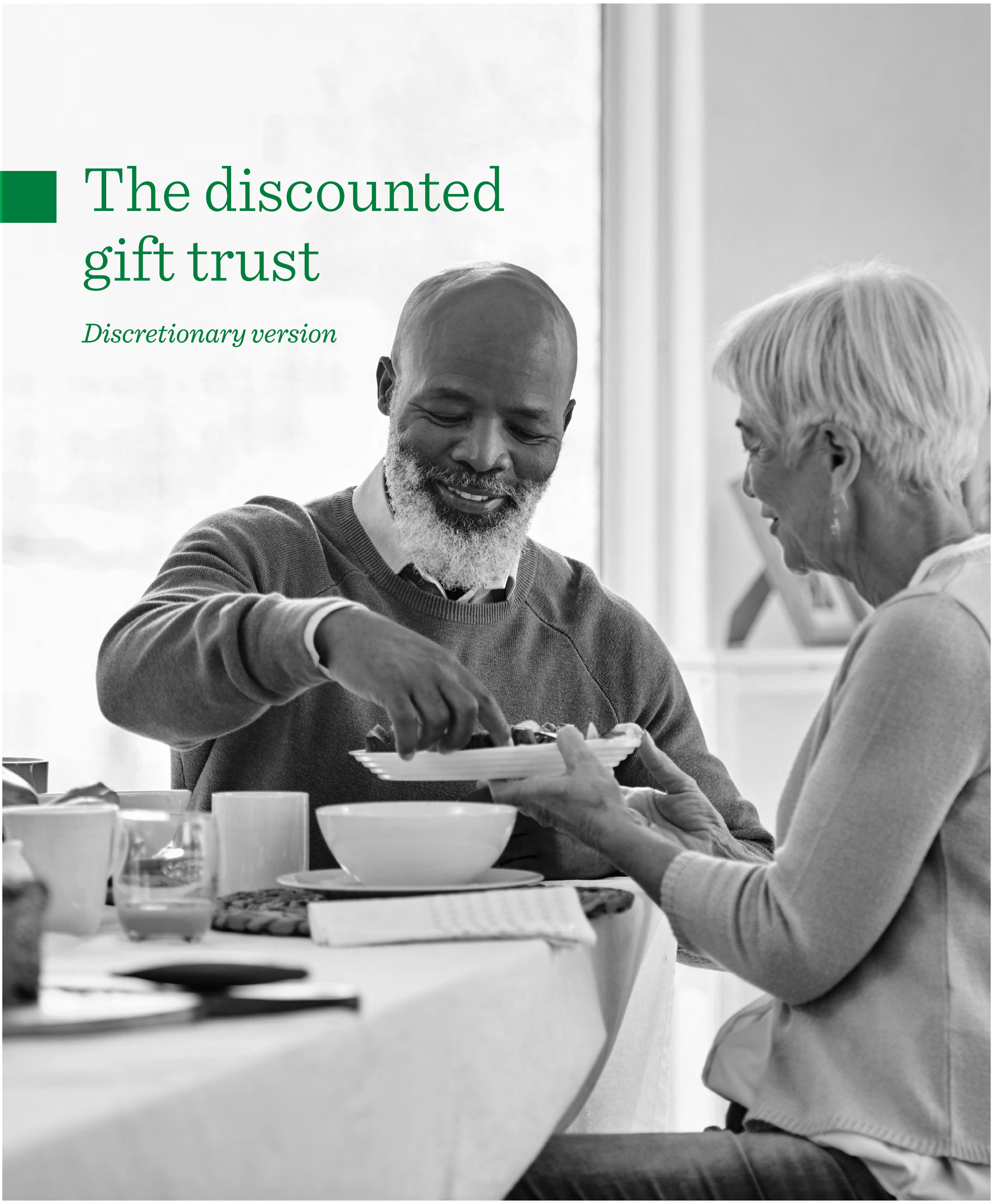
Quilter

# The discounted gift trust

*Discretionary version*



**We regularly update our literature;** your financial adviser can confirm that this **May 2023** version is the latest by checking the literature library on our website ***quilter.com***

# Introduction

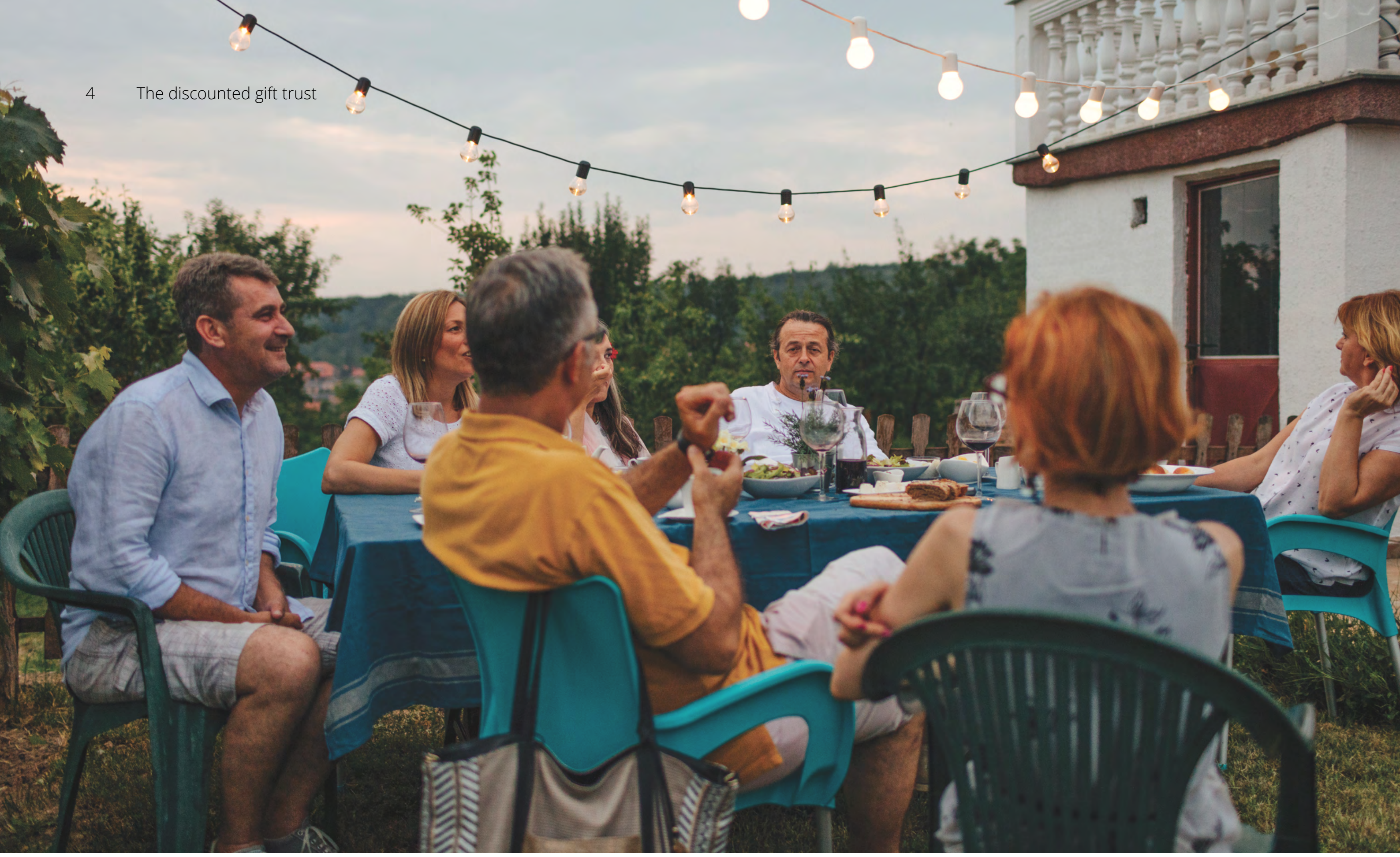
*The purpose of this guide is to give you the information you need to help you to decide whether the discounted gift trust is a suitable tax-planning arrangement for you. It explains what the trust is, who is involved, how it works and how those you wish to provide for when you die can benefit from it. Please discuss this with your financial adviser before making any decisions.*

