Legal & General's Business Property Will Trust solution

Legal & General

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Before you start

IMPORTANT NOTES

The Legal & General Business Property Will Trust Solution is designed to be used only in conjunction with Legal & General's Directors' appropriate share protection schemes.

Legal & General has drafted this guide to reflect the law as at 1 January 2020.

This guide refers to terms such as 'life insurance policies' and 'cross option agreement'. These terms are explained in the Policy Summary of your chosen life insurance policy and the Guide to Share Protection which you should read before taking out a life insurance policy or amending your will.

We therefore strongly recommend that you consult your own legal adviser before proceeding.

Where the guide refers to a 'spouse' the term also includes a registered civil partner.

Full details of our range of life insurance products are available from your adviser.

If you're unsure, please ask

If anything is unclear or you require further information, we or your adviser will be happy to help.

Inheritance tax planning with business property

Inheritance tax is designed to tax the value of a person's estate when they die and certain gifts they make during their lifetime.

An individual is entitled to their own separate inheritance tax exemptions, reliefs and nil rate band (the nil rate band is the amount on which there is no inheritance tax to pay). In addition, inheritance tax reliefs of up to 100% are potentially available where the asset being transferred is business or agricultural property (although agricultural property is not dealt with in this brochure).

BUSINESS PROPERTY RELIEF

Inheritance tax business property relief is potentially available on a transfer of 'relevant business property'. Where business property relief is available, it applies at either 50% or 100%.

Where the relevant business property is property consisting of a business or an interest in a business, or unquoted shares in a company 100% relief is normally available.

50% relief may be available where the business property consists of land, buildings, machinery or plant used wholly or mainly for the purpose of the owner's business.

50% relief may also be available on quoted shares in a company where a shareholder has control of a company.

Generally, a business interest or share in a business will not qualify for business property relief where it deals (wholly or mainly) in securities, stocks or shares, land or buildings or the making or holding of investments.

In order to qualify as relevant business property the property must usually have been held for two years immediately before the transfer (for example on death). Provisions are in place, however, where business property has been replaced, or where business property has been acquired on the death of a spouse.

Generally where business property is subject to a binding contract for its sale it does not qualify for business property relief.

SHARE PURCHASE AGREEMENTS

Share purchase agreements may be put in place in order that on the death of a business owner, the other business owners can purchase the deceased's share of the business from the deceased's estate. Such an arrangement can assist the surviving business owners by helping them to keep control of the business. It can also assist the family of the deceased, particularly where the beneficiaries of the estate would prefer to receive money rather than the share of the business. A life insurance policy may be used in conjunction with such an agreement so as to provide the funds with which the other business owners can purchase the share. There are different types of agreements.

A 'buy and sell' agreement requires that on the death of the deceased business owner, the surviving business owners will buy the deceased's shares. It is HM Revenue & Customs' view that such agreements usually constitute a binding contract for sale and as such any business property relief would be lost.

A cross option agreement (sometimes called a double option agreement) provides that on the death of a business owner, the personal representatives of the deceased have the option to sell the deceased's share of the business to the surviving business owners. Equally, the surviving business owners have the option to buy the deceased business owner's share from the personal representatives. If either party exercises their option then the other party would be bound to buy or sell, as the case may be. This method usually preserves any business property relief.

Following the purchase, the deceased's estate will have the sale proceeds and the surviving business owners will have the share of the business. The proceeds in the deceased's estate should pass in accordance with the deceased's will. If there is no will, the proceeds should pass in accordance with the laws of intestacy.

INHERITANCE TAX AND GIFTS BETWEEN SPOUSES

It is natural for spouses to want to leave the majority, if not all, of their personal wealth to one another to help provide the survivor with financial security. Gifts between UK domiciled spouses are usually free from inheritance tax: there will be no inheritance tax to pay when the first spouse dies and leaves their entire estate to the surviving spouse.

If a business owner dies and leaves relevant business property to their surviving spouse, business property relief is potentially available when calculating the inheritance tax liability on the surviving spouse's estate when the surviving spouse subsequently dies. However, where the business property is sold when the business owner dies and the spouse receives money instead of a share in the business, such money will not usually qualify for business property relief. Any money that the surviving spouse still has on death will be assessable for inheritance tax at that time. This will often be the case where there is a share purchase agreement in place (see above).

