year in accordance with normal accountancy rules. It is not necessarily the same as income for income tax purposes. Income is the net income after payment of income tax.

It is usually clear whether payments received are income in nature. Common sources of income are employment and self-employment, rents from property, pensions, interest and dividends. But, it is possible that payments received on a regular basis may appear to be income but are in fact capital in nature. An example would be receipts from a discounted gift scheme ([IHTM20424](#)).

Available income

You should initially look at the income of the year in which gifts were made to see if there was enough income available to make the gifts, before

Normal expenditure out of income?

as jewellery or securities does not qualify unless it was specifically purchased by the donor from income with the intention of making the gift.

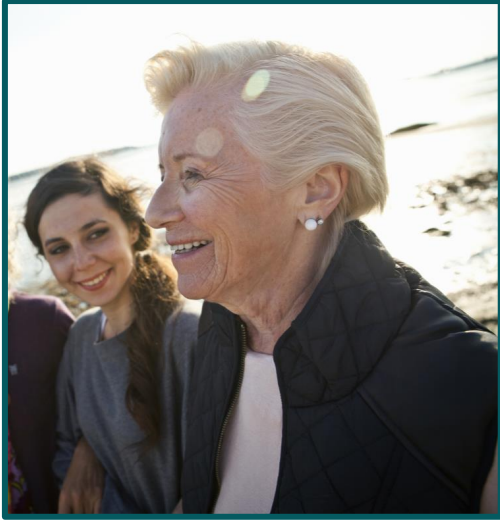
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What happens when the settlor dies?

Alice – death < 7 years



Alice dies after 6 years

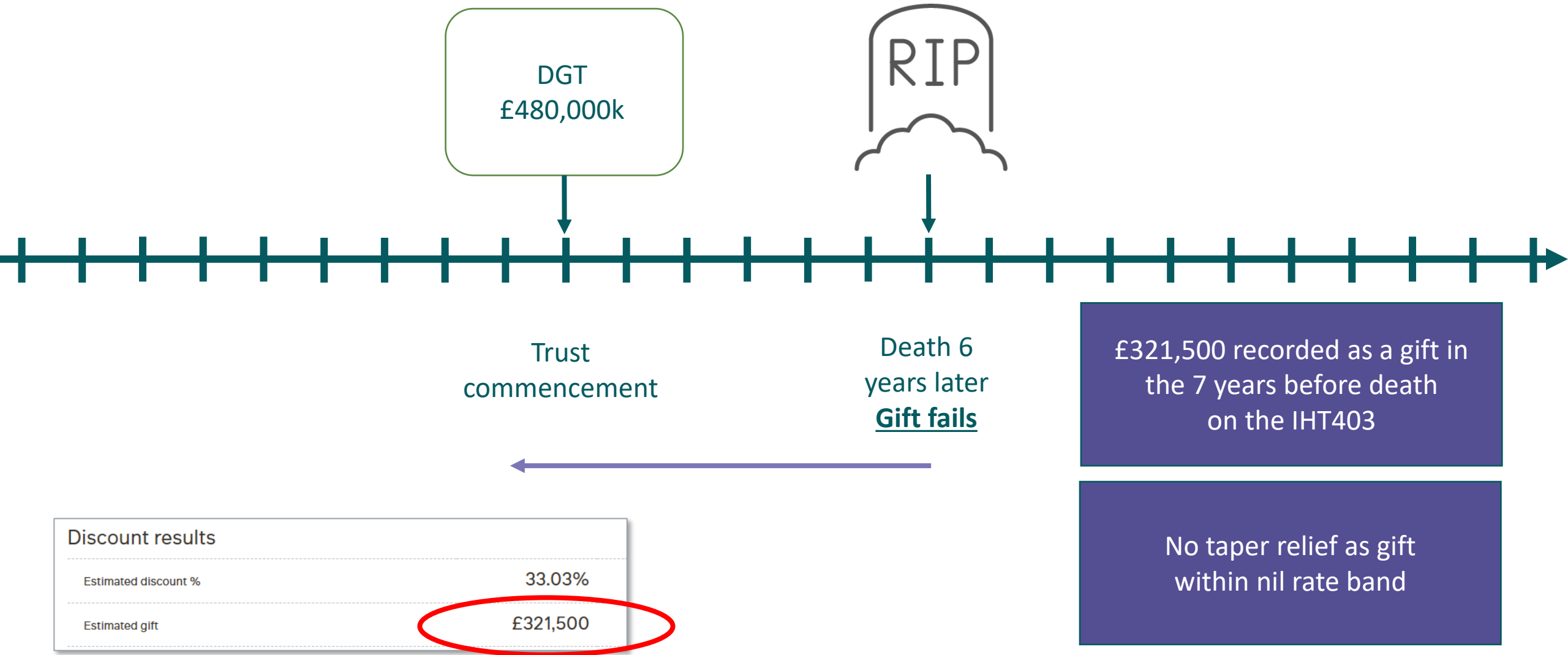
£480,000 went into the trust 6 years ago

