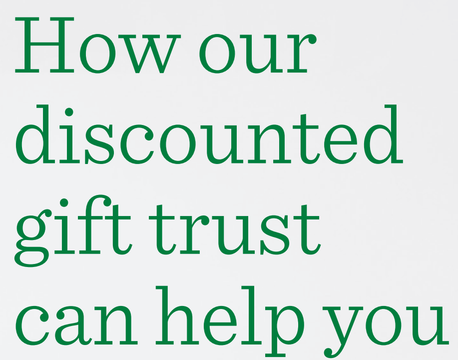
Quilter



How our discounted gift trust can help you

Reduce your potential UK inheritance tax liability

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We regularly update our literature; your financial adviser can confirm that this **October 2022** version is the latest by checking the literature library on our website

platform.quilter.com

Introduction

Inheritance tax (IHT) and the rules and regulations governing it can be complicated – just like many of the options for limiting any potential IHT bill. What may be an ideal tax-planning arrangement for one person may be wholly inappropriate for another. That is why it is essential to seek professional advice in relation to your particular circumstances and requirements.

The aim of this brochure is to give you a simple introduction to discounted gift trusts. More detailed information is covered in our discounted gift trust guides available from your financial adviser.

When we refer to Quilter, we, us and our in this document, we mean Quilter Life and Pensions Limited.

How IHT could affect you

Many people are finding themselves in the situation where the assets they leave behind on their death could be subject to IHT.

When you die, the value of the assets you own – your home, possessions, money and any investments you may have – is collectively known as your 'estate'. Currently the first £325,000 of your estate is taxed at 0% for UK IHT purposes. This is known as the nil-rate band. If the value of your estate amounts to more than your available nil-rate band then 40% tax is generally paid on the balance. Any gifts you have made in the seven years before your death may reduce your available nil-rate band.

In addition, since 6 April 2017, if you leave your home to direct lineal descendants which includes, amongst others, your children (adopted, fostered and stepchildren) and grandchildren, you may be entitled to a residence nil-rate band. This is currently £175,000 and is frozen until April 2026.

It is possible to transfer any unused nil-rate band and residence nil-rate band from a spouse or civil partner who died before you, thus giving the survivor up to twice the standard nil-rate band. However, even if you are in a position to take advantage of an increased nil-rate band, it could still leave a substantial portion of your estate subject to IHT.

So, whether your estate is currently worth more than the nil-rate bands or you think it could be in the future, you should consider some form of tax planning to reduce the potential IHT liability and, in doing so, leave more of your estate to those who you would like to benefit.

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The IHT dilemma

Perhaps the most effective way to reduce your potential IHT liability is to give your wealth away. Unfortunately few of us are able to afford to do this. We may need to live off our assets or use them to provide a regular income. Even if you give some of your assets away, but retain the option to have them back if needed, or if you continue to receive the income that the assets produce, this will still not be effective for reducing your potential IHT liability. In these situations, the assets are classed as 'gifts with reservation' and will still be included in your estate.

Fortunately there is a solution to this dilemma. This solution lets you pass on some of your wealth to future generations whilst receiving regular withdrawals from this 'gifted' capital during your lifetime (and that of anyone else's life with whom you have made the arrangement). This arrangement generally reduces the value of your estate immediately and, as a result, your potential IHT liability. It means the whole of the asset involved will not form part of your estate after seven years – the period required for gifts to be exempt from IHT.

This solution is called a discounted gift trust.

What is a trust?

Simply put, a trust allows you to transfer money or other assets to be held by your chosen trustees. The trustees manage the trust fund for the benefit of your beneficiaries.

With some careful planning, a trust can be a means of reducing or even eliminating a potential inheritance tax (IHT) bill.

Settlor

The settlor is the person who sets up the initial investment and trust. You can be a settlor either on your own (as a single settlor) or with someone else, such as a spouse or civil partner (as joint settlors). The settlor(s) transfers the ownership of the assets to their chosen trustees.

Trustees

The trustees become the legal owners of the assets once the trust has been created. They manage the assets for the benefit of the beneficiaries.

