

For financial advisers only | Bare Gift Trust

A detailed guide

Please note – this communication isn't for private customers and shouldn't be given out to, or relied on by, them.

What's a trust?

To put it simply, a trust is an arrangement to give money or assets to a third party to look after on behalf of another group of people. The people involved are:

- the trustees – the people who look after the trust fund
- the settlor – the person who gives the money or assets to the trustees
- the beneficiaries – the people who benefit from the trust fund

We offer discretionary and bare versions of certain trusts.

These trusts are similar in a lot of ways. Their basic purposes are the same:

- To reduce the amount of inheritance tax (IHT) liable on the settlor's estate.
- To give money or assets to the trustees for the benefit of selected beneficiaries.

However, there are also quite substantial differences, particularly regarding tax liabilities and how flexible the trusts are. It's important to understand these differences so that your clients can choose the trust that's right for them.

The basic differences between a discretionary trust and a bare trust are that with a bare trust are as follows:

- Adult beneficiaries over 18 in England and Wales and over 16 with a Scots law trust can demand their share of the trust assets at any time – the trustees have no control over when payments are made.
- Once the settlor has decided who the beneficiaries are going to be, they can't be changed. Their entitlements under the trust can't be changed either.

However, with a discretionary trust:

- there is a wide class of possible beneficiaries that automatically includes immediate and extended family
- no one beneficiary has any rights or entitlements to either the income or capital of the trust
- the trustees have control over the trust's assets – they decide who gets what and when
- the settlor can add other beneficiaries at any time.

This guide gives more details about the Bare Gift Trust. It should answer any questions you might have, but if you need any more information, please get in touch with your AEGON consultant.

How does the Bare Gift Trust work?

The settlor makes what's called a 'lifetime gift' to the trustees, which is a potentially exempt transfer (PET) for IHT purposes. The trustees then invest this in an AEGON bond. The settlor can also gift an existing bond to the trustees by assigning it into the trust. Any growth from this investment, from the date of the gift, won't be included in the settlor's IHT estate and, as long as the settlor lives for at least seven years from the date of the gift, the gift itself will also fall outside the IHT estate. The trustees hold the trust assets and can distribute all or part of them to the beneficiaries at any time during the trust period.

This is just a brief summary of how the Bare Gift Trust works. It's important that you read the rest of the guide, particularly the 'Taxation' section.

The settlor

Who can create the trust?

The settlor must be over 18 and of full mental capacity. For tax purposes, the settlor is regarded as anyone who provides assets to the trust either directly or indirectly. In England and Wales an attorney can't set up a trust on the settlor's behalf unless the Court of Protection approves. In Scotland it depends on the specific wording of the power of attorney whether the attorney has the authority to set up a trust.

Can there be more than one settlor for the trust?

Yes, there can be joint settlors. In this guide, references to the 'settlor' also include 'settlors'.

Can the settlor benefit from the trust fund?

No. The settlor can't, in any circumstances, benefit from the trust either directly or indirectly. The settlor has no right to either the capital of the trust or any income generated by it.

For IHT reasons, if a husband, wife or registered civil partner wants to create a trust that their spouse or registered civil partner can benefit from, and the spouse or registered civil partner also wants to set up a trust that their husband, wife or registered civil partner can benefit from, they should get legal and tax advice before setting up the trusts.

How much is taken for IHT purposes when the settlor dies?

If the settlor dies within seven years of making the gift, then it becomes part of their IHT estate and is liable for IHT. However, available reliefs could reduce the tax payable on the gift. If the settlor lives for seven years after making the gift, then its value won't be included in the settlor's estate. Any investment growth will also be left out of the estate. Please read the 'Taxation' section for more details.

Is probate needed for the trust assets when the settlor dies?

No, because the trust assets are legally owned by the trustees.

How is the trust set up?

The trust can be set up by:

■ making a cash gift to the trustees

The amount of the cash gift should be shown in the trust deed in the box titled 'Money'. The trustees will then invest in an AEGON bond to be held in the trust fund in the name of the trustees. The trust starts on the date when the cash gift is given to the trustees. This should be the date shown in the trust deed.

■ gifting an existing AEGON bond to the trustees

The details of the gifted investment should be shown in the trust deed in the box titled 'Policy(ies)'. The trust starts on the date when the gifted investment is given to the trustees. This should be the date shown in the trust deed.

The trustees

Who should be appointed as trustees?