The bond in the DGT is worth £500,527

Is the bond included in Alice's estate?

Will taper relief apply?

Alice – death < 7 years



Alice – death after 6 years IHT position





Can you stop the settlor's
withdrawals after 7 years?



Periodic charges

What's assessed for the periodic charge?

DISCOUNTED GIFT
TRUST

Discounted value
of the trust

Alice – 10 year anniversary discount

Discounted Gift Trust - Discount Estimator tool

built by M&G

Investment amount ?

£ 480000

Tax basis ?

Onshore Offshore

Regular withdrawal amount ?

£ 1500

Withdrawals

No of settlors ?

1 Settlor

Settlor 1 age next birthday ?

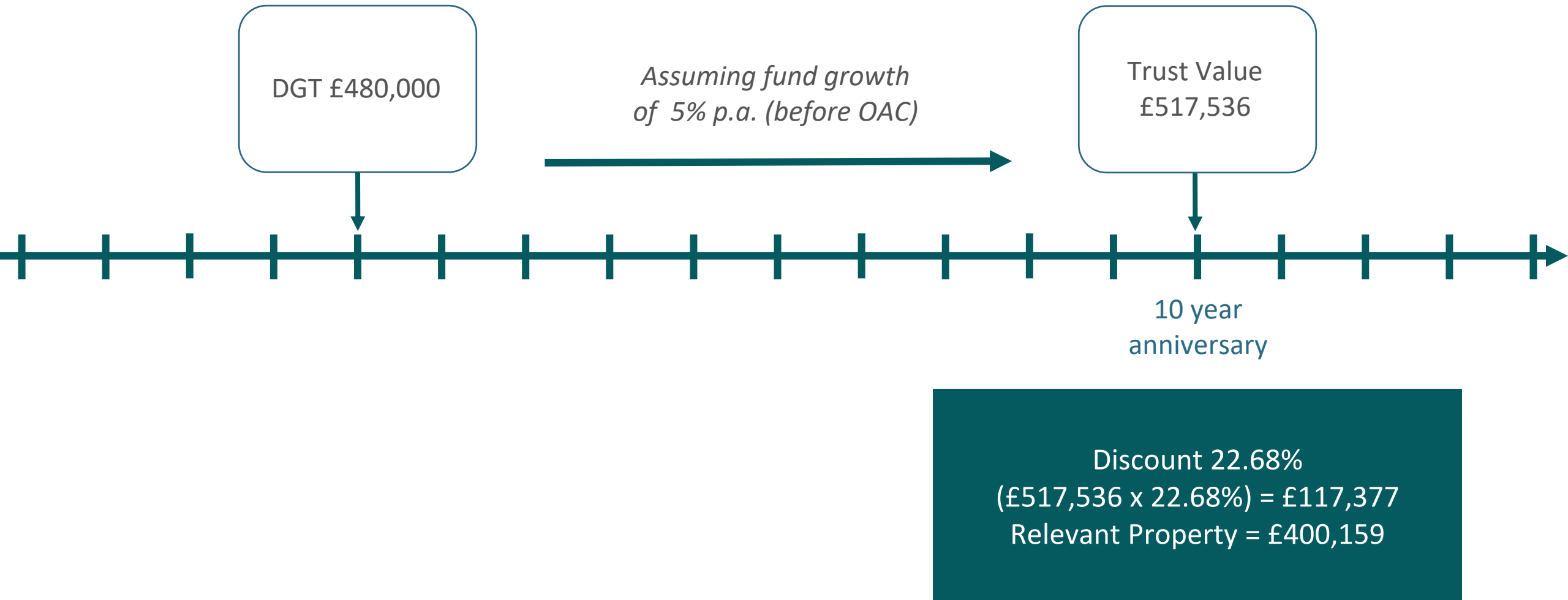
85

Discount results

Estimated discount %	22.68%
Estimated gift	£371,100



How does the discount apply at ten year anniversaries?



Periodic charge – simple calculation

Value of trust fund the day before the 10 year anniversary

£400,159

PLUS

Value of related settlements
(commenced on same day or added to on same day)

NIL

LESS

Trust's Nil Rate Band*

£325,000