The Solution

What is needed in these situations is an inheritance tax planning arrangement that is flexible enough to utilise business property relief on the death of the business owner, whilst allowing the surviving spouse to benefit from the proceeds but not in a way which puts all of those proceeds in the survivor's estate.

An individual may provide in their will for some or all of their assets to be left in trust (a Will Trust).

The arrangement we have produced is the Legal & General Business Property Will Trust Solution.

THE LEGAL & GENERAL BUSINESS PROPERTY WILL TRUST SOLUTION

It should allow:

- Each spouse access and control over the capital during their lifetime.
- The use of business property relief on the death of the business owner without having to compromise their surviving spouse's financial security.
- The surviving spouse to have access to capital from the will trust at the discretion of the trustees.
- A potential safeguard against the impact of nursing home fees and the costs of long-term care.

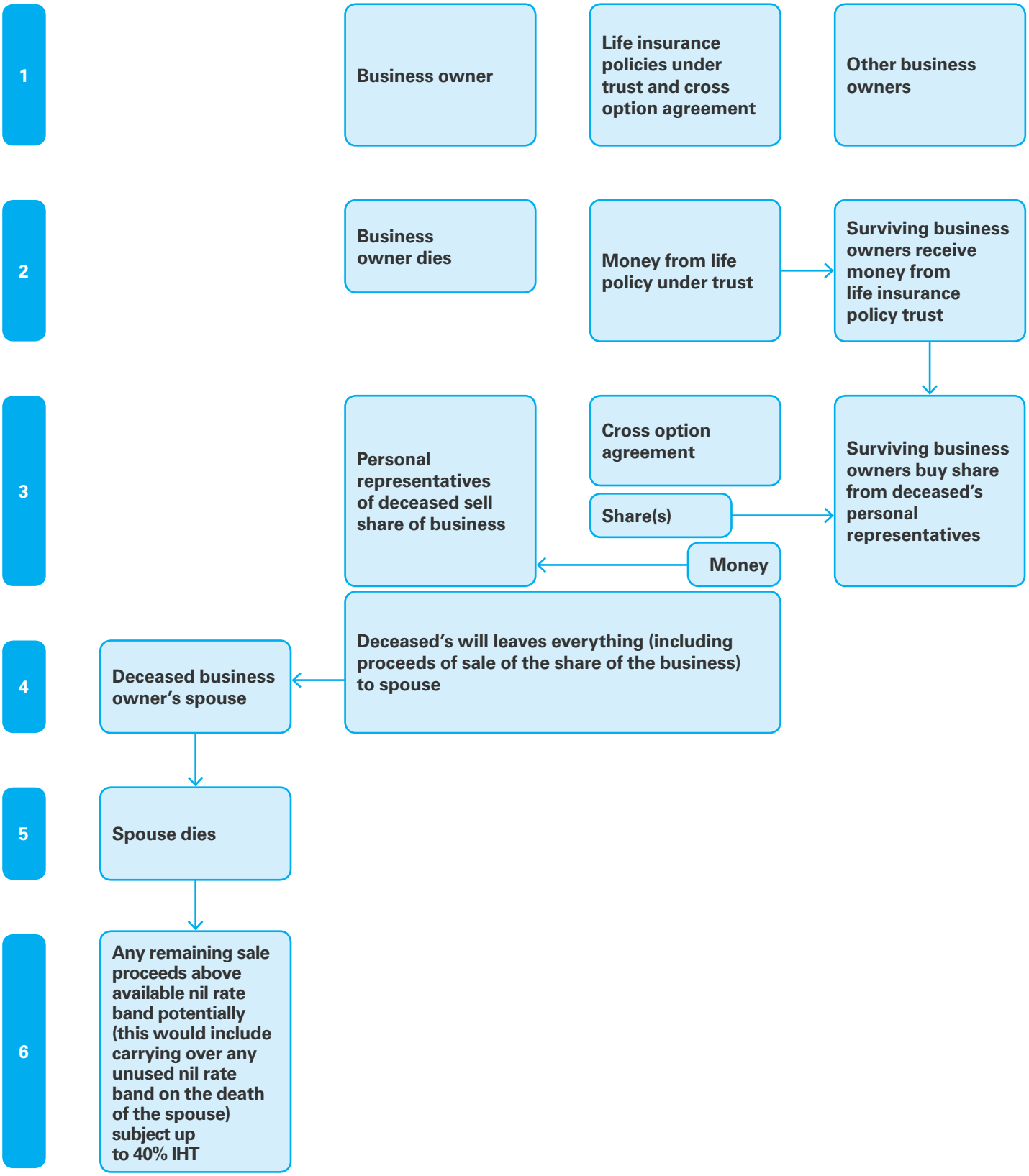
It is essential to arrange an appropriate will with your legal adviser. Specimen clauses are provided for consideration by you and your legal adviser.

