

first direct

Using trusts with life policies

A customer guide to our Flexible Trust

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Legal Disclaimer

The contents of this Guide are based on our understanding of Law and Inland Revenue practice as at January 2016. As both are subject to change, the accuracy of the guide cannot be guaranteed, particularly over the longer term. We cannot be held responsible for the actions of yourself and your trustees based on the contents of this guide. If you are in any doubt, please contact us or seek professional advice.

Part 1 – first direct Customer Guide: Flexible Trust for Life Policies

Why use a trust?

- Quicker payment out to your family and other beneficiaries following your death;
- gives you control and flexibility over who benefits; and
- inheritance tax benefits.

In the following pages where we use a technical term you will find it explained in more detail on page 7 in the Deed of Appointment. You will also find answers to common questions on page 15.

What is a trust?

A trust allows the owner of a life policy (the settlor) to specify who can benefit from the policy proceeds after they die (the beneficiaries). This is in a binding legal document (the trust deed) where two or more individuals (the trustees) hold the life policy and are bound to follow the wishes of the policy owner after he or she dies.

With a Flexible Trust the idea is that who might benefit is flexible to allow for changes in your circumstances before you die. So there are Potential Beneficiaries which is a wide group, for example, all your children, grandchildren and great-grandchildren (even if not yet born). You can add people to this list by name, for example, friends.

There are then Named Beneficiaries: here you specify who you would like to benefit in what proportions. So if there are no changes in your circumstances before you die these will be the beneficiaries.

The legal effect of the trust is that you have given away the life policy (and its proceeds). You cannot change your mind as it is not yours any longer.

You, however, remain responsible for paying the premiums.

Advantages of a trust for your life policy

Quicker payment on death

When someone dies there is a legal process of probate where all the assets are gathered in and then paid out to beneficiaries. This can take several months and sometimes even cash in a bank account cannot be paid out until the probate process is completed.

The trust is completely separate from your assets, it is not included in your Will and does not need probate. This means the cash from the life policy can be paid to your beneficiaries much more quickly.

Flexible choice of beneficiaries

You can include anyone in the list of beneficiaries. If circumstances change you can easily add (or remove) beneficiaries. Also, on your death the trustees have flexibility in how they benefit, for example, young children or grandchildren.

Inheritance Tax

The cash in the trust is not included in your assets on death and so is not liable for inheritance tax on your death.

For more detail on inheritance tax see page 6.

Why should I put my policy in trust?

Prompt access to funds for my family when I die

If your family will need money quickly a trust will help

Inheritance tax saving

If you have sufficient assets, especially if you are not married, the Trust has tax advantages

Why is flexibility important?

A Trust gives ability to add named beneficiaries up until you die

A Trust allows flexibility for further children or grandchildren

A Trust can benefit someone not named in your Will

When is a trust not appropriate?

If this Trust is for an Investment plan and you need to be able to access the proceeds/capital during your lifetime

If the policy is a joint life policy for the benefit of the joint party (the survivor) it shouldn't go into a trust

The Flexible Trust is also not suitable for:-

- business protection arrangements
- policies taken out by companies
- where there is an existing trust.

Note that, if your policy includes critical illness cover, you can still get the benefit of this yourself even though the policy is in trust, because the trust is drafted so as to separate this out. So it is fine to use the trust even though you need the critical illness benefit yourself.

Trustee Duties

- Trustees must act in the best interests of the beneficiaries
- They must follow the terms of the trust deed
- They must look after the trust money and keep accurate records
- Trustees are responsible for filing any tax returns required (this obligation will arise once the policy has paid out cash) and paying any tax due
- If in doubt they should take professional advice
- Trustees all need to act and take decisions together.

Trustee Powers

Trustees have lots of powers both as set out in the trust deed and given by law. The powers give them flexible ways to benefit the beneficiaries and allow them to look after and invest the trust money so they will mainly only be relevant once the life policy has paid out.

These powers include:-

- power to choose from the Potential Beneficiaries who should benefit and when (depending on the circumstances)
- power to make payments out to the beneficiaries including to guardians of children
- power to make loans, including interest free, to the beneficiaries
- investment powers.

Who picks the Trustees?

You pick the first trustees. Under our standard Flexible Trust Deed you are a trustee yourself when the trust is first set up and you choose who is to be appointed using our Deed of Appointment.

