Adviser guide

Nucleus Bare Gift Trust

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Introduction

This document consists of five sections:

1. The Nucleus Bare Gift Trust: an overview
2. The suitability of the Nucleus Bare Gift Trust
3. The Nucleus Bare Gift Trust provisions in detail
4. The UK tax implications of the Nucleus Bare Gift Trust
5. Frequently asked questions

Please note that the term 'donor' refers to both donors in joint donor cases.

Important note

The information in this guide is based on our understanding of current law and HMRC practices.

Tax treatment depends on the individual circumstances of each client and may be subject to change in the future.

This document is provided strictly for general consideration only. Any action taken or refrained from in connection with the Nucleus Draft Bare Gift Trust must be preceded by discussion with the donor's legal and other professional advisers. Accordingly, neither Nucleus nor any associated or affiliated company nor any of their representatives, officials or employees can accept any responsibility for any loss occasioned as a result of any of the content of this guide or any use of the draft Nucleus Bare Gift Trust in any circumstances whatsoever.

1. The Nucleus Bare Gift Trust: an overview

1.1 The aim

The main aim of the draft Nucleus Bare Gift Trust is to enable a person to undertake simple but effective lifetime inheritance tax (IHT) planning. It is essential that each potential user of the draft trust should confirm with their legal and professional advisers that it is suitable for their particular purposes. The tax position of the trust is complex and depends on each individual's circumstances. Nucleus cannot provide legal, tax or investment advice and accepts no responsibility for any reliance placed on the contents of this guide.

1.2 Who is it for?

The type of investors who may be interested in using the draft Nucleus Bare Gift Trust could be:

- new investors contemplating a Nucleus General account or a Nucleus Onshore or Offshore Bond in the Nucleus wrap.
- investors already holding collectives in a Nucleus General account in the Nucleus wrap.
- persons who already hold a Nucleus Offshore Bond or a Nucleus Onshore Bond on the Nucleus wrap.

An investor using the Nucleus Bare Gift Trust is called the donor and by using the draft bare gift trust deed, the donor will be making a gift of the cash or asset(s) transferred into trust.

For a new investment, the gift is of cash and the trustees will collectively apply for the intended investment in the Nucleus wrap.

For existing investments, the ownership of the investment will be transferred to the trustees.

The trust can be used regardless of whether the gift is to be made by one individual or two jointly. For IHT purposes, each of the joint donors is then treated as a separate donor who has created a separate trust of usually half the value of the cash or investments transferred to the trust.

1.3 Tax effectiveness and flexibility

The trust is an absolute or bare trust, which means that the named beneficiary(ies) is/are entitled to the trust property absolutely. However, the beneficiaries might not be able to demand access to their assets due to them not being legally capable due to their age as they are a minor or they are mentally incapacitated.

When a donor creates a bare gift trust the gift will be a potentially exempt transfer (PET) for IHT purposes.

As the gift is a PET, then there will be no lifetime IHT charge regardless of the size of the gift and the only time there may be an IHT liability is if the donor dies within seven years of making it.

To ensure that the bare gift trust is effective for IHT purposes, only the named beneficiaries can benefit from the trust absolutely.

Please speak to a regulated tax adviser for full details of the tax implications of a Bare Gift Trust.

1.4 Avoiding probate (confirmation in Scotland)

Investments held by the trustees in a Nucleus Bare Gift Trust will not be an asset of the donor's estate for probate purposes. This means that, when the donor dies, the trustees can carry on dealing with the investment without waiting for probate on the donor's estate.

To ensure that this is possible, there must be at least one trustee who survives the donor. Under the Nucleus Bare Gift Trust the donor is automatically one of the trustees and further trustees are appointed in the trust deed. If any of the additional trustees retires or dies before the donor a replacement trustee should be appointed.

It is important that additional trustees are appointed who are likely to survive the donor to make sure that any delays in being able to deal with the trust investments are avoided.

