

**The Lincoln Absolute Gift Trust
Key Features and Benefits**

Trusts

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Important notes

Validity and operation of Trusts

This Guide is based on Lincoln's general interpretation of the law of England and Wales and HM Revenue and Customs' ("HMRC") practice as at 1 February 2007. It is not intended to be a comprehensive guide to the law and the tax implications of using an absolute gift trust. The legal and tax implications of using a trust will depend on the circumstances and requirements of each party and on whether legislation and HMRC practice has changed since the guide was prepared. Accordingly, Lincoln cannot accept any responsibility for any loss arising from its use. Settlers/policyholders are strongly recommended to take independent professional advice before creating a trust.

Absolute Gift Trust

Please note that under an Absolute Gift Trust neither the beneficiaries nor their share of the trust fund can be changed.

What is the Lincoln Absolute Gift Trust?

A trust is a legal relationship which exists when an asset is held by a person or persons (called the trustee(s)) for the benefit of another person or persons (called the beneficiary(ies)). The trustees have the control and legal ownership of the asset but must use it for the benefit of the beneficiaries.

The Lincoln Absolute Gift Trust provides a way of holding an insurance policy for the benefit of another individual or individuals.

When the policy is made subject to an Absolute Gift Trust, the ownership of the policy is effectively split. The legal owners of the policy will be the Trustees. The Trustees collectively control all dealings with the policy on behalf of the Beneficiaries under the trust. The Beneficiaries will be entitled to enjoy the trust asset - in the case of a policy, the proceeds on encashment or part encashment and on payment of the sum assured.

The proposer (for a new policy) or the policyholder (for an existing policy) who creates the trust is called the Settlor and can not benefit from the policy in any way under the Absolute Gift Trust.

The Settlor names in the trust one or more individuals (normally but not necessarily a child /children under the age of 18) as the Absolute Beneficiary/ies. The Beneficiaries are absolutely entitled which means that their entitlement cannot be taken away or changed in any way. **It is therefore crucial that the Settlor is certain that he/she will not want to change his/her mind about this.**

One of the objectives of the Absolute Gift Trust is to ensure that the policy is held for the benefit of the chosen Beneficiaries outside of the inheritance taxable estate of the Settlor.

Who should consider using the Absolute Gift Trust?

You could use an Absolute Gift Trust if you:

- wish to make an inheritance tax effective lifetime gift of your policy or cash to be invested in a Lincoln policy;
- do not need to retain access to the policy for your own benefit in the future (this is a particularly important consideration in respect of an investment bond); and

- are certain who is to benefit from your gift, i.e. you do not wish to retain any flexibility over the choice of your beneficiaries.

When should the Absolute Gift Trust not be used?

The Absolute Gift Trust should not be used if you wish to retain access to the policy or part of it for your own benefit (especially important if the policy is an investment bond) or if you wish to make a gift but retain some flexibility or control over who should benefit.

How is the Absolute Gift Trust established?

The Absolute Gift Trust can be used with either a new policy or an existing policy which is not already held in trust.

The trust is established by the proposer for a new policy or the policyholder of an existing policy (known as the Settlor) completing the Absolute Gift Trust deed.

Once the trust is established, additional trustees should be appointed using a separate deed, a draft of which can be provided by Lincoln for the consideration of your legal advisers.

It is strongly recommended that at least one additional Trustee is appointed as, without additional Trustees, there will be a delay in securing access to the policy benefits following the death of the last surviving or only Trustee.

Once the policy is made subject to trust, any subsequent dealings with the policy will be between the Trustees (as the legal owners) and Lincoln.

Key provisions of the Absolute Gift Trust

- The Settlor(s) names, as Beneficiary(ies), the individual or individuals who are to benefit from the trust fund and if more than one the shares in which they are to benefit otherwise they will benefit equally. For tax purposes each of these Beneficiaries is treated as owning an appropriate share of the trust property (initially the policy).

- The Beneficiaries named in the trust are entitled to benefit absolutely. This means that once a Beneficiary attains age 18 he or she can demand that the Trustees pay over the benefits to him/her.
- Neither the Settlor(s) nor anybody else other than the named Beneficiary/ies can benefit from the trust in any circumstances.
- The Trustees have wide powers to invest and deal with trust property where the policy proceeds are not to be distributed immediately for the benefit of Beneficiaries, for example if the Beneficiaries are young children when the benefits are paid.

The law of the trust

The Absolute Gift Trust is governed by the law of England and Wales and is intended for use in those countries.

The Trustees

The Settlor (or both of them in the case of joint proposers/policyholders) is automatically one (or both) of the initial Trustees. It is strongly recommended that at least one additional Trustee should be appointed. This is done by completing a deed of appointment of additional Trustees. The Settlers also have the power to dismiss a Trustee provided at least one Trustee other than the Settlor remains.

The Trustees must act unanimously.

The Inheritance Tax (IHT) implications of the Absolute Gift Trust

Establishment of the trust

- For IHT purposes a transfer of value (a gift) takes place at the time the trust is created.
- Where there are two Settlers, each is treated as making a gift of one half of the value transferred.

