LIFETIME GIVING

INTRODUCTION

Making gifts during your lifetime is an efficient way to reduce the value of your estate for inheritance tax purposes as well as providing benefit for your family. Managing the succession of personal and family assets is often at the forefront for many individuals' minds and thus lifetime giving is very much the cornerstone of any successful tax and estate plan.

That said, lifetime giving can be fraught with difficulties and it is essential to consider the options available to the donor. When making lifetime gifts, it is important to take into account the personal circumstances of both the donor and donee. A gift should not be made to the detriment of the donor and likewise, the exact nature of the gift and its tax implications for all parties should be considered carefully.

With the above in mind, we have prepared a handbook to answer the most pressing and common lifetime giving questions and issues including; giving property to the next generation, gifts to vulnerable individuals, how best to fulfil an individual's philanthropic ambitions, foreign gifts and the tax benefits associated to gifts of art.

At Collyer Bristow LLP, we can help you navigate the intricacies of lifetime giving, mitigate any potential downsides and optimise the benefits for you and your loved ones.

- HOW CAN I HELP MY CHILDREN BUY A HOUSE?
- CAN I GIFT MY HOME TO MY CHILDREN (AND STILL LIVE IN IT)?
- CAN I GIFT MY HOLIDAY HOME OR RENTAL PROPERTY TO MY CHILDREN?

PROPERTY

HOW CAN I HELP MY CHILDREN BUY A HOUSE?

The Bank of Mum and Dad supported more than half of first-time buyers under the age of 35 in 2020 and is the sixth largest lender in the UK.

The average amount provided by the Bank of Mum and Dad in 2020 was around £20,000. As a first step, you therefore should ensure you are comfortable that you can afford to provide this level of financial support to your children and that you will not need the funds to supplement your income in retirement.

If you are happy, there are three principal ways parents can provide their children with funds to help them buy a house: outright gifts, trusts, and loans.

GIFTS

The principal tax to consider when making gifts is inheritance tax (IHT). You can give away up to £3,000 each per year tax-free (£6,000 if you haven't made any gifts in the previous tax year). You can also make a tax-free gift to a child of up to £5,000 in the year in which they get married.

Larger gifts will be 'potentially exempt transfers', commonly referred to as 'seven-year rule' gifts. If you survive the gift for seven years, it will fall out of account for IHT but if you were to die within the seven years, the gift will be taxable at 40% (with the potential tax liability tapering down after three years).

You should formally document any substantial gifts in a letter or deed of gift so that there is a record for future reference (a mortgage company may also require evidence of the gift). If your child will be purchasing the property with a partner, you may also consider a cohabitation agreement to determine how the property will be divided if their relationship ends.

TRUSTS

As further security, you may wish to put the money into a trust (of which you can be the trustees). These days, the principal benefit of trusts is asset protection, rather than tax mitigation. A trust may be especially useful, therefore, if you have any concerns about how your children might manage the money if it is not immediately invested in a house.

Provided you do not put any more than your tax-free allowance for IHT, or 'nil rate band' (currently £325,000 each) into trust, there will be no immediate IHT implications of doing so, apart from starting the seven-year clock running to remove the funds from your estates. As trustees, you can continue to control the funds until such time as your children are ready to purchase a property.

The taxation of trusts is a complex area and there will be administration and set up costs to consider. We would always suggest you take legal advice before going down this route.

PROPERTY

LOANS

An alternative might be to loan the money to your children. This will not reduce your IHT bill (as the loan will instead be an asset in your estates) but does offer a little more control than an outright gift. You should be aware that a loaned deposit may restrict the availability of certain mortgages.

If you later choose to waive repayment of the loan, you will make a gift of the outstanding balance at that point, which will be subject to the seven-year rule for IHT. As with gifts, any loans should be formally documented.

OTHER WAYS TO HELP

1. Specialised mortgage products

While not common, there are some mortgage products that might be of assistance, although they are not without their drawbacks.

Family Offset mortgages allow for parental savings to be offset against your child's mortgage debt, reducing their interest payments and making the mortgage more affordable for them. The downside to this is that you will lose access to your savings and will not earn interest while the arrangement is continuing.

Guarantor mortgages are another option that allows parents to stand as guarantor for their child's full mortgage debt, offering their own savings or home as security for their child's mortgage payments.

2. Buy jointly with your child

You could also buy jointly and/or take out a joint mortgage with your child so that your combined incomes enable them to access a larger loan, albeit you will be equally liable for the repayments.

However, there are some potentially significant tax downsides to this. If you are named as a purchaser and already own a property, you and your children will almost certainly pay an additional 3% in stamp duty. You may also be liable for capital gains tax on your share when the property is sold.

CAN I GIFT MY HOME TO MY CHILDREN (AND STILL LIVE IN IT)?

For many people, their home is one of their most valuable assets, if not the most valuable. It is therefore an obvious candidate for lifetime estate planning.

The question that often comes to us is whether it is possible for parents to give their home to their children and keep living there. The answer to this question is yes, but with significant caveats if the gift is to be effective for tax purposes.

