

Milan Conference

Trusts under English Law

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English Law?

- United Kingdom has 3 jurisdictions:
 - England and Wales
 - Scotland
 - Northern Ireland
- Separate trust laws
- United Kingdom taxation applies to all 3 jurisdictions
- Jersey, Guernsey and the Isle of Man are separate jurisdictions and are not part of the United Kingdom

English Trust Law

- Based on a combination of case law and statute
- Case law - hundreds of cases over many years *Keech v Sandford* (1726) and *Saunders v Vautier* (1841) - still relevant law
- Statutes:
 - Trustee Act 1925
 - Perpetuities and Accumulations Act 1964
 - Trust of Land and Appointment of Trustees Act 1996
 - Trustee Delegation Act 1999
 - Trustee Act 2000
 - Perpetuities and Accumulations Act 2009

Creating a Trust

- Usually created by written Trust Deed
- Signed by the Settlor and the Trustees
- Not signed by Beneficiaries
- Trust Deed
 - Sets out all the terms of the Trust
 - Identifies initial assets transferred into the Trust
 - Identifies Beneficiaries

Types of Trust (1)

- Discretionary Trusts
- Interest in Possession trusts
- Fixed Interests Trust
- Bare Trusts

Types of Trust (2)

Discretionary Trust

- Trustees have complete discretion to decide
 - Who to make distributions to (out of the class of Beneficiaries)
 - When to make distributions
 - How much to distribute at any one time
 - Whether to distribute income or capital
 - In relation to income whether to distribute income or accumulate it and add to capital

Types of Trust (3)

Interest in possession trust

- Trustees have no discretion over income
 - Income must be distributed each year to a named beneficiary
- Trustees have complete discretion over capital

Types of Trust (4)

Fixed Interest Trusts

- Trusts where the Trustees are obliged to distribute the capital out of the Trust to beneficiaries at a specific point of time in the future
 - e.g. “when my children reach the age of 40 years”

Types of Trust (5)

Bare Trusts

- Not really a trust at all
- Trustees have to deal with assets as directed by the beneficiary
- Trustees acting purely as nominees for beneficiary
- Fiscally transparent for UK tax

Trust Drafting Points (1)

Assets

- What assets will be transferred to the Trustees?
- Will further assets be added subsequently?

Trust Drafting Points (2)

Trustees

■ Choice of Trustees

- Individuals
- Family members
- Professionals – lawyer /accountant
- Corporate Trustees
 - Corporate Service Providers
 - Special Purpose Vehicle

■ Appointing New Trustees/Removing Trustees

- Specific power to Settlor?
- Specific power to Protector?

■ Trustees have to act unanimously

- Can be overridden by terms of Trust

Trust Drafting Points (3)

Avoiding Conflicts of Interest

- Two main conflict of interest rules:
 - Trustee cannot be a beneficiary
 - Trustee cannot buy assets from trust or sell assets to trust (*Keech v Sandford* 1726)
- **ALL** the conflict of interest rules can be overridden and specifically authorised by Trust Deed

Trust Drafting Points (4)

Income

- e.g. dividends received on shares held in Trust
- Trustees have discretion to decide whether to retain income or distribute?

OR

- Trustees are obliged to distribute income to named beneficiary(ies)?

Trust Drafting Points (5)

Beneficiaries

- Specifically named?
- Identified by a class
 - “All my children and remoter issue whether now living or born hereafter”
- Children - under English law references to a child automatically will include:
 - Legitimate child
 - Illegitimate child
 - Adopted child
- Children – age of majority under English law is 18

Trust Drafting Points (6)

Trustees holding shares in family/private company

- Dividends
 - Payable to Trust as shareholder
 - Retained in Trust or distributed to beneficiaries?
- Trust is not a separate legal person under English law
 - Shares registered in names of Trustees - not the name of the Trust
- Voting on shares
 - Trustees as shareholders would usually have the votes on the shares
 - Acting in the interest of beneficiaries

Trust Drafting Points (7)

