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TRANSFERABLE NIL RATE BANDS - AN UPDATE

In our February 2008 Private Client Brief Stephen Atkinson wrote about the proposed new rules for transferring the Nil Rate Band ("NRB") for Inheritance Tax , which rules had not come fully into force at that time. These have now been passed into law, and this article revisits the rules, and comments on whether NRB Discretionary Trust legacies are still sensible to include in Wills. Prior to the new rules this was the accepted way to ensure that both spouses' or civil partners' NRBs were available to reduce Inheritance Tax on the survivor's death.

Readers may recall that on the death of a surviving spouse or civil partner on or after 9 October 2007, where that marriage came to an end on the first spouse's death at any time (whether under the rules relating to Estate Duty, Capital Transfer Tax, or Inheritance Tax) or where that civil partnership came to an end where the first death occurred on or after 5 December 2005 (the date that the Civil Partnership Act became law), the NRB of the first spouse or civil partner to die may be available to increase the value of the assets that may pass free of Inheritance Tax when the surviving spouse or civil partner dies.

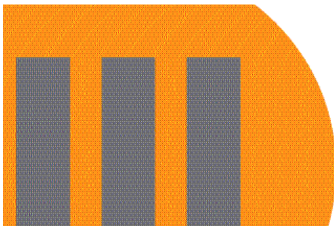
The legislation refers to unused NRB, rather than property passing to the survivor, and therefore it doesn't matter if the value of the estate of the first to die is under the NRB, as the full balance may be available for transfer. The way in which the legislation works is that the NRB at that time of the death of the survivor is increased by the proportion of the NRB not used on the first death.

Bearing in mind these rules and that the Conservatives, who may be the next party in power, first suggested increasing the Inheritance Tax threshold to £1m at their Party Conference in 2007, and that the Shadow Chancellor, George Osborne, said on 9 June 2009 "We are committed to raising the Inheritance Tax threshold to £1m so that only millionaires pay tax on what they have saved to pass on to their children" is it sensible now to include a NRB Discretionary Trust legacy in a Will?

Private Capital Team

These are three reasons for continuing to include NRB Discretionary Trust legacies in Wills.

First, historically the increase in the value of the NRB for Inheritance Tax has not been kept up with inflation. In Stephen's article in February 2008 he pointed out that if the NRB had increased at the same rate as the property market it would at that time have been over £0.5m. It is presently £325,000. Due to the present depressed values of stocks and shares and property, if there is a death of the first spouse or civil partner now, then it may be sensible to utilise some of these assets to fill up an NRB Discretionary Trust legacy in the expectation that these assets may increase in value at a greater rate than the value of the NRB itself.



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Second, if the survivor may have to enter a care home, and his or her assets may be means tested to ascertain whether there may be any Local Authority funding available, then assets held in an NRB Discretionary Trust legacy should not be included in this test.

Third, and more complicated, is the situation where spouses or civil partners are on their second marriage or civil partnership. A Transferable NRB can never exceed 100% of the NRB available on the death of the survivor. Say, Peter and Jane (see diagram) are on their second marriages. When Peter's wife died she left everything to him, and when Jane's husband died he left everything to her. Further, say, when Peter dies he leaves everything to Jane, and presuming that there are no chargeable lifetime gifts made in relation to any of these deaths, then on Jane's death there will be two NRBs available. However, if on Peter's death assets equal to twice the NRB at his death had been transferred into a NRB Discretionary Trust legacy, with the remainder of his estate going to Jane, free of Inheritance Tax, then on Jane's death, her estate is still entitled to two NRBs, as she is entitled to the transferable NRB from her first husband's estate. In effect, therefore, the combined estates of Peter and Jane have had the benefit of four NRBs

It should be remembered that access to a transferable NRB is only available where a marriage or civil partnership has ended in death, and not by dissolution, and that the personal representatives of the surviving spouse or civil partner must claim the transferable NRB, ordinarily within two years of the second death.