INHERITANCE TAX

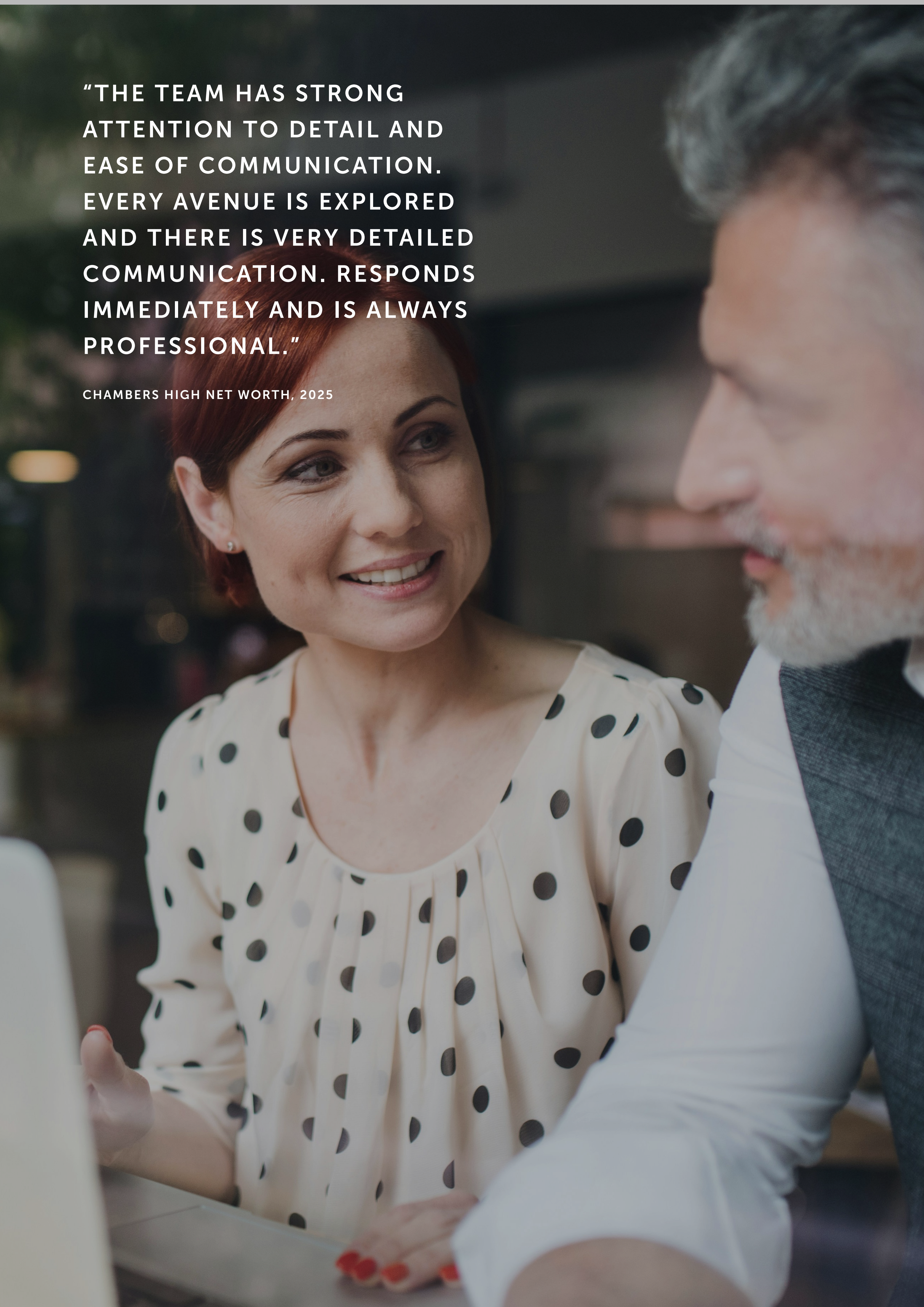
Generally speaking, if you make a gift to someone and then live for seven years afterwards, the gift is completely free of inheritance tax (IHT). However, one major exception to this is that, if you continue to benefit from the asset you have given away, the value of the asset remains in your estate for IHT purposes (known as a gift with reservation of benefit, or GROB). Continuing to occupy a property you have given away is a classic example of this.

There are, however, ways in which you can make an IHT-effective gift of your home, or a share of it, to your children even though you wish to continue living there:

- One is to pay a full market rent for your occupation of the property. This should be properly negotiated between parents and children, with evidence that it
- is a fair market rent. Clearly, this comes with significant cash flow implications, and also tax
- "leakage", because the children will have to pay income tax on the rent they receive from their parents.
- Another option is open if one or more children lives with their parents. There is an exception to the GROB rules where a share of a property is given, and the donor and donee share occupation. There is no statutory limit on the percentage of the property given, but HMRC will query it if the percentage is too large. It is also important that the parents continue to bear at least their fair share of the property's running costs. It must also be borne in mind that if the child moves out then the whole value of the property falls back into the parents' estate for IHT.

CAPITAL GAINS TAX

Another thing to bear in mind is capital gains tax (CGT). A gift of a property is a disposal for CGT purposes. Gains on your main residence are generally fully relieved from CGT. However, if you have not lived in the property for the whole time you have owned it, there is a risk that there may be some CGT to pay on the gift.



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CHAMBERS HIGH NET WORTH, 2025

CAN I GIFT MY HOLIDAY HOME OR RENTAL PROPERTY TO MY CHILDREN?

Gifting a second home or a rental property to your children can be a great way to pass an asset down a generation in a tax efficient way. However, there are number of points that you will need to be aware of before transferring a property to them.

The principal tax to consider when making gifts is inheritance tax (IHT). The gift of a property will be a 'potentially exempt transfer'. If you survive the gift for seven years, you will escape paying IHT on it, but if you were to die within the seven years, the gift will be taxable at 40% (with the potential tax liability tapering down after three years).

If you give away a property to your children but continue to derive some benefit or enjoyment from it, then this may be deemed a "gift with reservation of benefit" (GROB). The result of this is that the whole of the property will be treated as remaining within your estate for IHT purposes and taxed at 40% on your death notwithstanding the fact that you no longer own it.

A GROB can be avoided if the donor (i.e. the parent) pays a market rent to the donee (i.e. the child or children) for their occupation and enjoyment of the gifted property. This may be unattractive from a cashflow perspective.

