

Trusts created on death

The information that follows is based on our understanding of current taxation, legislation and HM Revenue & Customs practice all of which are liable to change without notice.

This is just for UK financial advice professionals.

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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.

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Learning Objectives

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

Identify the types of trust that can be created on a person's death

Describe the income tax and CGT treatment of trustee investments

Identify appropriate investments for a particular trust

Why are trusts used on death?

Statutory
Trust

NRB
planning

Control
successive
interests

Young
Beneficiary

Don't trust
your
Beneficiaries

Protect
Means
Tested
Benefits

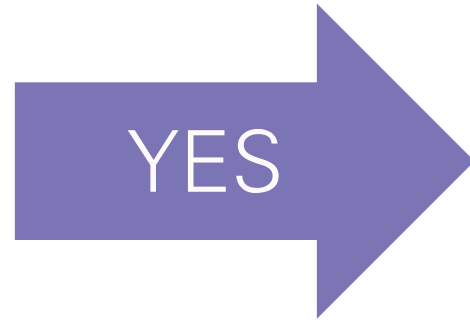
Keep out of
Beneficiary's
Estate - IHT

Disabled
Beneficiary

Trusts created on death

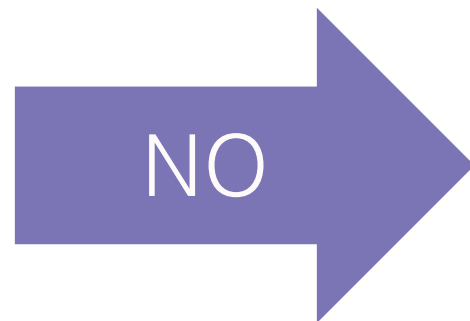


Is there a
Will?



The Will may create an Explicit trust

A statutory trust may arise



A statutory trust may arise

Types of trust



Bare



**Interest in
Possession**



Discretionary



Absolute/Bare Trusts

Bare/Absolute



- Unconditional gift – beneficiary entitled to income and capital
- If recipient is over 18 there is no trust and assets are distributed
- If recipient is under 18 the trustees hold on bare trust until age 18 (or whatever age stated)
- Trust fund in beneficiary's estate

Example - Bare

12) I bequeath the following pecuniary legacies, free of expenses and of government taxes on death namely:-

- a) To my grandchildren alive at the date of my death the sum of FIFTY THOUSAND POUNDS STERLING each
- b) I bequeath the sum of TWENTY THOUSAND POUNDS STERLING to each of my children Jekyll and Hyde absolutely

How old are they?

Example – Bare?

5.1.2 as to the other part for such of my grandchildren **Billy the Kid** and **Luke Skywalker** as shall survive me **and** attain the age of 25 and if both in equal shares absolutely

Not bare!

Example 1 - bare trust

Mrs A left the residue of her estate to such of her grandchildren as were alive at the date of her death.

She directed that the funds should not be paid to the grandchildren until they respectively attain age 21 years.

Example 3 - not a bare trust

Mr B left the residue of his estate to 'such of my grandchildren as survive me and attain age 21 years'. If any grandchild dies before age 21, his/her prospective share goes to the other grandchildren who do attain that age.

**2 CONDITIONS NEED TO BE
MET BEFORE BENEFICIARIES
HAVE A VESTED INTEREST**

Caution! Age contingent gifts

BEREAVED
MINORS
TRUSTS



18-25
TRUSTS



Discretionary Trusts

Discretionary



- Trustees hold trust fund and have control over who benefits - beneficiary entitled to nothing
- Could be named beneficiaries or classes of beneficiary
- Trust fund not in beneficiary's estate – Trust subject to relevant property regime for IHT

Example - Discretionary

- 12) I give the sum of £250,000 to my Trustees upon trust (hereinafter called the “Trust Fund”) to hold subject to the powers and provisions hereinafter declared.
 - a) My Trustees shall hold the capital and income upon such trusts in such shares with and to such powers and provisions as the Trustees shall at any time or times appoint by deed or deeds revocable or irrevocable.