* NRB is reduced by chargeable transfers in the 7 years before the commencement of the trust and any capital distributions subject to the exit charge in the previous 10 years.

Excess taxed at 6%

£75,159 x 6% = £4,509.54



Chargeable events

Chargeable event gains – who is liable?

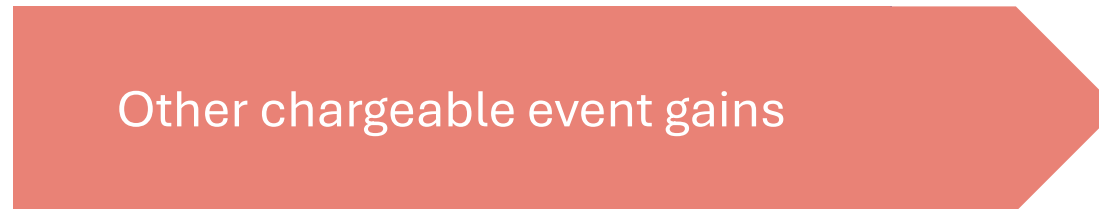
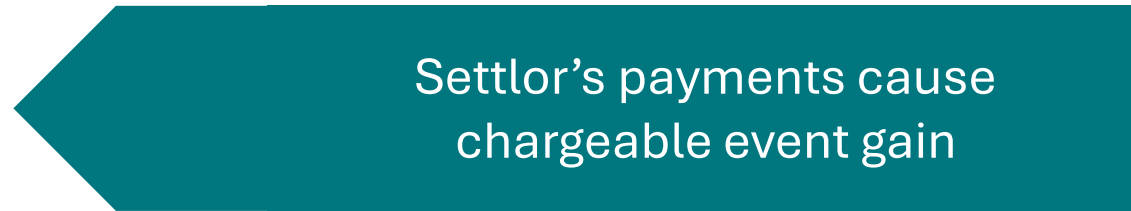


A diagram consisting of two rectangular boxes side-by-side. The left box is teal and contains the word 'Bare'. The right box is purple and contains the word 'Other'.

Bare

Other

Bare – Who is liable?



Not bare – Who is liable?

All trustees are resident in the UK

The trust is resident in the UK for Income Tax and Capital Gains Tax purposes.

All trustees are resident outside the UK

The trust is not resident in the UK for Income Tax and Capital Gains Tax purposes.

There is a mixture of resident and non-resident trustees acting at the same time

The trust is resident in the UK unless the settlor was:

- not resident in the UK and
- not domiciled in the UK

at the time the settlor made, or is treated as making, the settlement and any time when the settlor adds property to the settlement.

