SERVICES FOR INDIVIDUALS

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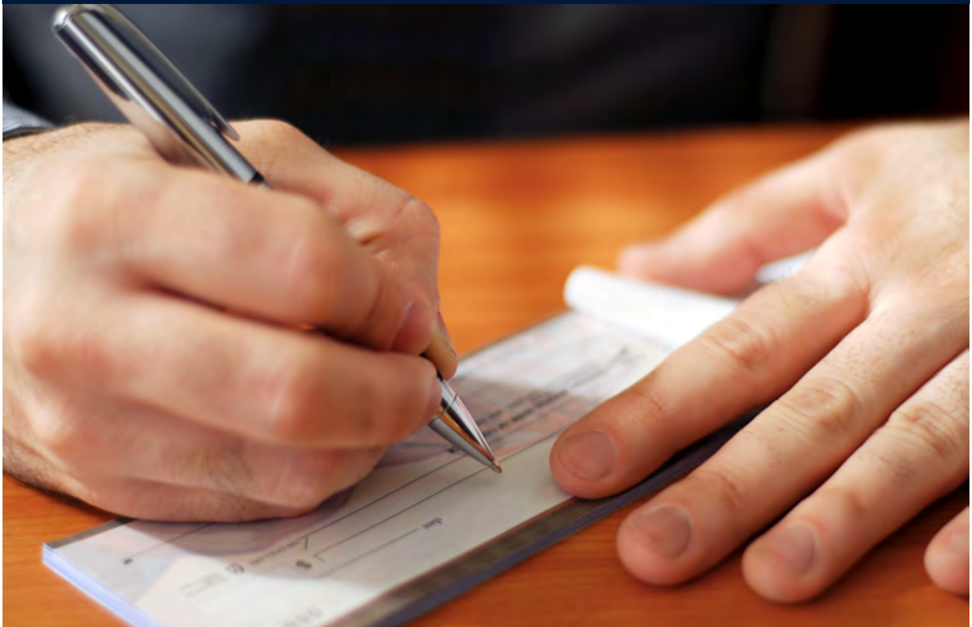

BANK OF MUM & DAD

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In recent years there have been lots of reports in the press about the reliance on Bank of Mum and Dad in order for younger generations to get on the housing ladder.

Even with the recent Government schemes to help with the funding of deposits there is generally still a requirement to find a minimum 5% deposit and reliance on Bank of Mum and Dad is unlikely to end anytime soon.

Parents are generally keen to help their children financially if they can. It is important that they make informed choices with an understanding of the range of ways in which financial support may be given and the legal and tax consequences in each case. It is important that parents think carefully about the most appropriate way in which to provide financial support depending on their views and objectives and the overall circumstances (their own and those of the children they wish to help).

With careful planning, there are ways to address common concerns people have about providing financial support to the next generation. This might be around having some control over what you have given to your children. You may wish to make sure it is put to good use and not wasted.

Even if you are happy to trust your children to 'do the right thing' you may be concerned that what you give might be vulnerable to changes in your child's circumstances, for example, in the event of a relationship breakdown.

You might be keen to start reducing the value of your estate which will be subject to inheritance tax in the future and have in mind that giving to the children sooner rather than later will achieve this. Alternatively, providing financial support may be intended as a loan if the sums you are making available to your children now may be needed by you in the future.

It is vital that parents and their children understand and acknowledge the basis on which financial support is being provided. Is what is being given a loan or an outright gift? Is the parent making an investment with the child in a property? The arrangements should be appropriately documented even in a close family scenario (because of the different tax consequences which can arise and the fact that the nature of the arrangements may be relevant to dealings with third parties).

Outright gifts

An outright gift means that what you are giving away cannot be recalled and is vulnerable to changes in your child's circumstances. That includes claims from 3rd parties such as creditors or in the event of a relationship breakdown.

It is not uncommon for high street mortgage lenders to insist that 3rd party contributions towards the purchase price of the property are documented as an outright gift.