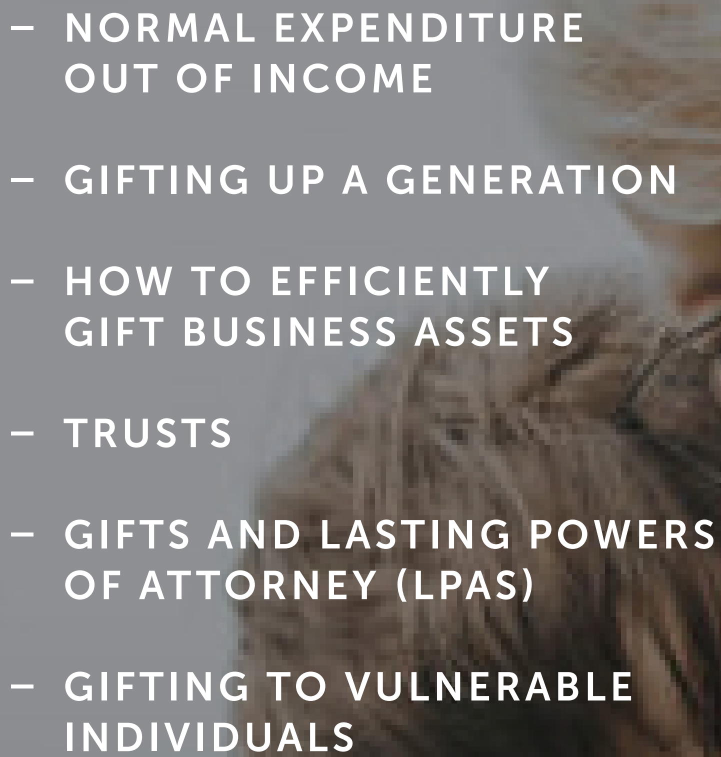
However, there is a potential way through the minefield which makes use of specific exceptions to the GROB rules. The first is that you could pay a market rent to your children for your occupation and enjoyment of the gifted property, albeit that this may be unattractive from a cashflow perspective. Alternatively, there are exceptions that apply to gifts of a share in land where you either: (i) do not occupy the land, or (ii) occupy the land along with your children and do not receive any benefit which is provided by or at their expense.

Practically speaking, there are a couple of ways to take advantage of these exceptions. In the case of a rental property, you will likely not occupy it and so you can give away a share, say 75%, to your children but could continue to receive some or all of the rents without being subject to the GROB rules for as long as the property continues to be commercially let. As a general rule, rent will be due to you and your children in proportion with your respective ownership of the property. However, if you depend on the rental income, you could separately agree with your children as co-owners that you will continue to receive all the rents without affecting the IHT position.

For a holiday home which is occupied to some extent by the whole family, there is no GROB as long as you do not receive any benefit from the property at your children's expense. This means that you should share any outgoings (e.g. bills, mortgage payments, council tax etc.) at least pro-rata to ensure that your children do not pay more than their fair share, as this would constitute a benefit to you. Alternatively, if you are feeling especially generous, you could choose to continue paying all the expenses.

While this planning may be effective to reduce your estate for IHT purposes, any gift will be subject to CGT at up to 28%. This is a lower rate of tax, currently, than IHT on death but is payable immediately. There may also be stamp duty to pay on the gift if the property is mortgaged.

Ultimately, any decision on gifting your holiday home or rental property will involve carefully weighing up the potential tax charges as well as considering your future intentions as regards to the property. We would always suggest you take legal advice on your specific circumstances before making any large gifts.



- NORMAL EXPENDITURE OUT OF INCOME
- GIFTING UP A GENERATION
- HOW TO EFFICIENTLY GIFT BUSINESS ASSETS
- TRUSTS
- GIFTS AND LASTING POWERS OF ATTORNEY (LPAS)
- GIFTING TO VULNERABLE INDIVIDUALS

ESTATE PLANNING:

NORMAL EXPENDITURE OUT OF INCOME

Although lifetime giving can be tax-efficient, inheritance tax will arise immediately if the donor makes outright gifts or transfers into trust in excess of their nil rate band (currently £325,000), and will also arise if the donor fails to survive an outright gift by at least seven years.

However, lifetime transfers that constitute a donor's 'normal expenditure out of income' will pass immediately free from inheritance tax. The exemption applies if each of three criteria are met:

- Payments are made out of the donor's 'normal expenditure', meaning that they must be typical of the donor according to a settled pattern of behaviour over time.
- Payments are made out of the donor's income (as opposed to capital). HMRC's view is that the donor's income is their net income after the payment of income tax.
- Having made the gift(s), the donor is left with sufficient income to maintain their usual standard of living. This means that a donor can only make gifts under this exemption up to the value of their 'surplus'income after payment of normal expenses to maintain their usual standard of living.

The 'normal expenditure out of income' exemption can be a highly effective tool for lifetime giving where the donor makes regular, manageable gifts over a period of years. This might include for example payments for a grandchild's education or the incremental funding of a trust out of the donor's surplus income. It is worth remembering however that if a donor survives outright gifts by at least seven years then the gifts will generally pass free from inheritance tax anyway.

GIFTING UP A GENERATION

A scenario frequently encountered is where a client has accumulated significant wealth during his or her lifetime and wishes to care for elderly relatives – often parents – but without triggering inheritance tax (IHT) on their deaths. It is a particular issue when someone wants to provide his or her parents with residential accommodation.

