

## TRUST NEWS

Welcome to the latest edition of Trust News. Trust tax continues to be a complex area and missing out on valuable reliefs can be expensive. As you will see in the following articles it is important to get the detail right. The new penalty regime for late filing of returns will be extended to Inheritance Tax from 2012 so it is important for trustees to keep on top of their compliance obligations . . . the details of the new regime are given below.

Please feel free to pass on Trust News to anyone to whom it may be of interest. Please contact me or your usual Creaseys contact if any of the articles are of interest or if you have any questions relating to trusts or other tax issues.

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### Will your trust pay 10% ... or 28% CGT?

Since 22 June 2010, the normal CGT rate of individuals and trusts has been 28% although for some, subject to stringent conditions, the rate may be 10% if Entrepreneurs Relief is available. Some key points to bear in mind are as follows:

- Discretionary trusts and estates of deceased persons will never get the benefit of Entrepreneur Relief and hence will pay CGT at 28%.
- Consideration therefore needs to be given to discretionary trusts changing their status to life interest trusts to get the benefit of 10% CGT in certain circumstances.
- Estates of deceased persons might look to distribute shares prior to any disposal so as to maximise the possibility of a 10% rate.
- Trusts may look to change the nature of their property arrangements such that a business is being carried on so that on a sale of the land or buildings, a 10% rate will be available.

It should be noted that even if a discretionary trust changes its status to life interest, it is normally necessary for the life tenant (person entitled to income) to have an interest in the shares or other asset concerned also.

Contact us for a review of your Trust's entitlement to the 10% rate ...

### Trusts to buy houses

We have seen many clients look to help their children buy properties and to protect the family's interests. This may usefully be accomplished through the use of a trust. With appropriate planning the trust can buy the property in question and allow the children to live there rent free. The property can be sold tax free in the normal way due to the main residence exemption and the parents can keep control of the situation through being trustees of the trust concerned and thus ensuring the property is not sold or badly maintained. Such a trust can also be beneficial from an Inheritance Tax angle in reducing the value of the parents' estates.

Such a trust is straightforward to set up and we can liaise with your lawyers on this or suggest a specialist firm should you wish.

### Avoiding a *double tax charge*

Many individuals like to provide for their families by way of a will trust. This allows the family to benefit from the assets but ensures that they are protected for future generations. A typical arrangement would be where a father leaves a gift on trust to his son for life, which passes to his grandchildren on his son's death.

This gift would be chargeable to Inheritance Tax both on the father's death and the son's death. In order to avoid the second tax charge on the son's death, the life interest would usually pass to the daughter-in-law and shortly thereafter the trustees would revoke the daughter-in-law's interest in favour of the children.

Prior to 2006, the effect of this was that there would be no Inheritance Tax on the death of the son, provided he is survived by his wife, and provided the daughter-in-law survives at least seven years from the date the interest passes onto the children.

This arrangement became *ineffective* after the changes to the Inheritance Tax rules for trusts in 2006.

It is however still possible to achieve the same effect by making some changes to the terms of the trust.

If your will includes a trust which is intended to last for more than one generation, it is advisable that you review the terms to ensure that any future Inheritance Tax is minimised. We will of course be happy to help you with this.

### Avoid the Inheritance Tax entry charge

One of the major barriers to setting up trusts during one's lifetime is the Inheritance Tax entry charge. This charge applies where an individual puts funds into trust that exceed the nil rate band. The nil rate band is currently

£325,000 and anything put into trust in excess of this is charged to tax at 20%.

For example, If Mrs White sets up a trust for her grandchildren with £400,000, she will pay inheritance tax of £15,000.

For this reason, many trusts are established with funds of under £325,000. The nil rate band effectively 'renews' itself every seven years, so once it has been used, any further transfers into a trust in the next seven years will be subject to the 20% tax charge.

However, the tax charge does not apply when transfers into the trust form part of 'normal expenditure out of income'.

This exemption applies if an individual routinely makes gifts out of their income and these gifts leave them with sufficient income to maintain their usual standard of living.

#### *Example:*

*If Mrs White has pension and investment income of £50,000 and usually spends £35,000 of this income, she could transfer £15,000 a year into the trust. If she initially sets up the trust with a lump sum of £325,000 and then transfers £15,000 a year into the trust, she achieves her aim of establishing the trust but with no Inheritance Tax charges.*

This is a valuable exemption which, when used over a number of years, can have a significant impact on Inheritance Tax liabilities. As such, H M Revenue & Customs are keen to ensure that the rules of the exemption are complied with before allowing the exemption. It is therefore important to keep the correct records. We will be happy to advise you on how to calculate and record your surplus income.

### Unfortunate consequences

For many years trustees may have believed that if they made decisions which turned out to have unfortunate tax consequences they could be saved by the so-called 'rule in Hastings-Bass'.

The rule generally allowed actions taken by trustees to be set aside if there were unforeseen consequences which, had the

trustees known about them, would have meant that they would not have taken those actions.

Two recent cases have however confirmed that this rule has been applied far too widely in the past.

The upshot is that if trustees make a decision which has an unforeseen tax consequence they are likely to be stuck with it.

The need for trustees to take timely, credible advice is therefore more important than ever.

Our Private Client team has a wealth of experience in advising trustees and we are always happy to advise trustees on decisions which may affect tax, however large or small.

### Increased penalties for inheritance tax returns

Penalties for incorrect Inheritance Tax returns are already in place. Executors and trustees are required to take reasonable care when preparing an account.

If reasonable care is not taken, penalties will be imposed. The penalty is a percentage of any additional tax payable as a result of the discovery of the error. The penalty ranges are as follows:-

	<b>Prompted</b>	<b>Unprompted</b>
Careless	0-30%	15-30%
Deliberate	20-70%	35-70%
Deliberate & concealed	30-100%	50-100%

A failure to take reasonable care would be, for example, not obtaining a professional valuation of a property. Including a valuation you know to be incorrect will be a deliberate error.

From 6 April 2012 there will also be new penalties for filing an inheritance account late. Generally, the filing deadline is twelve months after the chargeable event, but the tax will generally be payable six months after the event.

The late filing penalties will be as follows:-

One day late	£100
Three months late	£10 per day, up to max. £900
Six months late	Greater of 5% of the tax or £300
Twelve months late	Greater of 5% of the tax or £300.

The main events on which trustees will be required to submit an Inheritance Tax account are on each 10 year anniversary of the commencement of a trust and at any time when a beneficiary receives capital from a trust.

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