Sanlam Wealth

Sanlam Onshore Bond

SCENARIO 1: TRUST PLANNING

CASE STUDY

Exploring how one business-owning couple reduced their tax liabilities by organising their assets into a trust structure

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Client details

- A couple aged 63 and 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 five to seven years, when their son will take over the family business.

	Partner 1	Partner 2
Salary (gross)	£43,000	£43,000
Dividends (joint)	£15,750	

Current assets	Value
Primary residence (joint ownership)	£550,000 (mortgage free)
Cash (joint)	£25,000
Investment account (joint)	£450,000
Pension (joint)	£1,450,000
ISA (joint)	£280,000
Total	£2,755,000
Total subject to inheritance tax (IHT)	£1,305,000

Planning needs

- We're concerned about our current IHT liability.
- We'd like to maintain the same levels of income after retirement.
- We'd like to gift our 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 the 2018/19 tax year). As the investment account is held jointly, both of us can set our annual exemption against our 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 exempt amounts in future years.

3. Invest in ISAs
With the £450,000 investment account proceeds (if sold now), £40,000 (£20,000 each) could be used to maximise our 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 us.

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

5. Outright gift of £50,000 for our son's house deposit
This would be a potentially exempt transfer. If we were to pass away in the next seven 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. Given our age and the fact we are both 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 we passed away within seven years.
- The gift into trust should be done before the outright gift to our son, in case they become chargeable within the next seven years.
- While the gifts of £450,000 (less any discount) will take up some of our nil-rate bands, we will get our full nil-rate band back a full seven years after these gifts have been given. This will reduce our potential IHT bill while increasing our income in a tax-efficient manner.

The results

1. IHT liability could be £0 after seven years (assuming our estate remains 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 2020/21.
2. Potentially lower tax bills while increasing income (with no planning, we would be subject to higher rate tax on our dividend income, and IHT at 40%).

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