HOW DOES THE LEGAL & GENERAL BUSINESS PROPERTY WILL TRUST SOLUTION WORK?

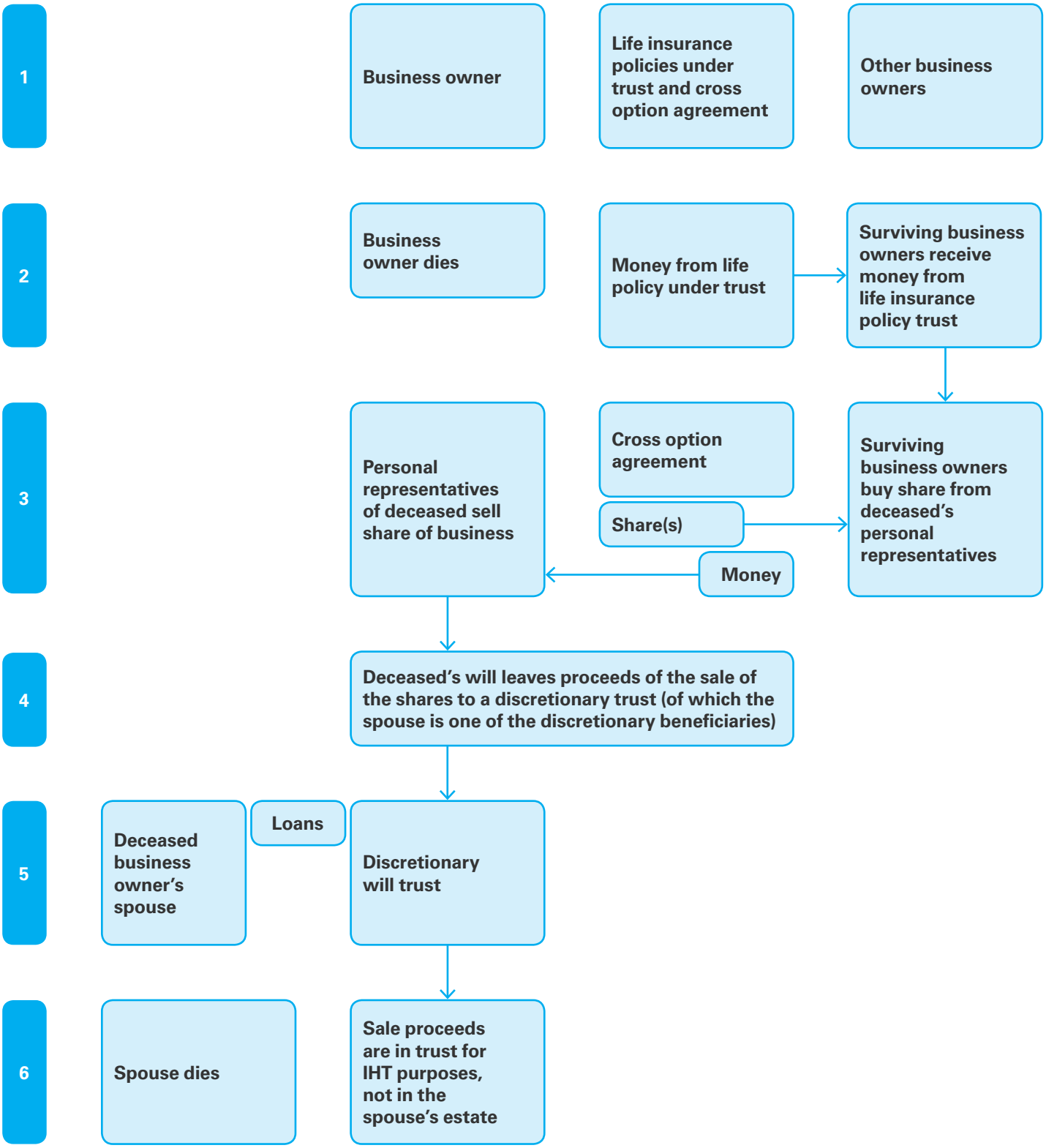
1. The business owner enters into an appropriate share purchase arrangement (supported by appropriately written Legal & General life insurance policies).
2. The business owner arranges for his/her will to be amended so as to leave the share of the business into a trust that the legal adviser has written into the will.
3. On the death of the business owner, the legal ownership of the share of the business passes to the personal representative of the estate to transfer to the trustees of a discretionary trust under the terms of the will or,

