Montpellier Guide to Estate Planning

Estate Planning is about wealth and ensuring that is transferred to the right people at the right time and that the asset is protected and safeguarded from threats such as bankruptcy, tax and poor decisions by those who have had limited experience with large sums of money.

Wealth can be passed to beneficiaries or protected by trusts in many different ways. Previously the focus of many clients has been on the mitigation of Inheritance Tax (IHT) alone without assessing the wider benefits of estate planning. While we adopt strategies that focus on reducing IHT, there are wider considerations which are more important to some people, these include ensuring that beneficiaries are provided for, but also that they are protected from themselves especially when they are young and do not always understand the consequences of having large sums of money.

Within this guide we will outline the issues that are linked with transferring wealth and also the methods by which this may be achieved.

Wills & Powers of Attorney

See our guide to Wills and Powers of Attorney.

In the event of your death, for your estate to be distributed in line with your wishes, it will be necessary for you to have created a valid Will. If you do not have a Will there is a very strict process as to where the assets go, over which you have no control.

You should keep your will up to date. We would generally suggest that a Will is reviewed every five years. It may be that upon a review no additional alterations are required, but any changes in your beneficiaries or from legislation may require some attention.

When discussing planning with our clients we always recommend a Power of Attorney. In many respects a Power of Attorney can be more important than a Will, as should you lose mental capacity a Lasting Power of Attorney (LPA) allows you to make your wishes known. This can relate to your financial affairs and will allow your attorney the power to make decisions on your behalf. Furthermore the LPA allows your Attorney to make decisions to your personal welfare should you wish for it.

We work closely with Solicitors who will be able draw up both your Wills and Lasting Powers of Attorney.

Tax Efficient Transfers on Death

It is important to structure your affairs so that on your death, your assets can pass to your estate tax efficiently and without too much complexity.

A Will is part of your estate planning strategy which can be used to pass assets to beneficiaries and also mitigate tax. There are steps that can be taken during your lifetime to structure your financial affairs as tax efficiently as possible so that your beneficiaries can have access to some of your assets in the event of your death which may be used to settle any potential IHT liability.

Poor planning could result in Inheritance Tax and Income Tax being paid on the sale of some assets. Our aim would be to structure your assets so that this double tax charge can be avoided where possible.

Lifetime Gifting

Assets may be transferred at any point and for any value. People do not always appreciate the impact of making gifts during their lifetime and while people think that they are doing the right thing, they could also be compounding their liability to IHT.

In the section below we will look at some of the methods, by which you can make gifts of assets, mitigate your IHT liability but also be in a position where your financial affairs are arranged in a structured and efficient manner.

Life Cover

A simple and often affordable method of dealing with an IHT liability is to create a fund which may be used by your estate to pay off the liability to tax.

Life Cover is an insurance policy which pays out a lump sum on your death. You will need to pay an annual or monthly premium. The cost of the premium is assessed on a number of factors the most prevalent being your age and health.

Life cover may be funded from Income or Capital but there are pro's and con's to funding in either way and the consequences of not understanding the implications may result in adverse tax implications. We understand the rules and advise clients on the most appropriate methods to mitigate their IHT liability and to protect assets for future generations.

Gifts into Trust

A transfer of an asset into a trust has some important considerations and will vary on the type of trusts. Below are a number of common trust types used in financial planning.

Gift & Loan

A Gift & Loan or Loan only scheme is a structure incorporating the transfer of assets into a trust. The cash that is held within the trust is then invested into various different investments. The scheme is used to allow any growth on the investment to fall immediately outside of your estate, allowing your designated beneficiaries to receive the growth at some point in the future.

Discounted Gift Trust

A discounted gift trust involves the transfer of an asset into a trust. You have a right to the income from the scheme for life or earlier fund exhaustion. The scheme allows the value of your gift to fall outside of your estate after 7 years, but also allows you a right to income for the duration of your lifetime. The value of the income is a percentage of the amount that you invest, traditionally 2.5% or 5% per annum and a calculation is undertaken assessing your age, sex and health to determine your longevity of life, which is then assessed against actuarial morbidity tables. A discount is then applied on the value of the total capital investment. The discount which is applied is your right to the income stream for life and this value will be immediately outside of your estate for the purposes of IHT.

CLTs & PETS

Most people are familiar with the rule that if you make a gift it forms part of your estate for Inheritance Tax purposes for at least 7 years.

There are various nuances and complexities, but in principle 7 years is around the length of time that an asset will still form part of your estate for the purposes of calculating any IHT, even though legal ownership will have passed at the date that you gifted the asset.

Different types of trusts are given different names and have different rules.

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Chargeable Lifetime Transfer (CLT) – A transfer of an asset into a Discretionary Trust, that does not pass as an exempt transfer for example a regular gift of income or the £3,000 annual exemption (see our guide to Inheritance Tax).

Potentially Exempt Transfer (PET) – This is an outright gift to a beneficiary, it can also include a transfer into an Absolute trust.

The differences in the types of gift are minor and on the face of it but have very different implications. It is important that you understand the rules and are familiar with the benefits.

Gifts With Reservation

It is important that people understand the impact of making gifts. Gifts must be irrevocable in nature for them to be effective for assessing any IHT liability. In basic terms if for example a client owns an investment property but wishes to make a gift of it to their children. The transfer of ownership will be a disposal for the purposes of Capital Gains Tax (CGT) and could result in a CGT liability. Once the asset has passed to their adult children, they will lose all entitlement to the income and future capital gain. The gift will be assessed for IHT for 7 years and will be an asset of their estate for the purposes of calculating any IHT liability for that period.

Once the asset has been gifted the previous owner may not benefit, should they stay in the property for extended periods, or should they receive the rental income then the asset will form part of their estate for IHT purposes even though they will not have legal ownership of the asset.

Business Property Relief Schemes

You can claim business relief on;

- a business or an interest in a business (such as a partner in a partnership)
- unquoted shares include shares which are traded in the Unlisted Securities Market (USM shares) or the Alternative Investment Market (AIM shares). Shares that are listed on a recognised overseas stock exchange are quoted for IHT purposes, even if they are also traded in the AIM or USM.
- a holding of shares or securities owned by the transferor, which are fully listed on a recognised Stock Exchange, which themselves or with other listed shares or securities give control of a company
- land, buildings, plant or machinery owned by a partner or controlling shareholder and used wholly or mainly in the business of the partnership or company immediately before the transfer (This applies only if the partnership interest or shareholding would itself, if it were transferred, qualify for business relief.)
- any land, or buildings, machinery or plant which was used wholly or mainly for the purpose of a business carried on by the transferor and was settled property in which the transferor was beneficially entitled to an interest in possession and used in the transferor's business.

A family business or a stock held on AIM is a good example of an asset that will qualify for BPR. An asset that qualifies for BPR will be free of Inheritance Tax after only two years. This is of significant advantage when clients have a family business that they wish to pass on through the generations but would be adversely affected if they had to include the value of the business within their taxable estate.

Estate Preservation & Succession Planning

The transfer of wealth is all about making sure that funds are available for future generations and that it is preserved for the long term. Our clients understand that IHT is an area of concern, but this is not the only area that requires financial planning advice. In many cases our clients focus is on safeguarding the future financial welfare of their beneficiaries and this often means protecting the beneficiaries from themselves.

We hope that you have found this brief guide useful. If you would like to find out how this may affect you or if you would like to learn how to implement elements of this planning within your financial affairs then please contact us on the details below.

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