Whether and to what extent gifted or inherited assets are treated as part of the "matrimonial pot" available for distribution between the parties on divorce depends on the circumstances of the case, but the starting point in a marriage of any length will generally be that the assets, irrespective of their source, will be divided equally. It will be rare that the court will completely ring-fence such monies so there is a real risk that at least half, possibly even more, of your hard earned cash, could end up in the pocket of your now not so doting ex son or ex daughter in law. There will usually be scope to protect the value of the gift in the event of your child's relationship breaking down via a carefully drawn up and implemented pre or post nuptial agreement or co-habitation agreement between your child and their spouse or partner.

You may be comfortable that what you are giving away is genuinely surplus to your lifetime needs and feel that your child is settled in life. You may take the view that once you have done your bit of providing a financial helping hand, what happens next is down to them.

A key advantage of making outright gifts to your children is to reduce the value of your estate on which they will eventually have to pay inheritance tax. Broadly speaking your beneficiaries will pay inheritance tax at 40% on all assets passing on your death in excess of the inheritance tax threshold. The threshold is currently £325,000 for an individual with married couples and registered civil partners having a combined threshold of £650,000 (leaving aside the new 'residence nil rate band').

Generally, value you give away only leaves your estate for the purposes of calculating inheritance tax on your death if you survive 7 years from making the gift (though there are some exemptions for gifts in certain circumstances which are useful exceptions to the 7-year rule).

Whilst a gift of cash can generally be made without any formalities, it is sensible to keep a record of gifts you have made. This is helpful to make sure that all relevant exemptions can be claimed by a person's executors when they are called on to report all gifts made by that person in the 7 years prior to his or her death. The main exemptions are for gifts of £3,000 capital each year per donor (with one year carry forward if the exemption was not used in the previous year) and gifts made as part of regular expenditure out of surplus income.

Co-ownership between you and your child

Giving your children a helping hand on the property ladder may be an opportunity for you to make an investment rather than a gift or loan. It may be attractive to you to contemplate that your contribution may at some stage be returned to you with any corresponding growth.

It is important to bear in mind that if your investment does well you will be adding to rather than diminishing the value of your estate for inheritance tax purposes. It is also important to bear in mind the likelihood in practical terms of seeing a return on your investment, if the property you are helping your child to buy is intended to be their long term home. Again, the understanding and acknowledgement of all parties as to what is intended is important to minimise scope for family fall out in the future!

With this in mind, the arrangements should be documented usually in a 'declaration of trust' drawn up by a lawyer recording the contributions each party has made to the purchase and the intention that this should be reflected in the 'beneficial ownership' (regardless of in whose name the legal title to the property is registered). Percentage ownership could be fixed based on contributions to the initial cost of purchase or floating by reference to a formula which brings into account not only initial contributions but later funding of improvements or unequal contributions to mortgage repayments.

It is important to understand that whoever is on the legal title will be party to any mortgage and jointly and severally liable for it notwithstanding any Declaration of Trust.

There is still a risk that in the event of your son or daughter divorcing, their share of the property could be taken into account or subject to a claim by their ex although your share would be protected. It might mean that the property had to be sold though.

Co-ownership between your child and others

If you are helping your child to buy a property with someone else, such as siblings, friends or a partner then a Declaration of Trust/Co-ownership Agreement will be important to record and protect your child's interest. This can also help avoid dispute if he and his co-owners fall out. It may, for example, include a mechanism for one co-owner to have an option to buy the other out should he or she wish to sell, cover who is responsible for repairs and require all to agree to other people coming to stay at the property for any extended period of time.

If your child is in a cohabiting relationship with their co-owner, they should consider a Cohabitation Agreement which can deal with other assets and issues which might need to considered if the couple split. And if they are a couple getting married they may want to look at a Pre-Nuptial Agreement. Drafted properly, a Pre-Nuptial Agreement can protect and preserve all sorts of assets including family gifts and inheritances and even shares in a family business. Such agreements must be fair to both parties and to be effective they must be signed well in advance of the wedding and incorporate full disclosure of the couple's circumstances. For those already married, a Post-Nuptial Agreement is possible. Correctly implemented, Pre-Nuptial and Post-Nuptial Agreements are an increasingly effective method of protecting family assets, particularly assets which emanate from parents and other relatives and which are intended to be retained for the benefit of children and grandchildren.