2. The suitability of the Nucleus Bare Gift Trust

2.1 Suitability

The Bare Gift Trust may be suitable for an investor who:

- would like to make a gift of existing investments in the Nucleus General Account or a Nucleus Onshore or Offshore Bond in the Nucleus wrap, or cash intended for a new investment in the Nucleus wrap.
- would like to make an outright gift which is potentially exempt from IHT
- knows who they want to benefit and by how much from the outset
- understands that they will not be able to benefit from the investment under any circumstances.
- would like the benefits of the investment to be outside their estate for probate purposes when they die.

The Bare Gift Trust is not suitable where:

- an investor requires some beneficial access to the investment.
- would like discretion on who benefits, when and by how much.

2.2 Matters to consider before establishing the trust

The Bare Gift Trust is suitable for cash or investments owned by one person or jointly, where the owner(s), after discussion with their legal and/or other professional advisers, are happy that the legal and tax implications of the trust are suitable for them and the trust will help them to achieve their objectives.

In particular, the potential donor(s) should understand that when a gift is made into a bare trust, neither the beneficiary nor their share, if more than one, can be changed.

Donors should also speak to their tax adviser about the implications of setting up a bare trust and parental settlement rules to see if this applies.

Before recommending the Nucleus Bare Gift Trust, it is important for the adviser to determine:

- the potential IHT liability on the investor's estate (including the history of previous gifts) if no action is taken.
- the practical objectives of the investor, including whether any flexibility is required as to who the potential beneficiaries should be.
- that the donor is happy to give up all future access to the investment.
- that the donor will never want to change their mind about their choice of the beneficiary or how much the beneficiary should receive and when.

3. The Nucleus Bare Gift Trust provisions in detail

The draft Nucleus Bare Gift Trust provides that the beneficiary named in the trust deed is entitled absolutely to both the income and capital of the trust. If there is more than one beneficiary named, they benefit in the shares specified in the trust deed. Neither the beneficiaries or their entitlements can be changed.

The following is a summary of the key provisions as they appear in the draft Nucleus Bare Gift Trust.

Please speak to a regulated tax adviser about the implications of setting up a bare trust and parental settlement rules to see if this applies.

Part 1 – Execution of the trust deed

The trust deed, if thought to be suitable, would be executed by the donor and the named additional trustees.

The trust applies alternative provisions depending on whether a new investment is contemplated or an existing investment is being transferred to the trustees.

The donor also chooses the name for their trust.

Part 2 – Definitions

Here, the trust terms used throughout the trust are defined to avoid repetition. The most important definitions are those of the beneficiaries.

The beneficiaries are the individual(s) who are named by the donor in the trust deed at outset. At least one person must always be named and, if more than one is named, the shares in which they are to benefit must be stated.

Part 3 – The main trust terms

This part provides that the beneficiary(ies) is/are absolutely entitled to the trust capital and income. Where the beneficiaries are minors, under the age of 18 (16 in Scotland), the trustees are also given powers to use the trust income (if any arises) and capital for the beneficiary's maintenance, education or benefit. When a beneficiary reaches the age of full legal capacity, they will be able to take control of their share of the trust fund.

Part 4 – Trustees' administrative powers

The trustees have wide administrative powers to deal with the trust fund and to reinvest the proceeds of any investment in any way they wish. They also have the power to borrow funds, to make payments to parents or guardians of minor beneficiaries and to delegate certain powers.

The exercise by the trustees of their powers requires the consent of the beneficiary who is over the age of legal capacity and otherwise capable.

Part 5 – Appointment, dismissal, retirement and remuneration of trustees

The power to appoint new or additional trustees is vested in the appointor, i.e. the donor(s) during their lifetime so long as they have full mental capacity and after their death, in the trustees. The donor, whilst alive and of full mental capacity, also has power to dismiss any trustee provided at least one trustee other than the donor and/or spouse/civil partner remains after such a dismissal.

After the death or loss of capacity of the donor, if any trustee loses mental capacity, they can be dismissed by the majority of the other trustees. In all other cases, trustees under an English trust must act unanimously.

If two people are joint donors, they exercise their powers jointly during their joint lives and after the death or mental incapacity of the first of them, the survivor exercises the donors' powers alone.