To discuss this in more detail please contact the writer

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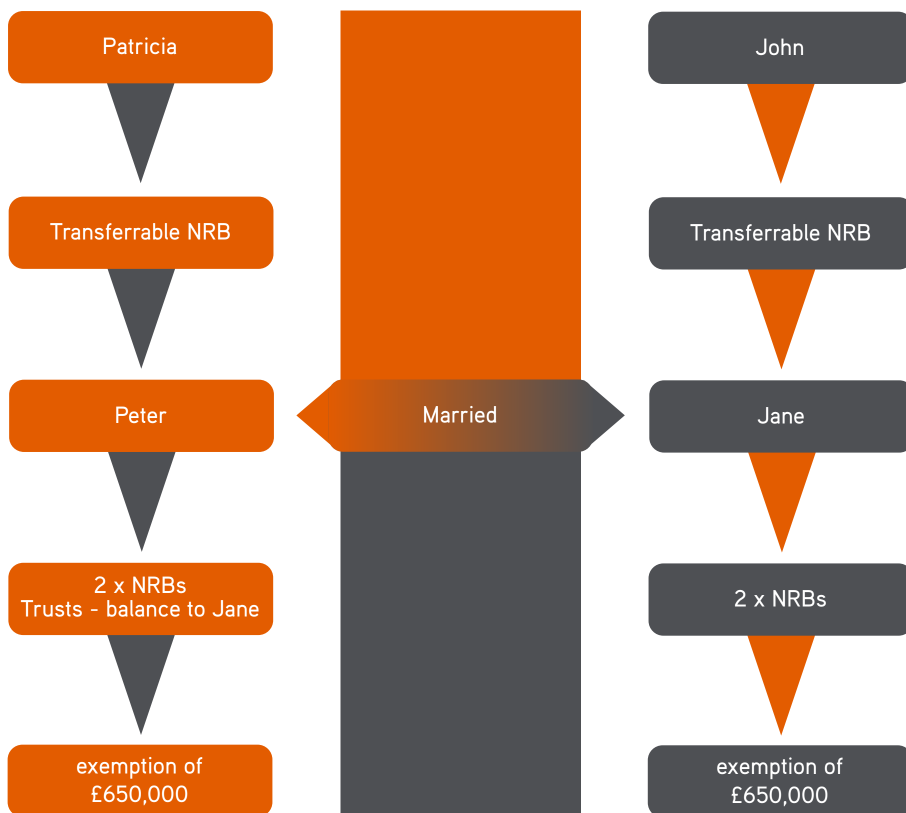
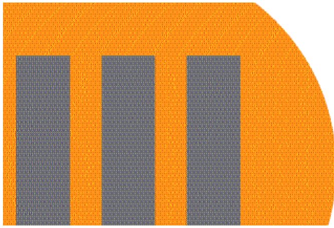


"In effect, therefore, the combined estates of Peter and Jane have had the benefit of four NRBs"

This Brief aims to update you on legal issues of concern or interest. It not a substitute for taking specialist advice in individual cases, for more information about these or any other issues please contact a member of our team



7 SIMPLE STEPS TO REDUCE INHERITANCE TAX

Whilst there are many complex ways of reducing one's inheritance tax liability it is important not to forget the simple, less controversial steps which can be taken during one's life. If action is taken early enough considerable sums can be passed to the next generation. The following should be considered:-

1. Annual Allowance

Up to £3,000 per annum can be given away free of inheritance Tax, for example, you could give £3,000 to one child or £1,000 each to three children. If the allowance is not used in one tax year it can be carried forward for one year and used in the following tax year. For example, a married couple who made no gifts in 2008/9 can now give away £12,000 between them.

2. Marriage Exemption

In consideration of a marriage or civil partnership each parent of the couple can give to either party £5,000 and each grandparent or remoter ancestor £2,500. Other persons can give £1,000.
For example, if each party to the marriage has two parents and four grandparents all eager to use the total exemption available they can be given a total of £40,000.

3. Normal Expenditure out of Income

Provided the gifts are regular and leave the person making the gift with sufficient income so as not to affect their standard of living there is no limit to the amount which can be given under this exemption. HM Revenue & Customs are, however, eager to restrict the use of the allowance and good record keeping is essential as after the death the Executors will need to demonstrate the commitment to regular gifts and produce records of income and expenditure showing that the gifts did indeed come from income.

