Inheritance Trust Case Study – Marjory White

Our prospective client Mrs White, aged 64 had been widowed 30 months previously after losing her husband to cancer. She has 2 children, both married, and five grandchildren. She explained her main concerns were to have enough income to meets her needs, to pay as little tax as possible, and to preserve as much capital as possible for the family on her death.

Her solicitor had calculated that her estate was around £1m made up of the family home worth £500,000, shares and unit trusts worth £180,000 and cash on deposit of £320,000. She confirmed her state pension and widow's pension from her late husband's company scheme amounted to about £20,000 p.a. after tax while she estimated her current outgoings amounted to around £36,000 p.a. including holidays and gifts for the grandchildren. She thought that this would reduce in future as she would probably move to a smaller house at some point.

Her solicitor had explained that although the option to vary the terms of her late husband's will had been discussed no action was ever taken and as her husband's entire estate had passed to her and he had not made any chargeable transfers, she had inherited his nil rate threshold. It had been calculated that the estate would have a prospective IHT bill of £150,000.

It became evident during the meeting that she was very undecided about how she wanted her estate to be divided up between children and grandchildren. She was also quite nervous about the idea of tying money up, and although her late husband had mentioned putting some capital into trust the idea had never appealed to her for that reason. This had also been one of her concerns about varying the will provisions by Deed of Variation. However, she had come to the conclusion that she should do something about Inheritance Tax. After considering the various options and taking into account her wish to retain access to capital we suggested that she transfer £300,000 to a Discretionary Capital Drawdown Trust, keeping £20,000 on instant access in case of emergencies.

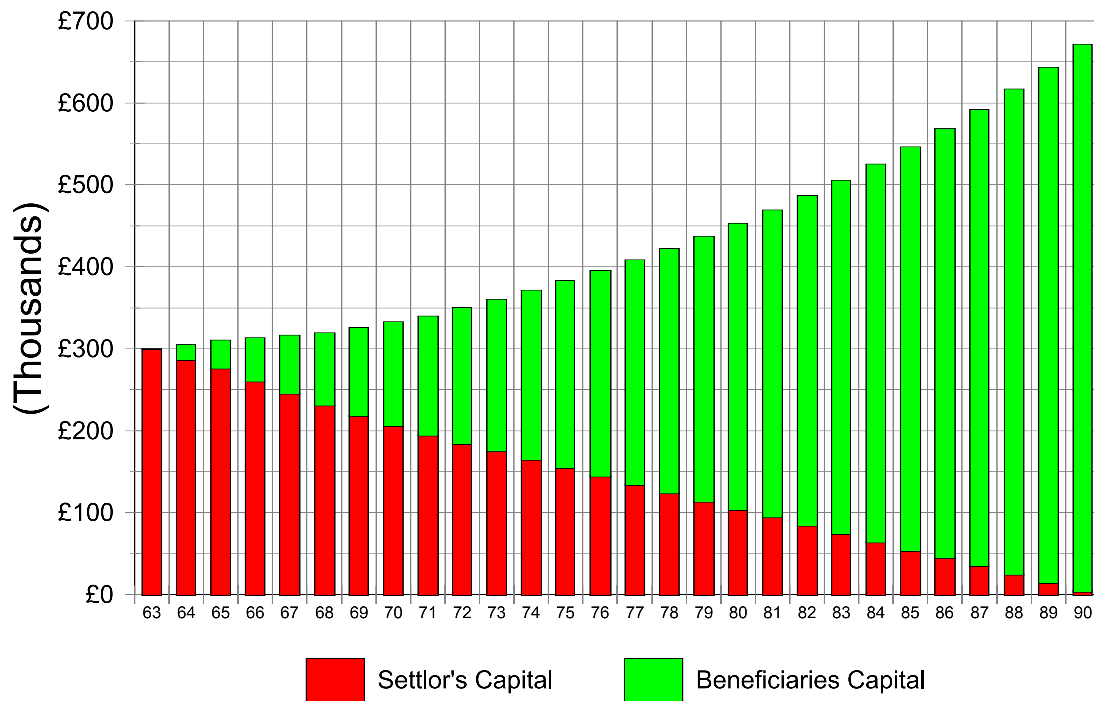
We explained that this involved her making an interest free loan to a trust with discretionary distribution powers so that she did not need to decide at the outset how the proceeds were to be split between her children and grandchildren. We also explained that she retained full access to the initial capital at any point on demand and that she could either draw down the capital from the trust on an 'ad hoc' basis or in the form of regular loan payments until the loan had been repaid in full.

We estimated that from her stock market investments which included PEPs and ISAs she would receive a net income of around £5,000 p.a. which could reasonably be expected to increase over time. Together with her other income this gave her about £25,000 p.a. towards her estimated outgoings of £36,000 p.a. We therefore proposed that she would initially take regular loan repayments from the trust starting at £12,000 p.a. or £1,000 per month which would then give her a total 'income' of £37,000 p.a. – a little more than her budget demanded.

We also explained that the level of her monthly capital drawdown would be reviewed with her each year, and could be reduced or increased according to her changing needs. We also explained that, as these payments were repayments of her own capital she had no tax to pay on the 'income'.

The benefits to Mrs. White of the Discretionary Capital Drawdown Trust are as follows:

- A regular and reliable 'income' with no tax
- Access to the 'principal' capital sum on demand, if necessary, giving her significant comfort.
- The gradual reduction of her taxable estate, and the accumulation of beneficiaries' capital under Discretionary Trust that could eventually pass to them free of Inheritance Tax.



As the initial transfer of capital is not by way of gift, there is no chargeable transfer on creation of the trust. As a Discretionary Trust there would be a possibility of a periodic charges to IHT every 10 years and an exit charge on distribution of capital to beneficiaries. In reality this would be unlikely or minimal given that the value of the beneficiaries' share of the trust would need to outgrow the nil rate threshold available to the trust.

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