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# Tax Dodgers - Revenue Throws Down Gauntlet

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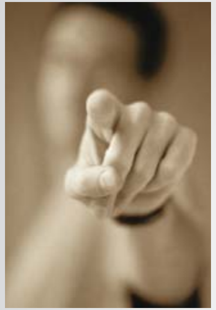

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HMRC have announced that they will proceed immediately to send out enquiry letters where they are aware of undeclared accounts belonging to taxpayers who have not taken advantage of the amnesty.

For those who have made a voluntary disclosure, HMRC's amnesty allows the back tax to be paid with interest plus a ten per cent penalty. As penalties for evasion of tax can amount to 100 per cent of the underpaid tax, the terms of the amnesty are generous. This makes it rather surprising that HMRC report that take up of the amnesty offer has been lower than expected, with over 40,000 people with income-bearing offshore accounts failing to declare them.

Recently, HMRC were given the right to obtain details of those who hold offshore accounts with the major High Street banks. This information is being collated by a recently-created civil investigations unit, set up to collect as much as possible of the several billion pounds of unpaid tax thought to be due on money currently held in offshore accounts. More recently still, HMRC have announced that they intend to extend their examination of offshore accounts to include all of the 550 banks which have a physical presence in the UK.

If you have a bank account outside the UK which earns interest, you will normally be liable to UK tax on the interest received, although you will also normally be able to claim a credit for foreign tax you have paid.

The taxation of foreign income is a complex area. If you have income from abroad, take professional advice on dealing with your tax affairs.

# Valuing Annuity Payments for IHT

When a person dies, there is often no right to receive any further payment under an annuity. However, many annuities are sold which have 'guaranteed minimum payment periods' - typically five years after the annuity first vests. In such cases, if a person dies before the end of the minimum payment period, further annuity payments will be receivable.

Valuing the right to receive such payments for Inheritance Tax (IHT) purposes can be problematic, but HM Revenue and Customs (HMRC) have an online calculator which provides an estimate of the open market value of the guaranteed annuity payments in straightforward circumstances. This consists of a form requesting the information necessary for the calculation to be made. In the view of HMRC, the estimate given by the electronic calculator constitutes a reasonable estimate of the open market value of the annuity for IHT purposes.

The form can be found at **http://www.hmrc.gov.uk/cto/forms/g_annuity.pdf.**

# IHT Planning

A Loan Trust provides a 'middle way' between making a gift of the original money and making no plans whatsoever. It is designed for those people who want to reduce their potential inheritance tax liability although wishing to retain access to the 'original' money but are prepared to 'gift' the growth on that money. Additionally they want to retain control over the gifted 'growth'.

This is achieved by the investor (settlor) establishing a trust and appointing trustees and beneficiaries. The settlor then makes an interest free loan of the original capital to the trustees. The trustees will use the loan to invest it, generally in a life assurance bond.

The loan is repayable to the settlor on demand. This provides the investor with access to the original capital. The settlor can also arrange to take 'repayments' of the loan on a regular bases, with access to the remaining balance of the loan. Once the loan is repaid the settlor cannot access any further monies from the trust and the total value is outside of their estate for IHT purposes. All that will be left at this stage is the growth and this is for the benefit of the beneficiaries.



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We have a substantial team of lawyers and support staff covering virtually all areas of legal work. If you need any advice or assistance please feel free to contact the following:-

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|---|---|---|
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| **Commercial and Civil Disputes and Employment Law** | Contact **David Pagett-Wright** | Tel: **01509 635433** |
| **Commercial Property and Company Law** | Contact **Tim Dunbar** | Tel: **01509 635458** |
| **Wills, Probate, Trusts and Wealth Management** | Contact **Kate Lees** | Tel: **01509 635405** |
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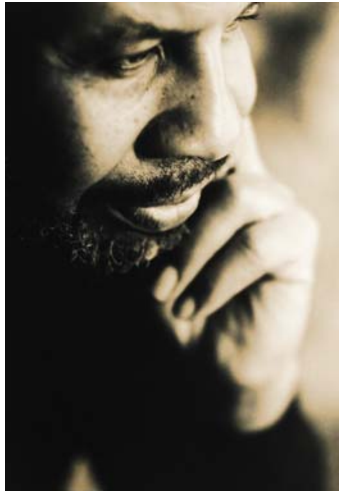
# DEPENDENCY CLAIM PERMITS LEGAL CHALLENGE TO WILL