Bereaved Minor's Trusts

1

Normally created by Will of a parent (or intestacy in England and Wales)

2

Bereaved minor - under 18 and at least one parent who has died

3

While under 18 no one else can benefit

4

Must become entitled to all the capital and any income arising from it by age 18

5

No IHT periodic charges

18 -25 Trusts

1

Normally created by Will of a deceased parent

2

Beneficiary must be under age 25

3

While under 25 no one else can benefit

4

Must become entitled to all the capital and any income arising from it by age 25

5

No IHT charges until age 18 – maybe IHT between 18 and 25



Interest in Possession Trusts

Interest in possession



**Interest in
Possession**

- Life tenant – entitled to income/enjoyment of trust property e.g. right to live in a house
- Remaindermen – entitled to capital
- Trust fund in Life Tenant's estate

Example – IIP

5) My Trustees shall hold the Trust Fund ON TRUST

- a) To pay the income to my Wife for her life and subject to that
- b) Absolutely for such of my children as are alive at my death and if more than one in equal shares PROVIDED that if any child of mine dies before me leaving a child or children who reach the age of 25 then such child or children shall take and if more than one in equal shares so much of the Trust Fund as that child of mine would have taken on attaining a vested interest

“alive at my death” = 1 condition = bare

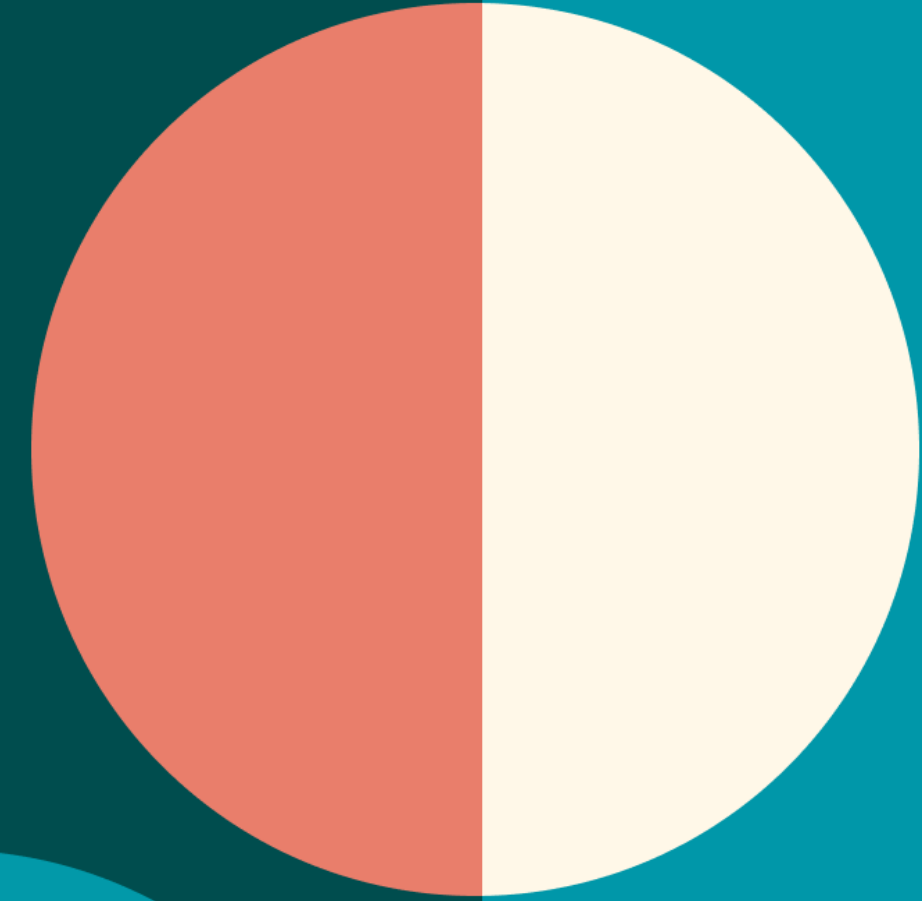
Example - IIP

- a) My Residuary Trustees shall pay the income of the Trust Fund to the Primary Beneficiary during their lifetime
- b) Subject to that, my Residuary Trustees may accumulate the whole or any part of the income of Trust Fund during the Trust Period and the income shall be added to the Trust Fund
- c) Subject to that, during the Trust Period, my Residuary Trustees shall pay or apply the income of the Trust Fund to or for the benefit of any of the Residuary Beneficiaries as they think fit.