The settlor appoints the trustees when the trust is set up. (For the purpose of this guide, the trustees are assumed to be individuals.) The settlor could be one of the trustees. The other trustees could be members of the settlor's family. It's a good idea to have at least two trustees, and it would be useful if one of these were a professional adviser such as a solicitor or an accountant. The trustees must be over 18 and of full mental capacity.

Can trustees be beneficiaries?

The trustees (but not the settlor) can be beneficiaries under the trust.

Does the settlor have the power to appoint and dismiss the trustees?

Yes. Trustees can be appointed by Deed of Appointment (or by Deed of Assumption and Conveyance in Scotland) and dismissed by Deed of Removal. Sample deeds are available from AEGON.

Can a trustee retire?

Yes, as long as:

- they give 30 days' written notice
- there's more than one trustee left – if not, a replacement trustee must be appointed before the trustee can retire
- they complete a Deed of Resignation as a Trustee – sample deeds are available from AEGON

The beneficiaries

Who are the beneficiaries?

The settlor decides on the beneficiaries and their share of the trust fund when the trust is first set up. It's very important to note that once these choices have been made, and the trust is in force, they can't be changed. This means that the settlor can't add or remove beneficiaries from the trust in any circumstances, or change the beneficiaries' shares of the trust fund.

If the settlor wants more flexibility then the Discretionary Gift Trust might be a better choice, as this lets the trustees decide which beneficiaries are to benefit, by how much and when. There are, however, important IHT differences between the Bare Gift Trust and the Discretionary Gift Trust. You should read the *Detailed guide* for the Discretionary Gift Trust before making a decision.

What entitlements do the beneficiaries have?

The beneficiaries become entitled to their shares of the income and capital of the trust fund when they're aged 18 years (16 if Scots law applies to the trust). They can demand that the trustees pay their full share at that time.

Trust flexibility

How long can the trust last?

The trust can last for up to 125 years. The trust ends when all of the trust fund has been distributed, if earlier.

What investment powers does the trust have?

The trust has very wide investment powers, meaning the trustees can invest in any AEGON bond.

Can the settlor add more investments to the trust after it has been set up?

Yes. The settlor can gift more cash into trust, which the trustees can use to buy, or top up, an AEGON bond. An existing bond can also be assigned into the trust.

Taxation

Inheritance tax – the settlor

If the settlor dies within seven years of making the gift, then the PET becomes part of their IHT estate and is therefore liable for IHT. However, this could be reduced by taper relief, depending on how long the settlor survived since the date of the gift and the amount of the gift.

If the settlor survives for a period of seven years from the date of the gift it will be excluded from their IHT estate.

Inheritance tax – the trustees

There are no inheritance tax consequences of the trust for the trustees.

Inheritance tax – the beneficiaries

Each beneficiary's share of the trust fund forms part of their IHT estate. When they die, their trust entitlement will devolve under the terms of their will or under the laws of intestacy.

Income tax – the settlor

The settlor won't be liable for income tax on any gains arising as a result of the trustees cashing in or surrendering the policy, unless the beneficiaries are the settlor's unmarried minor children and the gain is greater than £100.

Income tax – the beneficiaries

Beneficiaries will be liable for income tax on their share of the gain. The tax will be due at their own marginal rate of tax and subject to top-slicing relief, if appropriate.

Income tax – the trustees

The trustees won't be liable for income tax on a chargeable event gain.

Under HM Revenue & Customs regulations, we must send a 'chargeable event certificate' to the first named trustee, even if they have no liability for the tax. The trustees should tell the beneficiaries what their share of the gain is, as detailed above.

Capital gains tax

Investment bonds are generally exempt from capital gains tax, except where they have been acquired second hand for actual consideration.

Important note

Because the tax treatment of trusts can be complicated, a specialist tax adviser should be consulted as they can give specific advice for each client's individual circumstances. For more information about trustee investment in onshore or offshore bonds, please contact your AEGON consultant.

This guide is designed to give you some information about how the Bare Gift Trust works. You should read it together with the appropriate AEGON product brochures. It's essential that prospective users of this trust take legal and tax advice before going ahead. Accordingly, no responsibility can be taken for the legal or tax efficiency of the Bare Gift Trust in any particular jurisdiction.

This item is based on AEGON's understanding of current taxation law and practice in the United Kingdom and Republic of Ireland, as at June 2011.

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