HOW ADVISER CHARGING WORKS WITH INVESTMENT BONDS AND TRUSTS

Understanding how adviser charges interact with our International Portfolio Bond in combination with different trusts allows you to make informed decisions that are right for your clients.

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Where a trust is involved, it is important to make sure that adviser charges are paid by whoever receives the advice: the settlor or the trustees. This is particularly the case where charges are being facilitated by Canada Life International Assurance (Ireland) DAC (CLIA(I)).

If a charge that should be paid by the settlor were instead met from the trust, this would create a gift with reservation, which would wipe out the benefits of the trust for inheritance tax purposes. Conversely, if a charge that should be met from the trust were paid by the settlor, it would be treated as a further transfer of value to the trust, which could have additional tax consequences.

Below, we look at the payment process and options for each of the main trusts that CLIA(I) offers. For simplicity, we have used the word ‘settlor’ throughout, but the same process would apply to a donor with an absolute trust.

**NEW GIFT TRUSTS — GIFT OF CASH**

The settlor establishes the trust with a gift of cash, with the intention that the trustees use it to invest in an International Portfolio Bond.

We assume here that the settlor has received advice on the bond and the trust at the same time and has directed the trustees to apply for a bond. This will usually be the case – the advice will cover both the creation of the trust and the investment options. Our trust deeds allow for this – the establishment of the trust and the investment in the bond are integral.

**INITIAL ADVISER CHARGE (IAC)**

As the IAC is for the advice given to the settlor, it must be paid by the settlor and not from the trust. If the trustees were to pay the IAC from the trust fund, the whole gift would become a gift with reservation.

There are two options:

- The settlor can pay the IAC directly to the adviser’s firm, for example by cheque.
- The IAC can be deducted from the amount paid to CLIA(I) before investment into the bond. That is, CLIA(I) will deduct the IAC and pay it to the adviser’s firm, before investing the balance into the bond. We refer to this method as ‘Premium Plus’. The IAC must not be included in the trust deed.

**ONGOING ADVISER CHARGE (OAC)**

The OAC is for ongoing service from the adviser to the trustees, so the trustees must pay it, from the bond. Either the trust deed or the Trustee Act will allow this – CLIA(I)’s trust deeds specifically allow for adviser charging.

As the settlor has established the trust with a gift of cash, it is the trustees who apply for the bond and they can specify the OAC at outset.

Points to note are:

- The settlor should not pay the OACs from his own funds, as this would constitute further gifts into the trust.
- The trustees should pay the OACs directly to the adviser’s firm.
- All withdrawals from the bond to pay OACs must be included in the chargeable event gains calculations and will count towards the 5% annual tax-deferred withdrawal limit.
The settlor starts with £100,000. The adviser’s charges are £3,000 for the IHT planning and £2,000 for advice on the bond.

**FACILITATED INITIAL ADVISER CHARGE**

1. Settlor receives advice on IHT and bond; total charge is £5,000
2. Settlor signs Gift Trust deed for £95,000
3. Trustees give CLIA(I) £100,000 with application
4. CLIA(I) pays adviser’s firm £5,000 on behalf of trustee
5. CLIA(I) invests £95,000 in the bond
6. Adviser requires annual charges for ongoing advice to trustees; trustees have given authority for this in application form
7. CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

**NON-FACILITATED INITIAL ADVISER CHARGE**

1. Settlor gives adviser’s firm cheque for £5,000
2. The gift for IHT purposes is £95,000
3. Settlor signs Gift Trust deed for £95,000
4. Trustees give CLIA(I) £95,000 with application
5. CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

The same amount is in the bond (and trust), regardless of how the IAC is paid.

These payments are withdrawals that count towards the 5% tax-deferred allowance.
NEW GIFT TRUSTS – ASSIGNING AN EXISTING BOND

The settlor invests in an International Portfolio Bond and subsequently puts it into trust. The settlor may get advice on both the investment and the creation of the trust at the same time, or the advice for the trust may come later.

INITIAL ADVISER CHARGE (IAC)

As the IAC is for the advice given to the settlor to set up a bond, the settlor must pay it.

