Sanlam Onshore Bond case study

Scenario 1: For Trust planning

Client details

Mr Smith (63 years) and Mrs Smith (60).
Employed directors in a successful accountancy business.
Both in good health.
One non-dependent son who is looking to buy his first house.
Aim: to retire in 5-7 years when their son will take over the family business.

Mr Smith	Mrs Smith
Salary: £43,000 (gross)	Salary: £43,000 (gross)
Dividends: £15,750 (jointly)	

Current Assets	Value
Primary residence (joint ownership)	£550,000 (mortgage free)
Cash (joint)	£25,000
Investment account (jointly owned)	£450,000
Pension (Mr)	£750,000
Pension (Mrs)	£700,000
ISA (Mr)	£140,000
ISA (Mrs)	£140,000
Total	£2,755,000
Total subject to inheritance tax	£1,305,000

Planning needs

- Concerned about their current inheritance tax (IHT) liability.
- To maintain the same levels of income (post retirement).
- To gift their son with a deposit for his first house purchase.

Proposal

1. **Keep the cash.**
   Emergency funds for unforeseen expenses.

2. **Sell the assets in the investment account.**
   Capital gains tax will be due at a maximum rate of 20% where the disposal crystallises gains in excess of the annual exempt amount (£11,700 for 2018/19 tax year). As the investment account is held jointly, both Mr and Mrs Smith can set their annual exemption against their share of any gain. Where gains are significantly in excess of the annual exemption the disposal could be staggered over several tax years to benefit from future year's exempt amounts.

3. **Invest in ISAs.**
   With the £450,000 investment account proceeds, (if sold now), £40,000 (£20,000 each) could be used to maximise their ISA allowance for tax year 2018/19. While there are opportunities for IHT planning with ISAs holding AIM listed shares, it was agreed that this investment was too high risk for the clients.

4. **Invest £400,000 in an onshore bond (in a discretionary discounted gift trust (DDGT)).**
   The investment bond in a DDGT means the clients can continue to receive income while dealing with their IHT concerns. The investment of £400,000, (subject to underwriting) could, if the clients took 4% of the amount invested as a withdrawal per annum, provide an 'income' of £16,000, more than they are currently receiving from their dividends. As this is a capital withdrawal, there would be no immediate income tax liability, making it more tax efficient for these higher rate tax payers.

5. **Outright gift of £50,000 for son's house deposit.**
   This would be a potentially exempt transfer and if the clients were to pass away in the next 7 years it could become chargeable (depending on other gifts and the prevailing nil rate band at the time).

Things to consider

- The £400,000 gift into the DDGT, is subject to underwriting, providing a discount to the actual gift into the trust. For these clients, given their age and they are in good health, this discount could be significant, and so the actual gift for HMRC purposes could be much less than £400,000.
- The gift into the DDGT would be a chargeable lifetime time transfer and would become chargeable if the clients passed away within 7 years.
- The gift into trust should be done before the outright gift to the son, in case they become chargeable within the next 7 years.
- While the gifts of £450,000 (less any discount) will take up some of the client's nil rate bands, the client will get their full nil rate band back after a full 7 years after these gifts have been given and it would reduce their potential inheritance tax bill while increasing their income in a tax efficient manner.

The results

1. **IHT liability could be £0 after 7 years** (assuming the estate remaining a similar value and the increase in the residence nil rate band over the next couple of years as well as the nil rate band from tax year 20/21.
2. **Potentially lower tax bills while increasing income** (with no planning, clients would be subject to higher rate tax on their dividend income, and inheritance tax at 40%).

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Wealth

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