4. Small Gifts Exemption

There is no limit to the number of £250 gifts which can be made in any one tax year provided that they are each to different persons. It is, however, important to remember that this cannot be combined with the £3,000 annual exemption so that, for example, a gift to A of £3,000 and a gift to B of £250 is completely exempt but a gift of £3,250 to A leaves £250 chargeable.

5. Spouses and Civil Partners

There is no limit to the amount that one can give to one's spouse or civil partner provided that they are domiciled in part of the UK. While not to be undertaken for solely financial reasons couples in a long term stable relationship who are not married or in a civil partnership should consider formalising the relationship. This is particularly true following the introduction of transferable nil rate bands. For example, A and B are in a long term relationship. A has little or no assets but B has assets worth £650,000. A dies first followed by B who leaves his estate to their two children. If they are unmarried the inheritance tax on B's death is £130,000. If they are married the inheritance tax is nil. Marriage is not, however, to be undertaken lightly and careful consideration should be given to all the implications.

6. Live Seven Years

There is no limit on the amount which can be given away free of Inheritance Tax provided the person making the gift survives 7 years. For obvious reasons this type of planning needs to be undertaken sooner rather than later.

7. Sharing Your Home

Particularly useful where adult children continue to live with their parents s102 Inheritance Tax Act 1984 means that a share of the house can be given to the child without reservation of benefit problems.

Gifts can impact on other taxes and advice should always be sought before undertaking tax planning.

For more information on these and other inheritance tax planning strategies please contact:

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TO MARRY FOR LOVE NOT MONEY?

Marriage and Civil Partnership form a binding contract between two parties. Children are perhaps the strongest commitment of all. Parties can attempt to control their positions, in the event of a separation, by entering into written agreements to regulate their position, in the form of Cohabitation Agreements. Prior to, and following marriage or civil partnership, parties can enter into Pre and Post Martial and Civil Partnership Agreements. It is astonishing that more people do not seek legal advice with regard to their position, and put it in writing before they enter into such commitments.

It is for precisely this reason that there has been, particularly over the last fourteen or so years, a significant change in the judiciary's thinking surrounding these agreements.

Pre-marital and Pre-Civil Partnership agreements

Background

In a case in 1995 the judiciary considered that such agreements should not be part of their decision making process. It was considered that a judges' wide discretion should reign supreme to decide individual cases dictated by the legislation which has been in place since 1973.

Historically, a Pre-Nuptial Agreement was considered as one of the factors to take into consideration, often outweighed by other factors.

Agreements are no longer considered to be contrary to public opinion. The fact that parties are precluded from exercising their own autonomy has been seen as somewhat patronising. Adults may wish to exercise control in the event of their separation, in terms of avoiding emotional turmoil and significant costs, by providing in a written binding agreement what will happen upon separation.

There was a significant change in the judiciary's opinion following a landmark case of Crossley v Crossley (2008). In this case the agreement was considered to be elevated to the position of having "magnetic" importance. This appeared a "paradigm" example of when an Agreement should be upheld. The circumstances were that the parties were independently advised and it was a short marriage.

Most recently in an Isle of Man case the court sought to define when such agreements would be considered to be legally binding. It clarified that when a couple have entered into an Pre-Marital Agreement, and subsequently enter into Post-Marital Agreements, the last of those Agreements being in close proximity to the date of the parties' separation is likely to be extremely persuasive.

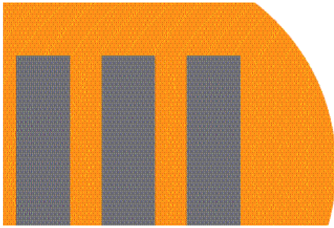
Further clarification was provided by the three Lords sitting in a Court of Appeal case known as Radmacher –v- Granatino (2009) EWCA Civ 649. It was confirmed in this case that the Agreement should be given decisive weight.

Facts

The judge provided the husband with an award in similar terms to that which he could have expected to have received, following a financial award providing for the children. It is interesting to note that a similar award could have applied if the parties were unmarried.

The settlement unanimously decided upon was to uphold the Pre-Nuptial Agreement. The fact that the Wife (39) was German and the Husband (37) was French was an important factor, because the Agreement would have been upheld in both jurisdictions of the parties' origin. However, the case was surprising because of the following factors:

- it involved a eight year marriage;
- there were two children, aged 7 and 9 years old;
- the husband had not been independently advised;
- the parties had not disclosed their assets to one another;



- the husband's earning capacity had reduced ten-fold (from when the Agreement was prepared) from £330,000 per annum to that of an academic. The wife was considered to be worth up to £100 million, with significant inheritance prospects.

