2 A SETTLED PURPOSE – INHERITANCE TAX PLANNING THROUGH TRUSTS

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Synopsis

This chapter considers using settlements to make effective gifts while maintaining control of the donated assets and how to maximise those gifts. All references are to the Inheritance Tax Act 1984 (IHTA 1984) unless otherwise stated.

An unpopular tax

Evelyn Waugh described taxes on the devolution of property on death as the means by which the State destroys property 'by literally robbing the widow and the orphan by confiscating bequests' (commentary to 'the Private Man' by T A McInerny (Ivan Obanskey 1962)). It is reassuring evidence of the survival of the British sense of fair play that Inheritance Tax is unpopular even with those whose estates are unlikely ever to bear it, for it is a tax which falls only lightly on the very rich and is brutally confiscatory in respect of the merely prosperous.

There are many reasons for that. The very rich will often hold their assets in forms which qualify for Business and Agricultural Property Relief at 100%. They are often internationally mobile so that they can establish domiciles in other countries. They can afford to forego the benefit of a substantial proportion of their assets without it affecting the style in which they live. For the merely prosperous, however, this is not the case. It is rarely appropriate for them to hold a large proportion of their wealth in business assets once they have ceased to be involved in the day to day running of that business. Similarly, only a small minority will have the experience to take on the risks associated with substantial holdings of agricultural land. If they are based in only one country the decision to change domicile will often involve a complete change of life and a weakening of the familial and social ties built up during their lifetime. Their assets will often be in such a form that it is extremely difficult for them to forego the ability to benefit from them. The expenses of taking and implementing Inheritance Tax advice may be disproportionate to the savings which it offers yet a person who has built up total wealth of, say, £3m from income which has suffered income tax and capital gains which have suffered capital gains tax will find that on his or her death he or she will pay well over £1 million to the Chancellor. The members of each generation have to find out for themselves the waste and profligacy of government in spending the money which it exacts from taxpayers. When they do, it is not surprising that they object to making the State their heir.

One could say flippantly, however, that Inheritance Tax is easily avoided. One has only to give all one's property away seven years before one's death except an amount sufficient to meet one's needs for the remaining period of one's life. The reasons people do not do so are that:

(a) their time of death is uncertain;

(b) their needs during the rest of their life are uncertain;

(c) the persons whom they wish to benefit are not necessarily capable of exercising responsible ownership of assets at the stage in life which they have reached when the gift may best be made for tax planning purposes;

(d) they are concerned that the persons to whom they give their assets will be the targets of claims which will jeopardise those assets.

In order to solve these problems, taxpayers have sought means of making gifts of assets without giving up the ability to control those assets or to benefit from them after the gift.

Gifts with benefit retained

Her Majesty's Revenue & Customs (HMRC), of course, see structures which enable a donor to continue to benefit from his or her gift as tax avoidance which defeats the purpose of the tax and which threatens its yield. The Inheritance Tax legislation is designed to prevent such avoidance; in particular, the Gift with Reservation Provisions (ss 102–104, Finance Act 1986 and Sch 20) and the Pre-Owned Assets Charge to Income Tax (s 84, Finance Act 2001 and Sch 15) are designed to do so.

Gifts with control retained

Until quite recently, HMRC and the government of the day were more relaxed about donors retaining control of assets. They had appeared to understand that children and young adults need to learn the skills of managing valuable assets gradually and to accept trusts as the appropriate mechanism by which this was done. In 2006, however, the Inheritance Tax regime for trusts was radically overhauled so that lifetime transfers into trust, except for a very restricted class, would create settlements within the relevant property regime which previously applied only to discretionary settlements (IHTA 1984 Part 3, Chapter 3).

Parents and grandparents who would like to set aside capital to help their children and grandchildren but do not wish to undermine their independence and sense of personal responsibility by giving them unfettered control of wealth at too early an age, now need to plan carefully and over a long period if they are to make substantial gifts into trust without triggering immediate Inheritance Tax charges.

