A SIMPLE MATTER OF TRUST?
Sept 08

You are sure to have heard of trusts and you may actually be involved with one, either as a settlor (the person who sets up a trust), a trustee or a beneficiary.

The Finance Act 2006 radically altered the way in which trusts are taxed - unsurprisingly perhaps, the basic result has been that more trusts will pay more inheritance tax ('IHT').

As a sweetener, the Government introduced a series of transitional measures which allowed trustees and beneficiaries to make tax-efficient changes to existing trusts. The deadline for those changes was originally set as 5th April 2008 but unexpectedly in the Budget 2008, it was announced that the deadline would be extended to 5th October 2008.

This means that there is still time to save tax and we can help you do so. To help you understand how, we set out some 'trust' basics and advice below.

'More trusts will pay more inheritance tax'

What is the 'relevant property regime'?

The regime involves IHT charges on setting up a trust, distributing assets and on 10-year anniversaries of the trust –essentially, more IHT is due. Traditionally, it only applied to discretionary trusts.

What does the Finance Act 2006 say?

The 'relevant property regime' is extended to apply to interest in possession trusts (broadly, where a beneficiary receives income for life) and to accumulation and maintenance trusts (a type of discretionary trust where beneficiaries are aged no older than 25). Previously, these types of trust enjoyed a favourable tax regime.

Broadly, the regime applies to all trusts set up after 22nd March 2006, with limited exceptions such as trusts for disabled persons.

How does this affect existing trusts (that is, those set up before 22nd March 2006 whether during lifetime or under a will)?

For interest in possession trusts, the favourable tax regime will continue until the death of the income beneficiary. Thereafter, if it continues, it will be subject to the 'relevant property regime'.

For accumulation and maintenance trusts, the 'relevant property regime' will apply after 5th October 2008.

What can you do to help?

For interest in possession trusts, until 5th October 2008, action can be taken to change the income beneficiary so as to allow the favourable tax regime to apply until the death of the new income beneficiary.

For accumulation and maintenance trusts, the 'relevant property regime can be avoided completely if the trust is amended so that beneficiaries become entitled to capital and income at 18 or partially avoided if the trust is amended so
that the beneficiaries become entitled to capital by 25.

'There is still time to save tax'

Does this affect my will?

Many wills do include trusts, often by choice but sometimes inadvertently. This is often the case when beneficiaries are under the age of 18 – the law will then impose a trust. The 'relevant property regime' will not apply to trusts imposed for children of the deceased.

A key concern, however, is that it will apply to trusts for any other minor beneficiaries and this includes grandchildren. The result is that additional IHT charges may apply when the beneficiaries do become entitled.

‘Wills certainly should be reviewed in light of changes’

I am involved with a trust – should I panic?

While trusts are a very useful and effective method of saving tax and achieving other objectives, it is an unfortunate fact that they are rarely simple. However, we will always give you clear focused advice to help you get the result you want.

If you or your family are involved with a trust or have a trust in your will, we strongly recommend that you have it reviewed **now**. Delay may result in your family paying more tax than is necessary.

Private Client Team