The Inheritance (Provision for Family and Dependants) Act 1975 exists to allow dependants - who are not provided for out of the estate of a person to whom they are related or on whom they were dependent - to claim against the estate in appropriate circumstances.



A recent case considered whether a person who was eligible to make a claim under the Act could contest a will they believed to be forged. The claimant, who had lived with the deceased for several years, would have no claim under the will itself but she could make a claim under the Act and her claim would be more valuable were the deceased to have died intestate.

The will in point left the man's entire estate to his long-estranged wife and family. It was believed to be forged on the ground that it was alleged to have been executed at his estranged wife's house at a time when he could not have been there.

The man's family argued that the claimant could not contest the will as she had no interest in the estate except by way of her claim under the Act.

However, Judge Mackie QC held that the right to claim could amount to an interest in the estate for the purposes of challenging the will.

The practical impact of this case is that a will can be challenged in appropriate circumstances by a person whose only interest in the estate is a claim for provision to be made for them out of it. The number of such cases is likely to increase as more and more couples choose to live together without marrying or entering into a civil partnership.

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# Valuing Chattels

When dealing with an estate, an increasing problem for executors is the valuation of assets in the form of the chattels of the deceased. In probate terminology, chattels are the 'everyday' assets such as furniture and ordinary possessions, as opposed to houses, investments and the like. These latter assets are relatively easy to value as estate agents and other specialist valuers can be called upon and in the case of listed investments, their market values at any point in time are readily available.

One difficulty is that an increase in wealth and estate values generally has brought an increasing number of estates into the Inheritance Tax (IHT) net. Where the value of the estate is well below the IHT threshold (£300,000 for 2007/2008), even placing a relatively optimistic valuation on the chattels would probably not create an IHT liability. Where IHT must be paid, however, a realistic and justifiable open market value must be ascertained.

A second aspect of the rise in living standards is that it is more normal than it was in the past for people to have a substantial value in chattels. A side issue arising here is that many households may have an insured value for 'contents' which is well below the actual value of their household contents.

In general terms, when valuing assets for probate purposes, the appropriate valuation is the 'open market value' - the value for which they could be sold if a bargain were made between a willing buyer and a willing seller. Specialised assets, such as works of art, stamp, book and coin collections and so on, should be valued by a professional valuer if likely to be of significant value. Cars can be valued by reference to a trade guide and boats by a yacht broker.

Any items specifically mentioned in the will should be separately valued and, as a rule of thumb, individual items worth more than £500 should be assessed individually. Items which are widely traded (such as musical instruments) can, in some cases, be valued by reference to the prevailing prices on Internet auctions.

Another problem that is becoming more common occurs when there are a number of chattels, some of which may be valuable and some of which are not, and the relative value of each is not easy for the executors to know. Where the executor is likely to have the contents of the house cleared, it is possible for quite valuable chattels to be disposed of for little value or even thrown out.

When chattels are being distributed (say where there are three children, each entitled to a third of the chattels), it is also important for values to be known, because the distributions made will need to be equal unless agreed otherwise by the beneficiaries. Since many assets are in the form of sets (china and furniture for example), some horse-trading may need to be done and having an idea of the values of the different chattels will prove helpful.

If you have specific items of value, consider listing these and putting the list with your will - it will save your executor time and possibly prevent a valuable asset going unrecognised.

**For advice on making a will or on any aspect of family wealth protection, contact us.**



# IHT Nil Rate Band Trusts - Pitfall Exposed

The use of 'nil rate band' trusts for Inheritance Tax (IHT) planning is quite common, but a recent court case, which has attracted a great deal of attention, has pointed out a possible pitfall in such arrangements.