This chapter looks at the mechanics of doing so and demonstrates that it is possible to settle quite substantial amounts in trust without triggering immediate Inheritance Tax charges and thus to make a substantial saving of Inheritance Tax.

The relevant property regime

Transfers into settlement

A transfer into a relevant property settlement will be a chargeable transfer. It is a disposition as a result of which the value of the transferor's estate immediately after the disposition is less than it would be but for the disposition (s 3). It is not a potentially exempt transfer because it does not constitute a gift to an individual or into a privileged trust (s 3A(1a)). If it is not an exempt transfer, it is, therefore, a chargeable transfer (s 2).

A gift into settlement of this sort, therefore, will only be free of an immediate Inheritance Tax charge to the extent that it is neither exempt nor exceeds the transferor's unused Nil Rate Band (currently at a maximum of £325,000). Even so, a husband and wife could transfer into a settlement assets with an aggregate value of £650,000 plus their unused annual exemptions (£3,000 per annum) without creating an immediate charge to Inheritance Tax and they could do so every seven years because previous chargeable transfers fall out of accumulation after seven years.

Planning Point

A couple who have not previously made chargeable transfers could transfer £662,000 initially ((£325,000 + £3,000 + £3,000) x 2) and £6,000 per year thereafter and a further £650,000 every seven years without triggering an immediate charge to Inheritance Tax. After 28 years, a couple could have transferred £3,430,000 into trust in this way (being 5 pairs of Nil Rate Bands and 30 pairs of annual allowances).

Inheritance Tax charges on the settlement

The Decennial Charge

Settlements are, in effect, treated as discrete taxable entities for Inheritance Tax purposes. The property in the settlement is subject to a charge (the Decennial Charge) on each tenth anniversary of the settlement being made. The rate of charge is calculated (s 66) by reference to a hypothetical transfer of value equal to the value of the property in the settlement, together with the value of property in any related settlement immediately after it commenced, had been made by an individual who had a cumulative total equal to:

(a) the value of chargeable transfers made by the settlor in the seven years prior to the creation of the settlement; and

(b) the amounts upon which Inheritance Tax has been charged on 'exits' (see below) in the previous ten years.

It is accepted by HMRC that undistributed income retained by the trustees but not as yet accumulated does not fall within the charge (Statement of Practice SP8/86).

Other settlements made on the same day by the same settlor are 'related settlements' unless the property is held for charitable purposes only (s 62, IHTA 1984). Whether or not they are relevant property settlements, the property comprised in them immediately after they commence is therefore taken into account when calculating the decennial charge and the exit charge. Where property is added to a settlement the decennial charge for that settlement is subject to an alternative calculation. If the settlor's cumulative total of chargeable transfers is greater before the addition than it was before the settlement was made then the cumulative transfers immediately before the addition can be substituted in the calculation of the decennial charge (s 67).

The exit charge

Where the property comprised in the settlement or any part of that property ceases to be relevant property or where the trustees of the settlement make a disposition as a result of which the value of relevant property comprised in the settlement is less than it would be but for that disposition there will be an exit charge (s 65). Except before the first decennial (s 68), that exit charge will be at a rate which is a fraction of the rate at which tax was charged on the previous decennial (s 69).

Limitations on settlement

The result of all this is that if one settles property equal to the Nil Rate Band and that property grows in value at a rate which is greater than the rate of increase in the Nil Rate Band then one will suffer a tax charge at the decennial of the making of the settlement and when there is an 'exit' under s 65.

One might think that one could easily deal with that problem by advancing, shortly before the decennial, an amount equal to the excess of the value of the relevant property over the then Nil Rate Band. That is not the case, however, because, as we have seen (s 66(5), (6) see above), the hypothetical transfer by reference to which the decennial charge is calculated, is a transfer by a transferor whose cumulative transfers are treated as including the amounts on which exit charges have arisen in the previous ten years in respect of the settlement concerned.