You can also remove a trustee and appoint a new one while you are alive.

After you die the surviving trustees can appoint any new trustees needed.

- Anyone over 18 years old can be a trustee.
- You don't need a professional (for example, a solicitor or an accountant) unless you want one: they can charge to be a trustee while all other trustees are not entitled to charge.
- For tax reasons all trustees should be resident in the United Kingdom.

The trust is drafted to last for 125 years – this being the maximum period allowed by law. However, a trust can be ended much earlier when all the money is paid out to the beneficiaries.

Inheritance Tax

Inheritance tax (IHT) is a tax on all assets on your death, (possibly including some assets you give away in your lifetime). It is levied at 40% on all assets over a certain limit other than those passing to a UK domiciled spouse or civil partner or held in trust.

There are four steps where you need to consider **IHT**:

- placing a policy in trust (see 1, below);
- payment of premiums to a policy which is in trust, (see 1b, below); and
- payment of benefits under a trust policy (see 1b below); and
- periodic and exit IHT charges levied against the trust (see 2 and 3, below) and HMRC returns (see 4, below).

Summary

Most regular premium term life or life and critical illness policies will not give rise to entry, periodic or exit charges (explained below). However, it is recommended that when the sum assured exceeds the nil rate band, or when the Settlor's position is complicated by the factors described above, or for large single premium investments, or if you are in any doubt as to the tax position, independent specialist legal and/or tax advice is obtained.

1. Entry Charge

- Putting a policy into a trust will result in a gift (or transfer) by the settlor for IHT purposes.
- Where there are two settlors (eg, a joint policy) each is treated as making a gift of one-half of the value transferred.
- The tax implications will depend on whether the trust fund consists of an existing regular premium policy or a bond, or a new regular premium policy.

a) Investment bond or an existing regular premium policy

- If you place an investment bond in trust you are making a gift. The value of this gift for IHT purposes is the surrender value immediately before the transfer or, where a new policy is placed in trust, the amount initially invested.
- Where an existing regular premium policy is placed in trust, the IHT value of the gift will be the market value immediately before making the gift (or the total premiums paid if greater). Where a policy has a surrender value, the market value will normally be similar to that surrender value. Where a policy does not have a surrender value, its market value will normally be negligible. However, where the life insured is in poor health the market value may be substantially more.

For IHT purposes the transfer of value (the gift) may be:

- exempt; or
- chargeable immediately to IHT as a chargeable lifetime transfer (CLT).
- A gift will be exempt if the total amount transferred (including previous gifts in the same tax year) is within the donor's annual allowance for gifts, which is currently £3,000 per person.
- If the amount of the CLT exceeds the prevailing IHT nil rate band, or, if when it is added to the cumulative amount of CLT over the preceding 7 years, the total exceeds this level, the excess over the nil rate band will be immediately chargeable to IHT at the lifetime rate of 20%. If the value is below the nil rate band there will be no immediate IHT consequences. However, there is a requirement to report the transfer to HM Revenue and Customs (HMRC) within 12 months of the date of the transfer if it causes total chargeable transfers in a tax year, or over a cumulative 7 year period, to exceed specified levels.

b) Paying regular premiums

- Usually the regular premiums payable by the donor will fall within the donor's annual exemption (currently £3,000) or the normal expenditure exemption, so there will be no IHT implications. If the premiums are too large to be exempt in this way they will be Chargeable Lifetime Transfers.
- On your death the sum assured will be paid to the trustees of the trust. Such payment itself will not be subject to IHT and will not affect the IHT calculations on your estate.

2. Periodic Charge

The trust will be assessed for a possible IHT charge on each 10th anniversary of its creation. In the most straightforward situation, the value of the trust fund is compared to the prevailing nil rate band and any excess is liable to IHT at a rate of 6%.

In the case of an investment bond, the value of the trust fund is generally the surrender value of the bond.

For a term life or life and critical illness policy the value of the trust fund is the market value of the policy. In straightforward cases this 6% periodic charge is only likely to arise in two circumstances:

- When the life assured is in serious ill health at the 10th anniversary and the sum assured exceeds the prevailing nil rate band. The appropriate market value would be agreed between the trustees and HMRC and would depend on the individual circumstances; or
- When the sum assured, in excess of the prevailing nil rate band, has been paid to the trustee prior to a 10th anniversary and remains in the trust at the 10th anniversary.