New policy

- When a new single premium plan is made subject to trust, the value transferred will initially be the amount of the first premium.
 - For a new regular premium protection plan it is the premiums that are the transfers. The premiums (the first and subsequent premiums) may be exempt as normal expenditure out of income or failing this may fall within the annual exemptions.
 - If the value transferred does not qualify for the normal expenditure exemption (not available for a single premium plan) and it exceeds the available annual exemption (in 2007/8 £3,000 for each Settlor or £6,000 maximum for each Settlor if the exemption for the previous tax year has not been used), it will be a potentially exempt transfer (PET) provided it is not paid directly to the life insurer but via the Trustees. This means that, regardless of the amount of the transfer, no IHT liability will arise at the time of the transfer, but may do subsequently if the Settlor dies within seven years of making the transfer and the value of the gift together with any chargeable transfers made in the seven years immediately preceding the gift exceeds the nil rate band at the date of death. If the Settlor should die

within seven years of making the gift the value of the gift when made will be taken into account in determining the inheritance tax liability on the Settlor's estate.

Existing policy

- When an existing policy is made subject to trust, the value of the gift will be the value of the policy. This will be the market value of the policy (surrender value or any greater value if the life/lives assured are in serious ill health) or, in respect of non-term policies only, the premiums paid to date if greater less any part surrenders less an allowance for any decrease in the value of units since allocation at inception of the policy. Other than this the tax implications will be as set out above for a new policy.

Payment of additional premiums by the Settlor

- Under a regular premium protection plan the premiums paid could be exempt as normal expenditure out of income or within the annual exemption (in 2007/8 £3,000 per transferor).
- Any additional single premium paid into a single premium plan by the Settlor will be a further gift and the tax implications will be as described above for the initial transfer. To the extent that the additional premium is not covered by the exemptions described, the amount of the transfer eligible to be treated as a PET (if not paid direct to the insurer) would be equal to the amount by which the value of the single premium plan is increased by the transfer.

Death of a Beneficiary

- For IHT purposes the Beneficiaries are treated as owning the trust property (initially the policy).
- On the death of a Beneficiary the value of his/her underlying interest in the trust property (the policy) will be included in the estate of that Beneficiary. If there is more than one Beneficiary then the value included will be the value of their share. For a protection plan where the life/lives assured is not in serious ill health the value would (and only in respect of non-term policies) usually not exceed the total of the premiums paid to date.
- If the Beneficiary is under the age of 18 (16 in Scotland) and unmarried the beneficial interest in the policy will normally pass to the deceased Beneficiary's parents under the rules of intestacy.

Death of the Settlor

- On the death of the Settlor (or, where relevant, either of the Settlers) the value of the policy should be outside of the Settlor's estate for IHT purposes.
- Inheritance tax could potentially be a problem where the value of the gifts (premiums) to the trust are not covered by any exemptions and the Settlor dies within seven years of creating the trust. This is because the original PET will become chargeable on the death of the Settlor. Even then, as stated above, if the value of the gifts made within seven years of death falls within the available nil rate band no liability will arise on the gifts themselves. However, the nil rate band available to determine the liability arising on the estate on the death of the Settlor will be correspondingly reduced.

Income tax

In all cases, it is assumed that the Settlor and the Trustees are UK resident - special rules apply where this is not so.

Income tax on chargeable event gains made under a policy is only likely to be relevant in connection with single premium investment bonds.

a) While the Beneficiary is under the age of 18

- **During the Settlor's lifetime or in the tax year in which the Settlor's death occurs**

For income tax purposes, any chargeable event gains arising under the bond will be assessed on the Settlor if UK resident. If there are joint Settlers, each will be assessed on one half of the gain.

- **After the end of the tax year in which the Settlor's death occurs**

Following the Settlor's death, any chargeable event gains arising in a tax year after that in which the Settlor died will be assessed on the UK resident Trustees at the special rate of 40% less a 20% tax credit (in 2007/8). If the Trustees are not UK resident special rules apply under which UK ordinarily resident beneficiaries are taxed when they receive benefits and so specialist advice should be sought regarding this. These rules also apply if the chargeable event occurs when the Settlor is non-UK resident.

b) When the Beneficiary is over the age of 18

Any chargeable event gains arising under the bond will be assessed on the Beneficiary even if the bond is still legally owned by the Trustees and the trust will be ignored for this purpose.

Money laundering

Under the Money Laundering Regulations 2003 we are required, in certain circumstances, to obtain independent documentary evidence of the identity and permanent address of persons seeking to invest with us. Until we receive the documentation, we may be required to delay processing your instructions and/or withhold any payments due to you from us in respect of your investment. We may check your details with credit reference agencies, who may add details of our search to your record, and with fraud prevention agencies, who may record details of any false or inaccurate information provided by you where we suspect fraud. We may also disclose details of your conduct in relation to your application, account or policy to these agencies. We or other organisations may use and search these records to help make decisions about applications, accounts, claims and other services for you and members of your household and to prevent fraud and money laundering. We cannot accept responsibility for the accuracy of information provided by these agencies nor can we accept any liability for the consequences of our undertaking these checks or declining to accept your application. Please contact us if you would like details of these agencies and how they may use your information.