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Disabled Persons Trust

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Disabled Persons Trust

A disabled persons trust clause can be put into an individual's Will to provide for a Primary Beneficiary who is disabled.

It would be set up as a discretionary trust of the residuary estate that, during the Primary Beneficiary's lifetime, they satisfy the requirements to qualify for a disabled person's interest (DPI) and those for a trust for a vulnerable person where the Primary Beneficiary is a disabled person at the date of the testator's death.

Why might I want to set up a Disabled Persons Trust?

If you have a potential beneficiary who has learning difficulties (and qualifies under the requirements), you should consider how you can protect and safeguard their financial needs will be looked after in the event of your death, whilst ensuring that any means tested benefits are preserved and continue.

By setting up a Disabled Person's Trust now, you can ensure that your child or family member's future needs are protected in a tax-efficient way. It's imperative that you make sure your Will is also up to date as this often links to the trust by ensuring some of your estate can be allocated to the trust when you die.

In order to set the trust up, this can be done via your Will or in your lifetime. However, it is important to ensure that the potential beneficiary meets the following criteria:

- During the disabled person's lifetime there is no interest in possession (IIP) in the trust property.
- Any capital applied during the disabled person's lifetime is applied for their benefit.
- Any income applied during the disabled person's lifetime is applied for their benefit.

When the disabled beneficiary passes away, the trust can then benefit their spouse, child or additional beneficiaries.

Do you qualify as a disabled person?

A person in disabled for tax purposes if one of more of the following apply:

- They are incapable of administering their property or managing their affairs because of mental disorder within the meaning of the Mental Health Act 1983

- They are receiving any of:
  - attendance allowance;
  - disability living allowance (DLA) based on entitlement to the care component at the highest or middle rate or the mobility component at the higher rate;
  - disability assistance for children and young people by virtue of entitlement to the care component at the highest or middle rate or the mobility component at the higher rate;

- disability assistance for working age people by virtue of entitlement to the daily living component at the standard or enhanced rate or the mobility component;
- personal independence payment (PIP);
- an increased disablement pension (for a person with an industrial injury who needs constant attendance);
- constant attendance allowance (for a person receiving industrial injuries disablement benefit or a war disablement pension); or
- armed forces independence payment.

- They would be entitled to receive:
    - attendance allowance, DLA as above, PIP, increased disablement pension or constant attendance allowance but for failing to satisfy prescribed conditions as to residence or presence in the UK;
    - attendance allowance, DLA as above, PIP or increased disablement pension but for being resident in a care home with public funding of specified services, in hospital, in prison or detained in legal custody;
    - attendance allowance or increased disablement pension but for receiving treatment for renal failure in hospital;
    - constant attendance allowance but for being maintained in a hospital or other institution; or
    - armed forces independence payment but for admission to the Royal Hospital, Chelsea.

(Section 89(4A), Inheritance Tax Act 1984 (IHTA 1984) and section 38 and Schedule 1A, Finance Act 2005 (FA 2005).)

What are the benefits?

The benefits of these trusts for clients is mostly from the availability of a favourable tax treatment, which are set out below:

IHT

- The residence nil rate band is still available on the death of the testator.
- During the beneficiaries lifetime, its outside the remit of the relevant property regime, therefore circumvents the ten year anniversary charges and exit charges usual discretionary trusts are penalised with.
- When the beneficiary passes away, there is a chargeable transfer for IHT and the assets in the trust (estate) are aggregated with their other assets so they are potentially subject to IHT. This is because the interest is deemed as a qualifying interest in possession. Therefore, its important to consider that elderly, vulnerable clients may not benefit from the trust.

Capital Gains Tax

- During the lifetime of the beneficiary the full CGT annual exempt amount £3,000 is available to the trustees, rather than only half (like other trusts of this nature).
- A vulnerable person's election can be made so that tax on capital gains in the trust is no more than it would be had the gains arisen directly to the beneficiary. This would work if the beneficiary was a basic tax payer, as this is lower than the trustees usual highest rate.
- There is an uplift in the value of assets in the trust at date of death.

Income Tax

- During the lifetime of the beneficiary, the Trustees can again make an VPE for income tax so that the trust income is taxed at the beneficiaries rates (i.e. a child could pay basic rate) as their marginal rate.
- The usual rules will apply if they do not make the election.

A Summary of the Taxation of DPT's

Assets under the trust:

Event	IHT	CGT
Settlor creates trust or adds assets in lifetime (lifetime DT)	Settlor is disabled person: no transfer of value Other settlor: PET	Disposal
Settlor creates trust or adds assets by will	Chargeable transfer at death rate	Tax-free uplift
Settlor dies within seven years of lifetime creation or addition	Settlor is disabled person: value of assets included in estate Other settlor: PET becomes chargeable at death rate	No disposal

During the Trusts Existence in lifetime

Event	IHT	CGT
Disabled person's interest ends in lifetime: assets do not leave the trust	Chargeable transfer at lifetime rate and assets become relevant property, unless followed by: • A new disabled person's interest. Then a PET and assets do not become relevant property • (If the disabled person's interest was created by will) a trust for bereaved minors or an 18 to 25 trust. Then a chargeable transfer at lifetime rate but assets do not become relevant property	No disposal
Disabled person dies within 7 years of IIP ending in lifetime	Chargeable transfer at death rate	Tax-free uplift
Disabled person's interest ends on death of disabled person: assets do not leave the trust	Chargeable transfer at death rate Assets become relevant property unless qualifying for other status at that time	Disabled person with an IIP: tax-free uplift. Disabled person with no IIP (death on or after 5 April 2013): tax-free uplift.

Assets Leave The Trust

Event	IHT	CGT
Disabled person becomes absolutely entitled to assets (appointed out of the trust)	No transfer of value	Deemed Disposal
Other beneficiary becomes absolutely entitled to assets	During lifetime of disabled person: PET On death of disabled person: chargeable transfer at death rate	During lifetime of disabled person: deemed disposal On death of disabled person with an IIP: tax-free uplift On death of disabled person with no IIP (death before 5 December 2013): deemed disposal On death of disabled person with no IIP (death on or after 5 December 2013): tax-free uplift
Trustees transfer assets to another trust	To a disabled person's interest: PET To other trusts: chargeable transfer at lifetime rate	Disabled person's interest: deemed disposal Other trust: deemed disposal with hold-over relief
Settlor dies within seven years of lifetime creation or addition	Transfer	No disposal