



2 October 2008

Trusts – Serial Life Interests: 5 October 2008 deadline

The government introduced significant changes to the trust tax legislation in March 2006.

Under the pre-existing trust tax legislation, if a trust was created prior to 22 March 2006 in which one or more people have a 'life interest', the person(s) with the life interest was treated as if they owned the trust assets directly for Inheritance tax (IHT) purposes. The consequence of this is that trust assets are accumulated with personal assets when calculating the IHT payable on death. Following the Finance Act 2006, all transfers of value after 22 March 2006 (except absolute gifts), are chargeable to IHT on any excess over the available nil rate-band (£312,000 for 2008/09) at the lifetime rate of 20%.

However, there is transitional relief available whereby the life interest can be transferred to someone else without incurring an immediate charge to IHT at 20%.

The deadline for the execution of such a transfer is 5 October 2008.

The practical applications of the 'life interest' legislation can be seen where, for example, a Grandfather has created a trust in which the Father has a life interest. The Father is now elderly and wants to carry out his own IHT planning. The Father arranges to revoke his life interest in favour of his own son.

By agreeing that the trustees should cancel the Father's life interest, the Father is treated as making a potentially exempt transfer, provided this is done before 5 October 2008. If the Father cancels his life interest after 5 October 2008 he will be treated as making a chargeable transfer of value and will be liable to IHT at the lifetime rate of 20% on the value of the transfer at the date the cancellation of the life interest took place. Clearly a Potentially Exempt Transfer ("PET") is more beneficial than an immediate IHT charge.

The deadline is only a few days away so time to implement any arrangements is limited.

Fortunately the process of advancing the life interest is straightforward and provided there are no other tax issues, such as capital gains tax, stamp duty, or VAT, then the lifetime beneficiary can simply draft a witnessed letter to the Trustees renouncing his interest in favour of the remaining beneficiaries.

No action should be taken until your specific circumstances have been analysed.

Would you like to save inheritance of £124,800?

The Chancellor of the Exchequer announced in his October 2007 Pre-Budget Report that for death on or after 9 October 2007 it will be possible for sponsors and civil partners to transfer their unused inheritance tax nil rate band allowance.

The extent of this is that the surviving spouse may have a nil rate band available on death of double that in force at the time. The nil rate band for 2008/09 is £312,000 and with IHT payable at 40% the tax benefit of this could be as much as £124,800.

To obtain the benefit of this the executors need to make a claim using a Form IHT 216 and submit this within two years of second death. The information reported on the Form IHT 216 relates to the estate of the first deceased. Given that the death may have occurred in the distant past and there is a tendency to keep records for only a relatively short period, it is important that the information is collated as soon as possible to secure this relief. Acting now will reduce the burden for the executors on second death.

Contact us and we can liaise with your solicitor to prepare the documentation that will be needed.

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