There are also powers dealing with the retirement of trustees and corporate trustees.

Trustees who act in their professional capacity are entitled to charge fees.

Part 6 – Further trust provisions

These mainly deal with the trustees' liability.

The liability of individual trustees is limited so that they will not be held liable for any loss to the trust fund provided they act in good faith. Trustees who are paid for their services are also liable for negligence.

Part 7 – Proper law

The draft trust deed specifies that the trust will be governed by the laws of England and Wales. If the donor wishes to have the laws of Scotland or Northern Ireland applying then they should seek legal advice about getting a bespoke trust deed created to suit their circumstances and the implications of this.

The schedule

The asset being transferred to the trust is identified in the schedule.

4. The UK tax implications of the Nucleus Bare Gift Trust

In what follows it is assumed that the donor, the beneficiary(ies) and the trustees of the trust are all UK resident and domiciled. Special rules apply where this is not the case and in these cases specialist advice must be sought.

4.1 Inheritance tax (IHT)

4.1.1 Establishing the trust

For IHT purposes a transfer of value (a gift) takes place at the time the trust is created.

Where there are two donors, each is normally treated as making an individual gift and this is usually half of the value gifted unless otherwise stated.

The value of the gift will be the value of the assets in the general account or the value of the bond that is or are made subject to the trust at the time of the gift. For new investments it will be the amount invested.

To the extent the gift exceeds the donor's available annual exemption, currently £3,000 for each donor (£6,000 maximum for each donor if the exemption for the previous tax year has not been used), it will be a PET. This means that, regardless of the amount of the transfer, no tax liability will arise at the time of the transfer.

A tax liability on the gift could only arise if the donor dies within seven years of making the gift. If this occurs, the value of the original gift will also be taken into account in determining the IHT liability on the donor's estate under the order of gifting rules.

4.1.2 Does HMRC need to be informed about the bare gift trust?

All UK express trusts, unless specifically excluded need to be registered on the Trust Registration Service (TRS). It is the responsibility of the trustees to ensure the trust is registered correctly and the record is kept up to date. If the trustees need assistance on this matter they need to seek advice, Nucleus cannot assist them with this.

The reporting of the income and gains of the trust via the beneficiary's or the parental donor's annual tax return (where relevant) also applies.

4.1.3 What are the IHT implications of the death of the beneficiary?

The beneficiary(ies) is/are treated as owning the trust property for IHT purposes.

On the death of a beneficiary the value of the beneficiary's underlying interest in the trust property will be included in their estate.

4.2 Income tax

The income tax implications of the bare gift trust depend on the assets held by the trustees as trust property.

4.2.1 UK and offshore investment bonds

If an existing UK or offshore bond is assigned by way of gift to the trustees, this will not be a chargeable event unless it is for money/money's worth.

When a UK or offshore bond held subject to a bare gift trust is encashed (fully or partially), a chargeable event gain can arise that will be subject to income tax.

With a bare trust, the chargeable event gains will normally be assessed on the beneficiary(ies). The exception to this applies when parental settlement rules apply. In those cases chargeable event gains will be assessed on the parent.

A basic rate tax credit will apply if the bond is a Nucleus Onshore Bond. Tax may be due if the beneficiary (or the parental donor) is a higher rate or additional rate taxpayer. This credit will not be available for gains made under offshore bonds.

Please refer to the relevant Nucleus Onshore and Offshore Bond literature for further details of the taxation of onshore and offshore bonds.

4.2.2 Offshore non-reporting funds

The transfer of the investment to the bare gift trust will be a disposal. If the investment has increased in value, and if a gain arises using CGT principles, this will give rise to an offshore income gain. This will be charged to income tax on the donor.

On disposal of the asset by the trustees, they should seek advice from their tax advisers as to how this will be taxed, which taxes apply and who will be responsible for this during the lifetime of the beneficiary (ies) and on their death.

4.2.3 Collective investments (UK and offshore reporting funds)

Income tax will be due on income arising from investments in collectives. This will apply to both accumulated and distributed income.

If parental settlement rules apply, the tax will be on the parents. The £100 limit applies per parent donor per child.

