

AVOIDING CGT PROBLEMS FOR IHT ACCUMULATION & MAINTENANCE ("A&M") TRUSTS

Ralph Ray¹

When assets leave an A&M trust, (as defined for IHT under IHTA 1984 s.71) e.g. on winding up the trust or advancement to beneficiaries, CGT holdover only applies if:

- (a) the assets are within TCGA 1992 s.165, eg business/agricultural assets, or
- (b) for other assets, i.e. investments, for occasions on which a beneficiary becomes beneficially, i.e. absolutely entitled to trust assets held on accumulation and maintenance trust (TCGA 1992 s.260(2)(d)), namely a time when no interest in possession exists. Unfortunately this is of limited use, because most modern flexible (s.71) type accumulation and maintenance trusts provide that the beneficiary only becomes entitled to income by the specified age (i.e. not exceeding age 25) not capital which remains in the trustees' discretion or at a later age, e.g. 30. Alternatively, the problem arises because the beneficiary's capital entitlement may be held for him at, say, 21 or 25, but under the Trustee Act 1925 s.31 the beneficiary would have been entitled to the income, (i.e. an interest in possession) from age 18. (This problem would not exist if s.31 had been excluded or amended appropriately).

Therefore, the CGT holdover problem for investment type assets exists because the beneficiary does not become entitled to the capital and income at the same time and therefore s.260(2)(d) is not satisfied.

Two possible solutions may exist:

1. It may be possible to advance the capital at the same time i.e. coinciding with entitlement to income arises, thereby satisfying that statutory requirement. This will depend on two main factors. First, that the income entitlement has not yet arisen, namely it is a future event. Secondly, that the trust is drawn in sufficiently flexible terms to permit the trustees to advance the capital earlier, and to coincide - as s.260(2)(d) in effect requires - with the commencement of the income entitlement; and being under powers contained in the trust deed.

Example:

Albert has created an A&M trust under IHTA s.71 for his grand-daughter, Victoria, whereby she becomes entitled to income at age 21 (thereby satisfying the condition in s.71(1)(a)), and the capital entitlement is left in the trustees' discretion (or alternatively accrues at, say, age 30). However, this is subject to powers in the trustees to advance the capital earlier. Victoria is now aged 20 and the trustees exercise a power of advancement under powers contained in the trust deed. Accordingly, Victoria becomes entitled to the capital and the income on her 21st birthday, thereby satisfying the CGT holdover, deferral requirement in TCGA in s.260(2)(d). Without the advancement of capital when Victoria becomes 21, the trust would change from being an A&M into an interest in possession and therefore s.260(2)(d) could not apply because the trust is no longer within the A&M regime. If the trust deed does not contain the requisite powers, an application to the court may be appropriate; or it may even be possible to make the advancement without an application to the court under the principles in *Pilkington v IRC* [1964] AC 612. The trustees are advised in writing that their available CGT taper relief ceases on the holdover disposal date and it is not available for Victoria by way of tack on; also, that the CGT holdover will, in most circumstances, be merely a deferral of the tax - unless Victoria still holds the assets on her death.

Beware also that if an absolute appointment is made to a beneficiary with an existing interest in possession, a charge to CGT (without TCGA s.260(2)(d) holdover) may well arise unless the appointment is of "business or agricultural assets", see (a) above.

2. The beneficiary of the A&M trust as settlor settles/assigns as from an "effective date" (and without apportionment and clearly before the entitlement to capital) all his income interest under the trust to be held by

the trustees on new trusts. Such income under the new trust is on A&M terms, e.g. with powers of accumulation and/or maintenance etc. From the date on which it is intended that the beneficiary is to receive the capital, eg 25, this new trust collapses so that the A&M regime ceases and the beneficiary becomes entitled to the capital and income at the same time and therefore TCGA 1992 s.260(2)(d) is satisfied and the holdover claim is available. The assignment of the interest in possession is not a CGT disposal – it is an assignment of an interest in income only.