Webinar

Trustee investments

Nottingham Insurance Institute – CPD event

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ican Technical Services

Learning objectives

By the end of this session you will understand:

- The responsibilities of trustees
- The relevant Acts that trustees can turn to when their trust deed is silent
- What to consider in a trust review
- Things that we have learned from existing cases that have come through the courts
- Considerations when looking at existing trusts
- Considerations when looking to move trust investments
- How trusts are taxed:
  - Discretionary trusts
  - Interest in possession trusts
  - Bare/Absolute trusts

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Trustee investments

- Trustee responsibilities
- Existing case law examples
- Existing trusts – what to look at
- Moving investments within a trust
- Trusts and their taxation

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Trustee responsibilities

Trustee responsibilities

Trustees have a duty to:

- act honestly and with prudence
- try to maximise return on trust fund
- not risk the trust fund in hazardous and speculative investments

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Trustee responsibilities

Comply with

Trustee Act 2000

covers England and Wales

Charities & Trustee Investment (Scotland) Act 2005

covers Scotland

Trustee Act (Northern Ireland) 2001

covers Northern Ireland

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Trustee Act 2000

Statutory duty of care

Previously

'Ordinary prudent man'

Now

'Trustees must show such skill as is reasonable in circumstances allowing for special knowledge, experience or professional status'

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Trustee Act 2000

Section 4(3)

'standard investment criteria' – suitable/diversification

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Standard investment criteria

the suitability to the trust of investments…

and the need for diversification…

Suitability relates to the type and features of the investment:

- taxation
- size and risk profile of the investment
- attention given to diversification as a means of risk control
- if needed, balance between income and growth
- if needed, ethical considerations

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Trustee Act 2000

Section 5(1)

'must... obtain and consider proper advice'

Section 5(2)

similarly when reviewing

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Reviews – regular

- Is the investment wrapper still appropriate?
- Are the investment funds still appropriate?
- Have there been any changes in tax rates?
- Have there been any changes in legislation?
- Can costs be reduced?
- Do you have a clear audit trail ? IMPORTANT

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Trustee Act 2000

Section 5(4)

proper advice

‘... of a person who is reasonably believed… to be qualified to give it by his ability in, and practical experience of, financial matters’

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Trustee investments

- The Solicitors Regulation Authority (SRA) – the regulatory arm of the Law Society – issued guidance to its members in 2009
- “Firms must always act in the best interests of their clients. This means that they must refer clients to **independent** financial advisers for investment advice”
- **From January 2013 the SRA have allowed solicitors to make referrals to restricted financial advisers**
- The SRA's caveat is that solicitors' clients need to be 'in a position to make informed decisions about how to pursue the matter'. Solicitors will have to satisfy not only themselves but also their clients that any referral will be in their clients' best interests.

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Opportunities with solicitors

- Do they currently offer a trustee service?
- Does this include regular investment review process?
- Does it fit with Trustee Act 2000?
- Would they prefer to outsource?

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Mutual benefit

- **Article in STEP Journal, August 2009**
  - '... one of the most valuable relationships I have nurtured is with our Independent Financial Advisor (IFA) team.'
  - www.step.org/mutual-benefit
- **Reproduced in New Model Adviser, January 2010**
  - Retitled as: 'A two-way street: Why gatekeepers need advisers too'
  - http://citywire.co.uk/new-model-adviser/news/a-two-way-street-why-gatekeepers-need-advisers-too/a374246

STEP
ADVISING FAMILIES ACROSS GENERATIONS

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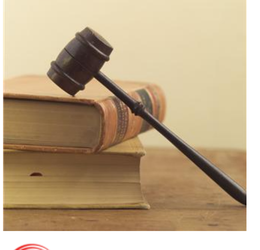
Existing case law

Existing case law

- **Nestle v National Westminster Bank plc (1993)**
  - Need to review periodically
  - Need to ensure fairness between beneficiaries



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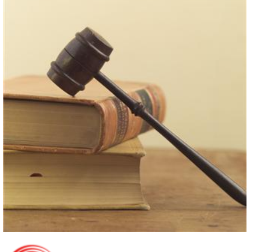
Existing case law

Hurlingham Estates Ltd v Wilde & Partners (1997)

Court held that a professional was expected to be aware of, and alert clients to, tax considerations impacting his advice



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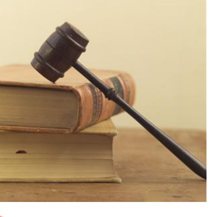
Existing case law

Jones v Firkin-Flood (2008)

- failure to have meetings to discuss matter (Court suggested that most trusts would require at least one meeting a year)
- failure of the solicitor trustee (the only professional trustee) to provide suitable investment advice
- unconscious bias in favour of one beneficiary
  (when it is a duty of the trustees to treat all beneficiaries fairly)
- failure to pay trust income as required under the trust
- failure to draw up trust account



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Existing trusts – what to look at

Existing trusts – what to look at

- What sort of trust is it?
- What are its apparent objectives?
- Income/capital appreciation – both?
- How are returns taxed?
- How would beneficiaries be taxed?
- Are there any investment restrictions/requirements?