THE ISSUE

The issue is that simple gifts by a wealthier child to his or her parents might be the worst of all worlds. This is because they would be Potentially Exempt Transfers (PETs) for IHT for the child, meaning that IHT would be triggered at 40% in the event of his or her own death within the following seven years. Perhaps worse still, they would also add taxable assets to the parents' IHT estates, ensuring a further charge of 40% in the event of their deaths.

NON-SOLUTIONS

Simple solutions might be thought to include making repayable loans to the parents, or making assets (such as residential property) available to them but without actually transferring the assets to them outright.

However, these apparent solutions would cause other difficulties: first, following a change in the law in 2013, any loans would need to be repaid from the parents' estates to avoid IHT being chargeable, and funds might not be available to make the repayments. Secondly, if property is owned by a child but occupied by the parents, whilst IHT would avoided on the parents' deaths, the acquisition would be subject to the supplemental 3% SDLT charge for second properties. Additionally, CGT – at the higher rate of 28% – would apply in due course when the property is sold, with no "main residence" relief available for the parents' occupation.

Similarly, it has been unattractive to make lifetime trusts in most cases since a 2006 change in the law, as a 20% IHT entry charge will apply to amounts exceeding the available Nil Rate Band (typically £325,000).

THE SOLUTION

In appropriate cases, it would be possible to create a new purpose-made trust with a nominal amount (£10, for example). A loan could then be made to the trustees to enable them to purchase property for the parents to use. This would have the following consequences: (1) the nominal sum creating the trust would theoretically be subject to IHT unless within the Nil Rate Band; (2) the loan to the trustees would trigger no IHT, though it would remain an asset of the child (and so be within his or her IHT estate); (3) none of the assets would be within the parents' IHT estates; (4) no IHT periodic charges (e.g. on every 10th anniversary of the trust's creation) would apply to the amount of the loan; (5) the parents would be able to occupy/use the property owned by the trustees; (6) the higher rate of SDLT ought not to apply to the acquisition of the property; (7) The CGT "main residence" exemption would apply in the case of residential property owned by the trustees (albeit subject to the loan) and occupied by the parents.

As a result, this solution will achieve the commercial objective of the child and his or her parents, of enabling the parents to occupy property, but without the tax disadvantages of the non-solutions referred to above.

HOW TO EFFICIENTLY GIFT BUSINESS ASSETS

For certain individuals, business assets can form a significant portion of their wealth and so considering how those assets might be passed to the next generation often forms a key part of their estate plan. Business assets can benefit from certain tax reliefs and so should be given special consideration.

INHERITANCE TAX

The starting point is that business assets are subject to the normal inheritance tax rules on outright lifetime gifts and gifts into trust and so, for example, if the donor survives an outright gift of business assets by seven years then no inheritance tax would fall due.

However, qualifying business assets can be partially or fully relieved from inheritance tax under Business Relief (often known by its previous name of Business Property Relief or BPR), once they have been held for two years. BPR can apply to gifts of qualifying business assets, whether outright gifts or gifts into trust, at either 50% or 100% relief (depending on the asset in question). In the case of a trust, if the trust continues to hold qualifying business assets, they will remain relieved from inheritance tax and therefore not subject to the usual 10 year charges and exit charges.

Please note, there are however clawback provisions to reverse the effects of the relief if the settlor of the trust dies and the BPR conditions do not continue to be met.

Another pitfall to watch out for relates to "excepted assets". While a business as a whole may qualify for BPR, if it holds assets which are not used in the business (such as excess cash) then those assets may reduce the amount of relief available.

CAPITAL GAINS TAX

A gift of business assets will be a disposal at the assets' open market value and any gain potentially chargeable to CGT. Given many entrepreneurs build up businesses from very little, their business assets can frequently stand at considerable gains.

Certain business assets (such as unlisted shares) are eligible for CGT hold over relief. Here the gift does not trigger any immediate CGT, but instead the gain is held over and the recipient acquires the asset at the donor's base cost. On a later disposal of the asset by the new owner, the gain is calculated by reference to that lower base cost (unless hold over relief is again available). This can allow business assets to be passed to the next generation without breaking up the business to pay an immediate tax charge.

Other CGT reliefs which may apply are Business Asset Disposal Relief (formerly Entrepreneurs' Relief) and Investors' Relief, both of which can reduce the amount of tax paid on a disposal of business assets. Depending on the circumstances, a donor may choose to make some use of these reliefs, rather than holding over the entire gain.

TRUSTS AND SCHOOL FEES: HOW CAN EXTENDED FAMILY MEMBERS LEND A HAND?

Many families contend with paying school fees running into hundreds of thousands of pounds per child over the course of their education. Most parents pay for these fees out of post-tax income or capital savings if needed.

This article will examine some tax efficient arrangements that other family members (typically grandparents) can use to contribute to these costs.

OUTRIGHT GIFTS

Depending on their recipient, gifts by individuals domiciled within the UK are taxed on one of two alternative bases. Gifts to trusts are dealt with below. Where gifts are made to individuals, or for their benefit, they will not be subject to inheritance tax if the person making the gift (the donor) survives it by seven years. These gifts are known as “Potentially Exempt Transfers” (PETs).

If the donor does not survive by seven years, their available “nil rate band” (the allowance for inheritance tax, currently a maximum of £325,000 for each individual) will pass tax-free, but the balance will be taxable at up to 40%. As a result, if other tax-efficient methods of giving (e.g. gifts from surplus income, see below) are unavailable, PETs are usually the easiest method for family members to contribute toward expenses such as school fees.

REGULAR GIFTS OUT OF SURPLUS INCOME

Making regular gifts out of surplus income is even more efficient, as there is no need to wait for seven years before the gift ceases to be relevant for inheritance tax.

This statutory relief only applies where gifts are made on an ongoing basis (as would typically be the case for school fees), out of income rather than capital, and where they leave the donor with enough income to continue their usual standard of living.