The trustees may need to submit a return to HMRC on each 10th anniversary even if no IHT is payable. Whether or not a return is required depends on the exact circumstances.

The tax position becomes more complicated (and is outside the scope of this guidance) if the Settlor had made any Chargeable Lifetime Transfers in the preceding 7 years, the Settlor had created other trusts on the same day as the trust under review, property had been added to the trust since its creation, distributions were made that were subject to an 'exit charge' (see below), or the trust holds accumulated income. The trustees should seek their own specialist legal and/or tax advice if they are in any doubt about their tax positions.

3. Exit Charge

Any trust distributions may be subject to a further IHT charge, the proportionate or 'exit' charge. This is only applicable:

- to distributions in the first ten years if an entry charge arose; or
- to distributions in any subsequent ten year period if a periodic charge arose at the preceding 10th anniversary.

The exit charge will not exceed 6% of the amount distributed. The trustees may need to report to HMRC any capital distributed from the trust.

Summary

Most regular premium term life or life and critical illness policies will not give rise to entry, periodic or exit charges. However, it is recommended that when the sum assured exceeds the nil rate band, or when the Settlor's position is complicated by the factors described above, or for large single premium investments, or if you are in any doubt as to the tax position, independent specialist legal and/or tax advice is obtained.

4. HMRC Returns

In connection with the IHT chargeable events that can arise under a trust subject to the discretionary trust regime, the main account to be submitted to HMRC Capital Taxes is the Form IHT 100.

It is a requirement that an event form accompanies the Form IHT 100. For a trust subject to this discretionary trust regime, the relevant event forms are

- 100a – for gifts into the trust ;
- 100c – for an exit charge on property leaving the trust eg. when capital is paid out to a beneficiary. This form may be needed even if no tax is payable; and
- 100d – for the ten-year anniversary (periodic) charge. The form may be needed even if no tax is payable

In certain circumstances a Form IHT 100 will need to be accompanied by Form D34 which is supplementary to Form IHT 100 and which deals with life assurance policies and annuities. Form D34 has to be completed if any transfer, which includes the payment of premiums, is linked in any way with a life assurance policy or annuity. The form is very short and requires only limited information.

Income Tax

Where a policy has an investment element you should also consider the impact of income tax. Tax can arise on chargeable gains if a chargeable event (such as the surrender of a policy or death of the last life assured) occurs.

1. Chargeable events

- You need to consider income tax where a policy held by the trustees is wholly or partly encashed. This will apply mostly where the policy is an investment bond, but may also apply to some regular premium policies.
- See the brochures and any additional product information for your policy for an explanation of chargeable events.
- During the donor's lifetime and in the tax year of the donor's death, any chargeable gains arising from surrendering a policy will be assessed on the donor provided he or she is a UK resident. However, where the donor does incur a tax liability following a chargeable event, he or she is entitled to recover the tax from the trustees.
- Following the tax year in which the donor dies (or if the chargeable gain arises while the donor is non-UK resident) any chargeable gains will be assessed on the UK resident trustees at their special rate. However, the trustees will be entitled to a tax credit.
- The amount of credit given is the basic rate.

2. Payments to beneficiaries

- Payment of capital to beneficiaries should normally have no income tax implications for the donor or the beneficiaries.

Capital Gains Tax

There are unlikely to be capital gains tax implications unless the policy is sold to another party, which is not usually relevant to policies subject to trust, or the policy proceeds are invested in a different type of asset.

Part 2 – Setting up a trust

How to complete the forms

A trust is usually set up by a written statement of what you are doing. This written statement creating the trust, together with the general principles of trust law, governs who will look after the trust assets (eg, the policy), how they will do it, and for whose benefit they will hold them.

All trust forms and Deeds of Appointment should be completed in capitals to ensure clarity.

In this next section we show you how to complete the trust documents.

The Flexible Trust (Declaration)

This Declaration of Trust is made by the person[s] named below (“the Settlor[s]”)

Title Mr Mrs Miss Ms
 Other (please specify)

The settlor is the person applying for the policy. Their details need to be input in this section

Explanatory Notes

Please insert full name(s) and address(es) of the Settlor(s). **DO NOT USE INITIALS.**

These should be the owners as shown on the Policy Schedule or the person(s) applying for the new Policy. So if there are joint owners of the policy there will be two Settlers.