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Considerations when choosing trust investments

- Investment criteria – suitability and diversification
- Time horizon
- Income requirement
- Immediate tax impact
- Tax returns
- Eventual tax

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Moving investments within a trust

Changing trust investments

- Investment criteria – suitability and diversification
- Justification
- Tax impact
- Tax returns

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Trusts and their taxation

Discretionary trusts

Income tax

First £1,000 income* each tax year is liable to basic rate tax (20% on savings/other income and 7.5% on dividends)

The trust rate for income above £1,000 is 45%

The trust rate on dividends is 38.1%

* £1,000 is shared among all discretionary trusts a settlor has in any particular year, down to a minimum of one fifth

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Discretionary trusts

Capital Gains Tax (CGT)

CGT rate for trustees – currently 20%*

Maximum** annual exemption for trusts = half annual exemption for individuals (£6,150 – 2020/21)

* Rate for residential property not eligible for Private Residence Relief is 28%

** The current trust annual exemption will be shared among all trusts in a particular tax year down to a minimum of one fifth – so if a settlor has five, each trust would claim £1,230 annual exemption

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Discretionary trusts

- **Inheritance tax (IHT)**
- Entry charge – 20% on excess above current nil rate band (NRB) (£325,000 – frozen until 5 April 2021)
- Cumulative – so add back in any other chargeable lifetime transfers (CLTs) done in last seven years
- Exit charge – on property leaving the trust. Will apply if there was an entry charge at inception / or if there is a periodic charge at tenth anniversary
- Periodic charge calculation on every tenth anniversary – maximum 6% on excess above available NRB

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Investment bonds in trust: chargeable event gains

- Assessed on settlor if alive and UK resident for all trusts other than non-parental absolute trusts
- If not, then on UK trustees at Rate Applicable to Trusts (RAT)
- Opportunity to assign to adult beneficiary
- If the settlor is dead/non-UK resident and trustees are not in UK then on UK beneficiaries who actually benefit

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Discretionary trust investment example: UK equities

	2020/21 position
Dividend received by trustees	**£800.00**
RAT at 38.1%*	**£304.80**
Amount available to trust	**£495.20**

* Assumes standard rate band used by other income

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Discretionary trust investment example: UK equities

	2020/21 position
Amount available to trust	**£495.20**
If trustees distribute, it has to have suffered 45%	
Additional rate taxpayer gets	**£440.00**

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Discretionary trust investment example:

	2020/21 position
Bond withdrawal received by trustees	**£800.00**
Amount of income tax?	**0 to 45%**

Assign segment(s) to adults

Appoint segment(s) to minors (where the parent isn't the settlor)

Take withdrawals within available 5% annual allowance

If settlor alive – based on their marginal rates

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Trusts with an interest in possession

Income tax

Tax on savings and other income is at 20%. Tax on dividends at 7.5%.

Trustees not liable to higher rate tax or additional rate tax (40%/45% 2020/21), although beneficiaries may be personally liable for higher rates on any trust income they are entitled to

If beneficiaries are non-taxpayers they can offset their own personal allowance first

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Trusts with an interest in possession

Capital Gains tax

Trustees usually have to pay Capital Gains tax when an asset held within the trust is sold or passed on to a beneficiary

The main exception to this is when the trustees apply for ‘hold-over relief' to defer payment of Capital Gains tax to the person who receives the asset

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Trusts with an interest in possession

Inheritance tax

Any interest in possession (IIP) trusts which commenced after 22 March 2006 are classed as relevant property and will be treated the same as discretionary trusts

With the exception of IPDIs (immediate post-death interests)

Any IIP trusts commenced before 22 March 2006 need to be looked at carefully as different rules apply

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Bare trusts

Income tax

- income belongs to beneficiary
- taxed at beneficiary’s rates
- personal allowance of beneficiary can be used

Where parent gifts money to unmarried, minor children, income (including chargeable event gains) normally taxed as parent’s income (£100 rule)

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Bare trusts

Capital Gains tax

- gains belong to beneficiary
- taxed at beneficiary's rates (10% or 20%)
- annual allowance of beneficiary can be used (£12,300 instead of trust maximum of £6,150 – 2020/21)

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Bare trusts

Inheritance tax

- As the beneficiary is absolutely entitled to the trust proceeds, the value would be included in the beneficiary's estate if they died before they actually received the benefits

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Discretionary trust created by Deed of Variation

If the trust assets are invested in collectives, how are they taxed?

- the income is assessable on the settlor*

Genuine and compelling reason to consider non income producing assets to avoid settlor interested provisions (RAT at 45% /38.1% won't apply for the time being)

*The settlor of a trust created by deed is not the deceased, but the person who was entitled to the gift prior to it going into trust

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Other strategies for trustees to consider

Investment bonds

- Greater tax deferment
- Ability to assign or appoint to low taxpayers

Convert discretionary trust into interest in possession trust

Convert discretionary into absolute trust

Consider distribution of assets sooner

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Summary

Opportunities to revisit existing trusts

On a regular basis

Excellent discussion area for professional connections

Integrated independent advice critical

Happy to assist

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