It is possible to make a binding promise that you will continue to meet termly school fees, and this promise would be sufficient evidence of intention that subsequent payments would immediately fall outside of your estate for inheritance tax purposes. This would leave your nil-rate band untouched and available for other lifetime gifts or to reduce the tax payable on your death.

TRUSTS FOR SCHOOL FEES

A third option, whilst slightly more complex, has a significant added advantage from an income tax perspective. Instead of making outright gifts, you could instead put money into trust for, say, grandchildren. It is possible to put your entire available nil-rate band of up to £325,000 (or £650,000 per couple) into trust every seven years without incurring up-front IHT. This trust can then be used to pay for school fees and/or other costs and expenses, e.g. university fees, housing costs etc.

If school fees had been paid outright out of income, this would be done net of income tax. Conversely, payment out of a trust can be more efficient as the grandchild could reclaim tax paid by the trustees if their income tax allowance is available. This is because the trust and its income are treated as the grandchild’s. Importantly, had the trust had been set up by a parent the trust and income would be treated as belonging to the parent and be taxable on them.

CONCLUSIONS

There are therefore several ways for people other than parents to contribute to school fees and save some tax in the process. While outright gifts and regular payments out of surplus income are simple and effective, in some cases the added income tax benefit of a trust may be preferable. In each case, it is important that specialist advice, taking into account all relevant factors, is taken in advance of any gifts being made.

GIFTS AND LASTING POWERS OF ATTORNEY (LPAS)

Making gifts as an attorney acting under a registered LPA for property and financial affairs is fraught with difficulties and is an area which could give rise to criticism of the attorney and potentially an investigation by the Office of the Public Guardian.

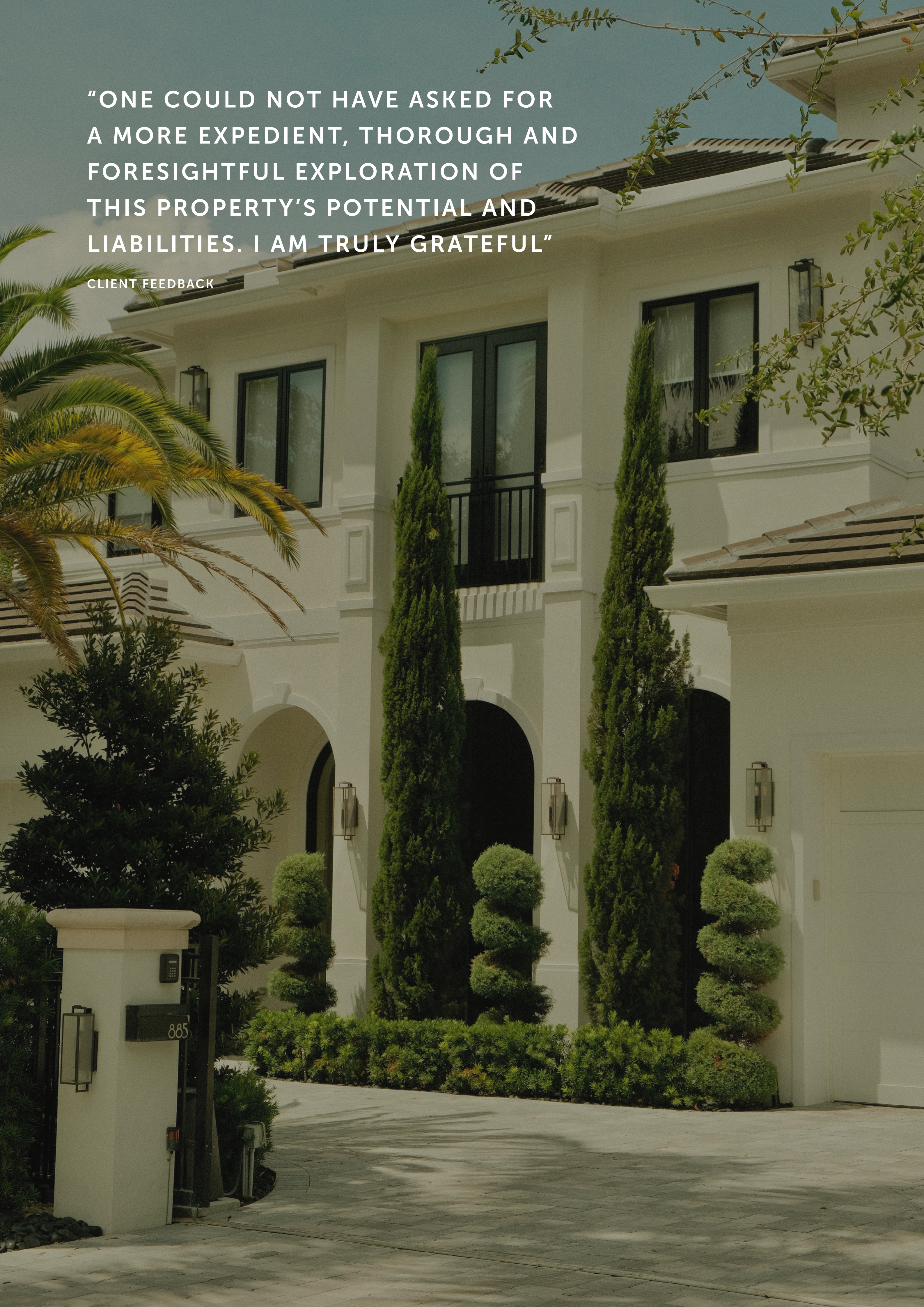
An attorney has limited powers when making gifts on behalf of the donor and they must be aware of the strict rules conveyed by the Mental Capacity Act 2005. Whilst the general rule is that attorneys cannot make gifts from a donor's estate, there are exceptions and an attorney should consider each decision individually taking into account the context and timing of a proposed gift.