Nor can one simply set up a number of settlements with assets equal to the Nil Rate Band divided among them. That is because, as we have seen above, the rate of tax on a decennial is calculated by reference to a hypothetical transfer of an aggregate amount which includes the value immediately after a related settlement commenced, of the property then comprised in it (s 66(4)(c)). One can, however, create a series of settlements with room to grow by careful regard to the rules for computing decennial charges. The following example shows how this may be done.

Example 1

Mr Redstreak who has made no previous transfers of value establishes five relevant property settlements A, B, C, D and E at three-monthly intervals, each with initial cash gifts of £5,000. He then makes further cash additions of £60,000 to each trust on the same day. Ignoring the availability of his annual exemptions, the margin for growth of each trust is as follows:

	£ A	£ B	£ C	£ D	£ E
Initial value	5,000	5,000	5,000	5,000	5,000
Added Property	60,000	60,000	60,000	60,000	60,000
Trusts' 'clock'	–	5,000	10,000	15,000	20,000
	65,000	70,000	75,000	80,000	85,000
Margin for growth	260,000	255,000	250,000	245,000	240,000
Nil-Rate Band	**325,000**	**325,000**	**325,000**	**325,000**	**325,000**

At the decennials of the settlements, the effect of s 67(3)(b)(i) is that each trust is looked at in isolation, ignoring the others. It is likely that these trusts will never be subject to Inheritance Tax either in respect of an 'exit' charge under s 65 or a decennial charge.

The total scope for future growth taking all of the trusts together is £1,250,000.

Discretionary v Fixed Interest Trusts

The form of the trusts used would depend on the assets in which the trustees were expected to invest. Other things being equal, it is normally best to provide trustees with the widest possible powers so as to preserve flexibility and so that one would normally establish discretionary trusts under which the trustees have a discretion whether to distribute income to the beneficiaries and, if distributed, to decide to whom it should be distributed coupled with a wide discretionary power over capital. Where discretionary trusts receive dividend income which is then distributed to beneficiaries, however, because the tax credit is not repayable, flowing the dividends through the trust substantially increases the total income tax charged on the dividend income.

In that case one would use an income in possession trust under which the beneficiaries would have a right to fixed shares in the income as it arises subject to broad powers of the trustees over capital and to defeat and restructure the income interests.

The exemption for normal expenditure out of income

Exempt transfers

So creating a cascade of trusts enables one to make use of one's Nil Rate Band and annual allowances so as to maximise the transfers into settlement which can be made without triggering an immediate Inheritance Tax charge. The reason that the annual exemption can be used in this way is both because the transfer of value by the settlor is, to the extent that it is an exempt transfer, not a chargeable transfer and because in the computation of the decennial charge, as we have seen, the added property provisions apply only where the settlor makes a chargeable transfer as a result of which the value of the property comprised in the settlement is increased. So if property is added by means of an exempt transfer, the added property provisions are not brought into play. Most exemptions are unlikely to be relevant to gifts into settlement (for example, transfers between spouses (s 18), a gift in consideration of marriage to a child or remoter descendant (s 22) or gifts for national purposes (s 25)). One important exemption, however, which can be utilised so as to greatly increase the amount of property which may be settled without creating Inheritance Tax charges is the exemption for normal expenditure out of income.

Section 21

Section 21 provides that:

> 'A transfer of value is an exempt transfer if, or to the extent that, it is shown:
>
> (a) that it was made as part of the normal expenditure of the transferor; and
>
> (b) that (taking one year with another) it was made out of his income; and
>
> (c) that, after allowing for all transfers of value forming part of his normal expenditure, the transferor was left with sufficient income to maintain his usual standard of living.'

Thus to fall within this exemption a payment must meet three conditions.

