Trust Range

Excluded Property Trust guide

For financial advisers only

What is the purpose of an Excluded Property Trust?

An Excluded Property Trust is suitable for individuals who are not domiciled in the United Kingdom and who want to protect their worldwide assets from Inheritance Tax (IHT).

On what is IHT charged?

IHT is charged in respect of the worldwide assets of individuals domiciled in the UK and in respect of the UK assets of those individuals domiciled elsewhere.

It should be remembered that domicile for IHT purposes includes 'deemed domicile'.

What is "deemed domicile"?

For the purposes of IHT, only an individual who is not UK domiciled as a matter of law is nonetheless treated as being UK domiciled in two situations:

a) if he/she was resident in the UK for more than seventeen of the twenty income tax years of assessment ending with the year in which a transfer falls

b) if he/she was domiciled in the UK within the three years immediately preceding a transfer.

What is 'excluded property'?

'Excluded property' is the term used in IHT legislation to describe assets that are outside, or excluded from, the scope of IHT.

What type of property is excluded?

1) Property situated outside the UK, owned by an individual domiciled elsewhere is excluded property. (For example, an Italian villa owned by a German domiciled individual would be excluded property.)

2) Certain exempt gilts, if beneficially owned by a person who is not UK domiciled and who is not ordinarily resident in the UK.

3) A holding in an authorised unit trust or shares in an OEIC where the beneficial owner is not UK domiciled.

4) Settled property where certain conditions are satisfied.

1 to 3 above deal with assets owned directly by an individual – the governing legislation is to be found in Inheritance Tax Act 1984, Section 6;

Point 4 above deals with property held in trust – the governing legislation is to be found in Inheritance Tax Act 1984, Section 48.

What are the rules relating to assets held in trust?

Settled property is excluded property if,

the settlor was not UK domiciled at the time the settlement was established

and,

the property is situated outside the UK.

A trust meeting these conditions is known as an 'excluded property trust'.

The domicile status of the settlor at the time the trust was established is the key factor. If the settlor's domicile later changes (for example he becomes deemed domiciled in the UK) the trust assets remain excluded property.

The residence status of the trustees is irrelevant.

The domicile status of the beneficiaries is irrelevant.

If the settlor is a beneficiary, do the 'reservation of benefit' rules apply?

The reservation of benefit rules do not apply to excluded property trusts.

Are there ongoing IHT charges on the trust?

Because the trust is an excluded property trust (and assuming that it remains so) the ten-yearly and exit charges associated with discretionary trusts will have no impact.

What are the legislative provisions?

"(3) Where property comprised in a settlement is situated outside the United Kingdom-

a) the property (but not a reversionary interest in the property) is excluded property unless the settlor was domiciled in the United Kingdom at the time the settlement was made, and

b) section 6(1) above applies to a reversionary interest in the property but does not otherwise apply in relation to the property."

[Inheritance Tax Act 1984 Section 48(3)]

Why is an offshore bond suitable for use in an Excluded Property Trust?

A RL360° bond is a Manx asset issued by a Manx-resident company and governed by Manx law. In a suitable trust it meets the test of being "situated outside the UK".

An offshore bond can be assigned without a capital gains tax charge, making it particularly suitable for use in trust arrangements.

An offshore bond does not generate any income. An excluded property trust will not therefore necessitate the completion of an income tax return unless/until a chargeable event occurs.

You can count on us

Who are the parties involved in an Excluded Property Trust?

The settlor is the individual who provides the funds for the trust.

The trustees are the individuals who administer the trust.

The beneficiaries are the people who will ultimately benefit from the trust.

The settlor is automatically a trustee where RL360°'s International Flexible Trust is used.

Who pays UK income tax if the bond is surrendered at a profit?

Where the trustees of an Excluded Property Trust own an offshore bond, the gains on a chargeable event are charged to UK income tax:

a) on the settlor whilst UK-resident;

b) on UK-resident trustees where the settlor is dead or non-resident;

c) on UK-resident beneficiaries where neither (a) nor (b) applies.

Income tax chargeable events will need to be self-assessed.

How is the settlor's gift treated for UK IHT purposes?

The settlor's gift is a not a transfer for UK IHT purposes.

Will establishing an Excluded Property Trust trigger a pre-owned asset tax charge?

No, the settlor will not be within the scope of pre-owned asset tax in relation to the trust fund.

Must the establishment of Excluded Property Trusts be reported to UK HM Revenue & Customs?

No. There may be a requirement to report the establishment of the trust if offshore trustees are appointed.

Does an Excluded Property Trust avoid the need for probate in respect of the bond on the death of the settlor?

Yes, as the trustees are the legal owners of the offshore bond, it will not form part of the settlor's estate for probate purposes.

What powers do the trustees have?

Where RL360°'s International Flexible Trust is used, the trustees have wide-ranging distributive, administrative and investment powers.

Within the International Flexible Trust the trustees have the power to distribute the trust fund (or part of it) to beneficiaries as, when and in such proportions as they see fit.

The trustees have the widest possible investment powers.

Who are the possible beneficiaries under the International Flexible Trust?

The possible beneficiaries include the settlor, the settlor's spouse or civil partner, children, grandchildren and remoter descendants, brothers and sisters, and any individual or charity named by the settlor as a beneficiary.

Case study

Anatoly was born in St. Petersburg in 1976.

He played as a goalkeeper for Zenit in the Russian Premier League and having spent two seasons playing in the Bundesliga, came to the UK in 1998.

He has enjoyed his time playing in the Premiership and he and his family have settled happily in London. Anatoly has a house in West London valued at £1.5 million and has accumulated approximately £1 million in cash (held in Jersey bank accounts) with a similar amount in equities managed by Jersey stockbrokers. He also owns an apartment on Nevski Prospekt which has recently been valued at £300,000.

Anatoly looks after himself and reckons he can continue playing football at a high level for another few years. After that he intends to go into football coaching and ultimately management.

His wife Irina works for an investment bank in the City of London and their two children, Vassily (8) and Valentina (5), attend school in London.

Anatoly intends to base himself in London until his children's education is complete. Thereafter he would consider moving throughout Europe as available work dictated.

He is worried about the impact of IHT on his family and has taken specialist advice on this. He has been advised that he has not acquired a UK domicile of choice (replacing his Russian domicile of origin) because he has no settled intention of remaining permanently or indefinitely in the UK. However there is a strong possibility that he will become 'deemed domiciled' in the UK as he may well be resident for a period of 17 tax years.

That being the case and having consulted his professional advisers, he decides to establish a RL360° bond with a premium of £750,000. When the bond has been issued it will be assigned to a RL360° International Flexible Trust. His London solicitors agree to act as trustees.

Anatoly has excluded the trust fund from the scope of UK IHT forever (even if he becomes UK domiciled as a matter of general law). He is a beneficiary of the trust and can benefit at the trustees' discretion. It is his intention that the trust fund be left untouched for as long as possible due to the IHT advantages it offers. Any special expenditure will be funded from those liquid assets which do not offer equivalent IHT advantages.

Important notes

For financial advisers only. Not to be distributed to, nor relied on by, retail clients.

This case study is an example only and while it highlights opportunities for planning, you should recognise that it is not an exhaustive description of the opportunities or pitfalls. The details shown are based on our understanding of current UK taxation law and practice as at 6 April 2015 and may be affected by future changes in UK legislation and the individual circumstances of the investor. Specialist tax and legal advice should be taken before any investment is made or tax strategy implemented.

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