   The personal representative may sell the business property (perhaps in accordance with the share purchase agreement), in which case the proceeds of the sale will pass to the trustees to hold under the terms of the will.
4. The remainder of the estate passes to the surviving spouse directly. Any gifts from the deceased spouse directly to the surviving spouse should be exempt from inheritance tax.
5. When the surviving spouse dies the value of the assets in the discretionary will trust should not form part of his/her estate.
6. The discretionary will trust allows the trustees to make appointments or loans to any beneficiary of the will trust including the surviving spouse. Therefore, if the surviving spouse needs additional funds, the trustees can arrange this.
7. Once the will trust is in operation, any growth in value of the proceeds should be outside the estate of the surviving spouse, unless any capital distributions or loans made to them have not been spent before the death of the surviving spouse.

Without will trust planning



With will trust planning



Case study

Kingdom's Engineering Consultants Ltd

James Hargreaves, Robert Stevenson and Jimmy Watt are all directors in a Mechanical Engineering Consultancy. They have each held their shares in the business continuously for the last 10 years.

Each shareholder effects a life insurance policy for an amount which matches the current value of their shareholdings. All three policies are written in an appropriate trust (Director Share Protection Trust W13227) for the benefit of the other shareholders. They enter into an appropriately drafted cross option agreement (Shareholders' Cross Option Agreement W13232) having confirmed with their advisers that the agreement is suitable and does not conflict with the company's articles of association.

James has left his entire estate to his wife Jenny, absolutely.

Unfortunately, James dies during the term of the policy, leaving his wife Jenny and their three children. As Jenny has a young family to bring up alone she has no interest or wish to be involved in the business.

The surviving trustees claim on the policy and pass the policy proceeds to themselves as beneficiaries under the trust.

The beneficiaries (Jimmy and Robert) exercise their option under the cross option agreement to buy the deceased's shares from his personal representatives.

CONSIDER THE FOLLOWING ALTERNATIVE SCENARIOS:

1 James Hargreaves leaves his entire estate to his wife, Jenny, absolutely.

Jenny will benefit from all of James' estate, including the proceeds from the sale of James' shares in Kingdom's Engineering Consultants Ltd.

Jenny will be absolutely entitled to the proceeds and can use them as she wants. On her death, any of James' estate that Jenny still owns (including any money from the proceeds of James' shares that Jenny has not spent) will be in her estate and assessable for inheritance tax.

James' shares qualified for business property relief on his death, however, Jenny could have received those shares free of inheritance tax anyway because of the exemption for gifts to spouses. However, on Jenny's death her estate is unable to benefit from business property relief on the money that resulted from the sale of James' shares since this money would not be relevant business property.

2 Instead of leaving his shares to Jenny, James leaves his shares in Kingdom's Engineering Consultants Ltd to a discretionary trust in his will. The classes of beneficiaries will include his wife Jenny and their children. The remainder of James' estate is left to Jenny absolutely and as she is the absolute beneficiary she can spend the money as she wishes.

The trustees of the discretionary trust receive the proceeds from the sale of James' shares in Kingdom's Engineering Consultants Ltd. The trustees can make appointments or loans to Jenny from the trust fund. This enables Jenny to benefit from the trust, however the value of assets within the trust should not be in her estate for inheritance tax purposes (although the trust itself may be liable to inheritance tax in the form of periodic and exit charges).

James' shares qualified for 100% business property relief and therefore passed into the trust free of inheritance tax. The sale proceeds were not subsequently added to Jenny's estate and were not assessable for inheritance tax on her death.

Specimen letter to legal advisers

Dear Sir/Madam,

[NAME OF SHAREHOLDER], SHAREHOLDER OF [NAME OF COMPANY].

The above shareholder is to take part in a shareholder protection arrangement. As part of this, the shareholder wishes to review his/her will with you. We are writing to you to provide you with some background information regarding the shareholder protection arrangement.