From the High Court's decision, an award to the husband was reduced from over £5 million to £1 million to capitalise upon maintenance for the children. The sum of £2.5 million was awarded for a property for the husband to care for the children. This was to be held upon trust until the youngest child reaches 22, at which point ownership of the Property will revert back to the wife. The wife had conceded that she would pay £700,000 for the husband's, not insignificant, debts! We await to see if the husband shall be successful upon House of Lords, upon his application for appeal having been refused by the Court of Appeal.

Judicial guidance

The Lords laid down clear guidance in this case which if followed, can lead to such agreements being upheld. The following guidelines should be followed:

- the parties entering into the contract should be independently legally advised;
- there should be no fraud, mistake or pressure applied to a party proposing to enter into an agreement;
- the parties should fully disclosed their full financial means;
- any significant change in circumstances should be provided for, or else trigger a review to meet a parties' basic needs in the future. Such matters should include significant changes in earning capacity, inheritance and to meet the parties' needs following the birth of children;
- the agreement should not be expressed to oust the jurisdiction of the Court;

Conclusion

Written contracts are not just for the wealthy. They provide a way for parties to protect their wealth and inheritance prospects. They should be a significant consideration for more mature couples, seeking to protect their assets for children of a previous relationship.

For these reasons it is, of course, important to give serious thought to the preparation of a Will alongside a Cohabitation Agreements and Civil Partnership Agreements which the parties would be well advised to consider revising at regular intervals of not more than every five years.

The judiciary are seemingly attempting to move the law of England and Wales in line with the rest of Europe.

It is important to restore the public's confidence with regards to awards in divorce cases, to avoid what could be considered excessive awards. This has been most particularly seen in, for example, high profile divorce cases, when considerable sums of monies are awarded to parties even in the case of very shortest of marriages, as noted in the case of Miller -v- Miller (2006). The facts of this case involved a wife who was awarded £5 million of the husband's fortune of £17.5 million, (plus interests in shares of in the region of £15 million), following a marriage which did not make its third anniversary.

> "Written contracts are not just for the wealthy they provide a way for parties to protect their wealth and inheritance prospects"

In summary, the Pre-Nuptial and Civil Partnership Agreement can be an extremely useful tool to be employed for wealth preservation.

They can be an extremely effective measure to preserve assets, alongside, for example, setting up particularly foreign trusts to avoid assets being subject to proceedings involving divorce or upon the dissolution of a Civil Partnership.

Provided the principles as outlined above are followed then such contracts should be upheld, because fairness should be achieved. If partners do not agree their position they are leaving the decision making process in the hands of the Courts, whose decision may not suit either party. A position which seeks to reduce the stress and significant cost to couples and families following a separation should be given serious thought.

The Law Commission are working to implement legislative provisions regarding such Agreements, in 2012.

The next Mr John Cleese or Mr Paul McCartney who steps into the office may certainly wish to have one!

To discuss this topic further please contact the writer,
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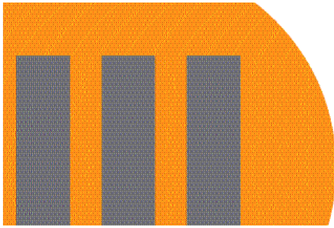

LASTING POWERS OF ATTORNEY - THE FACTS

What is a Lasting Power of Attorney (LPA)?

A Lasting Power of Attorney (previously called an Enduring Power of Attorney) is a legal document which allow you to appoint someone you trust, called your 'Attorney' to make decisions on your behalf and manage your finances and affairs (and potentially make decisions relating to your health and welfare) should you become unable to do so yourself.

Types of LPA

There are two types of LPA. One is called a Property and Affairs LPA and the other is a Personal Welfare LPA.

A Property and Affairs LPA gives your Attorney authority to deal with your bank and manage your financial affairs; buy and sell property on your behalf; handle your pensions, benefits and taxes; manage your income to pay your care costs and apply for NHS care funding or to social services for help financing elderly care.