Surname
 All Forenames
 House name and/or number
 Street or road name
 District (if any)
 Village, town or city
 County
 Postcode

Please use full names (no abbreviations)

If there is only one settlor, complete this section and draw a line through the unused box as shown in this example

Title Mr Mrs Miss Ms
 Other (please specify)
 Surname
 All Forenames
 House name and/or number
 Street or road name
 District (if any)
 Village, town or city
 County
 Postcode

Put a line through these boxes if there is only one Settlor.

If there are two settlor(s) please complete both sections.

Schedule A below is where you specify who you would like to benefit on your death. Schedule B is a wider group of potential beneficiaries to allow for changes in your circumstances which mean that it is no longer appropriate to just benefit those named in Schedule A.

Schedule A – Named Beneficiaries

Note: This Schedule MUST be completed.

The percentages allocated MUST total 100%

First Name(s)	Surname	Date of Birth (dd/mm/yyyy)	%
		D D M M Y Y Y Y	
		D D M M Y Y Y Y	
		D D M M Y Y Y Y	
		D D M M Y Y Y Y	
		D D M M Y Y Y Y	
		D D M M Y Y Y Y	

Schedule A will contain the names of the people that you as settlor(s) wish to benefit. It is essential that you state the FULL name(s).

If you specify the share it is vital that they total 100% eg, 60% + 40%, this must be whole figures with no decimal places. If you want all the beneficiaries to receive an equal share then there is no need to state any percentages.

Schedule B – Potential Beneficiaries

1. The Spouse/Civil Partner, Widow/Widower or Surviving Civil Partner of (either of) the Settlor(s) but excluding any Settlor.
2. The Children (including stepchildren, adopted children and other dependent children) and remoter issue (eg, grandchildren) of the Settlor(s).
3. Any person (other than the Settlor(s)) nominated by the Settlor(s) (or the survivor of them) in writing to the Trustees.
4. Any person named in Schedule A.
5. Any person(s) entitled under the will or intestacy of the Settlor(s).

Schedule B contains those people who are automatically able to benefit from the trust. So the spouse of the settlor is already a potential beneficiary.

Try to think beyond your immediate family, in order to introduce additional potential beneficiaries such as godchildren, brothers, and sisters etc. to ensure that there will be someone to whom the Trust Fund can be paid.

6. First Name(s)	Surname	Date of Birth (dd/mm/yyyy)

These details must be completed for each of the policies that are to be transferred into this trust.

Schedule C – Identification of the Original Policy(ies)

1. Date of proposal (if policy applied for)
 Policy Number (if existing policy)
 Type of Policy
 Life/Lives Assured
 Insurer

2. Date of proposal (if policy applied for)
 Policy Number (if existing policy)
 Type of Policy
 Life/Lives Assured
 Insurer

This box(es) MUST be signed by each settlor. If there is only one settlor, then only the first box needs to be signed.

The trust MUST be dated before or on the date of the commencement of the policy. If you are putting an existing policy into trust it must be dated at the same time it is signed by the settlor(s).

SIGNED as a Deed (but not delivered until dated) by the Settlor (1)

D J BARTON

Date of signature

D	D	M	M	Y	Y	Y	Y
---	---	---	---	---	---	---	---

SIGNATURE of witness

Name of witness

Witness address

Witness Occupation

Note - Each settlor must have their signature witnessed by someone who is not a settlor or a beneficiary. If there are two settlors the same person can witness signatures for both settlors.

SIGNED as a Deed (but not delivered until dated) by the Settlor (2)

D J BARTON

Date of signature

D	D	M	M	Y	Y	Y	Y
---	---	---	---	---	---	---	---

SIGNATURE of witness

Name of witness

Witness address

Witness Occupation

Choosing your trustees

Having set up your trust, the first thing you need to do is to appoint new trustees to act alongside you, and to take over if you die.

To do this you will use the Deed of Appointment of Additional Trustees, shown over the next three pages. As the name suggests, your trustees should be people you trust to do what you believe is right. The Flexible Trust sets out your instructions to them, but also gives them power to use their judgement if circumstances change.