The shareholder is entering into a share protection arrangement backed by a life insurance policy in trust. The objective is for the shareholder's personal representatives to have a purchaser for his/her shares in the company on his/her death.

Each shareholder will effect a life insurance policy on his/her life under trust for the benefit of the other shareholders. In addition, the shareholders will enter into a cross option agreement. The agreement would provide a 'put' option for the personal representatives of the deceased and a 'call' option for the other business owners. If a shareholder dies, the proceeds of the policy on his/her life are paid to the trustees for the benefit of the other shareholders. The other shareholders will then have the funds with which to purchase the deceased's shares should they exercise the call option, or should the deceased's personal representatives exercise the put option.

Such an arrangement can form an invaluable part of the company's succession plans and provide money for the deceased's beneficiaries at a potentially difficult time. However, if the shareholder's will is not appropriately prepared an inheritance tax problem could be generated for the people he/she leaves behind.

If, for example, the deceased's spouse were to inherit the proceeds of the sale then those proceeds would form part of the spouse's estate for inheritance tax on that spouse's subsequent death. The shareholding of the above shareholder has been recently valued at £_____.

One method of potentially mitigating this inheritance tax risk is for the shareholder's will to create a discretionary trust for the proceeds of sale to pass in to.

Yours etc,

This specimen letter is for guidance only and should be amended as appropriate, for example, if the business is a partnership or limited liability partnership or a different method of share protection is being used.

The information in the brochure is based on our understanding of UK tax law and HM Revenue & Customs' practice as at 1 July 2018, both of which may change. While we believe our understanding to be correct, we cannot guarantee it and cannot accept any responsibility for any loss or liabilities arising from action taken as a result of the information contained in this brochure.

Draft specimen clauses for Business Property Will Trust

NOTES FOR THE SPECIMEN WILL TRUST CLAUSES:

Please note:

1 The specimen clauses have been produced for consideration by you and your legal advisers for possible inclusion within your will or in a codicil to cover the position on the death of a business owner.

2 The legal and tax effects of the specimen clauses will depend on your individual circumstances. Legal & General Assurance Society Limited and its advisers accept no responsibility for ensuring that the specimen clauses meet your requirements or for any loss, damage or other claim that may arise from the use of these specimen clauses.

3 It is important that the specimen clauses are considered by you and your legal advisers in conjunction with any Articles of Association, shareholder agreements, partnership agreements, limited liability agreements or similar.

4 If the business property consists of anything other than shares in a limited company or share of a partnership or limited liability partnership, for example, agricultural property, then legal advice should be sought on this issue.

5 Care should be taken where you also wish to arrange 'nil rate band' planning within your wills. If this is the case you should discuss this with your legal advisers.

6 It is desirable to also complete a letter of wishes to provide guidance to the trustees in relation to the trust fund.

Business Protection

SPECIMEN CLAUSES FOR INSERTION INTO WILL

The Notes on page 3 should be read before using any of these clauses.

PART 1

Insert the full name and address of the individuals you wish to appoint as executors and trustees. You should appoint at least two individuals.

1.1 I appoint [full name] of [address] and [full name] of [address] to be the executors and trustees of this Will

1.2 In this Will the expression 'my Trustees' means its trustees for the time being or (where the context requires) my personal representatives for the time being

1.3 Any powers and discretions given to the Trustees of this Will (by the Will or any Codicil to it or by the general law) may be exercised by my Trustees before the administration of my estate is complete

PART 2

The term [my Husband/Wife/Registered Civil Partner] has been included in these draft clauses for ease of reference. That term should be defined when first used in the Will.

You may wish to give the Trustees the power to add to the list of beneficiaries (possibly with the survivor's consent during their lifetime) to give flexibility for the future.

*Delete as appropriate.

2.1 I declare that this clause shall only take effect if the gift to or for the benefit of [my Husband/Wife/Registered Civil Partner]* in clause 3 of this Will shall take effect and qualify or would apart from this sub clause have taken effect and qualified in its entirety for exemption under section 18 of the Inheritance Tax Act 1984

2.2 In this clause:

2.2.1 'the Beneficiaries' means

(i) [my Husband/Wife/Registered Civil Partner]*

(ii) Any child or grandchild of mine whenever born (including step-children and their issue)

(iii) Anyone descended from my father or mother and

(iv) Any surviving spouse (whether or not remarried) of anyone described in paragraphs (ii) and (iii) above

2.2.3 The 'Discretionary Trust Fund' shall mean My Business Property or if its reduced value exceeds my Nil Rate Band Sum such part or parts of it having a reduced value equal to my Nil Rate Band Sum as my Trustees may select together with accumulations (if any) of income and all assets from time to time representing the same

Clause 2.2.4 will need to be amended where other business property or agricultural property is to form part of the Discretionary Trust Fund.