The decision to place some of your assets into trust is such an important step, for you and others involved, that you should always take professional advice before making this decision.

Discounted gift trusts are specifically designed to help reduce your inheritance tax (IHT) liability whilst still allowing you the benefit of receiving regular withdrawals. You will not be surprised to learn that they are somewhat complex in structure. However, this is necessary to ensure they continue to provide the benefits they are used for.

Because of this complexity, it is particularly important that you consider all key aspects before making a commitment that cannot be changed. This guide aims to explain in plain English the way the discounted gift trust works. Inevitably in describing a legal document, it is sometimes necessary to use technical phrases. Where this is unavoidable, we have included explanations. Your financial adviser will also be able to provide further clarification.

As the trust arrangement may last many years, we have aimed in this guide to provide you with all the information you, and those who may deal with your estate after your death, may require over this period. As a result, some of the information may not appear applicable at the moment. However, if you do decide to set up a discounted gift trust, this guide can also act as a useful reference when questions arise.



# About us

*When we refer to Quilter, we, us or our in this document we mean Quilter Life & Pensions Limited.*

We are part of Quilter plc, a leading wealth management business, helping to create prosperity for the generations of today and tomorrow. Quilter plc oversees £99.6 billion in customer investments (as at 31 December 2022). It has an adviser and customer offering spanning financial advice, investment platforms, multi-asset investment solutions and discretionary fund management.

We enable financial advisers to deliver the very best service to customers and their families, to help them achieve their financial goals. We offer a comprehensive range of products and investments through our award-winning online investment platform.

## *The value of advice*

We don't sell or promote our products directly to customers. Instead we deal only through regulated financial advisers. We believe that decisions about your financial future are so important that you should always seek professional financial advice.

We do all we can to make sure that the people who are advising about our products fully understand them and the benefits and risks that need to be considered. We also try to make our product information as clear as possible in order to ensure you have all the information you need to make an informed investment choice.

# What is a trust?

It allows you (the settlor) to gift your assets (which then become the trust fund) to a group of people (the trustees) for the benefit of those you want to provide for (your beneficiaries). With some careful planning, a trust can be a means of reducing or even eliminating a potential inheritance tax (IHT) bill.

It is the responsibility of the trustees to take control of, manage and ultimately distribute, the trust fund to your beneficiaries in accordance with the trust's rules.

A discretionary trust is one where the trustees have the power to accumulate the income for the benefit of the beneficiaries, but no beneficiary has an absolute right to income or capital. The beneficiaries are normally named as a class of individuals, for example, 'on trust for my children or grandchildren'. The trustees have the right to distribute income and capital to the beneficiaries at their discretion.

**Throughout this brochure, wherever we want to explain a particular term we highlight it in boxes like this on the page where the term is first used. We also use this method to draw your attention to any potential risks.**

*Estate* – This means all the assets that a person owns (or, in some cases, is treated as owning) at the time of their death, less their liabilities (debts). Your estate will also include the value of any property or assets you have given away if either the gift you have made is subject to conditions or restrictions, or you keep back some benefit yourself. If you die within seven years of making a gift, then these may also be included in your estate.

# Why use a trust for IHT planning?

Set up correctly, a discretionary trust offers one way to move money out of your estate and possibly reduce your potential liability to IHT. A gift of your assets into this trust is called a 'chargeable lifetime transfer' (CLT) as it may be subject to one or more IHT charges during your lifetime. See page 16 for more details.

A trust can also avoid the prospect of lengthy delays often associated with the administration of estates so that, in the event of your death, the people you want to benefit from your estate do so as quickly as possible.

# Who is involved with a discounted gift trust – discretionary version?

*There are normally three parties involved in setting up a Discounted Gift Trust:*

- You, the settlor, either on your own (as a single settlor) or with someone else, such as a spouse or civil partner (as joint settlors). The settlor invests a cash sum in a bond (the trust fund) and then transfers the legal ownership of this investment to their chosen trustees.
- The trustees are the legal owners of the assets, and they manage the assets for the benefit of the beneficiaries. They are also responsible for dealing with and distributing the trust fund on the settlor's death. Trustees can be friends, family, trusted individuals; or you can use the services of a professional trustee provider.
- The beneficiaries of a discretionary version of the discounted gift trust are groups or 'classes' of people who may benefit from the trust following the settlor's death. This could be, for example, 'my grandchildren', including future grandchildren as yet unborn. The trustees will use their discretion to decide who should benefit from the trust, and although you can make your wishes known to them, they will ultimately decide. With discounted gift trusts, settlors (including your spouse or civil partner if they are a settlor) are only able to benefit from the right to receive withdrawals.

There may also be a fourth party involved, known as the protector.

- The protector monitors the trustees and ensures that their actions are in the best interest of the beneficiaries. You may appoint yourself as the protector.