Sub-section (1)(a) 'Made as part of the normal expenditure of the transferor'

There have been three decided cases on relief under s 21 (*Bennett & Others v Inland Revenue Commissioners* [1995] BTC 8003, *Nadin v Inland Revenue Commissioners* [1997] STC (SCD) 107 and *MacDowall and Others (Executors of MacDowall, Deceased) v Inland Revenue Commissioners and Related Appeal* [2004] STC (SCD) 2).

The leading case is *Bennett & Others*. In that decision it was said that normal expenditure 'connotes expenditure which at the time it took place accorded with the settled pattern of expenditure adopted by the transferor' (at page 8008 ibid).

'The Settled Pattern'

That settled pattern may be:

> '… established in two ways. First, an examination of the expenditure by the transferor over a period of time may throw into relief a pattern, eg a pattern each year of 10% of all income to charity or members of

the individual's family or a payment of a fixed sum or a sum rising with inflation as a pension to a former employee. Second, the individual may be shown to have assumed a commitment or adopted a firm resolution, regarding his future expenditure and thereafter complied with it.' (*Bennett & Others v Inland Revenue Commissioners* [1995] BTC 8003 at page 8005)

Assuming a commitment

As for the period over which the expenditure must be made Mr Justice Lightman explained in *Bennett* that:

> 'For an expenditure to be "normal" there is no fixed minimum period during which the expenditure shall have occurred. All that is necessary is that on the totality of evidence the pattern of actual or intended regular payments shall have been established and that the item in question conforms with that pattern. If the prior commitment or resolution can be shown, a single payment implementing the commitment or resolution may be sufficient. On the other hand, if no such commitment or resolution can be shown, a series of payments may be required before the existence of the necessary pattern will emerge. The pattern need not be immutable; it must. however. be established that the pattern was intended to remain in place for more than a nominal period and indeed for a sufficient period (barring unforeseen circumstances) in order for any payment fairly to be regarded as a regular feature of the transferor's annual expenditure. Thus a "death bed" resolution to make periodic payments "for life" and a payment made in accordance with such a determination will not suffice.' (See at page 8008 ibid.)

In its guidance on the exemption, HMRC says that 'a reasonable span would normally be three to four years' (Inheritance Tax Manual (IHTM) 14241).

Where there is a commitment to make future expenditure the commitment must envisage that the payments will 'remain in place … for a sufficient period (baring unforeseen circumstances) …' It need not be legally binding. Once that commitment has been made if, at a later time, the taxpayer changes his or her mind and resiles from the commitment that does not affect the application of the exemption to the payments previously made under the commitment.

Quantum

As to quantum, Mr Justice Brightman in Bennett quoted with approval the words of Mr Justice Lowry, in *Attorney General for Northern Ireland v Heron* ((1959) 53 TR3) in which it was said in respect of the phrase 'normal expenditure' in similar legislation under Estate Duty:

> 'To my mind the adjective in the sub-section is used in a qualitative and not a quantitative sense. The adjective, therefore, seems to refer to type or kind and not to size.' (See *Bennett & Others* at pages 8005 and 8006.)

In the case of *Nadin v IRC* one of the factors to which the Court referred as indicating that the expenditure under consideration was not 'normal' was its 'irregularity both in point of time and in amount' (see *Nadin* at page 111).

Mr Justice Lightman in Bennett said:

> 'The amount of the expenditure need not be fixed in amount …
> As regards quantum, it is sufficient that a formula or standard has been adopted by application of which the payment (which may be of a fluctuating amount) can be quantified, eg 10% of any earnings whatever they may be or the costs of a sick or elderly dependant's residence at a nursing home. As regards the payees, it is sufficient that their general character or the qualification for benefit is established, eg members of the family or needy friends.' (See page 8008 ibid.)

HMRC's guidance says:

> 'The gifts must be comparable in size but you need not query discrepancies unless the difference has the effect of placing a gift in a different category from those which are regarded as normal.' (IHTM 14244)

HMRC accepts, therefore, that gifts do not have to be of the same size for them to be regarded as part of the normal expenditure of the transferor but the fact that the gifts vary in size may indicate that they belong to different categories of expenditure, one or more of which is, or are, normal and one or more of which is, or are, not.

