

Trusts for Vulnerable Beneficiaries – part 1 (Lecture P1327 – 9.02 minutes)

Who is a 'vulnerable beneficiary'?

For income tax and CGT purposes, a vulnerable beneficiary is either:

- someone under 18 whose parent has died, or
- a disabled person eligible for any of the following benefits (even if not received):
 - Attendance Allowance (either the care component at the middle or highest rate, or the mobility component at the highest rate);
 - Personal Independence Payment;
 - an increased disablement pension;
 - Constant Attendance Allowance;
 - Armed Forces Independence Payment
- someone who is unable to manage their own affairs because of a mental health condition covered by the Mental Health Act 1983.

Tax issues

Special rules apply for income tax and CGT, where a trust has a vulnerable beneficiary. If there are beneficiaries who are not vulnerable, the assets and income for the vulnerable beneficiary must be:

- identified and kept separate, and
- used only for that person.

Only this part of the trust gets special tax treatment.

To claim special treatment for income tax and CGT, the trustees must complete the 'Vulnerable Person Election' form [VPE1], which the trustees and beneficiary must both sign. If there is more than one vulnerable beneficiary, each needs a separate form.

Income tax

The trustees are entitled to a reduction in income tax, calculated as follows:

- Work out what the trust income tax would be if there were no claim for special treatment; this will, of course, depend on the type of trust.
- Then work out what income tax the vulnerable person would have paid if the trust income had been paid directly to them as an individual.
- The trustees can then claim the difference between these two figures as a deduction from their own income tax liability.

Example

A discretionary trust is set up for a qualifying disabled person. During 2022/23 it receives £20,000 of gilt interest and £10,000 of dividends. There are no trust expenses.

The beneficiary has no income of their own.

Calculate the initial tax due by the trustees and the revised figure if a vulnerable beneficiary claim is made.

1. Tax due by trustees before claim

Interest	
£1,000 [standard rate band] @ 20%	200
£19,000 @ 45% =	8,550
Dividends	
£10,000 @ 39.35% =	<u>3,935</u>
	<u>£12,685</u>

2. Revised figure

If the beneficiary owned the investments directly, against the interest they would be able to use:

- PA of £12,570
- PSA of £1,000
- Starting rate band of £5,000

So, the tax calculation would be:

Interest	
£1,430 @ 20% =	286
Dividends	
£2,000 @ nil	-
£8,000 @ 8.75%	<u>700</u>
	<u>£986</u>

The trustees can therefore claim to reduce the income tax payable from £12,685 to £986, by making a claim for a reduction of £11,699.

Contributed by Kevin Read