

INHERITANCE TAX FOR TRUSTS

Relevant Property Inheritance Tax Regime

This regime applies to all Discretionary Trusts whenever created and most Life Interest settlements created after 22 March 2006. Where a UK domiciled settlor makes a lifetime transfer into any trust* this is a chargeable transfer for Inheritance Tax (IHT) purposes, charged at 20% (subject to Business Property Relief or Agricultural Property Relief if appropriate). Should the settlor die within 7 years of creating a trust or making additions to a trust then there may be a further IHT charge subject to taper relief. There will be exit charges when capital is appointed out of the trust, and 10 year anniversary charges. The rate of 10 year anniversary charge is currently 6% on the value of the trust assets at that date. Where the settlor is not UK domiciled, an IHT liability will apply to UK property only. Non UK assets are Excluded Property, and not subject to IHT.

* see the next section for exceptions to this rule.

***Interest in Possession Trusts created after 22 March 2006**

A Life Interest to a surviving spouse or civil partner arising under a Will or Intestacy commencing immediately on the deceased's death will result in the Life Tenant being treated as the owner of the underlying capital, and on the death of the life tenant the value of the trust will be added to the deceased's estate and IHT will be payable accordingly on the trust value.

Interest in Possession trusts which take effect on a testator's death under which the testator's minor children are immediately entitled to income (Bereaved Minors' Trusts), continue to enjoy the IHT regime as mentioned in the paragraph immediately above – i.e. the property forms part of the beneficiary's estate for IHT purposes, and there are no periodic charges or exit charges when/if the beneficiary takes the property outright. Specific rules apply to these trusts if they are to benefit from this IHT regime.

All other life interest trusts created and funded after 22 March 2006 will follow the relevant property IHT regime.

Interest in Possession Trusts created and funded up to 22 March 2006

Interest in Possession Trusts which were created and funded before 22 March 2006 will continue under the old regime until the current life tenant dies or no longer benefits.

Interest in Possession Trusts created and funded up to 22 March 2006 – (continued)

If, on the cessation of the current life interest, the capital is paid out absolutely then there is no change to the IHT regime. This means that on the death of the life tenant the whole value of the trust will be added to the beneficiary's personal estate to calculate the IHT charge due by the trust on that death.

If the trust continues, after the cessation of the current life interest it then falls within the relevant property IHT regime described above. This change may also apply to current 'excluded property' trusts in which the non domiciled settlor or his spouse or civil partner had an initial life interest, so that the trust may no longer benefit from excluded property status. The status will depend on where the life tenant is domiciled or deemed to be domiciled at the time of his/her death.

Accumulation and Maintenance (A&M) trusts.

(a) Trusts in place prior to 22 March 2006

Where children receive capital outright at age 18 the capital payment will not be subject to IHT.

Where the children become entitled to their share of capital at age 25, which is common with A&M trusts, the trust will be within a special 18-25 Discretionary Trust IHT regime from the time the beneficiary attains age 18. Therefore when capital is paid out at age 25, IHT will be payable at 4.2% on the capital appointed, (i.e. $7/10 \times 6\%$, as the payment will be made 7 years after the beneficiary attains the age of 18).

Where there is no certainty as to when the children will receive capital, the trust will, from 6 April 2008, be within the 'Relevant Property' IHT regime, as set out in the previous page 1.

(b) Trusts created on or after 22 March 2006

All A&M trusts created on or after 22 March 2006 will come within the Relevant Property IHT regime.

Tax Planning

Offshore trusts remain an extremely valuable tax and estate planning tool for non-UK domiciliaries.



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