

Supporting your children

Umesh Modi looks at the different ways parents can financially support their children and some of the obstacles to be wary of...



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If you are a parent, there are various ways in which you can provide financial assistance for your children, but it is always as well to be aware of the tax consequences of the method of help.

Income tax

The income of children is theirs in their own right, no matter how young they are. And they qualify for the standard personal allowance and the various tax bands and rates. Parents can make gifts to their children and so long as the income generated from such gifted capital in a year is less than £100 for each child from each parent, then the income is taxed as the child's and there are no further tax consequences. However if the income exceeds this limit, the whole amount and not just the excess over £100 will be taxed on the donor parent, where the child is under 18 and unmarried. There are certain investments where this "£100 rule" does not apply, and these are mentioned below. One can, of course, invest for capital growth, rather than immediate income - in some accumulation unit trusts, for example.

Inheritance tax (IHT)

In each tax year, each parent may give up to £250 to any number of people, plus further larger gifts

up to £3,000 in total. Regular gifts made out of income are not subject to IHT, and there are special allowances for gifts given in consideration of marriage. Most other gifts rank as potentially exempt, becoming fully exempt if the donor survives for seven years.

However, most trusts now come within the new mainstream IHT regime. This counts transfers into trusts as chargeable transfers attracting IHT at the lifetime rate of 20% and subject to a charge every subsequent ten years and on exit from the trust.

The only exceptions are qualifying interest in possession trusts, qualifying 18-25 trusts, qualifying trusts for bereaved minors and trusts for the disabled.

Children's Bank or Building Society Account

This is the very simplest way of providing money for your child. It is usual for these to be set up with the child's name linked with the name of the parent. This is the simplest example of a trust, known as a "bare trust," where the parent is the trustee and the child is the beneficial owner as regards interest and capital. The parent has control of the account until the child reaches an age specified by the bank etc, but is bound to apply the funds for the benefit of the child.

Cash ISAs

Junior ISAs, for those aged under 18 who do not have a Child Trust Fund account (see below), allow investment of up to £4,260 in cash or stocks and shares in 2018-19. Withdrawals are not permitted until the child reaches the age of 18, at which point the Junior ISA will become a normal adult ISA. 16-17 year olds can also invest up to £20,000 in an 'adult' cash ISA, even if they already have a Junior ISA.

Children's Bonds

These are National Savings products; the maximum holding per child is £3,000 in each issue

(five year investment term). All returns are exempt from tax, and the £100 rule does not apply. However, these bonds are no longer on general sale.

Premium Bonds

Premium Bonds can be bought for a child under 16 by the child's parent, guardian, grandparent or great grandparent.

The Child Trust Funds (CTF)

This is a special type of bare trust, set up by the government for children born between 31 August 2002 and 31 December 2010. Children born after December 2010 are not eligible for a CTF account. Family and friends can contribute up to a maximum of £4,260 in any one year into an existing CTF account. Growth in the fund is tax free and the £100 rule does not apply.

Interest in possession trusts

Trusts with an interest in possession are those where one or more beneficiaries has the right to trust income. The trustees have to pay tax calculated at the basic rates of tax, according to the type of income. They receive no personal allowance and have no liability to higher rate tax. The beneficiaries are personally liable to income tax on the trust income, calculated in the normal way. Children who are not taxpayers may be able to reclaim tax paid by the trustees.

Discretionary trusts

These are trusts where the trustees have discretionary powers over the distribution of income and nobody is entitled to it as of right. The trustees have to pay tax at special trust rates and any income payments to beneficiaries are taxed at 45%. Again there is scope for beneficiaries to reclaim some or all of this tax.

Pensions

Although the benefits may not be available for at least 37 years, parents may pay up to £3,600

gross (£2,880 net) a year into a personal pension on behalf of a child under 18. The contributions are paid net of basic rate tax, which is retained whether or not the child is a taxpayer.

Students

Many parents provide funds to help their children through higher education as an alternative, or top-up, to student loans. 25% of the available loan is subject to the parents' or child's income, so the level of parental contributions may affect the available loan.

There is considerable scope when it comes to student accommodation. By buying a house in the student area, your children can be assured of somewhere decent to live and should be able to cover most of the costs by renting rooms to other students. If the property is bought by the student, not the parent (and these days many lenders are happy to offer a mortgage to a student if the parents act as guarantors), the eventual sale may be free from capital gains tax under the principal private residence exemption.

Don't forget the grandparents

The strict rules which apply to gifts from parents do not apply in the same way to gifts from grandparents, who are very often more than happy to support their grandchildren.

The notes above in connection with tax liabilities cover some of the "headline" information but are not comprehensive.

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This article is based on current legislation and practice and is for guidance only. Specific professional advice should be taken before acting on matters mentioned here. Umesh Modi BA ACA is a Chartered Accountant and Tax Advisor, and a partner at Silver Levene LLP. He can be contacted on 020 7383 3200 or umesh.modi@silverlevene.co.uk