Alice – chargeable event gains

Settlor fixed withdrawal
3.75% p.a.

OAC 0.5% p.a. on fund
value paid monthly

Partial for £5,000 for
periodic charge

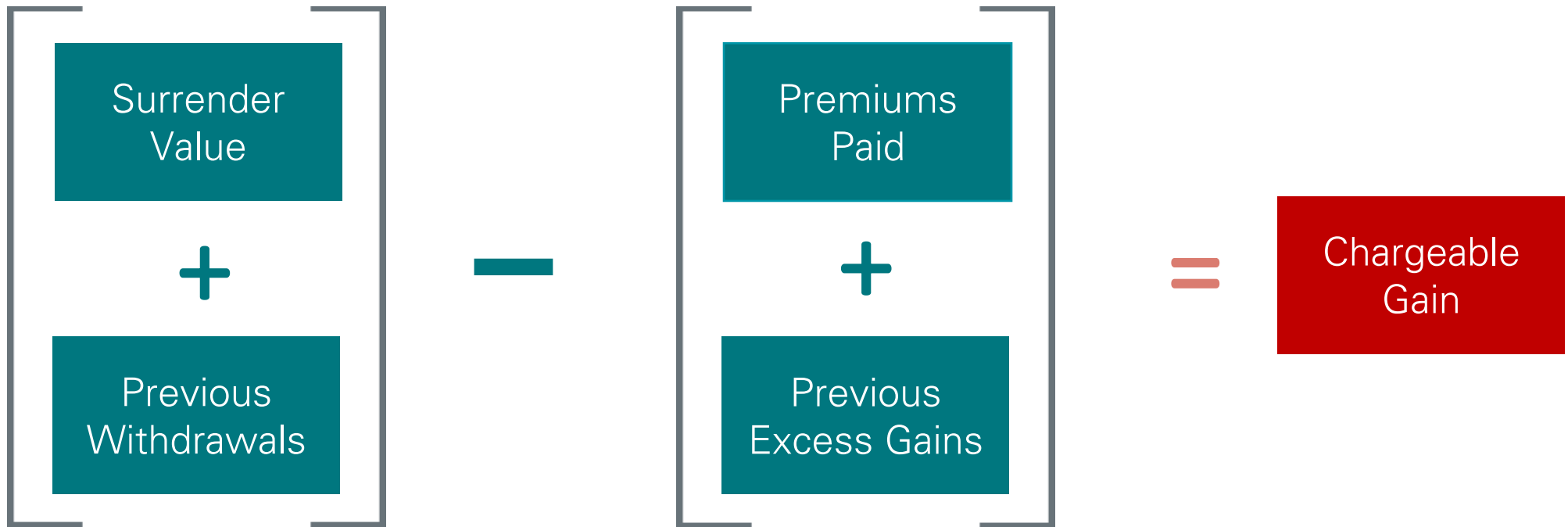
Tax deferred allowance
runs out after 24 years

£20,338 excess on 13th
May 2050

Alice would be 98!

Alice – death after 15 years

Bond is now worth £537,223 and the gain on encashment would be:

$$\left[\begin{array}{c} \text{Surrender Value} \\ + \\ \text{Previous Withdrawals} \end{array} \right] - \left[\begin{array}{c} \text{Premiums Paid} \\ + \\ \text{Previous Excess Gains} \end{array} \right] = \text{Chargeable Gain}$$


Alice – death after 15 years

Bond is now worth £537,223 and the gain on encashment would be:

$$\left[\begin{array}{c} \text{£537,223} \\ + \\ \text{£312,922} \end{array} \right] - \left[\begin{array}{c} \text{£480,000} \\ + \\ \text{nil} \end{array} \right] = \text{£370,145}$$