Accumulate income = Discretionary

Life Tenant may be allowed capital!

- (ii) my Trustees may at any time or times during the Trust Period as to the whole or any part of the Trust Fund to the income of which my Wife is for the time being entitled transfer or raise and pay the same to or for the absolute use or benefit of my Wife or raise and pay or apply the same for the advancement or otherwise for the benefit of my Wife in such manner as my Trustees shall in their absolute discretion think fit



Deeds of Variation

Deeds of Variation

1

Must be made within 2 years of death

2

Must be in writing

3

Requires consent of those affected

4

The DOV can create a trust

5

The settlor is the beneficiary who varies their inheritance
(deceased is the deemed settlor IHT/CGT)

Trust Registration



Will Trust

Exempt for 2 years
from date of death

**Deed of
Variation
Trust**

Within 90 days
of DOV

**Statutory
Trust**

Exempt

If the trustees have a tax liability the trust has to register by
5th October in the tax year after the tax year the liability arises



Taxation of Income

Taxation of income – Interest in possession

Trust income

Type of income	Income tax rate
Non dividend	20%
Dividends	8.75%



Trustees can “mandate” income directly to beneficiary



Income retains character - starting rate, PSA and dividend allowance available

Example – taxing IIP interest

- Trustees receive gross OEIC interest of £1,000 & pay tax @ 20%
- Beneficiary receives £800 from the trustees
- Beneficiary includes £1,000 interest in his/her tax return
- Beneficiary given credit for the £200 tax paid by the trustees
- The beneficiary can utilise their 0% starting rate for savings income and PSA as appropriate
- Beneficiary might pay more tax or be due a refund
- Mandating?



Dividend Allowance



2022/23



2023/24



2024/25

Discretionary Trust Taxation Change

23/24

Standard Rate Band
£1,000

Tax liability < £100
No tax return (by concession)
Tax payable on distribution

24/25

~~Standard Rate Band
£1,000~~

Income < £500
No tax return on receipt
Tax payable on distribution

Taxation of income – Discretionary

Trust income

Type of income	Income tax rate
Non dividend	45%
Dividends	39.35%

Taxation of income – Discretionary

Trustees of a discretionary trust receive interest of £5,000 and dividends of £10,000. How much tax will they pay?

	Interest £	Dividends £	Tax Due £
Received	5,000	10,000	
	5,000 @ 45%		2,250
		10,000 @ 39.35%	3,935
		Total	6,185

Trustees – Tax on distribution

	£
Net income distributed	8,250
Tax Credit (45%)	6,750
Gross trust income received by beneficiary	15,000
Tax already paid	6,185
Further tax due by trustees to satisfy tax credit	565



Trustees need to maintain records of income received and tax paid – the “tax pool”

Beneficiary – Tax on receipt

UK rates

Band/Allowance	Rate %
Personal Allowance	0
Basic Rate	20
Higher Rate	40
Additional Rate	45

Scottish Rate of Income Tax

Band/Allowance	Rate %
Personal Allowance	0
Starter Rate	19
Basic Rate	20
Intermediate Rate	21
Higher Rate	42
Advanced Rate	45
Top Rate	48



Personal Savings Allowance, Starting Rate for Savings and Dividend Allowance don't apply!



