An important aspect of the legal system of England and Wales is that property cannot be tied up in trust for an indefinite amount of time and future interests in property must take effect within what is called the perpetuity period. In practice, at the end of that perpetuity period, the trustees’ dispositive powers cease, the trust comes to an end and the trust property is held according to the default provisions i.e. the future interests vest. The Perpetuities and Accumulations Act 1964 (the ‘1964 Act’) allowed testators and settlors the opportunity to choose a fixed perpetuity period of 80 years, but the common law ‘lives in being’ option was still available. The 1964 Act also placed a restriction of 21 years on the length of time that income can be accumulated as part of capital within a trust.

The Perpetuities and Accumulations Act 2009

The Perpetuities and Accumulations Act 2009 (the ‘2009 Act’) received Royal Assent on 12 November 2009 and will come into force on a date yet to be announced (expected to be some time in 2010). The main aspects of the 2009 Act which are of immediate interest to settlors, testators and trustees are that: it introduces a single 125-year perpetuity period which will always apply (although a shorter trust period may still be chosen), and it provides that trustees will be able to accumulate income for the whole of the trust period. This places the UK in a similar position to offshore jurisdictions, promoting the UK’s position as a trust jurisdiction.

The change in the accumulation period is likely to have the greater impact on the drafting of new trusts and wills since it will prevent the situation where distributions of income have to be made to inappropriate or immature beneficiaries.

Trusts

The new 125-year perpetuity period and accumulation provisions will apply to all lifetime trusts set up after the 2009 Act provisions come into force.

Wills

Although in general a will is treated as coming into effect when the testator dies, the 2009 Act will not apply to a trust created under a will which is executed before the rules come into force, even where the testator dies after that date.

Although the 2009 Act is silent on the effect of a codicil on the perpetuity and accumulation periods applying to a will containing a trust, it seems that if a codicil is executed after the rules come into force and expressly republishes the will, it can be worded so that the new perpetuity and accumulation periods will apply.

Existing trusts

Where, under a trust created, or a will executed, before the rules come into force, there is a ‘lives in being’ perpetuity period, it can be difficult or not reasonably practicable to ascertain when the period will end. The 2009 Act provides that in such cases, trustees can execute a deed providing that the perpetuity period will become a fixed 100 years. The trust will be treated as if this had been the perpetuity period since the trust was established. There is no external check on whether it is truly impracticable for the trustees to trace the relevant lives in being, although they must act in a fiduciary manner, balancing the interests of beneficiaries who would benefit from a longer or a shorter period. This will not however affect the accumulation period of the trust.

The 2009 Act preserves the existing provisions which ‘save’ gifts from being void for perpetuity reasons, for example the ‘wait and see’ rules. It also provides for the exclusion of certain beneficiaries from a class of beneficiaries whose inclusion would cause an interest or estate to become void for remoteness.

Exercise of powers of appointment

Where a special power of appointment contained in a trust is exercised to create new trusts, the 2009 Act confirms the current law that (save for certain pension schemes) the perpetuity and accumulation periods of the new trust will be the same as the period relating to the trust containing the power. This does not apply to general powers of appointment (which may be exercised by an individual in order to transfer the property in the trust to himself), where the new periods will apply.

In some circumstances it may be preferable to create a new trust rather than to exercise a power of appointment under an existing trust, in order to take advantage of the new perpetuity and accumulation periods. However, the tax considerations of doing so will need to be carefully
considered before any such action is taken.

Charities

The accumulation period for all charities will become 21 years, save as ordered by a Court or the Charity Commission (previously income could be accumulated indefinitely if the settlor of the charity was a corporate entity). There is also an exception where the duty or power to accumulate ceases to have effect on the death of the settlor. This will ensure that trust income is actually used for charitable purposes rather than being rolled up with capital for too long.

What action should be taken now?

It is not yet clear when the new provisions will come into force and, in the meantime, the need to have a valid and appropriate will in place to avoid intestacy is likely always to outweigh any benefit which can be gained from deferring execution in order that the longer perpetuity or accumulation periods will apply. Additionally, an appropriately worded codicil or a new will can be executed later if the testator feels strongly about the length of the perpetuity or accumulation periods.

Likewise for lifetime trusts, the creation of a trust should not be delayed if it is required to make immediate provision for beneficiaries or the settlor wishes to ensure that it is created in the current tax environment (in case any adverse changes are announced in the Pre-Budget Report in December or the next Budget). Additionally, it may be useful for a transfer into a trust to be done now to take advantage of the inheritance tax nil rate band and to start the 7 year period before a fresh nil rate band is obtained.

Even after these changes, the law in relation to perpetuities and accumulations in England and Wales continues to be limited in comparison to other jurisdictions. Bermuda has recently approved legislation abolishing its perpetuity period altogether and trustees can now apply to court to extend the perpetuity period of existing settlements. The only comparable possibility in England and Wales is an application to Court under the Variation of Trusts Act which can be complex and expensive. Trustees may therefore wish to look into changing the proper law of a trust in order to extend the perpetuity period, or make an application to Court to enable this to be done. Both of these options involve complex legal considerations and specialist advice should be sought.

Withers LLP can assist settlors, trustees, and testators by advising on all aspects of the new 2009 Act rules and also the existing provisions which will continue to apply to existing lifetime and will trusts. We can guide you through the legal and tax issues, including the process of deciding whether to create a trust now or to vary an existing trust.