Sanlam

Wealth

Discretionary loan trust

AT A GLANCE

A discretionary loan trust helps people manage their inheritance tax liabilities by facilitating lending to trustees

Important information: This guide is for use by financial advisers only. It is not intended for onward transmission to a private customer and should not be relied upon by any other person.

The discretionary loan trust facilitates inheritance tax (IHT) planning for an individual when used in conjunction with a new Sanlam single-premium life insurance bond. It enables an individual (the 'settlor') to lend a sum of money (on an interest-free and repayable-on-demand basis) to the trustees to invest in a life insurance bond. This ensures that any investment growth that accrues falls outside of the settlor's estate for IHT purposes. The settlor can request ad hoc repayments of the loan at any time and as the trust is established with a loan to the trustees, there is no lifetime transfer for IHT purposes. The trustees hold the bond in trust for the beneficiaries, subject to the right of the settlor to have the loan repaid.

Definitions

Appointor: the settlor during their lifetime and, after their death, the trustees.

Default beneficiaries: the individual(s) who will benefit in the unlikely event that the power of appointment is not exercised by the appointor by the end of the trust period (125 years from the time the trust is created).

Discretionary beneficiaries: includes any spouse/civil partner, former spouse/civil partner, widow or widower, children, brothers and sisters of the settlor.

Settlor: the person who makes the loan to the trustees.

Objectives

- To reduce the value of the settlor's taxable estate and to reduce the IHT liability arising on their estate on death. The value of any outstanding loan will remain as part of the settlor's estate on death.
- To allow the settlor access to the loan through ad hoc loan repayments.
- To ensure that all capital growth on the investment accrues outside of the estate of the settlor and is passed to the beneficiaries of the trust.
- To allow the settlor to exercise continuing control over who will finally benefit from the trust fund.
- The settlor makes a loan to the trustees who invest in the policy (a new policy is therefore set up in every case).
- The settlor's spouse/civil partner could benefit under the trust (as a discretionary beneficiary), but it is recommended that the spouse/civil partner does not receive any benefit during the lifetime of the settlor.

The discretionary loan trust may be suitable where:

- The settlor is over 50 (joint settlor cases are not allowed).
- The settlor's estate exceeds the nil rate band.
- The settlor has capital to invest or realisable investments available for reinvestment. Capital gains tax liabilities may apply in some cases such as an in-specie transfer of assets.
- The settlor requires ad hoc access to capital to periodically supplement their income.
- The original capital invested (or part of) may need to be called upon at any time.
- The settlor has identified the beneficiaries whom he wishes to benefit, but wishes to retain control over who receives these benefits in the future.

Questions and answers

Can the trust be made jointly by two people?
No, the trust is only suitable for individual settlors – it cannot be made jointly by two people.

How many trustees should be appointed?
The settlor and at least one other individual (preferably two) must be appointed as original trustees. The settlor has the power to appoint trustees.

Can the settlor remove a trustee?
Yes, as long as there are at least two trustees remaining after the removal.

Who should draw the cheque for the loan?
The settlor from their own bank account and not a joint account. The cheque should be made payable to Sanlam Financial Services UK Limited.

When should loan repayments be made?
It is recommended they are made on demand (irregular amounts and at irregular intervals). A regular withdrawal amount could result in the loan repayments being regarded as income payments by HMRC.

How are loan repayments made?
By the trustees making ad hoc partial surrenders of the bond following receipt of a demand for payment from the settlor.

Can any 'income' not withdrawn in a policy year be carried over (the 5% tax-deferred annual allowance)?
Yes, it can be carried over to the following policy year and is cumulative.

Can the settlor retain any benefit under the trust?
No. To ensure that the arrangement is effective for IHT purposes, the settlor should not retain any benefit under the trust. If the settlor were to benefit from the trust, either directly or indirectly via their spouse/civil partner, the 'gift with reservation' rules may apply.

Entitlement to repayment of the outstanding loan on demand does not contravene the 'gift with reservation' rules.

Can further investments be made?
Yes. The settlor can make a further interest-free loan which is invested by the trustees.

Is the trust subject to periodic and exit charges?
Yes. As the trust is a discretionary trust, it is potentially subject to an IHT charge on the value of distributions from the trust and on each 10-year anniversary. For more information on how these charges are calculated, please refer to the *Discretionary loan trust – adviser's guide*.

Forms and guides

- *Discretionary loan trust – adviser's guide*
- *Discretionary loan trust – trust deed*
- *Discretionary loan trust – loan agreement*
- Acknowledgement of receipt of the loan by the trustees
- Appropriate Sanlam single-premium life insurance bond key features and application form

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8072/05.2020