An attorney may make gifts on a customary occasion (such as marriage or birthdays) to someone related or connected to the donor. The gifts must be of reasonable value bearing in mind the occasion and the value of the donor's estate. A similar but slightly narrower exception applies to attorneys acting under an Enduring Power of Attorney.

Nevertheless, an attorney should assist the donor to make their own decisions which may include making gifts. Where the donor cannot make their own decisions an attorney must act in the donor's best interests taking into account any instructions or guidance contained in the LPA itself.

If an attorney lacks sufficient authority to make a gift, it will be necessary to apply to the Court of Protection for approval.

When considering if a gift is 'reasonable' for these purposes the attorney should consider, amongst other factors; the impact of the gift on the donor's financial situation, whether the donor was in a habit of making gifts of this nature, the donor's life expectancy and how the gift interacts with the terms of the donor's Will. That said, it has been accepted by the Court of Protection that a reasonable gift could include the annual inheritance tax exemption of £3,000 and the annual small gifts exemption of £250 per person (for up to 10 persons).



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CLIENT FEEDBACK

GIFTING TO VULNERABLE INDIVIDUALS

When making a gift to a disabled or vulnerable person, it is not only important to consider the donor's position but also that of the recipient of the gift. For example, an ill-considered outright gift to a disabled or vulnerable person may do more harm than good for their own physical or mental wellbeing and in terms of affecting their entitlement to state benefits. You will also need to consider whether the recipient of the gift has sufficient capacity to give good receipt.

Rather than making a gift to the person directly, a trust can be a useful mechanism for avoiding some of the issues above. Generally, there are three trust options that may be available: a disabled person's trust, a discretionary trust and a protective trust.

Where the beneficiary is disabled, a disabled person's trust is an option. Firstly, it is imperative to consider if the individual qualifies as 'disabled' for the purposes of the Inheritance Tax Act 1984.

A disabled person's trust can come in the form of a life interest trust (i.e. an interest to the income and a right to enjoy the trust assets, whilst the capital is controlled by the trustees), or more commonly in the form of a discretionary trust. The discretionary trust allows the trustees to advance income and capital to the beneficiaries as they see fit. Crucially, however, a disabled person's trust can benefit from very favourable tax treatment and they can allow for the protection of the individual's entitlement to state benefits.

If the individual does not qualify as a disabled person for tax purposes (e.g. where the individual has addiction issues or is not sufficiently mature to receive funds outright), then a traditional discretionary trust may be a flexible option. As mentioned above, a discretionary trust allows the trustees to make decisions to meet the changing needs of the disabled or vulnerable person during their lifetime.

The final trust for consideration is a protective trust where the beneficiary initially receives a life interest (see above). It is 'protective' as the life interest automatically comes to an end if, for example, the beneficiary is declared bankrupt. On termination of the life interest, the trust fund can then be held on discretionary trust for a wider class of beneficiaries which can include the disabled or vulnerable beneficiary but can also include others.

– HOW SHOULD I APPROACH CHARITABLE GIVING?

– THE GIVING PLEDGE – WHAT IS IT, AND WHAT SHOULD BRITISH PHILANTHROPISTS KEEP IN MIND?

PHILANTHROPY

HOW SHOULD I APPROACH CHARITABLE GIVING?

Charitable giving should always be encouraged. However, there are various ways to give to charity, and which is most appropriate will vary depending on the circumstances.

SIMPLE DONATIONS

For small cash donations, particularly those to existing UK registered charities, simplicity is often best. Tax relief is given on donations and there is usually very low administration involved for the donor. However, although a donor can place some limits on how the donation should be applied, the simplicity of the process also means giving up long-lasting control.

SETTING UP A CHARITABLE FOUNDATION

For large donations, or where the donor wishes to retain control over the expenditure of the funds, or if the donor wants to obtain the immediate tax relief on the donation but is not yet ready for the funds to be dissipated, then the creation of a new charity may be preferable.

The donor can be one of the trustees, and the charity could be anything from a simple grant making charity up to a fully operational charity. However, the donor should be aware of the ongoing reporting requirements for charities (and particularly charitable companies). Additionally, once the donation has been made the funds have effectively become public money; the donor must accept that they cannot benefit from those funds after that point.

DONOR ADVISED FUNDS (DAFS)

DAFs are an alternative to creating a new charity, allowing the donor to donate to the DAF which in turn dissipates the funds in accordance with the donor's wishes. Using a DAF saves on much of the time, cost and effort of running a charity.

FOREIGN CHARITIES

Gifts to foreign charities should be handled with care. Importantly, many direct donations will often not attract tax relief for UK taxpayers. In part this can be because the organisation may have the status of a charity in its local jurisdiction, but it does not fit within one of the discrete heads set out in UK charity law.

DAFs prove a popular workaround to these issues; here the donor makes the donation to the UK DAF, claiming the appropriate UK tax relief, and the DAR then makes the onward donation to the foreign charity. Alternatively, some established foreign charities have a UK "friends of" subsidiary to which UK donations can be made. UK residents who are liable to tax in foreign jurisdictions (for example US citizens) should also check whether donations to UK charities qualify for tax relief in that other jurisdiction.

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THE GIVING PLEDGE – WHAT IS IT, AND WHAT SHOULD BRITISH PHILANTHROPISTS KEEP IN MIND?