There are three options:

- The settlor can pay the IAC directly to the adviser’s firm, for example by cheque.
- The IAC can be deducted from the amount paid to CLIA(I) before investment into the bond. That is, CLIA(I) will deduct the IAC and pay it to the adviser’s firm, before investing the balance into the bond. We refer to this method as ‘Premium Plus’. The IAC must not be included in the trust deed.
- The IAC can be deducted from the bond once it has been set up. That is, CLIA(I) will deduct the IAC from the bond and pay it to the adviser’s firm. In this case, the IAC will count towards the 5% annual tax-deferred withdrawal limit.

ONGOING ADVISER CHARGE (OAC)

If an OAC arises before the bond is put into trust, it will be for ongoing service from the adviser to the (prospective) settlor. Therefore, the settlor must pay it, either from the bond or from his own resources.

Once the bond has been assigned to the trust, CLIA(I) will need to get explicit permission from the trustees, as the bond’s new owners, to continue to pay any previously agreed OAC to the adviser’s firm. This can be done using the Change to Ongoing Facilitated Adviser Charges form (W13678).

If there is no new instruction from the trustees, any OAC previously specified by the settlor will be switched off. In practice, however, if form W13678 is submitted to CLIA(I) at the same time that the bond is assigned, and the OAC is for the same amount, it will not need to be cancelled and reinstated.

Points to note are:

- The OACs paid by the trustees should be paid directly to the adviser’s firm.
- All withdrawals deducted from the bond to pay OACs must be included in the chargeable event gains calculations and will count towards the 5% annual tax-deferred withdrawal limit.
- Once the bond has been placed in trust, the settlor should not pay the OAC from his own funds, as this would constitute a further gift into the trust.
The settlor starts with £100,000. The adviser’s charges are £3,000 for the IHT planning and £2,000 for advice on the bond.

**FACILITATED INITIAL ADVISER CHARGE**

- Settlor gives CLIA(I) £100,000
- CLIA(I) pays adviser’s firm £5,000 on behalf of settlor
- Settlor receives advice on bond and (subsequently) IHT; total charge is £5,000
- CLIA(I) invests £95,000 in the bond
- Settlor signs Gift Trust deed and completes the schedule in the trust assigning the bond
- Settlor assigns the bond to the trustees
- Adviser requires annual charges for ongoing advice to trustees
- Trustees give permission for OAC using form W13678
- CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

**NON-FACILITATED INITIAL ADVISER CHARGE**

- Settlor gives adviser’s firm cheque for £5,000
- Settlor gives CLIA(I) £95,000
- The same amount is in the bond, regardless of how the IAC is paid
- The gift for IHT purposes is the value of the bond at the date of assignment
- These payments are withdrawals that count towards the 5% tax-deferred allowance
EXISTING GIFT TRUSTS

INITIAL ADVISER CHARGE (IAC)
In this case, there is an existing trust now holding cash and it is the trustees who are given the advice to buy the International Portfolio Bond. So the trustees must pay the IAC from the trust fund.

There are three options:

• The IAC can be paid from the cash held in the trust directly to the adviser’s firm.

• The IAC can be deducted from the amount paid to CLIA(I) before investment into the bond – the Premium Plus basis.

• The IAC can be deducted from the bond after it has been purchased. In this case, the IAC will count towards the 5% annual tax-deferred withdrawal limit.

The settlor should not pay the trustees’ IAC, as this could be considered to be a further gift into the trust.

ONGOING ADVISER CHARGE (OAC)
Once they have applied for the bond, the trustees will receive the ongoing service from the adviser. Hence the trustees must pay the OACs from the bond. Either the trust deed or the Trustee Act will allow this – CLIA(I)’s trust deeds specifically allow for adviser charging.

Points to note are:

• The settlor should not pay the OAC from his own funds, as this would constitute a further gift into the trust.

• The trustees should pay the OACs directly to the adviser’s firm.

• All withdrawals from the bond to pay OACs must be included in the chargeable event gains calculations and will count towards the 5% annual tax-deferred withdrawal limit.
The settlor started with £100,000 and paid an IAC of £3,000 for the IHT planning. The trustees now hold cash of £97,000 and pay the adviser £2,000 for advice on the bond.