Beneficiaries

The beneficiaries are the individuals or groups of people named under the trust. These are often children or other family members. Depending upon the nature of the trust, it may also be possible to include future generations, such as grandchildren as yet unborn.

What is a Discounted Gift Trust?

A trust is a way to hold an amount of money which has been transferred outside of your estate. The amount of money which you transfer into the trust is known as the 'gift'.

Normally when making a gift into trust it would take up to seven years before it is free from inheritance tax (IHT) and you would not be able to benefit from or access the money. However, with a discounted gift trust, you and anyone else you have set the arrangement up with, if applicable, can benefit from the trust by receiving regular withdrawals.

The value of all these future withdrawals is called the 'discount'. It is calculated by Quilter, taking into account factors such as your age, health and withdrawals required.

The significance of the discount is that your estate should immediately be reduced by the calculated discount value. The discount provided by Quilter is an estimated discount, since the actual discount will need to be agreed with HM Revenue & Customs (HMRC). However, the actual discount will not be agreed until the death of the settlor.

For the discounted gift trust, we offer the Collective Investment Bond for the trustees to invest in. This brochure only provides information on the discounted gift trust. Details of the Collective Investment Bond and whether it is appropriate for your circumstances can be found in separate brochures available from your financial adviser.

Could a discounted gift trust be right for you?

Discounted gift trusts are generally designed for people who expect to have an IHT liability, the benefit being that you can receive regular withdrawals during your lifetime and that you are likely to have reduced your IHT liability by the time you die.

You would need to make a one-off investment, which should not be your only source of savings or future income.

The potential reduction in IHT liability with this type of trust is based on the fact that your access to the investment is restricted to the regular withdrawals. It is important therefore for you to decide on the level of withdrawals you will need when this arrangement is set up, as this cannot be changed at a later date even if your circumstances change. You need to be comfortable with this limited access to the money you have put under trust.

If you do not need withdrawals, or feel you may require greater access to your investment, then other IHT arrangements may be more suitable for you.

In all cases, we recommend that you seek financial advice as this is a complex area of financial planning.

What are the benefits of a discounted gift trust?

- You will normally benefit from an immediate reduction in the value of your taxable estate. This reduction is the 'discount' calculated according to your age, health and level of withdrawals required. Your financial adviser will be able to give an indication of the possible discount and provide further information on just how it is calculated.
- The remainder of your investment, the amount over and above the 'discount', will initially form part of your estate but will fall outside of your taxable estate after a period of seven years – the period required for gifts to be no longer subject to IHT.
- You can receive regular withdrawals from your investment which you can defer the start date for up to five years if you want to.
- **We offer a choice of two types of discounted gift trusts:**

  A bare trust, will give you certainty as to who will benefit following your death. You have to name the individuals who you want to benefit (the beneficiaries) when you set up the trust. This is also known as an 'absolute trust'.

  A discretionary trust, allows the trustees considerable flexibility as to who can benefit following your death. When the trust is set up, the beneficiaries will be identified as one or more 'classes' of people. A 'class' of people, for example, could be 'my grandchildren', including future grandchildren as yet unborn.
- When you die, the money can usually be paid out to your trustees to distribute to the beneficiaries quickly as there will normally be no need to apply for authority (known as probate) before the money can be distributed.

What risks should I consider?

- If you choose the **bare version** of the discounted gift trust then you will not be able to change your beneficiaries in the future under any circumstances. The trust fund will then form part of the beneficiaries' estates for IHT purposes.
- If you choose the **discretionary version** of the discounted gift trust, then the trustees will use their discretion to decide who should benefit from the trust and, whilst you can make your wishes known to them, they will ultimately decide.
- With the discretionary trust there may be immediate, ongoing and exit IHT charges. Full details can be found in **The discounted gift trust – discretionary version** available from your financial adviser.
- Although you have the right to withdrawals, if market returns are poor for a sustained period, the withdrawals could use up all the investment and any growth. The withdrawals would therefore stop. This could also happen if you, and any other person you have set the arrangement up with, live longer than originally estimated and therefore take withdrawals for a greater number of years.
- The level of your withdrawals cannot be changed once the arrangement is set up. If you anticipate that you may require greater access to the investment then a discounted gift trust may not be suitable.
- Whilst we have made every effort to ensure the estimated discount we provide you with is accurate, there is a chance that when you die your estate may not be reduced by the amount of 'discount' we estimate. This could happen if HMRC (the department of the UK Government who deal with IHT) interprets the existing legislation differently from our understanding and experience, or if they change their practices.

