



PENNINGTONS
MANCHES
COOPER



THE COURT OF PROTECTION AND DEPUTYSHIPS

NOTE ON PI TRUSTS

WHY SHOULD I SET UP A PERSONAL INJURY TRUST?

If you receive any means tested benefits and hold more than £16,000, your entitlement to these benefits would be stopped until you have less than this amount. If you hold anything between £6,000 and £16,000, your benefits entitlement would be reduced on a sliding scale. You can hold up to £6,000 in your own name before your entitlement to means tested benefits is affected.

Exemptions apply relating to personal injury awards. For the first 52 weeks from the date you first received any compensation in respect for your injuries you can continue to claim means tested benefits. This is known as the "52 week disregard period". After this period has passed, your means tested benefits will be affected by your award.

However, if you place your funds into a personal injury trust now, your entitlement to means tested benefits will continue after the 52 week disregard period has passed and the money held in the trust is ring-fenced.

Even if you don't receive means tested benefits now, setting up a trust now could preserve your future entitlement should your circumstances change and you need to rely on benefit income. Although you can set up a trust at any point in the future, you would need to be able to show that your personal injury award has not been mixed with other funds.

There can be other more long-term reasons why you may want to transfer an award for personal injury damages to a trust. The decision to use a trust might be prompted by concerns about:

- funding care home fees in later life;
- protecting assets from divorce or bankruptcy in the future;
- claiming means-tested benefits in the future as a result of bad health; or
- managing large amounts of money.

WHAT TYPE OF PERSONAL INJURY TRUST SHOULD I CHOOSE?

There are four main types of trust:

- **bare trust;**
- **life interest trust;**
- **discretionary trust; and**
- **disabled person's interest trust.**

Most people choose the simplest, most transparent form of trust: a bare trust. Using a bare trust is usually the default position unless there are good reasons why another type of trust is more suitable. For example, an injured person could know that, if they had the type of control available with a bare trust, they would use that to their detriment and they therefore wish the trustees to have greater control over the funds.

The tax treatment of each type of trust will often be a factor in deciding which to choose as well as the complexity of administering the trust.

It is possible to set up more than one trust, i.e. to have some funds in a bare trust and some in a discretionary trust, but you would need to think carefully about the costs and ongoing administration involved in doing so.

A BARE TRUST

A bare trust is the simplest form of trust that can be used. For tax purposes this type of trust is transparent. Any income or gains generated within the trust are treated as belonging to you, the beneficiary, and the assets in the trust form part of your estate for inheritance tax purposes on death.

This type of trust is easy to understand and administer and allows you to retain ultimate control over the assets (see more detailed information below about bare trusts).

A LIFE INTEREST TRUST

A life interest trust (also known as an interest in possession trust) splits entitlement to capital from entitlement to income. You would be entitled to receive all the income generated from the damages award during your lifetime. After your death, the damages award itself (the trust capital) would then pass to another beneficiary. Life interest trusts are treated, for inheritance tax purposes, as relevant property trusts with entry (20%), exit and ten-year anniversary (up to 6%) charges to tax to the extent that the assets in the trust exceed the Nil Rate Band allowance.

A life interest trust would need to be registered with HMRC and would have its own separate tax status.

A DISCRETIONARY TRUST

A discretionary trust gives trustees wide discretion to distribute or retain trust income and capital for the benefit of beneficiaries. Typically, a wide class of potential beneficiaries will be selected by you and the trustees will decide which beneficiaries should benefit and to what extent.

Discretionary trusts can offer protection for vulnerable injured persons because they have less control over the funds once the trust has been set up. Discretionary trusts are relevant property trusts for inheritance tax with entry, exit and ten-year anniversary charges to tax to the extent that assets in the trust exceed the Nil Rate Band allowance.

A discretionary trust would need to be registered with HMRC and would have its own separate tax status.

A DISABLED PERSON'S INTEREST TRUST

A disabled person's interest is defined in section 89 of the Inheritance Tax Act 1984 (IHTA 1984). The availability of this as an option therefore relies on you falling within the definition of a disabled person for tax purposes; generally this means that you need to be receiving disability living allowance at the middle or higher rate for care or at the higher rate for mobility or PIP.

HOW SHOULD I CHOOSE TRUSTEES?

The optimal number of trustees for a personal injury trust is two to four. You can select professional trustees, who are paid to take on the role, or lay trustees, who are often family members or trusted friends. It is possible for you to be one of the trustees yourself, but if so we advise you to appoint two other trustees. This is to prevent a situation where, if something happens to the other trustee, you are left as the sole trustee, which holds risks. Sole individual trustees cannot give good receipt when selling land that forms part of the trust fund. If you are the sole trustee:

- the trust could be attacked as a sham, for the purposes of disregarded capital for means-tested benefits; or
- in the case of a bare trust, a trust would not exist at all.