**FACILITATED INITIAL ADVISER CHARGE**

- Trustees give CLIA(I) £97,000
- CLIA(I) pays adviser’s firm £2,000 on behalf of trustees
- CLIA(I) invests £95,000 in the bond
- Adviser requires annual charges for ongoing advice to trustees; trustees have given authority for this in application form
- CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

**NON-FACILITATED INITIAL ADVISER CHARGE**

- Trustees pay £2,000 to adviser’s firm from the cash held
- Trustees give CLIA(I) £95,000
- The same amount is in the bond (and trust), regardless of how the IAC is paid
- These payments are withdrawals that count towards the 5% tax-deferred allowance
EXISTING GIFT TRUSTS – TOP-UPS

INITIAL ADVISER CHARGE (IAC)
The settlor gets advice to top up an existing Gift Trust with a further cash gift to the trustees, which constitutes a further gift into the trust. The settlor should pay any IAC relating to this advice, either separately by cheque or on the Premium Plus basis.

In most cases, the advice to invest the cash as a top-up to the existing bond will be given to the settlor, but occasionally it may relate to both the settlor and the trustees. In this case, the IAC should be paid by whoever receives the advice.

If the settlor receives the advice:
• payment can be directly to the adviser’s firm, separately from the gift, or
• it has to be clear that the IAC must be deducted from the amount paid to CLIA(I) before the bond is topped up – the Premium Plus basis.

In the second case, the gift is the net amount invested in the bond.

If the trustees also receive advice:
• the IAC in relation to the trust can be deducted from the amount paid to CLIA(I) before the bond is topped up, with the net amount invested in the bond – on the Premium Plus basis, or
• the IAC in relation to the trust can be deducted from the bond after it has been topped up, via facilitated initial adviser charges. This will count towards the 5% annual tax-deferred withdrawal limit.

ONGOING ADVISER CHARGE (OAC)
Once they have applied for the bond top-up, the trustees will receive the ongoing service from the adviser. The trustees must therefore pay the OACs from the bond to the adviser’s firm. Either the trust deed or the Trustee Act will allow this – CLIA(I)’s trust deeds specifically allow for adviser charging.

Points to note are:
• The settlor should not pay the OAC from his own funds, as this would constitute a further gift into the trust.
• The trustees should pay the OACs directly to the adviser’s firm.
• All withdrawals from the bond to pay OACs must be included in the chargeable event gains calculations and will count towards the 5% annual tax-deferred withdrawal limit.
The settlor starts with £100,000. The adviser’s charges are £3,000 for the IHT planning for the settlor and, separately, £2,000 for advice on the bond for the trustees.

**EXAMPLE**

The gift for IHT purposes is £97,000

This withdrawal counts towards the 5% tax-deferred allowance

FACILITATED INITIAL ADVISER CHARGE

- Settlor receives advice on IHT; charge is £3,000
- Settlor gives trustees £100,000, specifying that £97,000 is the further gift into trust
- Trustees receive advice on bond; charge is £2,000
- Trustees request withdrawal of £2,000 to be paid to adviser’s firm
- Adviser requires annual charges for ongoing advice to trustees; trustees have given authority for this in application form
- CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

NON-FACILITATED INITIAL ADVISER CHARGE

- Settlor gives adviser’s firm cheque for £3,000
- Settlor specifies that £97,000 is the further gift into trust
- Trustees receive advice on bond; charge is £2,000
- Trustees give CLIA(I) £100,000 with top-up application
- Trustees give CLIA(I) £95,000 with top-up application
- CLIA(I) pays adviser’s firm £2,000 on behalf of trustees
- CLIA(I) invests £95,000 in the bond
- CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees
- These payments are withdrawals that count towards the 5% tax-deferred allowance
LOAN TRUSTS

CLIA(I)’s Loan Trust can only be set up using a loan of cash. An existing bond cannot be placed into a Loan Trust.

The settlor receives the advice to set up a Loan Trust and to make a loan to the trustees. The trustees are directed to use the cash loan to invest in an International Portfolio Bond.

INITIAL ADVISER CHARGE (IAC)

As the IAC is for the advice given to the settlor, the settlor must pay it.

There are two options:

• The settlor can pay the IAC separately from the loan, for example by cheque.

• The IAC can be deducted from the amount paid to CLIA(I) before investment into the bond. That is, CLIA(I) will deduct the IAC and pay it to the adviser’s firm, before investing the balance into the bond. We refer to this method as ‘Premium Plus’.

