# The Benefits of Trusts and the use of Loans

## Risk of absolute distributions

- Disinheritance
- Increased estate value for Inheritance Tax.
- Inheritance completely attackable from marriage after death, divorce, bankruptcy and care.
- Funds can be easily wasted by spendthrift beneficiaries.

**In Detail**

### What is a Trust and what benefits can it provide?

It is important to understand what a Trust is and what benefits a Trust can provide.

A Trust is a legal relationship which is created when you as a settlor transfer assets to two or more people (the trustees) with instructions that they hold the assets for the benefit of your loved ones (the beneficiaries).

To achieve this, the Trust separates the legal ownership of the asset or property from the beneficial ownership. The legal ownership of an asset is given to the trustees who are bound by the terms and conditions of the Trust deed and subject to general Trust law. It is their duty to hold and administer the Trust property in the best interests of your chosen beneficiary(ies), who will ultimately benefit from it.

As a result of the trustees owning the Trust property, these assets are then not deemed to be part of your loved ones estate(s).

**So these Trust assets, managed properly, would not be subject to any claims on your beneficiary(ies).**

### The risks of full distributions

If your spouse or partner remarried after you died and you left them all of your assets, then the new spouse may inherit everything. The possible result is that your children may inherit nothing, as the new spouse could leave it to their own family and disregard any step-family.

If your children are going through divorce or separation then they may lose half or more of their estate(s) including anything you may have left them.

**In Detail**

Similarly, if your children are subject to creditor claims, then again they may end up losing their whole estate(s).

Generational Inheritance Tax (IHT) is also something many do not consider. You may not have an IHT issue but your loved ones may create their own wealth in their own lifetime. So, if they then inherit further assets, this could create or compound their own IHT problem. Furthermore, the issue can escalate down the generations, along with the possibility of the other risks as well, even an initial modest estate(s) can be diminished significantly over a matter of one or two generations.

The assets distributed from the Trust fully will increase your loved ones estate(s) accordingly and therefore could push the estate(s) further over the Inheritance Tax Nil Rate Band threshold.

Furthermore, if your loved ones require nursing care, the Local Authority assesses the individual's own assets which includes those assets fully distributed to them from the Trust. Arguably the whole distribution is then at risk to those care fees as your loved ones are likely not to gain any financial assistance from the Local Authority.

Each case should be considered on its own merit and it is the trustees who clearly have to consider the best strategy or strategies.

It would also be worthy to note that the trustees must use their utmost diligence to avoid any loss. If they are negligent and a loss arises they may be responsible for that loss to your beneficiary(ies).

## Our preferred strategy of using loans

A major strategy available to the trustees is that of loaning assets to your beneficiary(ies). This means that the asset is still technically a Trust asset. A tailored loan document would be drawn highlighting the basis of the loan in terms of the value and the potential criteria for it to be repaid back to the Trust. Your beneficiary(ies) can then do as they wish with the loan.

As an example, it would generally be agreed at the outset that the loan would be interest free and is to be repaid only on the death of your beneficiary(ies). This would further reduce your beneficiary(ies) own estate(s) and therefore reduce or negate Inheritance Tax on their estate(s), on their own death. Interest may be added in some circumstances, as this can further reduce your beneficiary(ies) own estate(s) (but increases the Trust assets for their issue going forward).

A common strategy relates to what the Trust funds would be used for. The trustees could agree to assist your beneficiary(ies) of the Trust with repaying a mortgage on their property. It would be feasible for the trustees to loan the monies to your loved ones as noted above but the Trust could decide to repay the lender direct and therefore the Trust would 'own' that proportion of the property, often secured by placing a restriction on title where possible.

The property is partially owned by a Trust and not your beneficiary(ies) which would be reflected on the title of the property. Therefore, part of the asset repaid does not add to your beneficiary(ies)' estate(s). That part of the property cannot be claimed by creditors, divorce proceedings or care fees. So your wealth is protected for your loved ones.

On agreement of the trustees, your loved ones continue to live in that property as normal. The settlor/beneficiary(ies) will almost certainly be a trustee, so there is no loss of control. The option of moving home in the future is also possible.

If your loved ones need care the Local Authority can only assess the individual's assets and that may only be a part of that property. The value of a joint interest in property will be affected by whether the other joint owner or another interested party is willing to buy the resident's share. If not, it is highly unlikely that an outsider would be willing to buy into the property. In these circumstances the value of the interest, even to a willing buyer, could be very low or could effectively be nil. Therefore, the full property could be protected from care.