Beneficiary can reclaim tax paid depending on their tax position



Taxation of Capital Gains

Capital Gains Tax

Bare

Other

Non Bare trusts & CGT

Trust capital gains up to £1,500*

Type of capital gain	CGT rate
Residential Property	Exempt
Other	Exempt

Trust capital gains over £1,500*

Type of capital gain	CGT rate
Residential Property	24%
Other	20%

- Trust exemption is half the personal exemption. The trust exemption is split between the number of trusts set up by the settlor subject to a minimum of 1/5th per trust.

Trustees and CGT

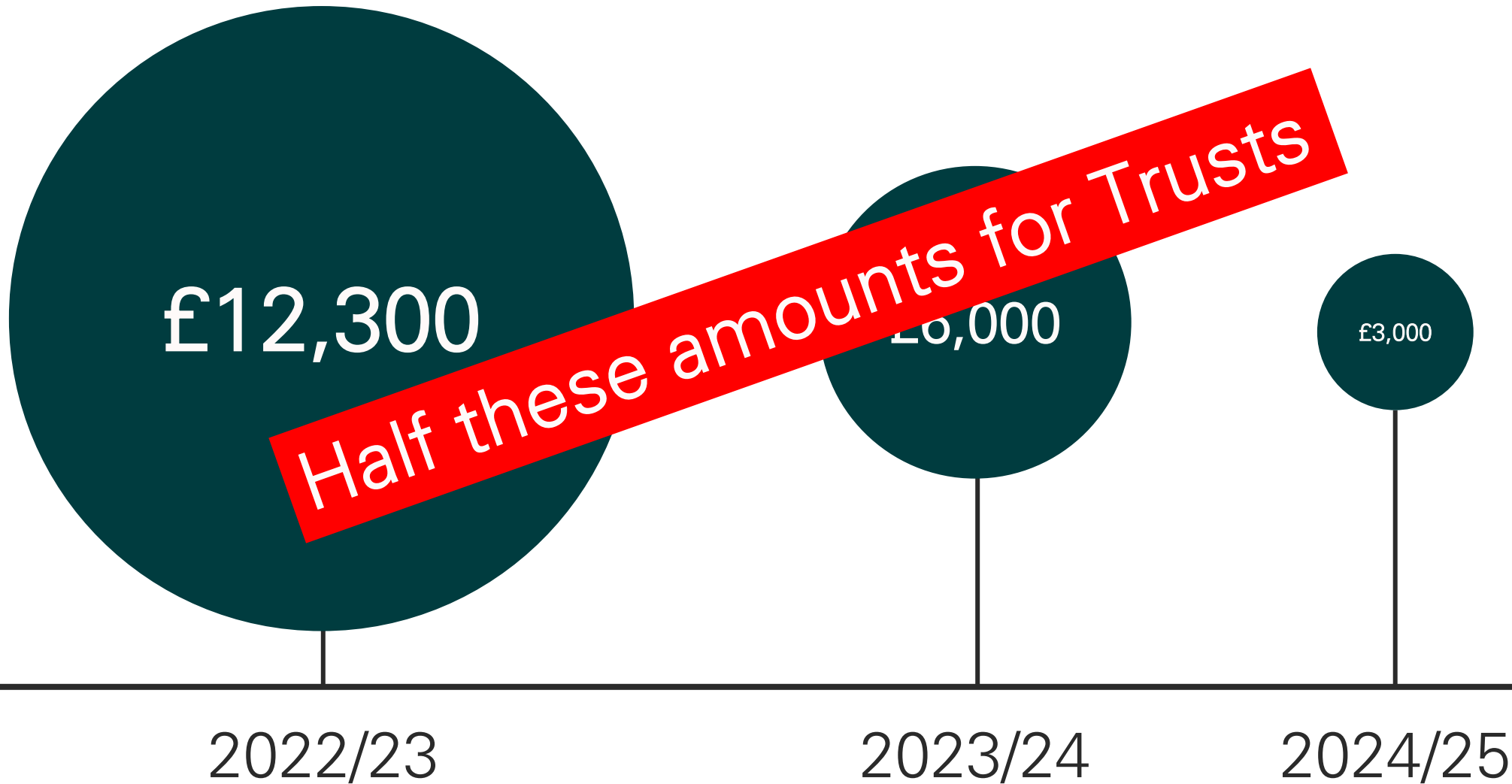
Trustees of a discretionary trust crystallise a £20,000 capital gain on disposal of an OEIC.