In both cases, the loan amount stated in the trust deed and invested in the bond should exclude the IAC.

ONGOING ADVISER CHARGE (OAC)

The trustees (as legal owners of the bond) must sign an agreement to allow CLIA(I) to pay OACs to the adviser’s firm. As these are paid directly to the adviser’s firm, and not routed through the settlor, they will not be considered as a part repayment of the loan.

Points to note are:

• The settlor should not pay the OACs from his own funds, as this would constitute a gift into the trust.

• The trustees should pay the OACs directly to the adviser’s firm.

• All withdrawals from the bond to pay OACs must be included in the chargeable event gains calculations and will count towards the 5% annual tax-deferred withdrawal limit.
The settlor starts with £100,000. The adviser’s charges are £3,000 for the IHT planning and £2,000 for advice on the bond.

**FACILITATED INITIAL ADVISER CHARGE**

- Settlor receives advice on IHT and bond; charge is £5,000
- Settlor signs Loan Trust deed for £95,000
- Trustees give CLIA(I) £100,000 with application
- CLIA(I) pays adviser’s firm £5,000 on behalf of settlor
- CLIA(I) invests £95,000 in the bond
- Adviser requires annual charges for ongoing advice to trustees; trustees have given authority for this in application form
- CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

**NON-FACILITATED INITIAL ADVISER CHARGE**

- Settlor gives adviser’s firm cheque for £5,000
- The gift for IHT purposes is £95,000
- Settlor signs Loan Trust deed for £95,000
- Trustees give CLIA(I) £95,000 with application
- The same amount is in the bond (and trust), regardless of how the IAC is paid
- These payments are withdrawals that count towards the 5% tax-deferred allowance
DISCOUNTED GIFT TRUSTS

The settlor receives advice to set up a Discounted Gift Trust and establishes the trust with a gift of cash. The trustees are directed to use the cash to invest in an International Portfolio Bond.

INITIAL ADVISER CHARGE (IAC)

As the IAC is for the advice given to the settlor, it must be paid by the settlor and not from the trust. If the trustees were to pay the IAC from the trust fund, the whole gift would become a gift with reservation.

There are two options:

- The settlor can pay the IAC directly to the adviser’s firm, for example by cheque.
- The IAC can be deducted from the amount paid to CLIA(I) before investment into the bond. That is, CLIA(I) will deduct the IAC and pay it to the adviser’s firm, before investing the balance into the bond. We refer to this method as ‘Premium Plus’. The IAC must not be included in the trust deed.

ONGOING ADVISER CHARGE (OAC)

One question that may arise is: ‘Does the payment of an OAC from the bond to the adviser affect the discounted value of the investment in any way?’

The OAC payments are made on behalf of the trustees and the settlor does not benefit from them. As a result, the OACs will not have any impact on the discounted value of the investment.

The trustees may instruct CLIA(I) to pay OACs directly to the adviser’s firm, but must not route these payments via the settlor. This would be a breach of trust and could amount to a gift with reservation.

OACs will always have a greater impact on Discounted Gift Schemes than other trusts, as the retained rights of the settlor (the regular fixed payments) are carved out in the trust, so there will always be regular withdrawals while a settlor remains alive. A combination of regular withdrawals and OACs that exceed the growth of the bond will deplete the bond value. This could shorten the life of the trust, reduce its ability to support the retained rights payments and, potentially, eliminate any residual value for the beneficiaries. It could also give rise to future chargeable events.

OACs AND THE TAX-DEFERRED WITHDRAWAL LIMIT

It is important to remember that the OACs count towards the 5% annual tax-deferred withdrawal limit. Any OAC to be paid should be taken into account before deciding the amount of the settlor’s regular payment stream, to avoid building in an automatic chargeable event every year.

If the OAC is expressed as a percentage of fund value, it is possible that it could cause a chargeable event in future, if the bond value is growing faster than the total withdrawals.

This is because the 5% withdrawal limit is based on the initial premium, not the fund value. For example, suppose the settlor has a payment stream of 4.5% of the original premium and the OAC is set at 0.5% of fund value. The total will exceed 5% of the original premium if the bond value is growing, after taking the withdrawals into account.