# Why use a discounted gift trust?

Normally for a trust to be effective in reducing an IHT liability, the settlor is not able to access or benefit from the trust fund.

A discounted gift trust is different in that it enables the settlor(s) to benefit from regular withdrawals. This right to receive the withdrawals takes precedence over the other beneficiaries' right to the trust fund. The remainder of the trust fund is held for the benefit of the beneficiaries.

# How a discretionary version of a discounted gift trust works

*To set up a discounted gift trust using a bond, you will first need to invest a cash sum in your bond (see page 9 for more details).*

Once this has been set up, it is transferred into the discounted gift trust and legal ownership moves to the trustees. The investment then forms the trust fund. You will no longer have any access to the investment other than the right to receive the regular withdrawals from it. Details of the withdrawal options are shown on page 12.

Based upon factors such as your age, health (see page 10) and the level of withdrawals requested, we will calculate the estimated value of your right to receive the withdrawals. This value is known as 'the discount'. This is the amount that will fall immediately outside your estate on your death, and is therefore not liable for IHT, even if you were to die within the first seven years. Whilst we use our experience and understanding of current legislation to assess the discount, the actual discount that applies will only be determined by HM Revenue & Customs after your death.

The value of your investment, less the discount, is what is referred to as the 'discounted gift'. For IHT purposes, this is a chargeable lifetime transfer (CLT). The CLT, if it exceeds your available nil-rate band, is subject to IHT at 20% on the excess at outset, and after seven years the CLT will fall outside your estate for IHT purposes. Should you die within seven years, additional tax of up to 20% may be payable. The trust fund may also be subject to periodic and exit charges (see page 15 for more details).

### *Nil-rate band*

The nil-rate band is not fixed and has, historically, increased year-on-year. Currently the first £325,000 (frozen until April 2028) in an individual's estate is taxed at 0% for IHT purposes. This is known as the nil-rate band.

Any assets above the nil-rate band may be liable to IHT at 40%.

*The following fictional example is for illustrative purposes only and is based on an investment of £250,000 in a bond subject to a discounted gift trust.*

*The settlor sets up a bond with £250,000.*

*The bond is transferred into a discounted gift trust.*

The value of the settlor's right to regular withdrawals (the 'discount') is calculated based upon factors such as age and health of the settlor, plus the level of withdrawals. We estimate the discount to be £100,000.

The discounted gift is a chargeable lifetime transfer (CLT).
This is your investment less the discount. This value falls outside the settlor's estate after seven years. £250,000 minus £100,000 = £150,000.

Immediately outside the settlor's estate

**Settlor's fund – the discount**
Based on the value of the right to withdrawals from the trust fund during the settlor's lifetime (£100,000).

Chargeable Lifetime Transfer (CLT)

**Residual fund – the discounted gift**
The remaining investment and all other rights (£150,000).

*Any growth within the bond will be free from IHT provided the fund does not exceed the nil-rate band on each 10-yearly anniversary.*

# Where is my money invested?

*Your cash sum is invested in a Collective Investment Bond (CIB). This provides a flexible method of investing your money and offers the potential for growth, over the medium to long term. The bond is designed to allow your investment to grow whilst you take regular withdrawals.*

Our bond offers a wide choice of investment options (funds), many linked to the performance of stock markets, enabling your trustees to choose funds to meet the investment needs of the trust. Because of the way the bond is structured, it also offers the opportunity to take advantage of certain tax benefits, depending on your personal circumstances and requirements.

Please be aware that the trust restricts some of the flexibility the bond offers in order that the discounted gift trust continues to be effective for IHT planning. This generally relates to the level of access you can have to the investment and your control over it.

*For example:*

- You will only be entitled to the amount of withdrawals which you specify at outset and you cannot change the level of your withdrawals in the future should your personal circumstances change.

- You will not be able to make additional investments into the bond, although you can set up a new bond subject to a new trust if required.

### *Risk warning*

If the bond comes to an end during the settlor's lifetime then the withdrawals will stop and the settlor will have no further right to receive withdrawals. This will also happen if all the individuals appointed as 'lives assured' die before the settlor. We therefore recommend that on these bonds, several lives assured are chosen to minimise this possibility. Although we have made every effort to ensure the discount provided is accurate, there is a chance that the value of your estate may not be reduced by the amount of 'discount' we calculate. At worst this could mean that you only receive a nominal discount. This could happen if HM Revenue & Customs – the department of the UK Government that deals with inheritance tax – interprets the existing legislation differently or they change their practices.

### *Life assurance/lives assured*

The Collective Investment Bond is set up as a life assurance bond so it can provide you with tax-planning benefits. This type of bond has one or more 'lives assured', which means the bond will come to an end when the person who is assured dies. You have a choice of having multiple lives assured (up to a maximum of 10) to ensure the continuity of your bond. Where there is more than one life assured, the bond will end when the last person whose life is assured dies. For discounted gift trusts to be effective for IHT planning, the settlor and their spouse or civil partner must not be lives assured. The beneficiaries, for example children/grandchildren, may be appropriate as lives assured in order to ensure that the bond continues beyond your death.

# Establishing your discount

*In order to satisfy HM Revenue & Customs (HMRC) requirements, and provide you with an estimate of your discount (immediate reduction in your IHT liability), we need to be able to calculate the part of your investment which is likely to be required to provide you with the regular withdrawals.*

So that we can do this as precisely as possible, we need to establish how long your withdrawals are likely to last. Basically, this involves estimating your life expectancy and that of any other settlor entitled to the withdrawals.

This is why we ask you to complete some health questions in the application form. We will also request a General Practitioner's (GP) report, as this can then be used to confirm your (and any other settlor's) state of health at the time you placed the bond into trust. This is known as underwriting. The estimated discounts initially quoted by us may then be amended to reflect your actual state of health once the GP's report has been received and reviewed.

The trust will not come into effect until the medical evidence has been assessed by us. However, the bond can start before we receive the medical evidence, unless you instruct us otherwise, and when we have completed the health assessment we will start the trust by dating it. This is called the 'declaration date'.

Alternatively, if you do not want us to start the trust automatically, you can ask us to inform you of the calculated discount before the bond is placed in trust, but you must tell us this when you apply.

## *Can we guarantee the discount?*

No, whilst we use our experience and understanding of current legislation to assess the discount, the actual discount that you receive will only be determined by HMRC following your death. We cannot therefore guarantee that HMRC will agree with our calculations. It will be for your executors to negotiate with HMRC and agree the amount of any discount, if necessary.

