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Private Client

Providing for Young Children by way of a Bare Trust

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In a time when the Capital Acquisition Tax (CAT) Group Thresholds are decreasing and it is anticipated that the rate of CAT will increase for the third time in two years, parents are seeking more tax efficient methods of distributing their wealth amongst their young children. Under the current tax regime, children may avail of the Group A Tax Free Threshold for gifts taken after 07th December 2012 and receive up to €250k from their parents without liability to CAT. Anything received over and above this amount is taxed at the current gift tax rate of 30%.

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An effective method of passing funds to children with decreased liability to CAT is by setting up a Bare Trust in their favour. As children under the age of 18 are legally incapable of holding property in their own right, funds can be vested in trustees appointed on their behalf by a Bare Trust Deed. A Bare Trust is similar in nature to a nominee account. Funds are added to the trust fund in the names of the trustees but are at all times treated as belonging to the children.

Under this bare trust scheme, each parent may utilise the annual small gift exemption and contribute €3,000 to the trust fund every year without the child beneficiary incurring CAT. Each child may therefore receive €6,000 tax free annually from their parents combined. If this is received every year until they reach the age of 18, the child will have received €108,000 without any liability to CAT. A further advantage is that these funds will not count towards the child's tax free threshold. It should be noted that this annual gift and the fiscal benefits thereof may continue indefinitely throughout the child's life. In the alternative, non cash assets such as shares up to the value of €6,000 could be added annually to the trust fund.

The option to contribute €3,000 tax free each year to the fund is not limited to parents. Grandparents, aunts & uncles, godparents and others may similarly contribute up to €3,000 annually. The net result is that the child, by the age of 18, may have amassed significant wealth without liability to CAT and without having affected his tax free thresholds.

It is important to note that the powers granted to Bare Trustees to deal with the trust funds are extremely limited under the Trustees Act 1893. The powers granted merely allow the Trustee to hold the property on behalf of the minor child and to ultimately vest it in him when the child reaches the age of 18. It is therefore wise to grant the Trustees additional powers under the terms of the Trust Deed. Such powers can include the power to invest the trust funds, to acquire property, to borrow, to mortgage, to accumulate income etc. The granting of additional powers enables the Trustees to deal with the funds more effectively and to hopefully increase their value over the years.

One thing to bear in mind is that under the terms of a Bare Trust, the children must be capable of calling on the Trustees to vest the property in them upon reaching the age of 18. From a parent's perspective, this may be far from ideal, as the child would have access to significant sums of money at a relatively immature age. This requirement to disclose can be dealt with using a number of practical solutions.

It should be noted that the creation of a Bare Trust is only one of a number of Trust mechanisms which may be set up with a view to striking a balance between tax efficiency and ensuring that children do not receive large sums of money at an immature age.

For further information in relation to Trusts, contact Mary McKeever of our Private Client Department.