Life Assured v Capital Redemption



Life assured basis

Bond ends when last life assured dies

Sum assured payable on death

Available Onshore and Offshore



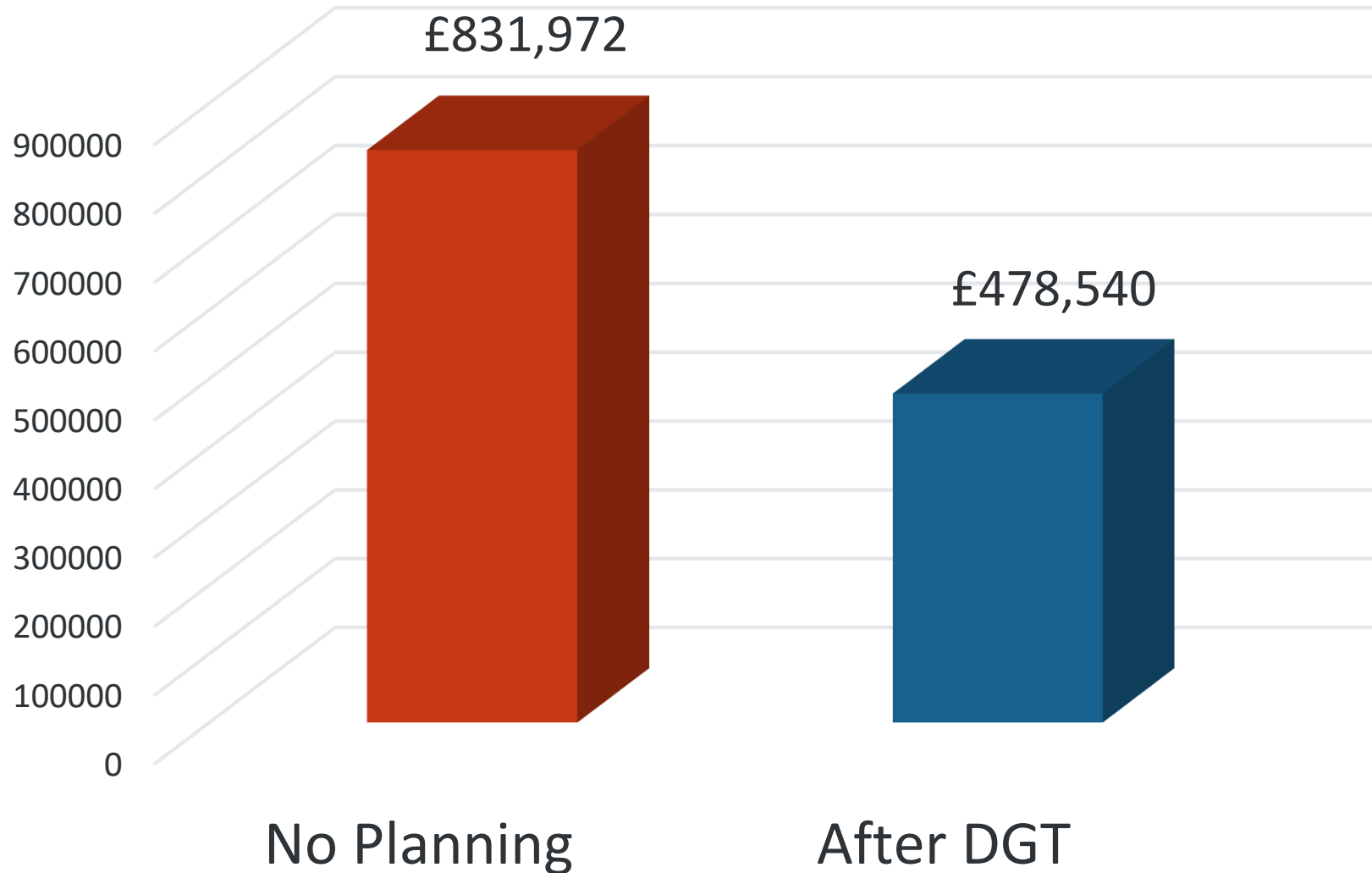
Capital Redemption basis

Ends at maturity date (term of 99 years)

