

## **Bonds & Trusts**

### **Using an Investment Bond as the trust asset**

In principle any kind of investment could be left subject to the Will Trust. However, where investments generating income, such as unit trusts or shares, pass to a trust this may create increased administration and a potential tax liability for the trustees. For this reason non-income and non-capital gains producing assets, such as single premium life assurance bonds, are particularly attractive as investments many trusts.

In such circumstances each of a husband and wife or civil partner will effect a bond in their sole ownership on a joint lives last survivor basis on the lives of husband and wife and possibly another person. This is to ensure that the bond owned by the first spouse to die can be left, subject to their Will, without the bond automatically encashing on the first death.

The tax advantages:

- A tax-sheltered investment while the bond remains in force.
- Full access to the benefits of the bond during the investor's lifetime. If necessary, they can fully encash the bond at any time.
- The ability for the investor to take tax efficient part surrenders during their lifetime, so long as those surrenders are within the 5% allowances.
- Control over income tax charges on encashment of the bond.
- The reduction in the potential IHT bill on the second death of a husband and wife.

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### **Loan Trust - Summary**

This type of arrangement is useful in containing the growth in your potential estate. The liability to Inheritance Tax does not remain static during your lifetime and will increase if the value of your assets, such as your house or investments, increases.

With a Loan Trust you place a sum, for example £100,000, into a loan scheme which is available from an Insurance Company. The trustees invest the money into a single premium investment bond with the objective of securing capital growth for the future. The initial investment (loan) remains an asset of your estate and it can be repaid to you on demand at any time. The initial investment (loan) remains in your estate. However, if the regular withdrawals are spent or gifted within the annual exemptions, the reducing loan will reduce your taxable estate. I.e. if you take income withdrawals at 5% per annum then 100% of your initial investment will be outside of your estate after 20 years.

Importantly, the capital growth on the investment bond is outside your estate from inception. This would prevent this part of your estate from growing in value and adding to your Inheritance Tax liability.

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### **Discounted Gift Schemes**

This type of scheme is particularly useful where you wish to reduce your estate potentially subject to Inheritance Tax immediately and you require a regular income from your capital.

Essentially, you invest a lump sum of say £100,000 in a Discounted Gift Scheme available from an Insurance Company. You retain the right to a regular stream of capital payments for example 5% per annum of the amount invested for the rest of your life.

At the outset you appoint trustees and beneficiaries. Part of the sum invested falls out of your estate immediately. This is called the discounted part. The amount of the discount depends upon the amount invested, the income level chosen and your expected lifespan.

The trustees hold the remaining part on behalf of the beneficiaries and this is the gift.

**\*By utilising the correct trust arrangement you will not incur the tax charges discussed below for amounts in excess of £285,000. This is a specialist area of financial planning and advice should be sought from an IFA who is an expert in this field.**

In some circumstances the gift is a chargeable transfer and if it exceeds your available nil rate band, there will be an immediate Inheritance Tax charge of 20% and so gifts that cause the nil rate band to be exceeded should not be made\*.

The taxation of trusts used for Inheritance Tax planning was subject to considerable change in the 2006 Budget. These changes mean that an inheritance tax charge can arise every 10 years or when capital is transferred out of the trust. However the maximum tax charge will be at 6% and frequently it will be much less or even nil.

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