No reasonableness requirement

Finally, to fall within this head there is no requirement for the expenditure to be reasonable or of the type commonly made by people generally. Normality is judged in respect of the individual.

Sub-section (1)(b) 'That (taking one year with another) it was made out of his income'

What does the phrase 'made out of income' mean? First, it is accepted that 'income', here, means income under the general meaning of that word, that is, income determined under normal accountancy principles, rather than amounts assessable to income tax under the Taxes Acts. Thus, it will not include amounts of capital such as gains arising on the surrender of life insurance policies or amounts received on the sale of government securities treated as income under the accrued income scheme. HMRC's guidance says:

> 'Income is not defined but should be determined; it does not necessarily coincide with income for Income Tax purposes.' (IHTM 14250)

Does the requirement that the transfer be 'made out of the [transferor's] income' require one to undertake a tracing exercise such as is required to determine whether there has been a remittance of foreign income or capital gains under the remittance basis? The decided cases do not specifically deal with the problem and indeed, none has been concerned with the construction of sub-section (1)(b).

Except where the remittance basis is in point, it is highly unusual for individuals to segregate their income from their capital and there is nothing in the decided cases which suggests that the individuals concerned in those cases did so. Does the fact that sub-section (1)(b) requires one to take 'one year with another' indicate that rather than tracing moneys from their source through the taxpayer's bank accounts to the payment one merely has to do an overall accounting exercise in which one identifies whether it is possible that a payment could be made out of income because there was a surplus of income over revenue expenditure?

HMRC guidance says that:

> '… the transferor should have made the gift out of their income. Thus the gift of jewellery or securities does not qualify unless it was specifically purchased by the donor with the intention of making a gift.
>
> Repeated renunciations of bonus issues of shares do not qualify for exemption although purchases of rights issues in the names of donees may do so.
>
> Income is considered to refer to current income. Gifts will not normally satisfy the second condition if made from a source which, although originally income, has by retention over a period of time acquired the nature of capital. The fact that the retained income has been invested or saved in a form that itself yields income will normally show that it has become capital. However, invested funds may remain income if the transferor was really saving them temporarily in order to accumulate an amount sufficient for some expenditure specifically contemplated.' (IHTM 14250)

This suggests that in HMRC's view a tracing exercise is required. It would be a logical corollary of the view expressed in the passage quoted above, for example, that, if the taxpayer held shares which were not merely a temporary investment and were capital assets which he then sold and applied to a gift, the exemption for normal expenditure out of income would not apply.

If that is HMRC's view, it goes beyond what is justified by the legislation or the case law. Nonetheless, the cost and uncertainty of challenging HMRC's view on any matter are so great that it is prudent to fall within their published views rather than outside them if one can. A counsel of perfection would be to segregate funds in the way in which, for example, a non-domiciliary segregates his offshore accounts, so as to clearly identify the regular payments as being amounts of income. In practice, few people would care to have their use of money restricted in this way. If there is a surplus of income over revenue expenditure it is unlikely that HMRC would be successful in asserting that a gift from a bank account which, although it also contained capital, contained sufficient income to make the gift, did not come wholly within sub-paragraph (b).

Sub-section (c): 'after allowing for all transfers of value forming part of his normal expenditure, the transferor was left with sufficient income to maintain his usual standard of living.'

What are 'transfers of value forming part of his normal expenditure'? We have seen that a transfer of value is a disposition by which the value of the estate of the transferor is reduced. Two specific rules, however, provide that, loosely, dispositions not intended to confer gratuitous benefit and dispositions for the maintenance of a spouse or minor child are not transfers of value (ss 10 and 11). A transfer of value could be a capital transaction. Most investment transactions, however, will not be transfers of value either because they do not decrease the investor's estate or because they were not intended to confer a gratuitous benefit. A capital gift to charity, for example, will be a transfer of value.

