Inheritance Tax – gifts and trusts

Independent Financial Advisers might suggest some vehicles to mitigate the impact of Inheritance Tax where some measure of control might also be required to avoid concerns that might relate to a simple gift where the recipient of the gift whatever their age would have total freedom to do what they will with the money so received.

Gift and loan trust

This is where a person establishes a trust and lends money to the trustees so unlike other options there is no significant gift involved. The trustees invest the money, and the donor can take loan repayments either on a regular basis or as and when to allow for unforeseen events.

This might not be as Inheritance Tax efficient as some other options, but it is a way of limiting the Inheritance Tax liability and can provide a valuable level of access to the funds.

Discounted gift trust

This is where an individual invests money at outset intended to provider fixed-regular payments for the rest of their life, effectively providing an income which can be sued to supplement retirement income.

This means that the donor (settlor) is exchanging part of a lump sum investment for an income, which as they do not gift provides a potential Inheritance Tax saving from outset. The balance of the investment is a gift, so the donor needs to survive 7 years before that gift falls outside of their Estate. As the trustees are obliged to provide thee payments they cannot pay any money to a beneficiary until the donor (settlor) has died and this can control access until the donor's (settlor's) death.

The withdrawals are provided using the tax deferred allowance from a bond. This means the arrangement is not only efficient from an Inheritance Tax perspective but also for Income Tax.

Flexible reversionary trust

This uses a similar concept to a Discounted Gift Trust but rather than retaining the right to an income the donor (settlor) has the right to periodic policy maturities thereby providing flexible payments to supplement income or for specific purposes later in life. The trustees could defer these payments if they chose where the money is not required. As the trustees control the maturities they can distribute money to the beneficiaries named in the trust at any time. This provides much more flexibility than a Discounted Gift Trust.

This may not be as tax efficient as a Discounted Gift Trust but will suit many who want to make a gift but are unsure about giving up full access not knowing what the future might hold in store for them.

Investment based solutions

Gifts carry with them a 7- year period before they fall out of the Estate for Inheritance Tax purposes. However, for those who are financially better off and with other investments might be attracted by a solution using business relief where there is only a 2-year period before the sum in question falls outside of their Estate for Inheritance Tax purposes. The government determines the qualifying investments eligible for this business relief easement.

As no gift is involved those assets pass to the beneficiaries on the death of the person making that investment. To qualify for this relief the risk profile of the investment is greater than many people might find comfortable.

Life assurance solutions

This option simply provides a pre-determined sum payable on death designed to settle the expected Inheritance Tax liability.

The use of a suitable trust can ensure that the sum payable on death remains outside of the Estate so not swelling the value of the Estate for the Inheritance Tax calculation while providing ready funds to meet the expected Inheritance Tax payment.