

When is a trust not a trust - Precatory Trusts (Feb 2010)

A precatory trust is not actually a trust at all but a gift to a beneficiary with a wish that the beneficiary will pass assets on to others in accordance with a letter of wishes left by the testator.

The reason that this does not create a binding trust is that there is a **lack of certainty**. By expressing a **'wish'** that the items be distributed there is **no binding obligation** on the beneficiary just an expectation that they will comply with the testator's wishes.

The precatory 'trust' is often used to allow flexibility in the distribution of personal chattels. By including the details of the distribution in a separate document the testator has the flexibility to change the distribution as often as he wishes. This also allows updating to reflect new family members or a change in property owned prior to the date of death.

A typical clause would leave all personal chattels to a single beneficiary expressing the wish that they should distribute them according to a letter of wishes. In most cases it is convenient to adopt the definition of 'personal chattels' in the Administration of Estates Act 1925 but it should be ensured that this is significantly wide enough or not too wide if the testator wishes to gift only jewellery for example.

Taxation implications of a precatory trust; for inheritance tax purposes the gift will be treated as an absolute gift to the beneficiary therefore if the gift was to the spouse it will be exempt for IHT purposes.

If no exemption is available then **tax becomes payable** on the testator's death. S143 of the Inheritance Tax Act 1984 states that, where a named beneficiary transfers property according to the testator's wishes within two years of their death, the gift will be treated as if it had passed under the Will to the transferee. This means that it will not be a 'transfer of value' and will not be a PET. This means that, if the beneficiary under the Will dies within seven years there will be no IHT liability.

There is no equivalent provision for Capital Gains Tax however there is only a liability if there is a gain on the disposal. As there is likely to only be a short time between the death of the testator and the distribution by the beneficiary it is unlikely that any taxable gain will arise.

It is, of course, essential that any **accompanying letter of wishes is kept up to date** and **stored with the Will** so that it can be easily identified and located on the testator's death.

The English Will company will help to advise you whether a Precatory "Trust" is suitable for your needs, however, in most cases there exists sufficient flexibility within the wording of a Trust to ensure that the assets pass to exactly who they should and in the proportion required without having to use a Precatory "Trust" which may cause a potential challenge to a Will if the validity of the final letter is in doubt or of the asset in question is very valuable.