The question is how one allows 'for all transfers of value forming part of his normal expenditure' in considering whether 'the transferor is left with sufficient income to maintain his usual standard of living'. Arguably, if an amount of expenditure is capital expenditure it cannot affect the amount of income which is left to the payer after the expenditure has been made.

The transfers of value taken into account under sub-section (c) must form 'part of [the transferor's] normal expenditure'. There is nothing to suggest that this phrase in sub-section (c) is to be interpreted differently than the same phrase in sub-section (a). So unless there is a commitment to make the expenditure for a sufficiently long period or the expenditure of that type is actually made for a sufficiently long period it will not be normal expenditure of the transferor.

Sufficient income

How does one determine whether the transferor was 'left with sufficient income'? Of the three cases which have been decided on s 21, sub-section (c) was considered only in *Nadin* (this was a case before the Special Commissioners which did not proceed to the High Court). In that case, in respect of certain years, the Special Commissioner found that the condition in sub-section (c) was not satisfied because the taxpayer's annual nursing home costs, personal expenditure and Income Tax exceeded her annual income. The decision does not record any argument on the construction of sub-section (c) except that the Appellant argued that capital sums on the sale of investments were income. What was not argued was whether sub-section (c) allows one to take into account the extent to which capital is available to supplement income and is actually applied to doing so.

HMRC assumes, in its guidance, that the exemption will not apply to the extent that 'the transferor had to resort to capital for living expenses' (IHTM 14251). It is arguable, however, that if one had such a large amount of capital that, on the basis of the most conservative estimates, it would be sufficient to fund one's living expenses for one's lifetime even a small amount of income would be sufficient to maintain one's usual standard of living. People in that position, therefore, would have sufficient income to maintain their usual standard of living even if all but a minimal part of their income were expended in making gifts. Such a construction would not empty sub-section (c) of effect because less wealthy people would need to retain capital if they were not to jeopardise, in the long term, their ability to maintain their usual standard of living.

The following example shows how the normal expenditure out of income exemption can be used, over an extended period, to make very substantial transfers into settlement.

Example 2 – normal expenditure out of income: Scope for increased gifts

Mr and Mrs Dabinett wish to settle funds on trusts for the benefit of their three sons, Harry, Dymock and Broxwood, to the maximum possible extent without suffering an immediate Inheritance Tax charge. Mr Dabinett's annual after-tax income fluctuates between £400,000 and £600,000. Mrs Dabinett's annual after-tax income fluctuates between £200,000 and £250,000. They make no other transfers of value. The amount they spend annually on maintaining their usual standard of living is as follows:

	MIN £	MAX £
Mr Dabinett	400,000	450,000
Mrs Dabinett	190,000	210,000

Mrs Dabinett is a non-domiciliary and much of her income does not bear UK Income Tax. As we have seen, however, income for this purpose is not taxable income. So the fact that her income is not brought into charge to Income Tax because she is taxed on the remittance basis does not prevent her taking that income into account in determining whether the normal expenditure out of income exemption applies.

Variability

The fact that the excess of Mr and Mrs Dabinett's income over expenditure fluctuates significantly from year to year does not mean that they can only take advantage of the exemption in respect of the minimum annual excess. It would be possible for them both to record their intention for the foreseeable future to make gifts out of income in favour of their children equal to the excess of their income from year to year over the amount of that income which they expend on maintaining their usual standard of living. They could determine this excess after the end of each fiscal year and make settlements in their children's favour on a fixed date in the year thereafter.

That would be sufficient to conform to Mr Justice Lightman's analysis of the requirements of sub-section (1)(a). There would be a commitment covering a sufficient period for the payment fairly to be regarded as a regular feature of the transferor's annual expenditure. Although the payment would be a fluctuating amount it would be determined by reference to a formula which would not differ very greatly from the formula considered in *Bennett* in which a mother who was the beneficiary of an interest in possession trust instructed her trustees to distribute to her sons so much of the income arising in each accounting year as was surplus to her financial requirements

An established pattern

Let us now assume that, over the period with which we are concerned, Mr Dabinett's average annual excess of income over expenditure is £100,000 and Mrs Dabinett's is £30,000. They might adopt the following strategy.