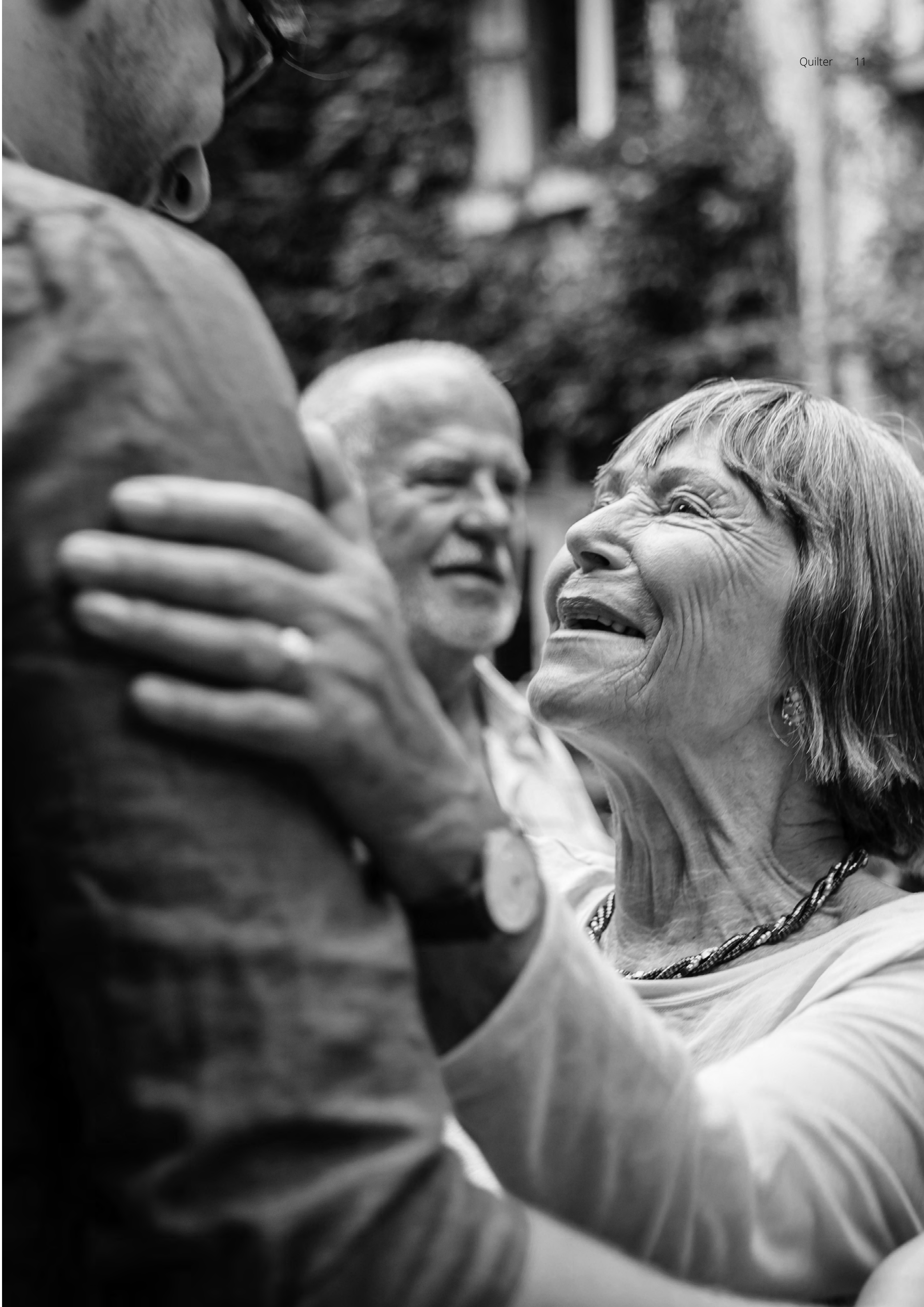
## *What if I'm not in good health for my age?*

If your life expectancy is less than average, the amount of discount we calculate will be lower than the example discounts we produce as these are based upon someone in good health. This means that although you will still be able to take withdrawals from the bond and there may be an IHT saving, the saving will be less than if you were in good health for your age.

In some circumstances, where your life expectancy is very low, you may only receive a nominal discount.

### *Executors*

The persons appointed in the deceased's will to supervise the administration and distribution of the deceased's estate in accordance with their last will and testament.



# Taking withdrawals

*You have a choice of withdrawal options to suit you. As the settlor, you can select at outset to take withdrawals of up to 15% of the initial investment each year, but bear in mind that the larger the level of withdrawals, the greater the chance of your investment decreasing, even taking into account investment growth.*

Potentially this could leave you with no investment from which to take withdrawals, or to pass onto your beneficiaries.

You can receive up to 5% of the investment each policy year, for at least 20 years, without having to pay any income tax. Withdrawals over 5% each policy year may also be subject to UK income tax.

Withdrawals are paid in arrears, either monthly, quarterly, half-yearly or yearly. The first withdrawal will be paid by reference to the declaration date of the trust, not the start date of the investment. So, where you ask for withdrawals yearly in arrears and your declaration date is 1 October 2023, the first payment will fall due on 1 October 2024. For trusts with more than one settlor, the payment must be made to both settlors jointly.

The amount of each withdrawal is determined at the outset, and will not increase.

## *Waiving withdrawals*

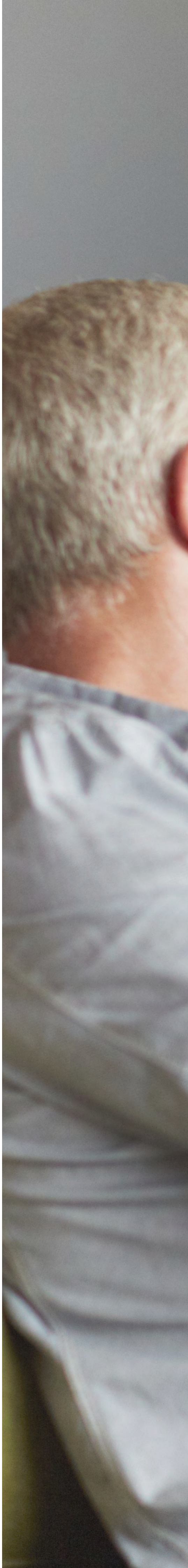
You may not want to receive withdrawals every year, in which case you can waive the withdrawals (ie not take them) and instead turn these withdrawals into a further 'gift' to the beneficiaries. You can do this by deed in advance of a payment. However, you should be aware that this amount will be treated as a further CLT for UK IHT purposes, and an immediate tax charge may arise. Once a withdrawal has been waived, you will not be able to access this money again.