This brochure deals only with the IHT applicable to the discounted gift trust. Other taxes such as income tax which may apply to our investment products are addressed in the relevant product brochure available from your financial adviser.

As IHT is extremely complex, we suggest you seek expert advice from your financial adviser, and possibly your legal representative, to discuss this investment.

Case studies

The following case studies demonstrate how the two types of discounted gift trust work in practice.

Case study 1 - bare version

Mr and Mrs Watt, aged 65 and 63 respectively, two children and two grandchildren.

Assets

- **House:** £750,000
- **Antiques:** £30,000
- **Savings and investments:** £300,000

Income

- State pensions and investment income from their savings and investments

Mr and Mrs Watt's financial adviser has discussed their potential IHT problem and concluded that, although little can be done to protect the portion of their estate held in property and antiques from IHT, they could protect some of their savings and investments by passing them down to other generations.

Their adviser recommends using £200,000 from their savings and investments to set up a Collective Investment Bond to be held under a discounted gift trust.

Because they want their two grandchildren, Paul and Marcia, as their beneficiaries and no-one else, their financial adviser recommends the bare version of the trust. Mr and Mrs Watt appoint themselves, their son and their daughter as trustees.

To maintain their standard of living, they set up the trust providing withdrawals of 5% of the investment, (£10,000) a year. Based upon their age, health and level of withdrawals, the individual 'discounts' for Mr and Mrs Watt are £75,715 and £78,568 respectively. Should they both die within seven years and assuming HMRC agrees with the calculations, their beneficiaries have been saved at least £61,713 (40% IHT on the total of the two discounts of £154,283).

Case study 1

Value of estate before setting up the trust:			*Value of estate after setting up the trust:*	
House	**£750,000**	£200,000 into a discounted gift trust, set up with withdrawals of £10,000 a year, giving discounts of £75,715 and £78,568 for Mr & Mrs Watt respectively.	House	**£750,000**
Antiques	**£30,000**	→	Antiques	**£30,000**
Savings & Investments	**£300,000**		Savings & Investments	**£100,000**
Total	**£1,080,000**		Mr Watt discounted value of gift*	**£24,285**
			Mrs Watt discounted value of gift*	**£21,432**
			Total	**£925,717**

* *The discounted value of the gift will remain in the estate for a further 7 years.*

In addition, any growth that this investment generates will be outside of Mr and Mrs Watt's estate for UK IHT purposes.

Mr Watt dies eight years later. The full withdrawals of £10,000 a year continues to be paid to Mrs Watt until she dies four years after that. Between them they will have received withdrawals totalling £120,000.

As the Collective Investment Bond has been held by the trust for over seven years, the full value of the investment product is not considered part of Mrs Watt's estate and can therefore be paid to their grandchildren without liability for IHT.

Assuming their chosen funds have performed reasonably steadily over the 12 years, and the withdrawals have not reduced the original investment, then the discounted gift trust will have saved Mr and Mrs Watt's beneficiaries around £80,000 (40% IHT on the £200,000 original investment), and any growth will also be outside Mr and Mrs Watt's estate.

Discounted gift trust (bare version)

More information on this trust can be found in **The discounted gift trust – bare version** brochure available from your financial adviser.

...the discounted gift trust will have saved Mr and Mrs Watt's beneficiaries around £80,000...

Case studies

The following case studies demonstrate how the two types of discounted gift trust work in practice.

Case study 2 - discretionary version

Mr Green, aged 67, semi-retired business consultant, married twice, three children from first marriage, two from second, two grandchildren.

Assets

- **House:** £850,000
- **London apartment:** £250,000 *(let to provide income)*
- **Savings and investments:** £350,000

Income

- State pension, private pension and income from the London apartment

Mr Green realises that although the value of his assets could expose his beneficiaries to a large IHT bill when he dies, maintaining his lifestyle means he cannot afford to give substantial amounts away. He also wants to ensure that the children from both his marriages are treated equally when he dies.