They both complete memoranda recording their intention to make annual gifts from their income on trust for their children equal to the excess of their income over the amount sufficient to maintain their usual standard of living.

Mr Dabinett sets up ten bank accounts and Mrs Dabinett sets up three bank accounts. They pay £10.00 into each bank account. The accounts set up by Mrs Dabinett are outside the United Kingdom and the moneys which she pays into the account are paid from an offshore income bank account. The moneys which Mr Dabinett pays are from the accounts into which his income is paid.

On each day from 1 to 5 December 2010 they each complete a deed per day declaring that they will hold the funds in a bank account which they have established on trusts for a class of beneficiaries which includes their children. Each trust deed provides that no child or grandchild of the settlor or the settlor's husband or civil partner may benefit under the settlement while they are under the age of 18. The trust deeds recite the existence of the memorandum made by the settlor of those trusts and that the settlements are intended to fulfil part of the settlor's intention to make gifts expressed in that memorandum.

On 1 January 2011 they add an amount to each settlement equal to the aggregate of the Nil Rate Band and unused annual allowance for the prior year, divided by the number of settlements they have made, less £10.00. So Mr Dabinett adds £32,790 ((£325,000 + £3,000) ÷ 10) – £10) to each settlement which he has settled and Mrs Dabinett adds £109,323 ((£325,000 + £3,000) ÷ 3) – £10) to each settlement which she has settled.

In January of each year, as part of the work done to prepare their tax returns, the excess of their income over their living expenditure is determined. On 31 January in each year they enter into a deed of addition and pay an amount equal to the aggregate of their excess income and the annual exemption divided by the number of settlements they have settled by way of addition to each of the settlements which they have settled. Once again, the deed would recite the existence of the memorandum and that the settlements are intended to fulfil the settlor's intention to make gifts expressed in that memorandum. So Mr Dabinett would add an average £10,300 ((£100,000 + £3,000) ÷ 10) per settlement and Mrs Dabinett would add an average £11,000 ((£30,000 + £3,000) ÷ 3).

Planning Point

The rate of tax on future decennials of the trusts and on assets being withdrawn from the trusts will be nil per cent unless the value of the assets in the settlement grow to exceed the Nil-Rate Band by the tenth anniversary concerned. It is for that reason that both have set up a number of trusts, the number being chosen to leave plenty of room for growth.

At the end of the seven years Mr Dabinett would have settled £104,900 ((£10 + £32,790) + (£10,300 x 7) on each settlement. Mrs Dabinett would have settled £186,333 (£109,323 + 10) + (£11,000 x 7)) on each settlement. So they would have settled £1,607,999 ((£104,900 x 10) + (£186,333 x 3) in all divided between 13 trusts.

The settled funds are unlikely to suffer any Inheritance Tax while they are in the settlement or on being distributed to the beneficiaries. The settlements could continue for 125 years if that was desired or even longer if they were written under a law with a longer perpetuity period.

What is more, this pattern could be continued every seven years until Mr and Mrs Dabinett judge that their children are sufficiently mature to receive outright gifts. Even then, there would still be advantages in creating settled funds which effectively are placed outside the scope of Inheritance Tax for 125 years.

Planning Point

It might be objected that creating so many trusts would create a major administrative burden. It is obviously true that the trusts will require some administration but perhaps less than clients might think. The use of standard documentation and of nominees to hold trust assets would greatly reduce the administrative work required. Much of the work would be at a relatively routine level so that it should not be too expensive per hour. A degree of organisation on behalf of the client or his or her accountants and tax agents would contain costs within manageable proportions.