It is essential that before you waive any withdrawals, you discuss this with your financial adviser.

## *Deferring the start date of withdrawals*

You may want to begin your IHT planning, but instead of having withdrawals starting when the trust starts, have the withdrawals starting from a future date of your choice.

Deferring the start date of your withdrawals would enable the seven-year UK IHT 'clock' to start. Your regular withdrawals will start at a later date. Once you state when you want your withdrawals to start, you cannot change or defer this date.



**Fictional example**

Mrs West, aged 60, invests a cash sum of £100,000. Withdrawals are set at 5% each year, but deferred for the first three years.

| Age | Withdrawals as a % of the investment | Withdrawal amount £ |
|---|---|---|
| 61 | 0 | 0 |
| 62 | 0 | 0 |
| 63 | 0 | 0 |
| 64 | 5 | 5,000 |
| 65 | 5 | 5,000 |

Deferring the start date of withdrawals will reduce the value of the discount you receive. Deferment must be for at least one month and up to 60 months (five years) from the date the trust is set up.

*Risk warning:*

If you do not spend the money you have withdrawn, it will form part of your estate and could be liable to UK IHT when you die.

If market returns are poor for a sustained period, then taking withdrawals could use up all the investment together with any growth. The withdrawals would therefore stop once the trust fund has no value.

During your lifetime, and that of any other settlor, no withdrawals can be paid to the beneficiaries.

The level and frequency of the withdrawals are set at outset and cannot under any circumstances be changed in the future.

# Other considerations

### *On my death, is any part of the trust fund subject to IHT?*

Assuming you have lived for seven years since making the gift into the discounted gift trust, then no part of the trust fund will be subject to IHT. Any growth on your investment will be outside of your estate from day one. You must be aware that the trust fund may be subject to periodic and exit charges. However, if you were to die within seven years, then the value of the discounted gift will be subject to IHT. Your IHT liability may still be reduced using what is known as taper relief where the gift, along with previous gifts, is larger than your available nil-rate band. Taper relief only applies to the amount of your gift that is above your available nil-rate band. Its effect is shown in the table.

*Taper relief*

| Years between making a gift and dying | Proportion of 40% inheritance tax payable |
|---|---|
| 0-3 | **100%** |
| 3-4 | **80%** |
| 4-5 | **60%** |
| 5-6 | **40%** |
| 6-7 | **20%** |

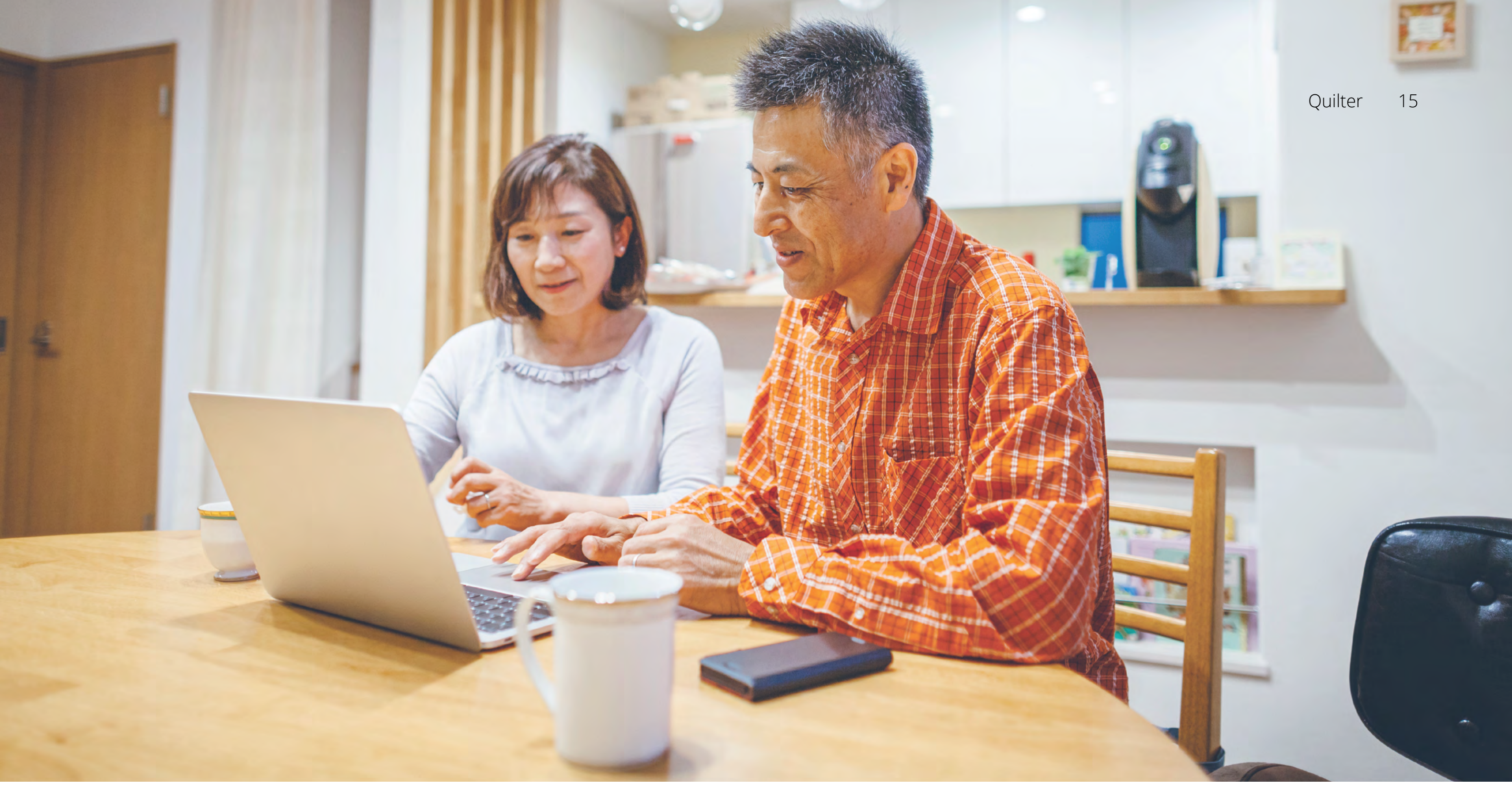
### *Do I need to report my gift to HM Revenue & Customs?*

As the gift is a chargeable lifetime transfer (CLT) there is a requirement to report the gift where it exceeds 80% of the current nil-rate band, taking into account the current CLT and all transfers made in the previous seven years. It is important that you keep a copy of the discount letter you will receive from us and any supporting evidence. This is because, if you die within seven years, HM Revenue & Customs may request information from your executors or legal representatives to verify the discount value, ie the amount of the gift which was deemed to be immediately outside your estate for IHT purposes.