A Personal Welfare LPA allows your Attorney to make welfare and healthcare decisions on your behalf, only when you lack capacity to do so yourself. This can include where you should live and what sort of care you should have. This could also extend, if you so wish, to giving or refusing consent to the continuation of life sustaining treatment.

Why do you need a LPA?

LPA's are predominantly used if a person has lost physical or mental capacity to deal with their own affairs, however the LPA can also be an invaluable document if someone just wants some assistance with their financial affairs. While LPA's are most often used to deal with the affairs of the elderly, if they are prepared much earlier in life they will give the same protection in the event of incapacity as the result of an illness or accident.

What about Enduring Powers of Attorney (EPA)?

If you have an existing EPA then this will remain valid indefinitely but you cannot make a new one. You may wish to consider making a Personal Welfare LPA to sit alongside your existing EPA (remember EPA's only cover property and financial matters).

The LPA in more detail

Your Attorney will only be able to act when the LPA has been signed by you and your Attorney, certified by a person (known as a Certificate Provider) who has checked that you understand the nature and scope of the LPA and that you have not been unduly pressured into making the power. The Certificate Provider will also need to confirm there has not been any fraud or another reason why you cannot make the power. It must then be registered with the Office of Public Guardian (OPG) before it can be used. Registration takes approximately 8 weeks depending on OPG workloads. The financial LPA can be used both when you have capacity to act, as well as if you lack mental capacity to make a financial decision. The welfare power can only be used if you lack mental capacity to make a welfare or medical decision. The OPG fee for registering an LPA is £120.00 (since 1st April 2009).

What's new?

After two years of teething problems with the LPA forms (in terms of it's length and some of it's limitations), the good news is that the OPG has now listened to representations from Solicitors for the Elderly, the Society of Trust & Estate Practitioners and the Probate Section of The Law Society (all of which many of Martineau Private Capital Team are members) and more user-friendly forms are to be issued in time for the second birthday of the LPA in October 2009.

What is the alternative?

If you do not have an EPA or LPA in place and you subsequently lose the mental capacity to make decisions, then someone, usually a family member, will need to apply to the Court for a Deputyship Order authorising them to make certain decisions for you. This procedure is ultimately more costly and complex as well as time consuming than making a LPA and can be very distressing and frustrating for family members who are trying to act in your best interests.

Martineau View

At Martineau, we look at having the LPA as a form of protection which might never been needed but would be crucial should such circumstances arise. No-one likes to imagine a time when they cannot manage their own affairs, but this could happen to you. We can tailor the LPA to suit your individual requirements and can assist you with deciding whether it is appropriate in your circumstances to include restrictions or guidance in the document itself.

For individual advice about making an LPA then please contact the writer.

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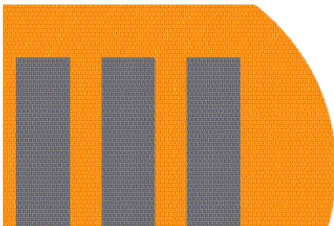

TREBLE YOUR LOCAL GIVING WITH COMMUNITY FOUNDATIONS

Places matter, and nowhere more so than your own community. Maybe this is why so many people choose to support the charities on their doorsteps. If you are one of them, a new government scheme can match your long-term local donations, making them worth up to three times more.

Whether you live in a city, town or village, local groups in your area will be running community projects. They have low overheads and make their communities better places to live.

Local benefactors who want to support such groups face hurdles. Without investing a lot of time and effort, how can you know which projects are the best? How can you be certain that your donation will be spent as you ask? And how can you get reliable feedback on the difference it made?

This is where Community Foundations can help. These are independent community grant-makers within a defined area, usually a county or city. There are 57 in the United Kingdom, covering 95% of the country. Collectively, they gave £66,000,000 to 20,500 projects last year.

They act as a channel between individuals, families and companies who want to support grassroots projects, and the groups that make those projects happen.

Community Foundations are rooted in local neighbourhoods and have excellent connections to small, volunteer-led groups. They also hold funds for many supporters of community activity. This enables them to match the right project to the right supporter. For example, an anonymous individual in South Warwickshire wanted to put some of his inheritance back into his community.