Maturity benefit payable at maturity date

Available on Offshore bonds only

Alice – death after 15 years IHT position





Other planning points

“Joint” settlor DGTs

Payments continue at same level until second death

Each settlor receives their own discount on the amount they contribute to the trust

Joint settlors - the discount

Discounted Gift Trust - Discount Estimator tool

built by M&G

Investment amount ?	£ 480000		
Tax basis ?	Onshore	Offshore	
Regular withdrawal amount ?	£ 2400	Withdrawals frequency ?	Monthly
No of settlors ?	2 Settlers		
Settlor 1 age next birthday ?	76	Settlor 1 investment split ?	50 %
Settlor 2 age next birthday ?	73	Settlor 2 investment split ?	%
		Reset to defaults	View results

Discount results

Estimated discount %	62.39%
Estimated gift	£180,550
Settlor 1 estimated gift	£96,750
Settlor 2 estimated gift	£83,800

“Joint” settlor DGTs

Payments continue at same level until second death

Marginally bigger discount overall than 2 single settlor trusts

Discount at ten year anniversary is apportioned between each settlement

Each settlor receives their own discount on the amount they contribute to the trust

If a settlor dies within 7 years their own gift is included in their estate

Chargeable event gains are split between each settlor (discretionary)



Can you change the underpinning
investment?



How does a DGT compare to the other main IHT solutions?

Other options?

Discounted
Gift Trust

Gift Trust

Settlor Access	Fixed withdrawals for life	None
Control	Yes	Yes
Beneficiary Access	Yes (subject to settlor rights)	Yes
IHT treatment	Discounted gift out of estate after 7 years, discounted value at TYA	Gift out of estate after 7 years, full value at TYA
RNRB taper	Gift out of estate immediately	Gift out of estate immediately
Chargeable events	Tax Deferred Allowance	TDA and/or Surrender

Other options?

Discounted
Gift Trust

Loan Trust

Settlor Access	Fixed withdrawals for life	Access to loan only
Control	Yes	Yes
Beneficiary Access	Yes (subject to settlor rights)	Yes
IHT treatment	Discounted gift out of estate after 7 years, discounted value at TYA	Growth out of estate
RNRB taper	Gift out of estate immediately	Loan included for the taper
Chargeable events	Tax Deferred Allowance	TDA and/or Surrender

Other options?

Discounted
Gift Trust

Business relief

Settlor Access	Fixed withdrawals for life	Yes*
Control	Yes	Yes
Beneficiary Access	Yes (subject to settlor rights)	Yes
IHT treatment	Discounted gift out of estate after 7 years, discounted value at TYA	Eligible for relief after 2 years
RNRB taper	Gift out of estate immediately	Full value included for RNRB
Chargeable events	Tax Deferred Allowance	Not applicable

Other options?

Discounted
Gift Trust

Reversionary
Interest Trust

Settlor Access	Fixed withdrawals for life	Unknown annual payments
Control	Yes	Yes
Beneficiary Access	Yes (subject to settlor rights)	Yes
IHT treatment	Discounted gift out of estate after 7 years, discounted value at TYA	Gift out of the estate after 7 years Full value included for TYA
RNRB taper	Gift out of estate immediately	Gift out of estate immediately
Chargeable events	Tax Deferred Allowance	Surrender only

Learning objectives

By the end of this session, you will be able to:

Explain how a discounted gift trust is structured and how they are set up

Describe the initial and ongoing IHT implications of setting up a DGT

Explain how the chargeable event regime applies to investment bonds held in DGTs

Identify clients who could benefit from using a discounted gift trust as part of their IHT planning strategy



Thank you for your time

Get in touch with your usual M&G contact if you need further help