### *Trust registration*

A trust must register with HMRC's Trust Registration Service (TRS) if it is considered UK resident or has a UK tax liability, unless an exemption applies. A trust must register within 90 days of the date of the trust deed. The trustees must submit evidence of registration (available from the TRS) or confirm exemption from registration to Quilter within 90 days of the trust date.

Further details regarding trust registration can be found here: ***quilter.com/TrustRegister***





# What are the IHT charges associated with a discretionary trust?

*Whilst it is possible to avoid having to pay inheritance tax (IHT) on your death, there may be other IHT charges to pay. These IHT charges relate specifically to discretionary trusts and are briefly summarised below.*

We strongly recommend you discuss with your financial adviser the taxation of a discretionary discounted gift trust and whether these tax charges will apply to you.

## *Entry charge*

When you place your investment into a discretionary trust there may be an initial tax charge of 20% to pay on some or all of your investment. This is called the 'entry charge'. It represents half of the current rate of IHT. To calculate if an entry charge applies, you need to work out the total value of all your chargeable lifetime transfers (CLTs) over the past seven years and then add the value of the discounted gift (the residual fund). If this total is above the current nil-rate band for IHT, then the excess (up to the amount of the discounted gift) will be subject to the 20% entry charge.

## *10-Yearly periodic charge*

If after 10 years, and every subsequent 10 years, the value of the trust fund, less the discount (the settlor's fund), is more than the current IHT nil-rate band, the trustees may need to pay a 10-yearly periodic charge. To work out if this charge applies, the trustees will first need to work out the value of the trust fund at the 10-year anniversary, less the revised 10-year anniversary valuation of the discount. This latter value is established in the same way as the original calculation of the discount (see page 10), taking into account the fact that you are ten years older. HM Revenue & Customs has confirmed that further medical information is not required for this unless the trustees are aware that your health has deteriorated, in which case, further medical information may be required as part of the discount valuation.

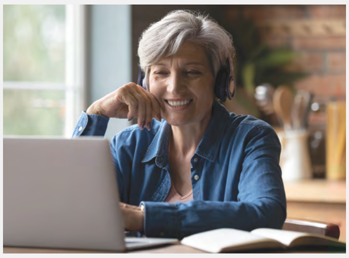
If this tax charge does apply, it will be no more than 6% of the value of the trust fund.

## *Exit charge*

There are no exit charges to pay on the withdrawals you receive as the settlor. However, any money paid to your beneficiaries may be subject to an exit charge of up to 6%. The charge is based upon the rate of the 10-yearly periodic charge at the last anniversary (see left) and how long it has been since that anniversary. Withdrawals paid to beneficiaries within the first 10 years of the trust's creation are subject to a different calculation.

Your financial adviser can guide you as to whether these charges may apply to you and your beneficiaries.

# How the trust works in practice



## Case study 1

*This shows how the discretionary version of the discounted gift trust works for a single settlor case. It also assumes that the available nil-rate band and exemptions have already been used.*

Mrs Wilkinson is aged 60, retired and in good health. She has an estate valued at £450,000 and she wishes to reduce her potential IHT liability. She has £100,000 available to invest, but also wants to take regular monthly withdrawals to supplement her pension, although she requires no further access to the investment. Upon her death she would like her growing family to benefit from the trust fund. Her financial adviser recommends that she invests in a Collective Investment Bond subject to a discounted gift trust – discretionary version.

*Mrs Wilkinson invests £100,000 into the bond.*

*The bond is transferred to a discounted gift trust – discretionary version.*

*Mrs Wilkinson requests that she receives 5% of the investment (£5,000) each year, paid monthly.*

**Settlor's fund – the 'discount'**

The value of Mrs Wilkinson's right to the requested regular monthly withdrawals is calculated taking account of her age and health, plus her level of withdrawals. We estimate the discount to be £58,240.

This part of Mrs Wilkinson's investment is immediately outside her estate for IHT purposes.

**Residual fund – the discounted gift**

This is Mrs Wilkinson's investment less the discount. £100,000 - £58,240 = £41,760.

This is a chargeable lifetime transfer (CLT). If this amount plus any previous CLTs in the last seven years exceed the nil-rate band at the time, then the excess will be subject to an immediate 20% IHT charge. In this example the maximum charge could be £41,760 x 20% = £8,352.

*Any growth within the bond will be free from IHT except for any periodic or exit charges that may apply.*

### *Death within seven years*

If Mrs Wilkinson dies within seven years of making the gift:

- the discounted gift of £41,760 will become chargeable to IHT at 40%. If an entry charge was paid, for example the maximum £8,352 quoted above, this can be used as a credit to reduce the tax due. It may be possible to reduce this IHT charge further if at least three years have passed, due to taper relief (see page 14).
- withdrawals to pay Mrs Wilkinson cease and the entire value of the trust fund can be distributed to her family.
- the growth on the bond will not be subject to IHT – except if periodic or exit charges apply (see page 15).
- Mrs Wilkinson's executors may need to negotiate with HM Revenue & Customs (HMRC) to determine the actual discount to be applied to the trust fund. If HMRC agrees with our calculations, then in Mrs Wilkinson's case the full discount of £58,240 will all be free from IHT.

If Mrs Wilkinson had not applied for a discounted gift trust to reduce her IHT liability, her tax bill could have been £40,000 (40% tax on the investment of £100,000). By planning ahead, even if she dies within the first seven years, Mrs Wilkinson, subject to HMRC's agreement on the discount amount, will have reduced her beneficiaries' IHT bill from £40,000 to £16,704 saving them £23,296 (40% tax on the discount £58,240). There may be a further IHT saving as a result of taper relief on the discounted gift of £41,760. In addition, any growth on this investment will also be free from IHT.

### *Death after seven years*

If Mrs Wilkinson dies more than seven years after making the gift:

- the discounted gift of £41,760, although originally a CLT, will now be completely free from IHT.
- withdrawals to pay to Mrs Wilkinson cease and the entire value of the trust fund can be distributed to her family at any future time.
- the trust fund will be liable to periodic and/or exit charges in future years.
- no refund would be payable on any entry or periodic IHT charge already paid.

