

The use of trusts continues to play an important part in tax planning for clients, despite successive governments changing the rules on how they are taxed. However, to many clients, trusts are something of a mystery. This brief guide is designed to explain the basic features of trusts and some of the words used in their connection. The information in this guide is limited to trusts set up and administered in the UK.

What is a Trust?

Put simply, a Trust is a way in which a person can give any kind of property to benefit others without them having control over what happens to that property. The terms of the Trust (which is usually set up by a trust deed during lifetime or by Will on death) will dictate who can benefit from the property transferred to it and in what circumstances – for example, children when they reach a specified age.

Definitions

- "the Settlor"* this is the person who sets the Trust up. For inheritance tax purposes, it is better if the Settlor cannot benefit from the Trust once it has been created;
- "the Trustees"* are appointed by the Settlor to look after the property that the Settlor transfers into the Trust (the Settlor may be one of them). The Trustees can be private individuals, suitable professionals (eg solicitors), or a company. Usually 2 to 4 Trustees will be appointed by the Settlor. The role of the Trustees is onerous and not to be undertaken lightly as they are responsible to the Beneficiaries for the Trust property. They must take decisions in view of what is best for the Beneficiaries, not themselves;
- "the Beneficiaries"* are the people, charity or company that can benefit from the Trust.

Basic Types of Trust

In general, although clients may come across all sorts of different names for Trusts, there are 2 main types in terms of how the Beneficiaries can benefit from them – Fixed Interest Trusts and Discretionary Trusts. The key difference between the two is that in a Fixed Interest Trust, the Settlor specifies who is to benefit from the capital and income of the Trust whereas in a Discretionary Trust, the Settlor leaves it up to the Trustees to decide how, when and which Beneficiaries (out of those specified by the Settlor) will receive any benefit from the Trust.

Why set up a Trust?

There are many reasons, including:

1. tax planning and asset protection – in the right circumstances, trusts can help clients to save tax for their families and shelter assets from means tested benefits, claims from creditors and where family members are divorcing their spouses;
2. avoidance of probate and administrative convenience – assets held in trust do not require a grant of probate for them to be dealt with when the Settlor dies, which could mean a cash saving and not having to wait some months for everything to be sorted out;
3. flexibility and control – often parents/grandparents like to provide financially for their children/grandchildren in ways which do not allow the funds to be squandered or dissipated.

Tax implications

Since 2006, a Settlor setting up a Trust in his lifetime (ie. not by his Will) will trigger an immediate inheritance tax charge at 20% on the amount by which the value of the property being transferred into the Trust exceeds his “nil rate band” of £325,000. This is subject to a very limited number of exceptions. It is therefore vitally important for you to take appropriate legal and tax advice from a suitably qualified professional before setting a Trust up. For more information on [inheritance tax, please use this link](#).

For further advice on trust issues, including the legal formalities for setting a Trust up, please contact Eddie Reynolds in the Wealth Management Team at Coffin Mew on 023 8048 3780 or by email: eddiereynolds@coffinmew.co.uk.