For example: imagine you have to put money into a trust to benefit your two children in equal shares. Years later, one of your children wins the lottery. Would you still want them to benefit in equal shares?

Your trustees may have to make this choice for you after your death.

Deed of appointment of additional Trustee(s)

Date

Parties

Settlor (1) full name of

Full Home Address and

Settlor (2) full name of

Full Home Address

The details of the person(s) who applied for the policy will need to be inserted into these boxes. Please show the full name. Initials such as D J Barton or abbreviations such as Dave John Barton are not to be used.

("the Settlor(s)") of the first part and....

Trustee (1) full name of

Trustee (1) date of birth

Full Home Address and

Trustee (2) full name of

Trustee (2) date of birth

Full Home Address and

Trustee (3) full name of

Trustee (3) date of birth

Full Home Address

The settlor is automatically a trustee. The settlor's details do not need to be repeated.

Please make sure that you use full names and addresses in these boxes.

At least one of the additional trustees should not be a beneficiary of the trust.

("the Additional Trustee(s)") of the second part.

Schedule 1

Date the Trust was signed

This should be the date the flexible trust is signed by the settlor.

Made in respect of the following policy of assurance:

Life (lives) assured

Type of Policy

- 1)
- 2)
- 3)

Insurance Company

HSBC Life (UK) Limited

Policy Number(s)

- 1)
- 2)
- 3)

If you wish you can leave these boxes blank for completion by HSBC Life (UK) Limited.

Schedule 2

Insurance Company

HSBC Life (UK) Limited

Policy Number(s)

- 1)
- 2)
- 3)

SIGNED AND DELIVERED AS A DEED on the date written above.

Signed as a Deed and Delivered by the Settlor (1)

Signature D J BARTON

in the presence of

Signature M WITNESS

NAME MARK WITNESS

Address

5 WITTS COURT
ANY TOWN
ANY COUNTY
A04 4XL

Please note that the settlor is already a trustee. The settlor should not sign in this box as they are not being appointed as an additional trustee.

Signed as a Deed and Delivered by the Settlor (2)

in the presence of

Address

Remember that ALL signatures of the settlor(s) and trustee(s) MUST be witnessed.

Signed as a Deed and Delivered by the New Trustee (1)

Signature S L BARTON

in the presence of

Signature M WITNESS

Name Mark WITNESS

Address

5 WITTS COURT
ANY TOWN
ANY COUNTY
A04 4XL

Signed as a Deed and Delivered by the New Trustee (2)

Signature H CARR

in the presence of

Signature M WITNESS

Name Mark WITNESS

Address

5 BRIDGE STREET
ANY TOWN
ANY COUNTY
A04 4XL

Signed as a Deed and Delivered by the New Trustee (3)

Signature D CARR

in the presence of

Signature M WITNESS

Name Mark WITNESS

Address

5 BRIDGE STREET
ANY TOWN
ANY COUNTY
A04 4XL

The same person can be a witness to all signatures if you wish. However, the witness MUST sign against all signatures he is witnessing. Don't forget that the witness CAN'T be a trustee, settlor or beneficiary.

Please return this deed to Customer Services Centre, HSBC Life (UK) Limited, PO Box 6176, Coventry CV3 9HN. After recording the details the original deed will be returned to you and should be kept by the Trustees.

Common Questions: Answered

Q: Can I continue to benefit under the Trust?

A: No. However, if your policy has both Life and Critical Illness cover, then in the event of a pay out for a critical illness, that can be paid to you while any remaining life cover will be paid into the trust. Children's Critical Illness Benefit will also be paid to you.

(Note, however, that pay outs for terminal illness are held for the beneficiaries in the same way as the death benefit).

Q: Can I unravel the trust and get access to the policy?

A: No. Once you have set up the trust you cannot have access to the policy benefits, other than the critical illness benefits payable as described above.

Q: Do I need to review my trust arrangements?

A: Yes, you should regularly review your trust arrangements. In particular, the beneficiaries and trustees since these may need to change where your family circumstances have changed (for instance a new child, separation etc).

Q: How much will it cost to set up the trust?

A: We make no charge for providing the Flexible Trust.