Founded in 2010 by a group of ultra-wealthy individuals (including Bill and Melinda Gates and Warren Buffet), the Giving Pledge invites other wealthy people to publicly commit to giving away the majority of their wealth to philanthropy. Initially a purely American group, since 2013 there have been signatories from the UK, Germany, India, and Russia to name a few. But what should an aspiring British philanthropist be thinking about if they want to give away the majority of their wealth, whether through their own charitable foundation or simple donations?

WHAT SHOULD YOU GIVE AWAY?

When giving to charity in the UK, cash gifts are generally the simplest approach. However, many wealthy entrepreneurs and business people hold large portions of their wealth in business assets like shares. Although more complicated than cash giving, there are potential tax advantages to giving away business assets. If say a certain asset is likely to significantly increase in value, moving this out of your estate and into the hands of a charity will prevent this capital growth increasing the value of your estate.

WHEN SHOULD YOU GIVE AWAY ASSETS?

Many signatories to the Giving Pledge wish to give away most of their assets during their lifetime. This gives them the opportunity to have some oversight and see the fruits of their donations. However, others might decide to hold onto their assets during their lifetime and leave assets to charity on death. Any charitable giving on death will still be tax free, and if at least 10% of an estate is given to charity it can reduce the rate of inheritance tax on the rest of the estate.

WHO SHOULD YOU GIVE TO?

In the UK, gifts to a domestic charity will benefit from a 100% relief from inheritance tax. However, gifts to foreign charities may not be treated the same way, so care needs to be taken over exactly who should receive donations. While the case of Routier v HMRC opened the door to the relief being available on gifts to foreign charities, this was based on an interpretation of EU law and so the current position remains unclear. Certainly it seems likely that HMRC would seek to tax donations to foreign charities, so unless there is a specific desire to test this in the courts it may be simpler to select domestic charities (or domestic branches of international charities) to receive philanthropy.

WHAT ABOUT THE REST OF YOUR FAMILY?

If someone's ambition is to give away large portions of their wealth to charity before they die, it may be sensible to discuss this with their family and anyone who might otherwise expect to inherit. It may be that lifetime giving to potential heirs is a preferable option to leaving assets on death, and there are varied possible approaches (see our articles on 'normal expenditure out of income' or 'how to efficiently gift business assets' for example). Whether this is the plan or if potential heirs are simply to fend for themselves, it is likely preferable to discuss this sooner rather than later to minimise nasty surprises and disruption.

– GIFTING IN THE ARTS (CGS V AIL)

ART

GIFTING IN THE ARTS (CGS V AIL)

The Arts Council England saw a record-breaking year in 2020 with the value of cultural objects and art entering public ownership equating to an impressive £64.5 million with £40 million of tax liabilities being settled in return.

Philanthropic giving of this nature is typically facilitated by the Acceptance in Lieu scheme (AIL) and the Cultural Gifts Scheme (CGS), both of which were introduced to encourage giving in the arts and cultural sectors to museums and other institutions for the nation to enjoy.

The Arts Council England advises HM Revenue & Customs as to which items qualify as pre-eminent for these purposes, with the emphasis on items showing a significant association to British history, national life or a particular historic setting, objects of artistic or art-historical interest and items of academic value. Typical items may include archive collections, paintings, prints and sculptures.

AIL – INHERITANCE TAX (IHT)

In exchange for a qualifying gift under the AIL scheme, the HM Revenue & Customs agree to forego all or part of an estate's IHT liability. Whilst this scheme can only be utilised by the executors of an estate following the death of the owner of these qualifying items, it can be very generous and beneficial to the deceased's heirs.

Once a value for the qualifying object(s) has been agreed and the potential net value after the deduction of IHT has been quantified, the AIL scheme offers an additional refund of IHT, known as the 'douceur' or 'sweetner', equal to 25% (10% for land and buildings) of the IHT that would have otherwise been paid. With the benefit of the douceur, this effectively results in items being worth more in real terms if offered in lieu of IHT than sold on the open market.

CGS – INCOME (IT) AND CAPITAL GAINS TAX (CGT)

In contrast, the CGS allows an individual to gift qualifying objects during their lifetime and claim a tax reduction equal to 30 percent of its value against their IT or CGT liabilities (or a combination of the two). To fully utilise this tax saving incentive, the tax reduction can be spread over up to five tax years beginning with the tax year in which the offer is registered by the Arts Council England.

If you are fortunate enough to own objects of pre-eminent significance and you are considering giving them to the nation, there are potentially sizable tax benefits and it is worthwhile analysing the best case scenario for your personal tax and financial circumstances.

- GIFTS WITH INTERNATIONAL ELEMENTS
- US/UK GIVING
- WHAT OPTIONS TO NON-DOMICILIARIES HAVE?

INTERNATIONAL

GIFTS WITH INTERNATIONAL ELEMENTS

When considering making lifetime gifts, international elements can complicate matters. The international dimension may arise because you have assets in foreign jurisdictions or because you are resident or otherwise subject to tax in another country. In such circumstances, it is crucial to consider not only the UK tax position, but also the laws of the other jurisdictions and how they interact.

FOREIGN ASSETS

For a UK resident and domiciled person, the UK tax position on gifts of foreign assets is exactly the same as for UK assets. Broadly, an outright gift may suffer inheritance tax if you die within seven years of making it, and capital gains tax may be payable. However, the story does not end there, because there may also be foreign tax implications.

Many countries, unlike the UK, impose a gift tax on lifetime gifts. Other taxes which may apply are capital gains taxes, stamp duties or equivalent and other transfer taxes. Such taxes could apply to any type of asset, but you should be especially wary if you plan to give foreign real property (i.e. land and buildings). Also, bear in mind that, while gifts between spouses are broadly tax-neutral for UK tax purposes, the same is not always true in other countries.