Trustees holding shares in family/private company

- **Trustees' obligation to diversify investments**
 - Rule of trust law that trustees should not hold shares in a single company as their sole investment
 - Rule can be overridden by express clause in Trust Deed
- **Power to sell shares**
 - Trustees as the shareholder would normally have rights to sell their assets and investment
 - Express terms of the Trust Deed can alter this rule
 - Beneficiaries could be given a power to force trustees to sell

Trust Drafting Points (8)

Trustees holding shares in family/private company

- Trustees' obligation to oversee management of company where Trust holds a controlling interest
 - Rule in *Bartlett v Barclays Bank* (1980)
 - Can be overridden by express clause in Trust Deed
- Conflicts of Interest
 - Trustee who is also a paid Director of company whose shares are held by Trust has a conflict of interest
 - Can be expressly authorised by terms of Trust Deed
- Future succession to the shares
 - How long will shares be retained in the Trust?
 - Can be held in Trust for 125 years for the benefit of future generations

Trust Drafting Points (9)

Flexible Trust Drafting

- Powers to add to the class of beneficiaries?
- Powers to subsequently exclude persons from the class of beneficiaries?
- Powers to amend the terms of the Trust?
- Powers to transfer the assets of the Trust to a new Trust?
- Powers to appoint new trustees and remove trustees?
- Powers to change the proper law of the Trust?
- Power to move the Trusteeship to another jurisdiction?

Continuing role of Settlor?

■ Letter of Wishes

- Gives guidance to the Trustees as to how they should exercise their powers
- Trustees normally place great weight on wishes of settlor
- Not legally binding

■ Settlor can be given specific powers in Trust Deed:

- Power to appoint new trustees
- Power to remove trustees
- Consent required to exercise of specific powers by Trustees

■ Position after Settlor's death

- Settlor can appoint someone else to have the Settlor's powers after the settlor's death
- Person usually called a "Protector"

Liability of Trustees

- Trustees liable if they :
 - Fail to comply with the terms of the Trust
 - Fail to act in the best interests of the beneficiaries
- Trustees strict liability position can be relieved by express clause in the Trust Deed
- *Armitage v Nurse* (1998) - Trust Deed cannot exclude liability for
 - Fraud
 - Dishonesty

Terminating a Trust

- Trust terminates when all assets transferred out of the Trust to beneficiaries
- Automatically under terms of trust
 - e.g. “when my children reach the age of 40 years”
- By Trustees exercising a power to distribute all the capital
- By Beneficiaries under the rules in *Saunders v Vautier*
 - If all the beneficiaries are sui iuris (all ascertained and of full age and capacity) they can force the Trustees to distribute the assets to them
- By Court Order

UK Taxation of Trusts

- 4 different taxes to consider
- Income Tax
- Capital Gains Tax
- Inheritance Tax
- Stamp Duty, Stamp Duty Reserve Tax, Stamp Duty Land Tax

Income Tax

- Charged by reference to
 - Residence
 - Source of Income (UK or non-UK)

- NO charge to UK Income tax if
 - Trustees resident outside UK; and
 - All income from non-UK source (or from UK source but all beneficiaries are non-UK resident)

Capital Gains Tax

- Charged primarily by reference to residence
- NO charge to UK CGT if
 - Trustees resident outside UK
 - Only exception – UK residential property within CGT charge for non-UK residents since 6th April 2015

Inheritance Tax

- A tax on death, lifetime gifts and trusts
- Charged by reference to
 - “Domicile” of individuals
 - “Situs” of Assets
- NO charge on Trusts if
 - Created by non-UK domiciled individuals; and
 - Assets gifted are non-UK situs

Stamp Duties

- Stamp Duty charged on transfers of UK shares on sale
- Stamp Duty Reserve Tax charged on contracts for sale of UK shares
- Stamp Duty Land Tax charged on sale of UK land