He established a fund with the Heart of England Community Foundation, which covers Coventry and Warwickshire. His fund has all the tax benefits of a private trust but none of the legal responsibilities. The Foundation finds projects that match his criteria – youth work within a 15-mile radius of his village – and he decides which he wants to support. He gets regular reports, and is delighted with the service he receives.

Companies are also choosing to use the grantmaking expertise of their local Community Foundations. This means they can meet corporate social responsibility targets in the same place that their staff and customers live. Rolls Royce, AXA and National Grid are just three that have chosen to invest in their local community in this way.

Until March 2011, most Community Foundations are running a programme called 'The Grassroots Endowment Challenge' which can double – and in some cases even treble – your net contribution to your local community. In a ground-breaking initiative, the Office of the Third Sector is offering £50 million matched funding for gifts of money, shares and property which provide long-term benefit for grassroots groups. Community Foundations running this scheme on a £1 for £1 basis can therefore more than treble the net contribution of a higher-rate tax payer:

Donation	10,000
Community Foundation recovers Gift Aid (~28%)	2,800
Donation plus Gift Aid	12,800
Plus match funding (1:1)	12,800
Total donation	25,600
Tax recovered by higher rate tax payer	2,500
Net cost to donor	7,500

Donors who give on a larger scale can create their own 'Named' Grassroots Fund and smaller donations will go into shared funds. The earnings will be awarded as grants, and the capital remain to help small groups for years to come. This gives a vital source of future support.

There are some provisos. You cannot name specific groups to be supported; grants must support small, volunteer-led organisations; and the scheme only applies in England. But if you want your charitable contributions to stay local, this offer is a good way to boost your own giving levels.

The programme finishes in March 2011, and if you want more information, or to find your local Community Foundation, call the Community Foundation Network on 020 7713 9326 or go to www.communityfoundations.org.uk.

For more information please contact our guest writer direct.

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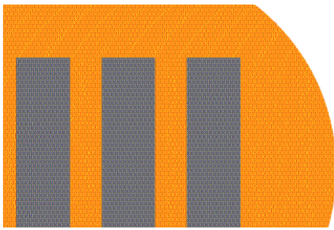

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WHAT HAPPENS IF YOU DIE WITHOUT MAKING A WILL

ARE YOU MARRIED?

YES

- Is your estate worth more than £250,000
  - NO → Spouse gets everything
  - YES → Do you have children?
    - YES → Spouse receives:
      - Household contents & personal effects
      - First £250,000
      - A life interest in half of the residue
      - Rest shared equally between your children (or their descendants)
    - NO → Are either of your parents still alive?
      - YES → Spouse receives:
        - Household contents & personal effects
        - First £450,000
        - Half of the residue
        - Rest shared equally between your parents or all to the surviving parent
      - NO → If you have brothers or sisters, are both of their parents the same as yours?
        - YES → Spouse receives:
          - Household contents & personal effects
          - First £450,000
          - Half of the residue
          - Rest shared equally between your brothers & sisters (or their descendants)
        - NO → Spouse gets everything

NO

- Do you have children
  - YES → Shared equally between your children (or their descendants if any have died)
  - NO → Are either of your parents still alive
    - YES → Shared equally between your surviving parents
    - NO → If you have brothers or sisters, are both of their parents the same as yours?
      - YES → Shared equally between such brothers & sisters (or their descendants, if any have died)
      - NO → Is only one parent the same as yours?
        - YES → Shared equally between such brothers & sisters (or their descendants, if any have died)
        - NO → Are your grandparents still alive?
          - YES → Shared equally between your grandparents
          - NO → Do you have uncles or aunts who share both parents in common with your mother or father?
            - YES → Shared equally between such uncles and aunts (or their descendants, if any have died)
            - NO → Do you have uncles or aunts who share one parent only in common with your mother or father?
              - YES → Shared equally between such uncles and aunts (or their descendants, if any have died)
              - NO → Everything will go to the Crown

Notes:
1. children includes adopted and illegitimate children but excludes stepchildren
2. children receive their inheritance on reaching 18, or earlier marriage
3. descendants share equally the parts that the deceased parents would have taken
4. same principles apply to civil partners

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Making a Will is the only way to make sure that your estate passes to the people you want it to. Don't delay, make a Will today!