In all other cases, all trust income will be assessed on the beneficiary who may have tax allowances available to offset against this income. They should seek tax advice to see how this income will be taxed and how to report it.

4.3 Capital gains tax

4.3.1 Creation of the trust

When collectives in the Nucleus General account are transferred to the bare trust this will be a disposal for CGT purposes, made at the market value of the investments transferred to the trustees on the date they are transferred. Any gain will be calculated in the usual way after utilising the donor's available annual exemption and taxed at 18% or 24%, unless the collective is an offshore non-reporting fund, in which case the gain (without the benefit of the annual exemption) will be taxed as the donor's income.

4.3.2 Trust capital gains

For CGT purposes all capital gains arising when the trustees sell shares or units in collectives are assessed on the beneficiaries. Each beneficiary is entitled to a CGT annual exemption before any tax is actually payable. Subject to the special rules for offshore non-reporting funds the death of a beneficiary will cause the revaluation of the collective for CGT purposes but with no liability to tax arising.

Please seek tax advice to understand the full implications of how holding certain assets within this type of trust are taxed, which taxes are applicable and who is liable.

5. Frequently asked questions

Who can be a trustee of the bare gift trust?

The donor will automatically be a trustee. Additional trustees must be appointed. Anyone aged 18 or over and of sound mind may be appointed. It may be appropriate to appoint a professional adviser, such as a solicitor or accountant, as a trustee, although such a person is likely to charge a fee for acting as trustee. It is essential that at least one additional trustee survives the donor if the need for probate is to be avoided following the donor's death to determine who the successor trustee will be.

Is the bare gift trust available for joint donors?

Yes, but only where the couple are married or registered civil partners. In those circumstances the funds for investment must come out of a joint account or the donors must already jointly hold a Nucleus General account or a Nucleus Onshore or Offshore Bond.

Each will normally be treated as gifting 50% of the assets, unless otherwise stated.

What is the role of the nominee company and why is the notice of trust necessary?

The nominee company holds the legal title to the collectives held in the general account. The notice of trust applies only to collectives held in a general account. As the underlying investments of the general account (i.e. shares and units in collectives) are held in the name of the nominee (as the 'legal owner'), the investor holds a 'beneficial title' to those assets and it is this beneficial title that the donor transfers to the trustees. In order to perfect the gift, the donor must also instruct the nominee company to re-register the beneficial title in the name of the trustees. This is done by giving the 'notice of trust and direction to the nominee' to the nominee company. A form of words to effect this is included in the trust deed and takes effect when the trust deed is sent to Nucleus.

Can the trustees encash investments held in the Nucleus wrap and pay the proceeds to the beneficiaries?

Yes, but if the beneficiary is a minor, the payment will normally be made to the parent or guardian of the child to use for the child's benefit.

For new investments, can the donor get their money back under the cooling off rules?

No. As the application for the investment, be it a bond or general account, will be made by the trustees, if they exercise their right to cancel, the refund (which may be less than the amount invested) will be sent to the trustees. For full details of the cooling off procedure please refer to the relevant product literature.

How do the trustees find cash to pay the fees of their investment advisers?

The fee for the initial advice (leading to the investment and the trust creation) will be paid by the donor.

The responsibility for adviser charges made in relation to the trust and trustee investments after its creation will usually be that of the trustees of the trust. As a matter of trust law, such fees are normally paid out of trust capital (not the trust income).

If there is available uninvested cash (that is not the trust income) in the General account then the adviser charges can be paid from that. If none available, the trustees may have to sell some of the shares/units of the collectives in the General account to raise the necessary cash. If the underlying investment is a bond, the trustees may need to take a part-withdrawal to meet the adviser charges. Either action could give rise to a tax charge and advice should be sought before proceeding.

Alternatively, the donor may offer to pay the advisers' fees so as not to deplete the trust funds. In such circumstances, as the donor will, in effect, pay the fees on behalf of the trustees, any such payments will be treated as further gifts made by the donor which may have IHT consequences, and advice should be sought prior to doing so.

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