Through proactive planning, and assuming Mrs Wilkinson lives for at least a further seven years, she may have reduced her beneficiaries' IHT bill from £40,000 (40% tax on the investment of £100,000) to £0 (or £8,352 if the full entry charge applied). In addition, any growth on this investment will also be free from IHT.

# How the trust works in practice

## Case study 2

*This shows how the discretionary version of the discounted gift trust works for a joint settlor case. It also assumes that the available nil-rate band and exemptions have already been used.*

Mr and Mrs Povey are aged 65 and 62 respectively. They are both in good health for their age. They have a joint estate of around £1,100,000. They wish to reduce their potential IHT liability and have £100,000 available to invest. However, they do need to take regular monthly withdrawals to supplement their pensions but can afford not to have any further access to the investment. They would like their expanding family to benefit from the trust fund upon their death. Their financial adviser recommends that they invest in a Collective Investment Bond subject to a discounted gift trust – discretionary version.

*Mr and Mrs Povey jointly invest £100,000 in a Collective Investment Bond.*

*The bond is transferred to a discounted gift trust – discretionary version.*

*Mr and Mrs Povey request that they receive 5% of the investment each year, which equates to £5,000, paid monthly.*

**Settlor's fund – the 'discount'**
The value of Mr Povey's right to his half of the £5,000 each year is calculated taking account of his age and health.
We estimate the discount to be £30,065.

Mrs Povey's half is valued at £31,338.

**The total discount is £61,403.**

This part of Mr and Mrs Povey's investment is immediately outside their estates for IHT purposes.

**Residual fund – the discounted gift**
This is Mr and Mrs Povey's halves of the investment less their discounts.

For Mr Povey it is £50,000 - £30,065 = £19,935.

For Mrs Povey it is £50,000 - £31,338 = £18,662.

**The total discounted gift is £38,597.**

These are chargeable lifetime transfers (CLTs). If these amounts plus any previous CLTs in the last seven years exceed the nil-rate band at the time, then the excess will be subject to an immediate 20% IHT tax charge.

In this example:

£19,935 x 20% = £3,987 for Mr Povey

£18,662 x 20% = £3,732 for Mrs Povey

*Any growth within the bond will be free from IHT except for any periodic or exit charges that may apply.*

## *Death within seven years*

If Mr Povey dies within seven years of making the gift:

- his discounted gift of £19,935 will become chargeable to IHT at 40% but this is reduced by the credit paid on entry. It may be possible to reduce this if at least three years have passed due to taper relief (see page 14).
- the withdrawals of £5,000 each year, payable monthly, will continue to be paid in full to Mrs Povey.
- his executors will negotiate with HM Revenue & Customs (HMRC) to determine the actual discount to be applied to the trust fund. If HMRC agrees with our calculations then the full discount of £30,065 will be free from IHT.

If Mrs Povey dies within seven years of making the gift:

- her discounted gift of £18,662 will become chargeable to IHT at 40% but this is reduced by the credit paid on entry. It may be possible to reduce this if at least three years have passed due to taper relief (see page 14).
- the withdrawals of £5,000 each year, payable monthly, will continue to be paid in full to Mr Povey.
- her executors will negotiate with HMRC to determine the actual discount to be applied to the trust fund. If HMRC agrees with our calculations then the full discount of £31,338 will be free from IHT.

If Mr and Mrs Povey had not applied for a discounted gift trust to reduce their IHT liability, their tax bills on the £100,000 invested could have been £20,000 (40% tax on their respective halves). By planning ahead, even if one of them dies within the first seven years, subject to HMRC's agreement, Mr Povey will have saved his beneficiaries £12,026 (40% tax on the discount of £30,065) and Mrs Povey's beneficiaries £12,535 (40% tax on the discount of £31,338). In addition there may be a further IHT saving as a result of taper relief on their respective discounted gifts.

## *Death after seven years*

If either Mr or Mrs Povey survives more than seven years after making the gift:

- the discounted gift of £19,935 (if only Mr Povey survives) or £18,662 (if only Mrs Povey survives), although originally a CLT, will now have no further IHT liability.

If Mr and Mrs Povey both die more than seven years after making the gift:

- the total of the discounted gifts (£19,935 + £18,662 = £38,597), although originally CLTs, will now be completely free from IHT.
- withdrawals will continue to be paid until the surviving spouse dies. Then the entire value of the trust fund can be distributed to their beneficiaries.

Through proactive planning, and assuming Mr and Mrs Povey both live for at least a further seven years, they will have reduced their joint IHT bill on the £100,000 investment from £40,000 (40% tax on the investment of £100,000) to £0 (or £7,719 if the full entry charge applied).
In addition, any growth on this investment will also be free from IHT.

*They wish to reduce their potential IHT liability and have £100,000 available to invest.*

# The ‘discount letter’ explained

*When you receive your ‘discount letter’ from your financial adviser, it will contain the following information. Your financial adviser will be able to guide you through this and explain the illustrative discount before your discounted gift trust is underwritten.*

## Premium

This shows the investment you have made into the Collective Investment Bond.

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## Terms of the settlor’s income

This shows the percentage of the premium paid to the Collective Investment Bond you have requested as withdrawals each year. This amount will be paid in instalments throughout the year at your chosen frequency.

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## Value of interest retained

This is the estimated ‘discount’, based on the number of withdrawals we estimate will be needed during your lifetime taking into account your life expectancy.

For joint settlors, this shows the combined discount. For UK IHT purposes this value will be proportioned and based upon individual life expectancy.