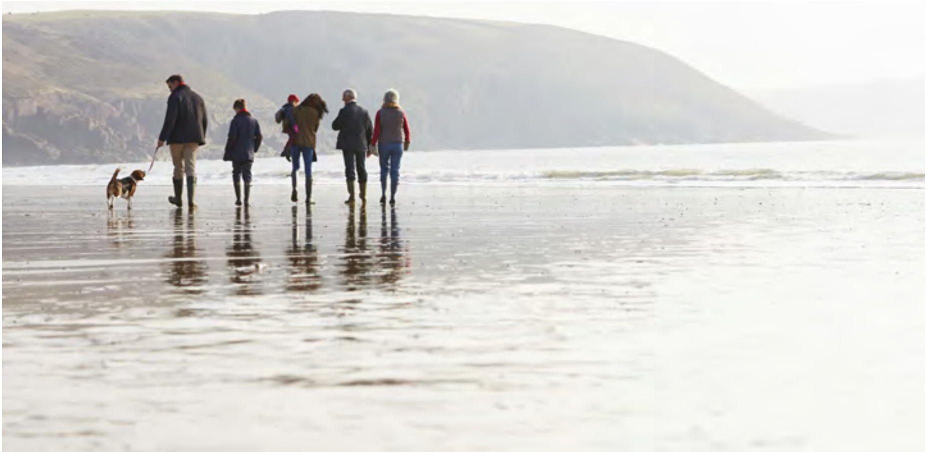
Loans

A loan rather than an outright gift gives parents the option to recall the value given away and is therefore an attractive option in the short term. This is provided that, where there is also a mortgage lender, there is no objection by the mortgage company to any 3rd party contribution being by way loan rather than gift (unfortunately it is not uncommon for high street mortgage lenders to insist on the latter).

A loan may be appropriate where parents are able to offer some financial support now but may have need of the funds themselves in the future. It might also be appropriate if they want to ensure that the financial support they are providing is not vulnerable to claims from third party claims against their children, such as creditors or in the event of a relationship breakdown.

In such circumstances, it is important that the loan is appropriately documented so as to be legally enforceable even if that seems a little at odds with the relationship of trust between parent and child in a close family scenario. You may also wish to consider taking some security for the loan, for example, by way of a charge over a property your child is purchasing.

It is wise to have the benefit of expert advice in drawing up the arrangements to make sure they do not fall foul of Consumer Credit Act regulations or requirements of any institutional lender if there is also a mortgage on the property your child is buying and so that all parties have an understanding of the legal position.



From an inheritance tax perspective, the value of what you have loaned will remain part of your estate in the event of your death. On the plus side, any growth in the value of any fund or asset in which your loan is invested by your child will be outside of your estate particularly if the loan is made interest free.

If you make a loan and later decide to waive all or some of the loan, you will be making a gift at that stage. To the extent the value being waived does not fall within one of the exemptions for lifetime gifts, it will fall outside of your estate for the purposes of calculating inheritance tax in the event of your death once you have survived 7 years.

For some people initially making a loan and gradually waiving parts of it over time, as your child becomes more settled in life and as you feel more confident that the value you have loaned is surplus to your own lifetime needs may be a balanced and tax efficient way forward. As with the loan, any waiver of it should be appropriately documented with the benefit of legal advice.

Trust planning: The best of both worlds?

If you are keen to mitigate inheritance tax exposure, have surplus income or capital that you would like to set aside to help your children now or in the future but want to retain some control and provide at least a layer of protection for the funds or assets you are giving away then a trust could be the answer.

If you set up a family trust and the gift you make into it is well within the inheritance tax threshold this won't create any inheritance tax charge when the trust is set up. Unless the value of what you put into trust increases significantly, it should also be possible to avoid any periodic inheritance tax charges which apply to trusts (at a marginal rate of up to 6%) on the value in excess of the nil rate band (the trust having a nil rate band equivalent to the inheritance tax threshold relevant for an individual).

By making a gift into trust you can start the 7-year clock running to remove value surplus to your lifetime needs from your estate into an environment which you control (as trustee). This can allow you to provide for your children or other intended beneficiaries in a measured way. Loans can be made from the trust so that the sums loaned may be re-called if the beneficiary's circumstances change. Property could be purchased in or transferred to a trust (which can help manage Capital Gains Tax due to scope to postpone or 'holdover' the gain).

