Bare Trust Guide

Health warning and disclaimer

This Trust and this Guide are based on Novia Financial plc’s understanding of UK law and HM Revenue and Customs’ practice as at 6 April 2018.

Novia Financial plc cannot accept any responsibility for its interpretation of the law and tax implications.

This Guide is given on the strict understanding that potential investors will take independent professional legal and tax advice before taking, or refraining from taking, any action in connection with this Guide and before creating any trust.

This Guide is a potted summary of the key issues. It is not intended to cover every conceivable implication of the Trust.

What is a Trust?

A trust exists where someone (a trustee) holds property (trust assets) for the benefit of someone else (a beneficiary). A trust is not a separate legal entity like a company. Rather, it is a bundle of rights and duties binding the trustee and the trust assets for the benefit of the beneficiary.

The purpose of the trust deed is to set out the terms on which trustees hold trust assets for the benefit of the beneficiary. This trust deed creates a BARE TRUST. The key feature is that a child – the BENEFICIARY – is absolutely entitled to the trust assets outright.

Why use a Bare Trust?

Setting up a bare trust is usually done for two reasons - first, to save inheritance tax for the Settlor by getting assets out of their estates (more on this below), and, secondly, to set up a savings fund for an infant child (often a grandchild).

It is called a BARE TRUST because the Trust assets belong to the Beneficiary in the eyes of the law. Effectively the trustees hold the trust assets like nominees for the Beneficiary.

The trustees have no discretion to benefit anyone else, and must hand the Trust assets over to the Beneficiary at the age of 18 if the Beneficiary so requests. The Trustees are like nominees, but while they hold the Trust assets they have the discretion to make the most appropriate decisions regarding the investment and management of the Trust assets.

The nature of the Trust means that the Trustees do not need to make separate trust tax returns. And the normal high rates of income tax on trustees do not arise. Subject to what is said below, income and gains will be taxed on the Beneficiary personally and should be reported in the Beneficiary’s tax return.

If the Beneficiary dies, what happens to the Trust assets will be governed by the Beneficiary’s will or, if the Beneficiary is a child or has no will, by what happens under the intestacy rules.

If an unmarried infant Beneficiary dies leaving parents, then they will be entitled to the Trust assets under the intestacy rules and will also be entitled as the administrators of the child’s estate to call for the Trust assets.

Section 1 – When is the Trust set up?

Insert in section 1 the date on which the Trust deed has been signed by the Settlor and the other Initial Trustees.

Section 2 – Who sets up the Trust?

The person or persons setting up the Trust are called the SETTLOR, and their full names and addresses should be entered in section 2.

Section 3 - Who are the Trustees?

The Initial Trustees, and anyone else who may subsequently act as trustee, are called the TRUSTEES.

The Settlor should circle ‘YES’ or ‘NO’ in the relevant boxes to say if the Settlor is to be an Initial Trustee, AND sign in the boxes concerned.
The details of any other/additional Initial Trustees should be added. It is wise to avoid having just one Trustee.

The Settlor is given the power to appoint new and additional Trustees while alive. Subject to that, the Trustees have the power to appoint new and additional Trustees.

Trustees can retire at any time.

If there is no surviving Trustee, the Trust will nevertheless continue to exist. The personal representatives (prs) of the last surviving Trustee will act as Trustees. Although the Trust assets will not be part of the last surviving Trustee's estate for tax and probate purposes, getting probate or letters of administration to the Trustee's estate will still be necessary to ensure that the prs can act as Trustees.

**Section 4 - Who is the Beneficiary?**

The full name and address and date of birth of the Beneficiary, and how the Beneficiary is related to the Settlor, should be put in the box provided.

If the Settlor wants to benefit more than one Beneficiary, then use separate bare trust forms for each one.

**Section 5 - What goes into the Trust?**

The Trust is set up at the start with the **INITIAL ASSETS**, i.e. Cash or investments which should be described in the box provided.

Of course further property may be added to the Trust after it has been set up.

**Section 6 – How does the Beneficiary benefit under the Trust?**

The Beneficiary is entitled to the trust assets and any income arising absolutely. That means that when they reach 18, they can call for all or any of the trust assets and income to be paid out.

A Beneficiary who is under 18 will not be legally able to call for the assets. And a Beneficiary who is over 18 may wish the Trustees to keep holding and managing the trust assets for them.

The Trust further provides that the Trustees can pay out capital to a Beneficiary who is under 18. As regards Trust income, the Trustees will pay it out to the Beneficiary unless they decide to keep and reinvest it.

**Section 7 – What powers do the Trustees have?**

The Trust sets out a set of administrative powers to help the Trustees invest and manage any assets they hold. Subject to any direction a Beneficiary who is over 18 may give, the Trustees have discretion in exercising their powers. The Trustees are given a wide power of investment and power to delegate their powers if ever necessary.

The Trust contains an indemnity clause. This provides that Trustees will not be liable for loss unless it is caused by their own fraud or negligence. The Trust also allows professional Trustees to charge for their services.

**Section 8 - Execution**

Each Settlor and Initial Trustee needs to sign in section 8. Each needs to sign before an independent adult witness who should sign and add their personal details where indicated.

The Trust should be dated in section 1 when everyone has signed.

**What are the tax considerations?**

In the following sections it is assumed that the Settlor, the Beneficiary and the Trustees are UK resident and domiciled. Special rules – not covered here - apply where this is not the case.

**Tax on putting assets into the Trust – (1) Inheritance Tax**

Each time the Settlor puts assets in the Trust, there is a gift for inheritance tax. There will be no inheritance tax charge unless the Settlor dies within seven years of the gift.

Where there are two Settlors who put in jointly held assets, they are each treated as making a gift of their share of the full value of the assets given to the Trustees.
Although the Trust says that everything in it is for the benefit of the Beneficiary, it is spelt out that the Settlor cannot benefit in order to reinforce this inheritance tax treatment.

The Settlor should ONLY put assets into the Trust if they do not need access to the assets ever again. If that is not the case, then don’t set up the Trust!

**Tax on putting Assets into the Trust – (2) Capital Gains Tax**

A gift of assets into the Trust is a taxable disposal for capital gains tax and will, unless the gift is of cash, need to be put in the Settlor's tax return.

Where there are two Settlors who put in jointly held assets, they are each treated as making a disposal of their share of the full value of the assets given to the Trustees.

No tax charge will arise if the gift is cash.

But if the Settlor transfers investments into the Trust, there could be a capital gains tax charge if the market value of the investments is higher than the purchase price when the Settlor acquired the investment and higher than the Settlor's available tax allowance.

**Tax on Trust Assets – (1) Income and Capital Gains**

Subject to what is said below about parents, income and gains arising in the Trust will be taxed on the Beneficiary personally. The Beneficiary’s tax rates and allowances will apply.

**Tax on Trust Assets – (2) Inheritance Tax**

If the beneficiary dies, the market value of the trust assets at that date will be subject to inheritance tax as part of the beneficiary’s estate.

**Tax on Trust Assets – (3) Income and Gains - anti avoidance**

If the beneficiary is a child under 18 and unmarried, and if the beneficiary’s parent put assets in the trust, if the income is over £100, then all the income (including the first £100) will be taxable on the parents. Capital gains will be taxed on the child, not the parents, however.