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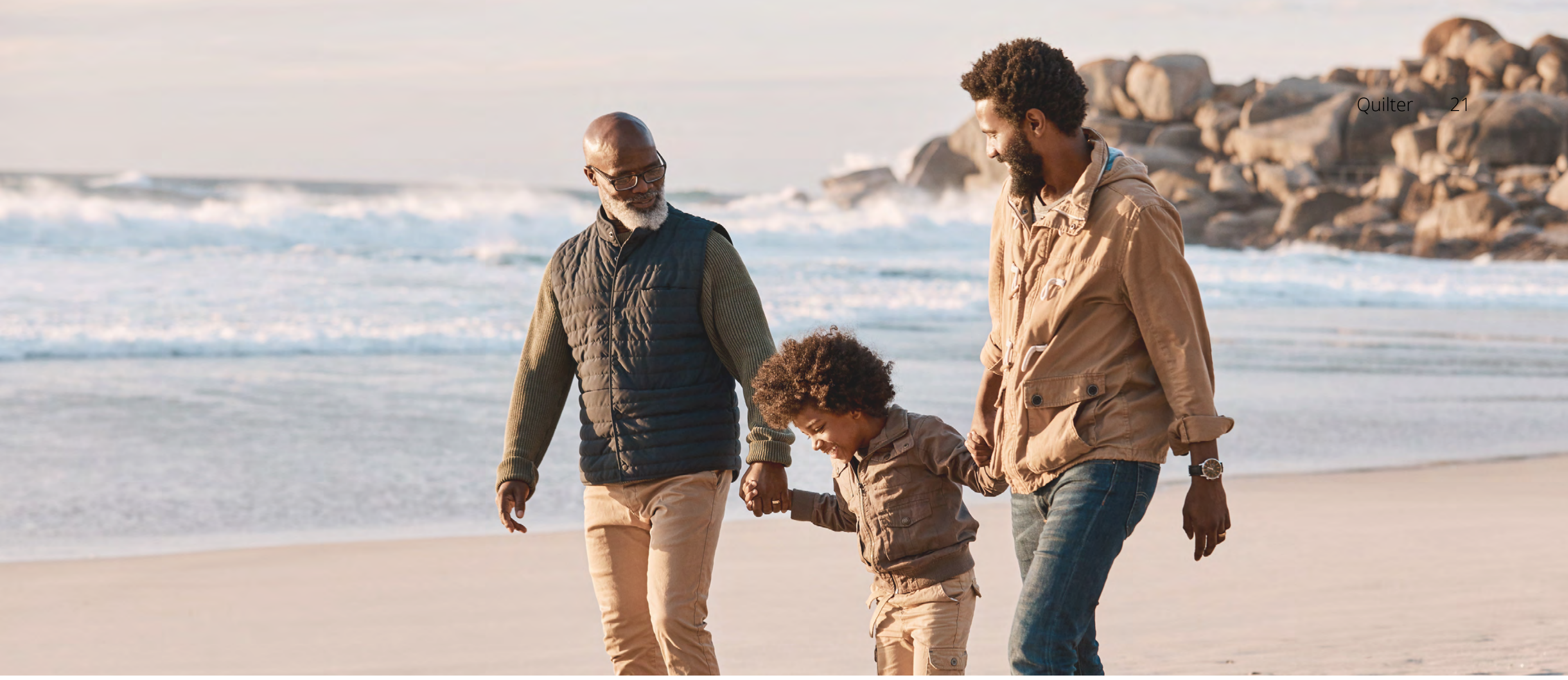
## Discounted value of gift

This is the value of your investment less the discount.

It is the value of the chargeable lifetime transfer (CLT).





# How do I set up the discounted gift trust – discretionary version?

1 *Complete the Discounted Gift Trust application form for the Collective Investment Bond.*

We recommend that at least two people are named as lives assured so that the bond has an increased chance of remaining in force for the length of the trust. However, neither you nor your spouse/civil partner should be a life assured to ensure that the trust is effective in reducing your IHT liability.

You will also need to complete the necessary form in order for us to obtain a **general practitioner's report**.

2 *Complete the trust deed 'discounted gift trust – discretionary version'.*

- As the Settlor, you decide who you want to appoint as trustee – you are not automatically included as a trustee.
- You need to complete the Second Schedule of the trust deed to choose which type of withdrawals you require.

3 *The trustees will need to complete the discounted gift withdrawal authority which is included with the trust deed.*

4 *We require the following:*

- Application form, which includes some medical questions.
- General Practitioner's report authority, also included in the application.
- Trust deed.
- Withdrawal form.
- Payment of a cash sum into your bond (your premium)
- Tax Declaration and Confirmation of Verification of Identity.

# How to set up the withdrawals

*Below are notes on how to complete the second schedule of the trust deed.*

## The Second Schedule: The Settlor's Fund

The payments to be made in accordance with this schedule are indicated by completion of boxes A, B and C.

*Level Payments*

A % per annum of the single premium for the Trust Property shown in the First Schedule, the first payment arising B months after the Declaration Date ('**the Start Date**'), and subsequently payable C thereafter and ceasing with the last payment to arise before the death of:

(a) the Settlor if this is a Single Settlor Trust; or

(b) the later to die of the two persons comprising the Settlor if this is a Dual Settlor Trust.

**Box A**
State the amount of the settlor's income as a percentage of the premium paid to the Collective Investment Bond. For example if the settlor wants 5% of the premium, '5' should be inserted here.

**Box B**
State how long after the declaration date the settlor wishes the payment to start. For example, if you want payments to start three months after the declaration date, insert '3' in here. It should always be expressed in number of months, not years.

**Box C**
Frequency of payment must be entered here. The options available will be dependent on what has been entered in Box B as payments are made in arrears. See table below.

| How long after the declaration date would you like payments to start? | What should be written in Box B? (the deferred period) | What could be written in Box C? (frequency options) |
|---|---|---|
| **1 month** | 1 | M |
| **3 months** | 3 | M, Q |
| **6 months** | 6 | M, Q, 1/2Y |
| **1 year** | 12 | M, Q, 1/2Y, Y |
| **2 years** | 24 | M, Q, 1/2Y, Y |
| **3 years** | 36 | M, Q, 1/2Y, Y |
| **4 years** | 48 | M, Q, 1/2Y, Y |
| **5 years** | 60 | M, Q, 1/2Y, Y |

Please note **As payments can only be made in arrears, the minimum deferral period for each type of withdrawal is:**

- **Monthly –** one month
- **Quarterly –** three months
- **Half yearly –** six months
- **Yearly –** twelve months

This document is based on our interpretation of UK law and HM Revenue & Customs practice as at May 2023. While we believe this interpretation is correct we cannot guarantee it. Tax relief and the tax treatment of investment funds may change. The value of any tax relief will depend on the investor's financial circumstances.

We cannot accept any responsibility for any losses or liabilities arising from action taken as a result of the information contained in this document.

Investors should be aware that the value of our investment products cannot be guaranteed as investments may fall as well as rise. Further details are available in the relevant product brochures available from your financial adviser.

All case studies are purely hypothetical.

Trusts and inheritance tax planning are not regulated by the Financial Conduct Authority.

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*Please be aware that calls and electronic communications may be recorded for monitoring, regulatory and training purposes and records are available for at least five years.*

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