Having considered Mr Green's needs, his financial adviser proposes a discretionary discounted gift trust. Because this does not oblige him to specify the names of his beneficiaries at the outset, it can be used, for example, to benefit any grandchildren as yet unborn.

It also means that he can reduce his potential IHT bill whilst still receiving regular withdrawals to supplement his income.

Mr Green is advised to invest £300,000 from his savings and investments into a Quilter Collective Investment Bond (CIB). The bond is then transferred to the trustees of the discounted gift trust. He has chosen himself and his solicitor as trustees.

Mr Green decides to request regular withdrawals of 4% of his investment, £12,000 a year.

Based upon Mr Green's age, health and level of withdrawals, the 'discount' is considered to be £158,202. Assuming HMRC agrees with the calculation, Mr Green's beneficiaries have been saved £63,280 (40% IHT on £158,202).

Case study 2

Value of estate before setting up the trust:			*Value of estate after setting up the trust:*	
House	**£850,000**	£300,000 into a discounted gift trust, set up with withdrawals of £12,000 a year, giving a discount of £158,202 →	House	**£850,000**
London apartment	**£250,000**		London apartment	**£250,000**
Savings & Investments	**£350,000**		Savings & Investments	**£50,000**
Total	**£1,450,000**		Discounted value of gift*	**£141,798**
			Total	**£1,291,798**

** The discounted value of the gift will remain in the estate for a further 7 years.*

Mr Green dies less than three years later but his estate, after agreement from HMRC, still benefits from the full £158,202 discount despite Mr Green having received less than three years of withdrawals.

The discounted gift trust has saved Mr Green's beneficiaries £63,280 in tax (40% of £158,202), assuming all the income he's received has been spent and is no longer within his estate, and any accumulated growth is completely free from IHT.

As Mr Green died within seven years of making the gift under the discounted gift trust, the discounted value of the gift will be included within the valuation of Mr Green's estate.

The proceeds from the investment product to his family from both marriages in what he considers to be a fair and equal manner. This can take account of the current family position and any requests left by Mr Green, or he may decide it is prudent to hold some funds within the trust for minors, or beneficiaries not yet born.

Discounted gift trust (discretionary version)

Discretionary trusts may incur immediate, ongoing and exit IHT charges. More information relating to these charges can be found in The discounted gift trust – discretionary version brochure available from your financial adviser.

Please note that these case studies are entirely fictional and used for illustration purposes only.

...the discounted gift trust has saved Mr Green's beneficiaries £63,280 in tax (40% of £158,202)...

This document is based on Quilter's interpretation of UK law and HM Revenue & Customs practice as at October 2022. While we believe this interpretation is correct we cannot guarantee it. Tax relief and the tax treatment of investment funds may change.

The value of any tax relief will depend on the investor's financial circumstances.

We cannot accept any responsibility for any losses or liabilities arising from action taken as a result of the information contained in this document.

Investors should be aware that the value of our investment products cannot be guaranteed as investments may fall as well as rise. Further details are available in the relevant product brochures available from your financial adviser.

All case studies are purely hypothetical.

Trust registration

A trust must register with HMRC's Trust Registration Service (TRS) if it is considered UK resident or has a UK tax liability, unless an exemption applies.

- A trust must register within 90 days of the date of the trust deed.
- The trustees must submit evidence of registration (available from the TRS) or confirm exemption from registration to Quilter within 90 days of the trust date.

Further details regarding trust registration can be found here: ***platform.quilter.com/TrustRegister***

platform.quilter.com

Please be aware that calls and electronic communications may be recorded for monitoring, regulatory and training purposes and records are available for at least five years.

Quilter is the trading name of Quilter Investment Platform Limited which provides an Individual Savings Account (ISA), Junior ISA (JISA) and Collective Investment Account (CIA) and Quilter Life & Pensions Limited which provides a Collective Retirement Account (CRA) and Collective Investment Bond (CIB).

Quilter Investment Platform Limited and Quilter Life & Pensions Limited are registered in England and Wales under numbers 1680071 and 4163431 respectively.

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