

The Accumulation & Maintenance trust is dead; long live the Accumulation and Maintenance bond!

Accumulation & Maintenance (A & M) Trusts were an exceptionally beneficial form of discretionary trust, which were popular with parents and grandparents looking to provide for minor children and grandchildren. The Finance Act 2006 aligned A & M trusts with the 'relevant property regime' applicable to discretionary trusts. This effectively ended the use of A & M trusts. Clients wishing to undertake similar planning at this point are effectively restricted to making:

- Gifts to bare trusts where the beneficiaries will receive the full value of the gift at age 18 as of right.
- Transfers to discretionary trusts within the current nil rate band, £312,000 for 2008/09, or pay a 20% tax charge on any excess.
- Retain the capital and make gifts when beneficiaries are of an age when they are deemed to be financially responsible.

Is there a suitable alternative? Yes, the Accumulation and Maintenance Bond provides the following benefits:

- A PET (potentially exempt transfer) for inheritance tax (IHT) purposes.
- No income tax or capital gains tax on any income or growth retained in the bond.
- Allows withdrawals of up to 5% per annum of the original investment amount with no immediate tax charge. Withdrawals can be utilised for the maintenance and benefit of the beneficiary.
- Allows the donor to specify the date when the beneficiary can access the capital.
- A very simple investment which avoids the reporting requirements, expenses and tax implications of a discretionary trust.
- Open architecture investment platform allowing access to all the major asset classes ranging from cash deposits to hedge funds.

How does it work?

The donor invests into an offshore life assurance bond and assigns the bond to bare trustees to hold for the chosen beneficiary or beneficiaries. To prevent the beneficiary being able to access the capital of the bond at age 18, the bond has the surrender option removed for a set period of time. It would also be possible to restrict the cumulative annual withdrawal level if required. Restriction of the surrender value ensures that although the beneficiary can receive the bond at age 18, he/she cannot actually encash the bond until the surrender option becomes available. This could be set to age 25 or whatever point the donor feels is suitable for the beneficiary. The beneficiary could potentially sell the bond in the open market, but the market to purchase such an investment would be very limited.

What are the Inheritance tax implications?

The assignment of the bond to the bare trustees will be a PET, and the value of the PET will be the higher of the market value of the policy or the amount of the initial premium. The value of the PET will fall out of the donor's estate after seven years. The donor does not retain any rights to any element of the gift, so the gift with reservation of benefit rules or pre-owned assets charge cannot apply.

What about income and capital gains tax?

The bond will be treated in accordance with the normal 'chargeable event' legislation applying to offshore life assurance bonds. Any income and gains within the bond will accumulate free of any tax (bar any non-recoverable withholding tax).

A chargeable event will occur when the bond is fully surrendered; a withdrawal in excess of the 5% per annum cumulative allowance is made; the bond is sold to a third party, or upon the death of the last surviving life assured. Any chargeable event gain will be subject to income tax at the beneficiaries' marginal rate. The beneficiaries can benefit from 'top-slicing' relief which may reduce the tax charge, particularly if they are basic

rate taxpayers. Any potential tax charge may also be reduced if the beneficiary makes encashments over a number of years.

A by-product of the removal of the surrender option is that if the last life assured dies when the surrender option is still restricted, then the bond has an effective nil value under the chargeable event rules. This could dramatically improve the tax situation in certain circumstances.

Who is the Accumulation & Maintenance bond suitable for?

- Those wishing to choose the exact age when beneficiaries can receive capital.
- Those who will not need to alter beneficiaries' entitlements in the future.
- Those looking to fund school fees and the maintenance of minor children or grandchildren in an IHT effective manner whilst making use of the PET regime.
- Those wishing to provide a regular income to beneficiaries without providing the beneficiary with outright access to capital.
- Those wanting to avoid the administrative requirements and taxation implications of discretionary trusts.
- Those who have already utilised or wish to retain their nil rate band allowance for other IHT planning.
- Those who wish to make gifts in excess of the nil rate band.
- Those who wish their chosen beneficiaries to receive capital after a set period or after the death of the donor/s, whichever is earliest.

Summary

Mitigating IHT is often an important requirement for many clients, but Finance Act 2006 considerably reduced the attractiveness of certain transfers into lifetime trusts. Clients looking to replicate the nature of an A & M trust can utilise the A & M bond, which provides a simple, uncontroversial and cost effective planning solution. As always, it is imperative to receive personalised advice to ensure that you successfully achieve what should be the overriding aim of any estate planning exercise:

“To place the right assets in the right person’s hands at the right time, with the minimum of Inheritance tax.”

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