Conversely, if the bond value is falling, due to the combination of the settlor’s payments and the OACs, this could eventually affect its ability to support the retained rights payments and possibly eliminate any residual value for the beneficiaries, as mentioned above. It is worth bearing this in mind when deciding on the amount of the settlor’s payments.
The settlor starts with £100,000. The adviser’s charges are £3,000 for the IHT planning and £2,000 for advice on the bond.

**FACILITATED INITIAL ADVISER CHARGE**

1. Settlor receives advice on IHT and bond; charge is £5,000
2. Settlor signs Trust Deed for £95,000 and chooses level of regular fixed payments
3. Trustees give CLIA(I) £100,000 with application
4. CLIA(I) pays adviser’s firm £5,000 on behalf of settlor
5. CLIA(I) invests £95,000 in the bond
6. Discount is determined, based on regular fixed payments and the settlor’s age, health and other relevant factors
7. Adviser requires annual charges for ongoing advice to trustees; trustees have given authority for this in application form
8. CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees

**NON-FACILITATED INITIAL ADVISER CHARGE**

1. Settlor gives adviser’s firm cheque for £5,000
2. Settlor signs Trust Deed for £95,000 and chooses level of regular fixed payments
3. Trustees give CLIA(I) £95,000 with application
4. The same amount is in the bond (and trust), regardless of how the IAC is paid
5. CLIA(I) pays OACs to adviser’s firm from the bond on behalf of the trustees
6. These payments are withdrawals that count towards the 5% tax-deferred allowance – as do the regular fixed payments to the settlor
EXCLUDED PROPERTY TRUSTS

The settlor receives the advice to set up an Excluded Property Trust and to make a transfer of cash to the trustees, with the intention that the trustees invest in an International Portfolio Bond.

INITIAL ADVISER CHARGE (IAC)

As the settlor is a beneficiary of the trust, a payment made by the trustees in respect of advice given to the settlor could be considered as a permissible distribution.

Hence the settlor can pay the IAC independently or the trustees can pay it either before or after investment into the bond. However, if the trustees pay it, there may be tax consequences as a remittance to the settlor and if it is paid from the bond it could also give rise to a chargeable event.

ONGOING ADVISER CHARGE (OAC)

The OACs will be paid by the trustees and must be included in the chargeable event gains calculations.

Points to note are:

• The trustees would normally pay the OACs directly to the adviser’s firm. As the settlor is a beneficiary of the trust, any payments made by the trustees via the settlor could be considered to be a permissible distribution of the trust property. However, this could have tax consequences for the settlor.

• The settlor should not pay the OAC from their own funds, as this could have inheritance tax consequences for both the settlor and the trust.

GENERAL

PORTFOLIO HOLDINGS – DIRECT ADVISER CHARGES BILLED TO THE SETTLOR

Where the settlor is getting advice across a portfolio of investments, such as a bond, pension arrangements and a trust, care should be taken that the trust is not included in the overall portfolio value when setting and paying the OAC. If the settlor pays any OACs in respect of the service the trustees receive, these could be considered as further transfers of value into the trust.

Instead, the trustees should arrange for the OACs relating to the trust to be deducted from the International Portfolio Bond.

The settlor, the adviser and the trustees should take professional tax and legal advice when considering taking any Ongoing or Ad Hoc Adviser Charges from the settlor’s own assets or from the bond in respect of any trusts they have created.

IMPACT ON TAX-DEFERRED WITHDRAWAL LIMIT

If the Initial Adviser Charge is deducted from the amount prior to investment into the bond, this will have no impact on the tax-deferred allowance (other than reducing the amount of the premium). If the Initial Adviser Charge is deducted from the bond after it is set up, this will reduce the tax-deferred withdrawal allowance. Ongoing Adviser Charges deducted from the bond will always reduce the tax-deferred withdrawal allowance.

As discussed above, in combination with the retained rights of a Discounted Gift Trust, Ongoing Adviser Charges will make chargeable events more likely to occur and they will occur regularly if the combined total is greater than the 5% tax-deferred allowance.

Please note that the value of an investment in a bond can fall as well as rise and your clients could get back less than they invest. This document is based on our current understanding and interpretation of current legislation in the UK and Ireland and HMRC and Irish Revenue Commissioners practice, which may change at any time.
For further information about Canada Life International Assurance (Ireland) DAC, please visit www.canadalifeinternational.ie or call us on +44 (0) 1624 820200.