If you decide to consult a solicitor or other professional adviser before completing the trust form, they may charge you a fee. They should be able to tell you what this is in advance. Similarly, if you appoint a professional trustee or trust company as trustee they may charge for their services.

Q: Which trust forms do I need?

A: You will need to complete the Flexible Trust.

In addition, you will need to use the Deed of Appointment of Additional Trustees.

Q: Is running a trust difficult?

A: No. Until you die the Flexible Trust is basically dormant (unless there is critical illness or terminal illness cover). It is then straightforward for the trustees to distribute the proceeds to your chosen beneficiaries.

For more guidance on running a trust see our Trusts Guide.

Q: Do I need to see a solicitor or other professional adviser?

A: Whilst we have taken great care to ensure the Flexible Trust can achieve its objectives if you have individual circumstances or concerns on which you require advice you should consult your own advisers.

Q: Can I put existing policies into trust?

A: You can use the Flexible Trust to put existing HSBC life, or life and critical illness policies in trust, but not policies issued by another life company.

This trust will separate life and critical illness benefits where you wish to retain the benefit of the critical illness but give away the death benefit.

Q: What if I were to be declared bankrupt?

A: Generally speaking, any assets held in trust (under which you cannot benefit) are safe from creditors. The exception is where the assets were transferred when you were already insolvent or made with the specific intent to defraud creditors. In such circumstances the court may set aside the trust and pay the asset over to the trustee in bankruptcy for the benefit of creditors.

Q: What if I get divorced or dissolve a civil partnership?

A: A life policy held in trust is owned by the trustees and does not belong to you legally.

It will not usually be taken into account in any settlement. However, if you and your spouse/civil partner owned the policy jointly or you both pay premiums under the policy, it is important that you make arrangements in any divorce or other settlement to ensure that no future disputes will arise.

Q: Can I change trust terms?

A: Yes, but it is rarely needed. Your trust already gives the opportunity to choose between potential beneficiaries and whether to pay income or capital sums, or to make administrative changes.

Q: Is a trust suitable if my policy provides critical illness cover?

A: Yes. The Flexible Trust separates out the death benefits to be held in the trust for the beneficiaries, whilst the Critical Illness Benefits (including any Children's Critical Illness Benefit) are held for you.

Q: Do I need to refer to the trust or the policy in my Will?

A: No. A policy held subject to trust is no longer yours to dispose of on your death.

Q: Can I add other beneficiaries?

A: Yes. The Flexible Trust includes a wide class of potential beneficiaries. However, there is also a provision that allows you to add new names to the list of potential beneficiaries later. You would simply need to write to your trustees to let them know.

Q: Can I change the beneficiaries?

A: Yes. You have this power under the trust during your lifetime. Following your death the trustees can also add new beneficiaries, and there is flexibility as to who is to benefit from the list of potential beneficiaries.

Q: Will I be a trustee?

A: Yes, under our Flexible Trust you are automatically a trustee. The trustees have to act unanimously so you, and all the other trustees that you appoint, have to agree on what to do. There is another advantage too. With you as trustee, we will continue to write to you on the progress of your policy. We will expect you to share this information with your fellow trustees.

Q: Should there be other trustees as well as me?

A: Yes, although this is not legally essential, it is strongly recommended. The trust is basically dormant until you die. If you die as the sole trustee there is no-one able to immediately act as trustee. Instead your executors or administrators will need to act as trustees which will involve a delay until probate is granted.

Q: How many trustees should there be?

A: The best number is between 2 and 4.

Q: Can a beneficiary also be a trustee?

A: Yes, however a trustee cannot appoint benefits to themselves without there being at least one other trustee acting who will not benefit.

Q: Can I appoint further trustees later?

A: Yes, under the terms of the trust you can appoint further trustees later. You will need a special deed, which you can obtain from us on request.

Q: Should I appoint my solicitor or other professional adviser as a trustee?

A: It is up to you who you appoint as a trustee.

There is usually no need to appoint professional trustees such as solicitors or accountants, as running the trust in most family circumstances is not complicated. They may lack the personal knowledge of family circumstances. You should also remember that if you appoint a professional trustee they will charge fees for dealing with the trust.

Q: Can I remove trustees?

A: Yes, you have this power under the trust deed. However, it is advisable when removing a trustee to appoint a new trustee in their place.

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