Savings for disabled people: the case for a simpler approach

Inheritance tax and trusts | Personal tax

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Research into UK savings options for disabled people supports the existing trust regime while proposing an additional simpler, more accessible complementary savings vehicle.

Key Points

What is the issue?
Saving for the future needs of disabled people may not be straightforward given issues such as decision-making capacity and the means testing of care and certain benefits.

What does it mean to me?
An existing disability trust regime offering specific tax treatments is available – but it

may not be the right approach for more modest savings levels given cost and complexity, leaving some individuals reliant on informal and potentially risky arrangements.

What can I take away?
There is a strong case for retaining the trust regime but complementing it with a simpler, more accessible savings vehicle, drawing on international models, to broaden access to effective long-term financial planning for disabled people.

For many disabled people, and for those who support them, the ability to build up savings can be critical. Some individuals may not be able to provide for themselves; others may face significant additional costs as a result of their disability. In some cases, relatively modest funding for training or equipment not otherwise provided by the state could make a substantial difference to their lives and prospects.

Notwithstanding current levels of public provision, parents, relatives and friends of disabled people who are unable to live independently may be anxious about the future, particularly given the prospect that the disabled person may live for many years beyond their lifetime.

Against this backdrop, in January the Tax Law Review Committee of the Institute for Fiscal Studies published a discussion paper entitled ‘Tax and disability in the UK: review of trusts and other savings options’.

There are options available, but the paper argues that more can be done. Drawing on comparative analysis with disability trusts and other arrangements in Australia, Canada and the US, the paper reviews the existing UK trust-based savings regime for disabled people and explores alternative approaches, considering both tax and non-tax dimensions.

In summary, the paper recommends that:

- The existing UK trust-based regime should be preserved, albeit with some modest legislative amendments.
- The UK should consider introducing a simplified savings account for eligible disabled people to sit alongside the disability trust regime, for those for whom the cost and complexity of trusts mitigate against their use.

This article summarises the background to the paper and its key findings.

Savings and disability: the context

‘Disability’ is a broad-ranging term with hugely diverse implications for disabled people and those who care for and support them.

While many disabled people are able to work, live independently and provide for themselves, they may face significant additional ‘costs of disability’. Others – for example, people with certain genetic syndromes – may never be able to work or provide for themselves and may require ‘24/7’ care. Some may also lack the capacity to manage their own financial affairs.

In the UK, subject to meeting eligibility criteria, disabled people may be entitled to state-provided care and welfare benefits, in addition to public services such as healthcare. Some benefits, such as the Personal Independence Payment, are not means-tested; however, the provision of care and a number of benefits (including Universal Credit) usually are.

Against this background, parents, relatives and other benefactors may wish to set aside funds to meet future needs not otherwise covered by the state, whether as a contingency or to fund disability-related expenditure. However, there is an obvious disincentive if doing so results in the withdrawal of care or benefits because those funds are taken into account for means-testing purposes.

In practice, there are two main ways in which funds may be made available for the future care and provision of a disabled person, short of outright gifts.

The first is through a trust-based arrangement (see below). In a discretionary trust, assets are managed by trustees and do not legally belong to the disabled person, unless and until they are appointed to them as the beneficiary. They are therefore generally disregarded for means-testing purposes. Nonetheless, trusts may be relatively costly and complex to establish and operate, particularly for more modest sums.

The second is an informal arrangement, such as giving funds to a trusted relative or friend in the hope that they will use them for the benefit of the disabled person if needed. Such arrangements are inherently uncertain and carry obvious risks.

The existing trust-based regime

Tax legislation has for some time provided a trust-based regime for eligible disabled people. The current provisions span inheritance tax, income tax and capital gains tax.

Broadly, gifts into eligible trusts are treated as potentially exempt transfers (PETs) for inheritance tax purposes under Inheritance Tax Act (IHTA) 1984 s 89, rather than as chargeable lifetime transfers subject to an immediate tax charge and periodic charges under IHTA 1984 s 64. Separate provisions under s 89A apply to ‘self-settled’ trusts, established by individuals who have, broadly, a reasonable expectation of becoming a ‘disabled person’ for the purposes of the legislation (see below).

In addition, trust income and capital gains can, subject to ‘vulnerable beneficiary’ election, broadly be treated as if they were those of the disabled beneficiary themselves, rather than being taxed at the higher rates applicable to trusts. The vulnerable beneficiary regime (which also covers eligible bereaved minors) is set out in Chapter 4 of the Finance Act 2005.

The definition of a ‘disabled person’ both for disability trusts for inheritance tax purposes, and for the vulnerable beneficiary regime is set out in Finance Act 2005 Sch 1A para 1. Broadly, this includes both a criterion relating to a beneficiary’s mental capacity and, subsequently, eligibility for a specified range of benefits.

Since its introduction, the trust-based regime has been subject to a number of modifications. For example, the original requirements of IHTA 1984 s 89 broadly required that not less than half of the settled property applied during the lifetime of the disabled person was applied for their benefit, subject to certain exceptions.

This requirement was amended by Finance Act 2013 in relation to trusts created on or after 8 April 2013. Capital or income must now be applied for the benefit of the disabled beneficiary during their lifetime, although funds may be retained in trust and paid to a non-disabled beneficiary on death. In addition, up to the lower of £3,000 or 3% of the maximum value of the settled property during the relevant period may be appointed annually to someone other than the disabled beneficiary.