However, in spite of the adverse publicity, the case should not create undue concern, as a well thought out arrangement can avoid the problems.

IHT nil rate band trusts are used to avoid IHT on a couple's estate by passing an amount equivalent to the IHT nil rate band (£300,000 for the year 2007/2008) into a trust on the death of a spouse or civil partner, so that on the second death that sum is no longer part of the estate.

The case in point involved a transfer of a share in a property jointly owned by a husband and wife. When the wife died, her half share in their home was transferred into a trust, which transferred it back to the husband in exchange for his IOU.

The intended effect of the arrangement was that his estate would be reduced for IHT purposes by the extent of his debt due to the trust and that any further increase in the value of the property would be wholly exempt from Capital Gains Tax (CGT) because of the 'principal private residence' exemption. Had the trust retained ownership of a share in the house, the increase in the value of the trust's share would be subject to CGT.

When the husband died, the sum due under his IOU (£153,222.99) was claimed as a deduction from his estate, but HM Revenue and Customs (HMRC) argued that the sum was not deductible. Their reasoning was based on a section of the Finance Act 1986 (S103) which provides that a liability is not deductible if the consideration for the debt consists of property which 'derived from the deceased'. In this case, the wife had never worked so, in HMRC's view, the whole of the value of the house was derived from the husband's estate. The Special Commissioners of Tax upheld the decision.

However, this case need not cause undue alarm, since nowadays it is usual for both spouses or civil partners to work (at least at the beginning of the relationship) and in such circumstances HMRC's argument would be difficult to sustain. Secondly, had the husband predeceased his wife, or the transfer been dealt with by the creation of a formal charge over the property, the problem would not have arisen. Thirdly, alternative arrangements can be made which circumvent the problem.

The message for clients with substantial assets is clear - 'cookie-cutter' IHT and will planning should be avoided. Make sure that estate planning of any kind is only undertaken with legal advice.

# Variation of Wills after Death

Wills are made to give effect to a person's wishes as to how their property should be distributed after death. However, sometimes this does not produce the desired effect, for example where the family circumstances have changed since the will was made. There are a number of remedies which can be used in such cases.

To rectify a will, a court could declare it invalid, or it could add or omit words to give effect to the testator's true intentions. Wills can be declared invalid if the testator was not mentally capable or created it under undue influence from another person. Under the Inheritance (Provision for Family and Dependants) Act 1975, it is possible for anyone who can prove they were dependent on the testator to a material extent during their lifetime to claim a share of the estate if they have been excluded from the will. A long term cohabitee is also entitled to claim a share. A claim under the Act must be made within six months of the testator's death. A valid claim can be resolved either by a settlement between the claimant and the beneficiaries or by an order of the court.

Where the will is not disputed, variation can occur if a beneficiary disclaims a gift or if all the beneficiaries agree to vary the clauses. The latter option is called a Deed of Variation and it will give the new clauses the same effect as if they had been in the original will.

A Deed of Variation must be a written instrument and must have the written agreement of all beneficiaries. It must be made within two years of the testator's death. Minors cannot give consent. If any of the beneficiaries are minors, an application must be made to the court to obtain consent on their behalf.

A variation is normally sought where the will does not provide the outcome desired by the testator's family. Examples of this are when a beneficiary does not want to inherit an asset, where a person was excluded from the will when they were led to believe otherwise or where no provision was made for some of the testator's dependants. It may also be carried out to clarify or improve ambiguous drafting.

A particularly common reason for a beneficiary to refuse property is in order to reduce the Inheritance Tax (IHT) burden on the estate. For example, a Deed of Variation can be used to pass property to the testator's children, rather than to his or her spouse, in order to avoid IHT payable on the spouse's estate when he or she dies. The spouse might therefore refuse the gift and request it to be passed directly to the children. If the IHT bill is affected, HM Revenue & Customs Capital Taxes Office must be informed within six months.