It is, however, likely to be difficult for trustees to obtain or take out a mortgage from a high street lender.

Trusts are not a tax free zone, expert advice is essential when considering how to structure the trust and whether to fund with cash or assets to make sure the trust runs tax efficiently.

Generally speaking, a gift into trust is not tax efficient if you or your spouse/civil partner can also still benefit from the assets in the trust (as where the person making a gift reserves a benefit then generally speaking the gift will not be effective for inheritance tax planning purposes). It is usual, therefore, for the person setting up the trust and his or her spouse or civil partner to be excluded from the class of potential beneficiaries.

Passing on an inheritance to your children

Receiving an inheritance can often be the trigger for parents to think about making some onward provision for their children.

If you have inherited within the last two years you should take advice about tax planning opportunities which involve making a 'deed of variation' within two years of the death of the person from whom you have inherited. This allows you to make an onward gift of some or all of the value of your inheritance with no 7 year wait before the value given drops out of your estate. Alternatively, there may be scope to vary some or all of your Inheritance.

In favour of a trust of which you can be a trustee and a potential beneficiary without this being a 'gift with reservation of benefit'. This is because for Inheritance Tax purposes a Deed of Variation can be drawn up so it is as if gift or trust was made by the person who has died rather than by onward gift from you as the original beneficiary.

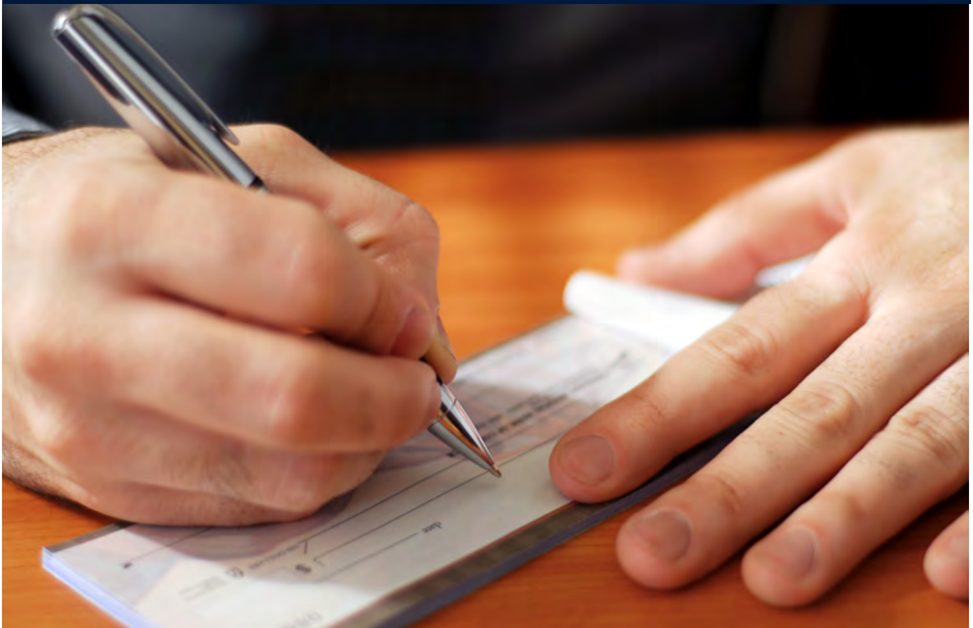
What should I do next?

If you are thinking about giving children financial helping hand, there are a whole range of options you may wish to consider. It is important for you to understand the legal and tax implications and the extent to which what you are considering will address your concerns and achieve your objectives. Your chosen route should balance your needs, those of your children as well as having an eye to tax efficiency and asset protection. It is vital that you and your children are clear as to basis on which any financial support is being given so as to avoid any future dispute between you and them or with third parties.

How we can help

Our team of experts will take time to understand your circumstances and goals, providing tailored advice so you can make informed choices. This can help to make sure that you make the most of opportunities for tax planning and asset protection. It can also help you to avoid tax pitfalls and to make sure all appropriate legal documentation is in place.

It is not possible to deal comprehensively with all of the legal and tax aspects involved when parents are providing financial support to children. This note highlights some of the key issues to consider is no substitute for specific advice based on your particular circumstances at the relevant time.



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