Proposed legislative amendments

Building on existing work, the discussion paper identifies a number of proposed amendments to the disability trust regime. In particular, these include:

- streamlining the approach to taxing income as if it was that of the beneficiary;
- removing the need for ‘tax pool’ arrangements by deeming income to be that of the beneficiary when it arises; and
- reconciling Conditions 1 and 2 in IHTA 1984 s 89A(2) and (3).

Further detail is provided at Appendix 3 of the paper.

Relationship with means testing

A key feature of discretionary disability trusts is that assets are not legally those of the beneficiary unless and until they are appointed. Accordingly, assets held within such trusts are generally disregarded for means testing purposes in relation to care and welfare benefits. However, where assets are appointed to the beneficiary (so that they become ‘in funds’), they will then be taken into account.

Cost and complexity

Notwithstanding the services provided by organisations such as Mencap, establishing and administering trusts may for many people appear neither cost-effective nor straightforward. (Details of Mencap Trust Company, the services it provides and details of its charges can be found online at www.mencaptrust.org.uk.)

Many parents and relatives of disabled people already devote a huge amount of time to supporting them, including interacting with a range of authorities and service providers. Against this background, simplicity has considerable value, while vehicles such as trusts may seem simply overwhelming, particularly where the sums involved are relatively modest.

Current usage

Based on a Freedom of Information Request to HMRC, a comparatively modest number of disability trusts filed self-assessment returns in 2022-23. However, this figure cannot be seen in isolation, as many disability trusts may not be required to file returns.

The case for a simplified savings vehicle

In addition to disability trust regimes, Canada and the US operate alternative savings accounts for eligible disabled people: Registered Disability Savings Plans (RDSPs) and Achieving a Better Life Experience (ABLE) accounts respectively.

The objectives and detailed provisions of these vehicles vary. For example, while earlier withdrawals are possible, the RDSP has a later life, pensions-type focus. ABLE Account programmes are operated at state level. Broadly, both arrangements allow savings by and for eligible disabled people for a range of purposes, subject to certain specified limits, included targeted tax reliefs, and with defined ‘carve out’ provisions in relation to means-tested benefits. The take-up of both arrangements has been significant, with around 263,000 active RDSP beneficiaries as at December 2022 and approximately 204,000 ABLE Accounts as at 31 March 2025.

Against this background, and given the cost and complexity of trusts for many people, the discussion paper recommends consideration of a simplified UK savings account arrangement for disabled people to operate alongside the existing trust regime. Such a vehicle could be delivered through the UK financial services industry using standardised processes.

In any such arrangement, it is important to recognise how broader public provision for disabled people in Canada and the US varies compared to the UK. It is therefore vital to avoid ‘cherry picking’ individual features of RDSPs or ABLE Accounts without considering the wider policy context of public provision.

Policy considerations

The discussion paper highlights a number of policy considerations that would need to be addressed in advance of introducing a simplified savings account. In several areas, it adopts as a ‘default setting’ an approach aligned with the framework underpinning the existing trust-based regime, while also identifying reasons why alternative approaches might be appropriate.

Eligibility: Consistent with this ‘default setting’, eligibility for a simplified savings account could be based on the definition of a disabled person in Finance Act 2005 Sch 1A para 1. However, alternative approaches could be developed, drawing for

example on the eligibility criteria used for ABLE Accounts in the US.

Relationship with means testing: As with the existing disability trust regime, the paper recommends that funds which are held within a simplified savings account should be excluded from means testing. Without such treatment, there would be little incentive for relatives or others to contribute. The treatment of withdrawals for means testing purposes would also require careful consideration. One option could be to disregard, for means testing purposes, amounts used to meet defined categories of disability-related expenditure.

Tax treatment: Again, drawing on the existing trust-based regime, the paper suggests as a starting point that income and gains arising within the simplified vehicle could be taxed at the disabled beneficiary's marginal rate, mirroring the effect of the vulnerable beneficiary rules. However, a more explicitly tax-advantaged approach could be adopted, for example along the lines of ISAs, to encourage take-up and reduce administrative burdens.

Other matters: A number of further issues would need to be considered as part of launching any simplified vehicle, including governance arrangements where the disabled person lacks capacity, appropriate investment parameters, and whether simplified savings accounts might be subject to defined financial limits.

The paper also outlines an illustrative process for establishing and operating a simplified account in practice, and emphasises the importance of engagement with disability groups and the retail financial services industry in developing a workable model.

Conclusions

There are clear reasons why people may wish to set aside money for the future provision of disabled people, particularly those who are unable to provide for themselves or who may face substantial additional 'costs of disability'. The existing, well-established trust regime offers one option, but may not be suitable for everyone on grounds of cost and complexity.

The discussion paper concludes that, building on overseas experience, there is a powerful case for introducing a simplified savings vehicle to sit alongside the trust regime. As the paper observes: 'This would mean that the peace of mind that can

come from putting aside money for, say, the future of a disabled child can be available to a broad range of people, not just those who can afford the time and resources to set up and run trusts.'

The discussion paper, Tax and disability in the UK: review of trusts and other savings options, is at: tinyurl.com/86b885wm. It was written for the Tax Law Review Committee by Paul Brice, with input from members of the Committee, including Emma Chamberlain, Judith Freedman, and the law firms Withers and Bentleys (Australia). The Committee authorised its publication to inform and promote debate in this area.

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