FOREIGN RESIDENTS

If you are resident in a foreign country, you will almost certainly be subject to tax there. If a non-resident (or a dual resident) makes a gift of assets in the UK, then UK tax may also apply. If the taxes in the respective countries are of a similar type, double tax relief may be available. However, advice should always be taken to ensure that there are no nasty surprises.

It should be noted that US citizens are always subject to US tax, regardless of where they live, so US tax must always be considered when an American makes a gift.

GIFTS INTO TRUST

Even when looking purely at UK tax, gifts into trust must be considered carefully, given the risk of triggering an immediate inheritance tax charge if the value transferred is over £325,000 and no reliefs apply. When other jurisdictions are involved, things only become more complex.

Not only do you need to consider the cross-jurisdictional tax questions described above, but you also need to be aware that trusts are an alien concept in many jurisdictions, and they can impose punitive or unusual taxes on trusts. For example, it is unlikely to be wise to establish a trust if there are French connections, whether in the form of the assets or the individuals involved.

NON-DOMICILIARIES

While making lifetime gifts with an international dimension can be a minefield, in the right circumstances it can also present opportunities. People who are neither domiciled nor deemed domiciled in the UK only have an exposure to UK inheritance tax on their UK assets. Therefore, gifts of their non-UK assets can be very efficient, particularly if they are made into trust, in which case the inheritance tax benefits can be “locked in” for the future benefit of their family.

US/UK GIVING

Considering the UK tax rules on lifetime gifts can be complex, but having to marry these with the corresponding US rules if the donor and/or recipient are also US taxpayers can make the task yet more difficult.

A donor can generally make gifts free from UK inheritance tax (IHT) if they survive that gift by at least seven years. By comparison US taxpayers, for example US citizens and long-term green card holders, have an annual US gift tax allowance of currently $15,000 per recipient. Gifts over this allowance will use up the donor's lifetime gift and estate tax allowance, currently $11,700,000, although this allowance is due to reduce considerably over the coming years.

Gifts are disposals for UK capital gains tax (CGT) purposes, and a UK resident donor will pay CGT at their marginal rate on gifts subject to various factors, such as the donor's annual allowance (currently £12,300) and the remittance basis of taxation, if relevant. In turn the recipient receives the asset at its uplifted open market value for their own future CGT purposes. Cash is generally not a chargeable asset and so gifts of cash do not attract a CGT charge.

By comparison, gifts are not disposals for US income tax purposes and so the recipient receives no step-up in tax basis, instead acquiring the asset at the donor's acquisition cost. This can lead to a mismatch in the future tax consequences of a later disposal if the recipient is a US and UK taxpayer (for example a UK resident US citizen), since the asset can have two different acquisition costs for the two taxes.

The donor and recipient also need to contend with exchange rate fluctuations, since the respective acquisition and disposal values are calculated in dollars and sterling which might have changed between the two dates.

These are only some of the reasons why the US consequences need to be considered when US taxpayers are considering making or receiving lifetime gifts.

WHAT OPTIONS DO NON-DOMICILIARIES HAVE?

When it comes to the UK tax implications of lifetime gifts, non-domiciliaries are in a special category. Often, non-doms have far more options for tax-efficient planning than UK domiciliaries.

WHAT IS A NON-DOM?

A non-dom is someone who is neither domiciled nor deemed-domiciled in the UK.

Broadly, a person's domicile is the place they consider to be their permanent home. Your domicile of origin is your father's domicile when you were born. Then, once you are over 16, you can acquire a domicile of choice elsewhere if you move there and intend to remain permanently or indefinitely.

Even if you do not acquire a domicile of choice in the UK, once you have been resident here for 15 of the last 20 tax years, you become deemed-domiciled for all UK tax purposes.

WHAT PLANNING OPTIONS DOES A NON-DOM HAVE?

Unlike a UK domiciled person, non-UK assets owned by a non-dom are completely outside the scope of UK inheritance tax (IHT). So, if a non-dom makes a gift of their assets held outside the UK, then that gift will never be exposed to IHT.

One step further than that is for the non-dom to transfer non-UK assets into trust (known as an "excluded property trust"). By doing that, the assets can be kept outside the scope of IHT indefinitely, provided that the trust itself never holds UK assets. This can be particularly valuable if the non-dom themself or their family members are in the UK and may stay there longer term. The IHT benefits are be "locked in" for the benefit of the family for years to come.

One other positive of this type of planning is that the excluded property rules take precedence over the "gift with reservation of benefit" rules (which treat assets as remaining in your IHT estate if you give them away but retain the use of them). So, unlike a UK domiciled person, a non-dom can settle non-UK assets on trust and also be a beneficiary of that trust without the assets being treated as if they still belonged to the individual

WHAT IF I INHERIT ASSETS FROM A NON-DOM?

If a non-dom leaves assets outright to a UK domiciled person, there will be no IHT at that point provided the assets were non-UK assets. However, from that point on, those assets, those assets will immediately form part of the IHT estate of the UK domiciled beneficiary.

All is not lost, though. It is possible for that beneficiary to enter into a deed of variation within two years of the non-dom's death to redirect the assets into a trust. Because the trust will then be treated as having been established by the non-dom for IHT purposes, it will be an excluded property trust. Bear in mind, though, that the trust is still treated as having been created by the UK domiciled beneficiary for income tax purposes, which brings into play a series of settlor-interested trust rules.

WHAT ARE THE PITFALLS?

While there are a variety of valuable estate planning options open to non-doms, there are also complexities. Simply establishing where someone is domiciled is not always straightforward; inevitably there will be laws and taxes in other jurisdictions to consider; and trusts, particularly non-UK resident trusts, come with complex tax rules which need to be navigated. Expert advice should be taken, and certainly before a non-dom has been UK resident for fifteen tax years.

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