2.2.4 'My Business Property' shall mean any business property in my estate which qualifies for relief under the provisions of Chapter I of Part V of the Inheritance Tax Act 1984 and

(i) if business property is only partly eligible for relief the expression includes only the share which is eligible

(ii) if liabilities which are incumbrances on property fall to be deducted from its value before the relief is applied the expression nonetheless includes all the property and

(iii) in this Will any reference to the reduced value of My Business Property is a reference to its value for inheritance tax purposes as reduced by any such incumbrances and by the relief itself (and if the relief reduces its value for those purposes to nothing is to be read as referring to a nil value)

PART 2 (continued)

2.2.5 'My Nil Rate Band Sum' means the greatest sum of cash that I can give to my Trustees without creating an immediate liability to pay inheritance tax

2.2.6 The 'Trust Period' means the period starting with my death and ending on the last day of the period of 125 years from the date of my death (which is the applicable perpetuity period) or such earlier date as my Trustees shall at any time specify by deed not being a date earlier than the date of execution of such deed or later than a date previously specified

2.3 I give the Discretionary Trust Fund to my Trustees upon trust to invest it in exercise of the powers of investment given them in this Will and to hold the Discretionary Trust Fund upon the trusts and with and subject to the powers and provisions set out in sub clauses 2.4 and 2.5 provided that the Discretionary Trust Fund shall bear its own share of any inheritance tax which may be payable on or by reason of my death.

2.4

2.4.1 My Trustees shall hold the Discretionary Trust Fund and the income thereof for the benefit of any one or more of the Beneficiaries upon such trusts (including discretionary and protective trusts) in such shares and with and subject to such trusts powers and provisions (exercisable by any person) as my Trustees shall at any time or times appoint by deed or deeds revocable executed during the Trust Period or irrevocable

2.4.2 My Trustees shall have the power during the Trust Period to pay transfer or apply the whole of any part or parts of the capital of the Discretionary Trust Fund as they in their absolute discretion think fit to or for the benefit of any Beneficiary

2.4.3 Subject thereto:

(i) My Trustees may accumulate the whole or part of the income of the Discretionary Trust Fund during the Trust Period

(ii) Subject thereto my Trustees shall pay or apply the income to or for the benefit of such of the Beneficiaries as my Trustees think fit

(iii) Subject to all the trust powers and provisions of this clause and if and so far as (for any reason) not wholly disposed of by it the Discretionary Trust Fund shall be held in trust for my children and if more than one in equal shares

2.5 The powers in sub clauses 2.4.1 and 2.4.2 shall only be exercisable when there are at least two Trustees or a trust corporation

PART 3

3 Absolute gift of residue of estate to spouse/registered civil partner

I give all the residue of my estate (out of which shall be paid my funeral and testamentary expenses and my debts) and any property over which I have at my death any general power of appointment to [my Husband/Wife/Registered Civil Partner]*

*Delete as appropriate.

PART 4

4

4.1 I declare for the avoidance of doubt that my Trustees may exercise the powers given by sub clauses 2.4.1 and 2.4.2 before the administration of my estate is complete and even before my Will has been proved and that no such exercise shall operate as an assent or prejudice or affect the rights and obligations of my personal representatives

4.2 This Will incorporates the Standard Provisions of the Society of Trust and Estate Practitioners (1st Edition) with the deletion of paragraph 5 and where there is conflict between those provisions and this Will prevails and in addition to those powers and the powers given to them by law, my Trustees shall have power to retain or effect any life insurance policy on the life of any person or persons, accept assignments of a policy to the Discretionary Trust Fund and exercise, assign or surrender the whole or any part of such policy

4.3 In this Will

4.3.1 references to any statutory provision shall include any statutory modification or re-enactment of such provision

4.3.2 words importing the singular shall include the plural and vice versa and words importing a gender include every gender

4.3.3 'spouse' shall include a civil partner registered under the Civil Partnership Act 2004 and 'husband' 'wife' 'widow' and 'widower' shall be construed accordingly

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