

Wills, Trusts and Probate Briefings

Trusts for children and other family

Trust basics

- trust is a flexible way for someone (the "settlor") to give away assets.
- You can set up a trust during your life, or under the terms of your will.
- Legal ownership of the assets (the trust property) passes to the trustees of the trust, who look after them in the interests of the beneficiaries.
- Trustees do not normally benefit from the trust, unless a trustee is also a beneficiary. Trustees can claim expenses from the trust and professional trustees can claim their professional charges.
- Different beneficiaries may receive different benefits from the trust: for example, one beneficiary might receive the income while another later receives the capital. The trustees have a legal duty to act fairly, balancing the interests of different beneficiaries.
- Details of how the trust operates and who the trustees and beneficiaries are should be included in a trust deed, or in your will.
- You can also prepare a letter of wishes to provide non-binding guidance to your trustees, particularly if the trust deed gives the trustees wide-ranging discretion over how the benefits are to be shared out.

Types of trust

Different types of trust can be used to achieve different goals.

- A bare trust is a simple form of trust where the beneficiary is absolutely entitled to the trust property (provided the beneficiary is 18 or over and mentally capable). Bare trusts are often used to hold investments for children.
- An interest in possession trust is one where a beneficiary is entitled to the net income of the trust - the trustees must hand over all the income after expenses and taxes. These are often used in wills, giving your spouse (or another dependent) an income for life but then leaving the assets to your children.
- A discretionary trust is one where the trustees have more discretion over how they distribute income. For example, several children might be the beneficiaries of a discretionary trust, and the trustees could provide money as they need it (eg to pay for their education).
- An accumulation and maintenance trust is a special kind of trust set up for the benefit of a group of grandchildren. These are becoming less common since changes to the tax rules eliminated their tax advantages.
- A variety of other kinds of trust can be set up for specific purposes. Flexible discretionary trusts are often the best way of achieving the desired results.

Taxation

The tax treatment varies for different types of trust. This is a complex area where you need advice on your particular circumstances.

- Income and capital gains in a bare trust are normally treated as the income and gains of the beneficiary. However, if assets provided by a parent of the beneficiary produce income of £100 or more, that income is taxed as the parent's.
- Tax rates for an income in possession trust depend on the source of the income: 22% for rents and trading income, 20% for savings income and 10% for dividends.
- Income in a discretionary trust is taxed at 40%, or 32.5% for dividends. The first £1,000 is charged at the lower rates applicable to interest in possession trusts.
- Trusts are subject to capital gains tax on any gains over their annual capital gains tax allowance.
- Beneficiaries are liable to income tax on any income they receive from the trust, but can offset the tax already paid by the trust.

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Beneficiaries are not liable for tax on distributions of trust capital.

- The inheritance tax treatment of trusts depends on the type of trust and the amounts gifted into the trust. Gifts into "relevant property trusts" (most kinds of trust) are subject to an immediate 20% IHT charge on amounts in excess of the nil rate band (£325,000 for 2009/10). There is a further 6% charge every ten years on the value of the trust's assets, with a proportionate charge on any assets withdrawn from the trust between ten-year anniversaries.
- If you die within seven years of making a gift into trust, there may be a further inheritance tax liability.
- Bereaved minor's trusts and 18-25 trusts are trusts set up under your will for the benefit of a child. These have tax advantages compared to ordinary discretionary trusts.
- There are also tax advantages to trusts set up under your will for your spouse, and to some trusts where the beneficiary is mentally or physically disabled.