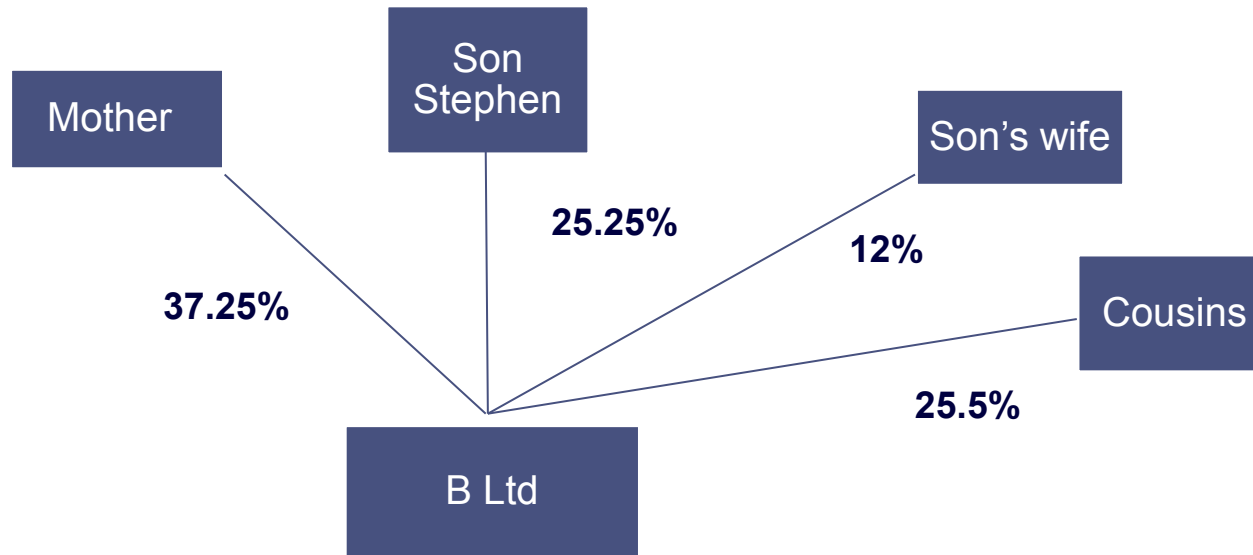
Trusts and Italian Nationals (1)

- Italian National gifts shares in Italian Company into English law trust
- No charges to UK tax arise on gift provided
 - Italian National non-UK domiciled; and
 - Italian National non-UK resident
- No subsequent charges on Trustees provided
 - Trustees non-UK resident
 - Assets of Trust remain non-UK situs

Trusts and Italian Nationals (2)

- A Trust governed by English law does not of itself bring the Trust within the scope of UK tax

Case Study (1)



- B Ltd turnover £60 million
- Stephen - Director

Case Study (2)

Mother died 31 December 2015

Mother's shares pass to Stephen

Stephen gifting mother's 37.25% shares to Discretionary Trust to take advantage of:

- UK tax rules enabling a beneficiary to vary a Will within 2 years of death
- 100% Inheritance Tax relief on shares in unquoted trading companies

Case Study (3)

Trustees – Stephen and wife

Beneficiaries – Stephen, wife, daughters, future grandchildren

Advantages for Stephen:

- Control of Company through Trust and personal shareholding
- Protects against future Inheritance Tax
- Dividends - flexibility
- Asset protection
- Control over future succession

Terminology (1)

- **Settlor** - the person who creates and funds the Trust
- **Trustees** - the persons who hold the trust assets and administer them in accordance with the terms of the Trust for the benefit of beneficiaries
- **Beneficiaries** - the persons who can benefit from the Trust

Terminology (2)

- **Trust Period or Perpetuity Period** - trusts have to come to an end within the “perpetuity period” which under English law is 125 years
- **Protector** - a person whose consent is required before the Trustees can take certain actions, or who has certain powers such as the power to change trustees
- **Issue** - refers to the direct descendants of a person

Terminology (3)

- **Accumulation** - the process where income of the Trust is retained and added to capital
- **Proper Law** - the law which governs the Trust
- **Settlement** - an alternative term for a trust
- **Interest in Possession** - where a beneficiary has the right to receive the income of the trust as it arises
- **Letter of Wishes** - a non legally binding letter of guidance given to the Trustees by the Settlor

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