	£	Tax Due £
Capital Gains for tax year	20,000	
Less Annual Exempt Amount	1,500	
Taxable Gains	18,500 @ 20%	3,700
		3,700



Holdover relief is potentially available when assets are transferred out of the trust.

CGT Annual Exempt Amount





Taxation of Bond Gains

Chargeable Event Gains



Bare

Other

Chargeable Event Gains - Who is liable?

Is settlor alive and UK resident?

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graph TD; A[Is settlor alive and UK resident?] --> B["• Settlor is assessed on the gain<br/>• Top slicing relief may apply<br/>• Statutory right of recovery"]; B --- C[No? Then look to the trustees]; C --> D[Is the trust UK resident?]; D --> E["• Trustees are assessed on the gain<br/>• Trustee rates apply<br/>• Top slicing relief does not apply"];
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- Settlor is assessed on the gain
- Top slicing relief may apply
- Statutory right of recovery

No? Then look to the trustees

Is the trust UK resident?

- Trustees are assessed on the gain
- Trustee rates apply
- Top slicing relief does not apply

Is the trust UK resident?

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.

Chargeable Event Gains – Taxed on trustees

Trustees of a Discretionary Will Trust crystallise a bond gain of £100,000. How much tax will they pay?

	Bond Gain £	Tax Due £
Received	100,000	
Trustee Rate	100,000 @ 45%	45,000
		45,000



Onshore bond gains come with a 20% tax credit. Further 25% tax to pay



No 45% tax credit for the beneficiary. The tax paid is not reclaimable.



Investment Considerations

What can we buy?

5. ANY monies liable to be invested hereunder may be invested by my Trustees as if they were the absolute owners thereof

to resign office, and my Trustees shall have the fullest powers of and in regard to retention, realisation, investment, administration, management and division of the Trust Fund as if they were absolute beneficial owners; and in particular and without prejudice to these general

Power to sell or otherwise liquidate and deal with any asset whatsoever comprised in the Trust Fund and to invest in any property of whatsoever nature and wheresoever situate and whether producing income or not, including land, heritable property and investment in any policies of assurance or capital redemption policies as the Trustees may in their absolute discretion think fit

(i) to invest any money requiring investment in any property of whatever nature (including any policies of assurance or capital redemption contracts) and wherever situated whether producing income or not and upon such security (if any) as the Trustees shall in their absolute discretion think fit.

What can we buy?

7.1 The standard provisions and all of the Special Provisions of the Society of Trust and Estate Practitioners (2nd Edition) (the 'standard provisions') shall apply to this Settlement excepting paragraph 5 (trusts for sale).

Consider tax status of beneficiaries

Capital Gains

£3,000 gain within annual exempt amount

Dividend income

£500 dividends taxed at 0%

Savings income

£1,000 / £500 Personal Savings Allowance @ 0%
£5,000 starting rate taxed @ 0%

Personal allowance

£12,570 tax free income within personal allowance

Bare - considerations



Is it definitely bare??

Beneficiary probably 18

OEICs – utilise beneficiary's allowances

Bond – utilise beneficiary's allowances

Bond – offshore likely to be more appropriate

Interest in possession - considerations



Treat beneficiaries fairly!

May need income producing investments

OEICs produce income - Bonds don't

How much income is required?

Large trust fund - diversify?

Power to advance capital?

Discretionary - considerations



Undistributed income expensive

Tax returns – trustee and beneficiary

Vulnerable beneficiary? (VPE1)

£1,500 AEA

CGT – 20%

Low income/gains – OEIC?

Bonds may be appropriate

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QUESTION TIME



Thanks for your time

Get in touch with your usual contact if you need further help.





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