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A Guide to Providing for Minor Beneficiaries

0161 941 4000 | myerson.co.uk | lawyers@myerson.co.uk

Providing for Minor Beneficiaries

We all want to ensure that we have provided for our families in the best way after our death. When considering how to benefit children it is common to be concerned that giving too much at a young age could be detrimental rather than beneficial for that child's well-being. It is sensible to want to ensure that any inheritance provided is used in the best way for the child's future.

We are each free to choose at what age a beneficiary can have full access to any inheritance we choose to leave them. However, exactly what option is chosen can have tax consequences. In this guide, we aim to highlight to you these implications to help you in making decisions about the best way to benefit your loved ones.

What options do we have?

If the beneficiary does not have immediate control over or access to the monies involved, a trust is created. This means that there will need to be Trustees who are placed in the position of responsibility to make the decisions regarding the investment and distribution of the inheritance.

Trusts will require consideration over rights to the original capital of the trust fund and any income generated by it. You can decide whether your beneficiaries have a right to any income or whether the trustees have the discretion to decide how and when this is distributed.

You can decide at what age the beneficiary is to have a right to demand the trust fund is transferred to them. Until that age the Trustees have standard powers under law to make advancements of the trust fund if they feel it is appropriate to do so. These powers can be widened by the Will. You can also provide a letter of wishes to your Trustees to explain how and when you would like them to exercise these powers. Holidays? Education Expenses? Driving lessons? All these things can be set out within the letter to help guide your Trustees as to their decision making.



Three Main Types of Trust

Bare Trusts:

With a bare trust, the beneficiary has an outright entitlement to the trust assets, but purely due to the fact that whilst under 18 a beneficiary cannot provide a valid receipt for the funds the trustee holds the assets on the beneficiary's behalf. Ultimately the assets are treated as if they belong to the beneficiary outright and at 18 the beneficiary could demand that the ownership of the assets is transferred to them to do with as they choose.

Life interest trust:

In a life interest trust, the beneficiary would have a fixed right to benefit from the income generated by the trust assets so if for example, the asset is a share in a company, the dividend that is paid out on the share would belong to the income beneficiary, if the trust fund was invested in a bank the beneficiary would have the right to the interest. To qualify for special tax treatment as set out below this entitlement must commence within two years of the date of death of the Testator. It may be that the capital would pass to the beneficiary at a certain age or pass to another beneficiary following the death of the income beneficiary.

Relevant Property trust:

If a beneficiary does not have an immediate right to income from the trust assets, and the income is only due to the beneficiary on satisfying any age contingency, (and this does not occur within two years of the date of death) then this will constitute a relevant property trust. This type of trust also covers full discretionary trust where no beneficiary is given any fixed rights in the trust fund.



The Tax Implications

Bare Trusts

With a bare trust all tax implications relating to the trust assets are applied as if the beneficiary owned the assets outright. Therefore, any income or capital gains tax is assessed on the individual taking into account their own allowances and exemptions.

If the individual was to die when the trust assets were still held by the Trustees, then the assets would be considered as being part of the individual's estate and assessed as they would any other assets belonging to an individual.

Interest in Possession Trust or Life Interest Trust

Where a beneficiary has a right to income from the start of the trust (or within two years of the date of death of the testator) then for income tax purposes, the trustees have a liability to pay basic rate tax. The beneficiary must also consider this income as part of their overall tax position and seek a reclaim of any tax paid above their personal liability. For Capital Gains Tax (CGT), the trust has a limited allowance which is half of that of an individual.

For inheritance tax the assets are simply taxed on the income beneficiary's own estate if it still held in the trust at the date of their death.

Relevant Property Trust

The Trust is subject to higher rates of income tax. Where the income received is less than £500 from 5th April 2024 the Trustees no longer must report this but where the income exceeds this amount then the Trustees must pay tax at the higher rate applicable to trusts (currently 39.35% for dividend type income and 45% for all other income). Again, the trust would have a limited allowance for CGT.

For inheritance tax, this type of trust is taxed every ten years and when assets leave the trust. The maximum rate of tax payable is 6% or proportionately reduced dependent on the amount of time the trust fund is held.



Tax Implications for Parents

The tax treatment of trusts left for someone's own children are different that the options for other friends and relatives wanting to provide for minor beneficiaries.

Trusts for Bereaved Minors

Where a parent leaves assets to their children to which they will become absolutely entitled upon reaching their 18th birthday, even if their entitlement to income is limited, the trust will not be subject to the additional inheritance tax as set out above in relation to the relevant property trusts.

18 to 25 trusts

Where a parent leaves assets to children but their outright entitlement does not occur until an age somewhere between 18 to 25 this trust will be deemed an 18 to 25 trust. Until the beneficiary turns 18 years, the trust would not be subject to inheritance tax assessment. Once the beneficiary has reached 18 the trust will be taxed in the same way as a relevant property trust but with a maximum charge of 7/10ths or 4.2% (representing the maximum number of years between 18 and 25) would apply.



You're in safe hands!

If you would like further information about how we can help you provide for minor beneficiaries, or if you have any questions, please don't hesitate to contact a member of our **Private Client Team** today.

Call: 0161 941 4000

Click: myerson.co.uk

Email: lawyers@myerson.co.uk



Myerson Solicitors
Grosvenor House, 20 Barrington Road,
Altrincham, Cheshire, WA14 1HB
Tel: 0161 941 4000 | lawyers@myerson.co.uk
www.myerson.co.uk



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