The size of the fund is often an important factor in deciding whether to employ professional trustees. Whilst a relatively small award of damages would not normally support the fees charged by a professional trustee, there may be more justification with a larger award. One option would be to have a professional trustee for an initial period and then, once the lay trustees are confident that they know the procedures involved in administering the trust, for the professional to retire and hand over to lay trustees.

If a discretionary, life interest or disabled person's interest trust is selected, a professional trustee may be useful to provide advice on tax and trust issues. Even if a professional trustee is going to be appointed, it is often useful to also appoint family members or trusted friends who are often more familiar with the injured person's needs.

Please do let us know if you would like to discuss the option of a professional trustee and we can provide an indication of the likely costs involved. Our charges would be based on a time spent basis at fixed hourly rates (which we can provide details of on request).

HOW DOES A BARE TRUST WORK?

SETTLOR:

As it is your money, you will need to settle the money into the trust and will be known as the settlor. This means you sign a document to confirm it is your money from a personal injury award and you are putting it in trust.

TRUSTEES:

You will then choose your trustees who manage the money. It is important you choose people you trust to act as trustees as they will be responsible for managing the money placed in trust. They have a duty to act in your best interests. You can change your trustees at any point and the trust can be dissolved if you choose.

It will be necessary for you to pick at least two trustees to manage the trust fund (see above re considerations when choosing trustees). We would need the names and addresses and dates of birth for your trustees.

BENEFICIARY:

You will be beneficiary of the trust, which means the money is held in trust for your benefit.

MECHANISM FOR REQUESTING FUNDS:

If you want money from the trust you will need to consult with your trustees and ask them to release the money. They can pay funds directly to you or make payments directly to third parties. For example, if you want to buy a car, you can tell your trustees what car you want to buy, arrange the order and then ask the trustees to pay the garage directly for the car. This means the car is purchased using trust money and if you sold it at a later stage you can put the sale proceeds back into the trust. We would advise that if you want to purchase something worth more than £6,000 your trustees pay the item directly from the trust account as this will avoid your personal account exceeding the £6,000 limit.

If there are circumstances where you need to purchase something that is worth more than £6,000, but the trustees cannot pay for it directly or you do not want them to, then you can ask them to pay the money into your personal account, but pay it out immediately. There should be a clear link from the money to the trust so you can evidence you are just using your account to facilitate the purchase. We advise that you ask your trustees to put the exact amount required for the purchase in your account for clarity. For example, if the purchase is for £6,499, we would advise your trustees to transfer this exact amount to your account to be paid straight to the third party.



If possible, you should purchase items in the name of the trust. For example, if you purchase your property, you should consider placing the property in the name of the trust rather than your name. This means if it is ever sold during your lifetime, the sale proceeds can be paid back into the trust and remain ring-fenced for means tested benefits purposes.

You are advised not to take a regular income from the trust as this can be deemed as capital by the benefits agency and could affect your entitlement to means tested benefits. For example, a regular monthly payment of £1,000 could affect your benefits entitlement. If you need money from the trust, we advise you request it as and when required. You can keep a balance in your personal account to cover expenditure as long as it does not exceed £6,000.

All trustees would need to authorise the release of funds. You will not have a cash card to the trust account because you cannot access money without their approval. It is important the bank account is set up properly to comply with the trust rules and to ensure your benefits are not affected.

You cannot put non-personal injury money into the trust. You should keep your award in a separate bank account to your personal money until the trust deed is signed and the trust bank account has been opened to avoid any confusion. If the award is mixed with personal money, this could make it hard to determine what should and should not be ringfenced. The benefits agencies will only disregard your award when assessing your benefits entitlement.

TAX

The tax implications of a bare trust are as follows:

- **Inheritance tax** – There is no inheritance tax liability arising on the creation of the trust. The trust funds will fall into your estate on death and will be subject to inheritance tax if they exceed the relevant thresholds in the same way as assets in your own name.

- **Capital gains tax** – There are no capital gains tax implications arising on the creation of the trust. There may be capital gains tax to be paid on any gains realised by the trust fund. They will be taxed by HMRC as personal gains arising to you directly.
- **Income tax** – Any income arising in respect of the trust fund is taxed by HMRC as income arising to you directly. This means that income arising in the trust should be included on your own, personal annual income tax return form.

You should contact HMRC regarding this to see what they require from you regarding your tax return. You will need to do this whether the personal injury award is held in a trust or not.

WILL

The trust fund forms part of your estate in the event of your death. Therefore, it will pass in accordance with any will you have prepared or, in the absence of any will, in accordance with the intestacy provisions. We would advise you to consider making a will or reviewing your existing will.

BANK ACCOUNT

Once the trust deed has been signed, you would need to open a trust bank account. You and your trustees should be able to do this by producing the trust deed along with identification. You should check with your local banks to see if they offer this service. We are unable to open a bank account for the trust unless a professional trustee is appointed.

The account should be opened in the name of the trust with your trustees as signatories. As advised, if you wish to withdraw money from your trust you will need to ask your trustees to authorise and action the withdrawal.



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