Deeds of Variation are best suited to families who can agree on a desirable outcome - indeed, they are sometimes referred to as Deeds of Family Arrangement. They are not normally suitable where the will is disputed. Their most useful function is probably as an IHT planning device where the testator has not considered this.

Contact us if you would like advice on will or estate planning.

Partner Note: See articles in Accountancy Age, 19 April 2007 and 6 June 2007. http://pdf.accountancyage.com/aa_fe_190407.pdf?id=0.



# Inheritance Tax Planning or Legacy Planning?

David Wright, of Woodgate Financial Services looks to the questions facing individuals and families when considering Estate Planning.

I read an article recently which referred to 'Estate Planning' or what many people call Inheritance Tax planning. It referred to a survey of 2600 'baby boomers' people born between 1946 and 1964 - and their parents. It found that as children, parents and grandparents confront the issue of inheritance, they are discovering that they stand on opposite sides of a generation gap rife with misperceptions, misunderstandings, and the potential for lasting family conflict.

They found that everyone was focused on the wrong thing; many people wrongly assume the most important issue is money. While money isn't trivial, it belonged way down the list.

Today's inheritance issues are unlike any previous generation's. First, there's more property and wealth to be disbursed than ever before. People who grew up in the war years worry about the spendthrift ways of their children, who have grown up with state healthcare as well as an unprecedented boom in property and share values.

Secondly, family values have changed as families become more complex than ever before. Rises in the rates of divorce and remarriage as well as today's less conventional living arrangements have created a kaleidoscope of stepchildren, step-grandchildren, and children from multiple marriages.

Communication between generations is more vital than ever to ensure that the needs of elders and heirs are aligned. Unfortunately, while a majority surveyed claim to feel highly confident discussing the key elements of inheritance planning, less than 1/3rd of either generation has actually done so. And when they do, they often find that the discussions ignore the topics that each generation values most.

The miscommunications start with deep-seated reluctance to raise the topic of estate planning and inheritance in the first place. When they describe attempts to discuss inheritance and legacy, elders typically report that their children have their heads firmly buried in the sand.

"Most of my children don't want to hear about death," said one survey participant. "It's like, 'Don't talk about it. You're not going to die.'" Meanwhile, the children don't raise the issue because they're afraid their parents might think they're just after their money. "We're scared that our motives may be misinterpreted, that Mu m and Dad may think I just want their stuff.'"

For most people, "estate planning" and "inheritance" are dry terms. "Legacy," on the other hand, was found to be an immensely positive and emotionally resonant word. It suggests a road map for the future, a memorable and enduring imprint of someone's life or simply the implication that someone's life had meaning. Young and old uniformly agree that the most important pillar of a complete legacy is memories, values and life lessons.

Surprisingly, only 10% of children put high priority on financial assets. For them, money is the least-important aspect of a legacy. Personal possessions of sentimental value are three times as important. Even more surprising, nearly four times as many elders differ, ranking cash above a personal possession. Such statistics show the rifts that can rupture family ties and lead to bitterness and resentment.

Bridging the legacy Gap – Leaving a legacy that everyone can love depends on elders and adult children being able to bridge the communications gap. Clarifying plans and explaining intentions can make otherwise contentious decisions understandable and avoid lasting resentments. "My mother explained her motives and her emotions," one respondent recalls, "so it as easier for me to understand where she was coming from."

Knowing their parents' intentions helps adult children chart their financial future more reliably. Some 40% of children surveyed said that knowing what they would inherit made it much easier for them to make plans to pay off debt, to fund their children's education, and to boost their retirement plans. Similarly, more than 2/3rds of elders greed that such conversations would help them understand their children's wishes, so that they would better decide how to satisfy them whether those wishes were about money, a family holiday cottage, or a battered copy of Winnie the Pooh.

It doesn't help that whilst many adviser are competent in tax and trust issues, few are trained in how to understand and interpret family values and needs. As a result a huge opportunity is lost to make a lasting legacy during your lifetime. At Woodgate we are experienced in working with clients to leave them with a lasting legacy and not just a legal document, if you would like to learn how this approach may help you, why not ring our office on **01509 635467.**