INVESTMENT QUORUM
UNIQUE, BOUTIQUE WEALTH MANAGEMENT

Loan Trust

What is a loan trust?

A loan trust involves an individual establishing a trust. But rather than making a gift, the settlor lends money to the trust. The trustees then invest this money, typically into an investment bond, on behalf of the beneficiaries.

The settlor (the person who made the loan) can demand either partial or full repayment of the outstanding loan at any time. If regular loan repayments are needed, the trustees can repay the loan by using the 5% tax-deferred withdrawal facility from the bond. The settlor cannot benefit from growth within the trust fund - any fund growth must be used for the benefit of the trust beneficiaries.

A Loan Trust allows clients access to their original capital at any point whilst the growth on any investments will not be included in their estate for IHT purposes from day one. The outstanding loan remains in the settlor's/donor's estate for IHT purposes.

Who is it appropriate for?

A loan trust is typically used for individuals who want to start estate planning but are concerned about forfeiting access to their capital.

Creating a loan trust means any future investment growth is immediately outside the estate and this can help cap the value of assets included within the estate.

If the settlor decides that they no longer need access to all their capital, they can choose to waive the right to the repayment of some or all of the loan. Any loan given away will be outside the settlor’s estate after seven years, unless covered by an exemption.

Creating the Loan Trust

Typically, the creation of a loan trust requires the following steps:

1. Trust is created.
2. Loan agreement is completed between the settlor and trustees and a loan of cash is made to the trustees.
3. Trustees invest the cash from the loan into an investment bond.
4. These are typically all packaged together and included in the provider's documentation.

Creating the trust

Under the discretionary trust, no beneficiary has a right to either income or capital. The trustees are able to appoint income or capital at their discretion to any beneficiary within the class of potential beneficiaries named in the trust deed.

The settlor(s) are generally automatically included as trustees. The settlor(s) should also appoint at least one additional trustee to ensure the validity of the loan agreement. The appointment of additional trustees also avoids the need to appoint replacement trustees after the settlor(s) death.

IHT on the setting up of a loan trust

The trust is first created by making a small gift, which is unlikely to give rise to IHT. There is then no transfer of value for IHT when the loan is made as the settlor loans the money to the trustees rather than gifting it.

There's no Gift with Reservation (GWR) provided the settlor's access is restricted to the repayment of the outstanding loan and they cannot benefit from growth within the trust.

Death of the settlor

The trust doesn't come to an end if the settlor passes away. The trust will remain until such time as the trustees have appointed all the assets out to the beneficiaries.

Negatives

- Only the growth on trust-invested assets are outside of the settlor's estate.
- The original loan remains in the settlor's estate unless waived.
- The settlor is not entitled to the growth from the investment.

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