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## Note from the editor



**Lizzie King**  
CTA ATT

Tel/Fax: 01993 886404  
E: lizzie@landtax.co.uk

Welcome to the March edition of our newsletter. With the rush to meet the self assessment filing deadline slowly becoming a distant memory, the anticipated wait for this years Budget and the end of yet another tax year, this issue looks at Inheritance Tax and related matters.

My thanks go to Rosamond McDowell of Collyer Bristow LLP who has kindly contributed two articles, on

Wills and Powers of Attorney. In addition to this, HM Revenue and Customs (HMRC) released a technical note on 13 December 2010 withdrawing some of their Extra Statutory Concessions, the full technical note can be found on the revenue website: [www.hmrc.gov.uk/menus/extra-stat-con-tn.pdf](http://www.hmrc.gov.uk/menus/extra-stat-con-tn.pdf).

## Inheritance Tax – the basics

### Lizzie King

Inheritance Tax (IHT) can be payable by Trustees or on gifts in an individual's lifetime. In this article I will be considering IHT payable on an individual's estate on death.

The Government brought IHT planning back into the spotlight in the 2010 Emergency Budget when it was announced that the IHT threshold would be frozen at £325,000 until 2014. With the possibility of house prices rising in the coming years, it may be the case that individuals who don't expect to pay IHT will be caught out.

If the value of your estate is below the IHT threshold (£325,000 provided you are not able to utilise any nil rate band from a pre-deceased spouse) then tax would normally not be due (unless lifetime gifts have been undertaken in

the 7 years prior to death). Where an estate exceeds the threshold and it does not directly pass to the deceased's spouse or civil partner, a 40% IHT charge will be levied on the value exceeding the available IHT threshold. Therefore, if your estate is worth £400,000, £30,000 in IHT would be payable.

Quite often IHT is overlooked during a person's lifetime because it is not a visible tax. Simple actions such as making gifts during your lifetime, writing a life insurance policy into Trust or making a bequest to charity might prevent an estate being subject to IHT.

Each individual can make gifts up to £3,000 in each tax year which are exempt from IHT. You can carry

forward any unused part of the £3,000 exemption to the following year but that years exemption must be used before any of the carried-over allowance, if you do not use it in that year, the carried-over exemption expires. The annual exemption is in addition to the other gift exemptions.

### Bits and pieces...

#### IHT

As much Inheritance Tax was collected in the first half of 2006/07 (£2.1 billion) as was collected for the whole of the 1996/97 financial year.

Some gifts made during your lifetime are exempt from IHT because of the type of gift or the reason for making it.

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Wedding or civil partnership ceremony gifts are exempt from IHT, subject to certain conditions and dependant on your relationship with the recipient. You can make small gifts up to the value of £250 to as many people as you like in any one tax year however; you cannot give a larger sum and claim exemption for the first £250. Finally, any regular gifts you make out of your after-tax income, not including your capital, are exempt from IHT. These gifts will only qualify if you have

enough income left to maintain your normal lifestyle.

On the death of the second spouse or civil partner you may now use any remaining allowance of the first spouse or civil partner to die, on top of their own allowance. In the current year, this would mean that potentially £650,000 worth of assets could be left without IHT being payable.

Many farm owners have previously thought they will be eligible for

Agricultural Property Relief and therefore their estate will not be subject to IHT on their death. With HMRC making prolonged and detailed enquiries into claims for agricultural relief this can no longer be assumed.

If your personal estate is worth more than £325,000 (£650,000 for a couple), tax planning could ensure that substantially more of your assets pass to your chosen beneficiaries rather than the Government.

# From lifetime planning to peace of mind



**Rosamond McDowell**  
Collyer Bristow LLP

Tel: 020 7468 7308  
Fax: 020 7470 4483

For many people, making a Will is a daunting prospect, raising questions of mortality which they would prefer not to address. It is, however, our legal privilege to provide for our nearest and dearest, as well on death as during our lifetimes.

## a, b, c... Three reasons to make a Will

### a. Planning

- Making a Will allows you to take stock of your property and plan how you would like it to devolve. You can appoint one or more executors to deal with the administration.
- You could set up a Trust in your Will to ensure your assets pass down the generations, to protect them from creditors or irresponsible

stewardship, or in second marriage situations.

- You may wish to make provision for charitable or philanthropic purposes.

### b. Avoiding the rules of intestacy

- In the absence of a Will, your estate could devolve according to the English rules of intestacy. These may not deal in accordance with your wishes, so for example the assets of a person who is married or in a civil partnership do not automatically pass in full to the surviving spouse or partner.
- The rules of intestacy may lead to an unnecessary charge to tax. This may sometimes, but not invariably, be avoided after your death by a deed of variation. Even then, if young children are involved, this could involve great expense.

### c. Saving tax

- It is no longer necessary for spouses to make specific provision for their

nil rate bands (ie the part of the estate which passes free of tax), since any unused portion will be transferred to the survivor. However, widow/ers in second marriages may be able to make use of three or even four nil rate bands, a tax saving of up to £260,000.

## Bits and pieces...

### Wills

One in three people die in the UK without making a Will.

- The impact of the rules of intestacy may give rise to a charge to tax on the death of the first of two spouses or civil partners, which can be deferred or even avoided by making an appropriate Will.
- With an appropriate Will and careful planning, the value of real property for Inheritance Tax may be significantly reduced.

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## 1, 2, 3... Five basic Will types

### 1. The Traditional Will

For partners who wish their assets to pass to the survivor. On the second death, children will take all in equal shares. Children's entitlement may be made contingent on them attaining a given age (eg 21, 25 or 30).

### 2. The Flexible Will

For partners who wish the survivor to have the right to the income of their estate. Capital may be distributed at the discretion of the trustees, but in principle will be preserved for children or other persons.

### 3. The Individual Will

For persons who wish to distribute their estate between named individuals or charities.

### 4. The Discretionary Will

For persons with complex affairs or wishes, who would prefer to leave their

trustees with ultimate discretion. Your wishes may be recorded in a separate letter.

### 5. The Generational Will

For persons who wish instead to skip a generation. Children or grandchildren will not take the property outright, but in trust.

## do, re, mi... Three potential complications

### do. Domicile and citizenship issues

If you hail from somewhere outside of the UK, your position may be complicated. For example the country of your domicile may not permit freedom of disposition, and certain jurisdictions, including the UK and the USA, have worldwide taxing regimes which attach to their citizens or domiciliaries, irrespective of their residence at death. With appropriate planning, your estate may escape the UK inheritance net entirely.

### re. Foreign property

If you own property outside the UK, community of property regimes, or rules of forced heirship or limitations on ownership may apply.

### mi. Second marriages

Providing for two families in a tax efficient manner can create complications. In some circumstances, the nil rate band may be doubled or even tripled, and with careful use of flexible trusts, you may be able to make tax free provision for your children.

Whether one of the five basic Wills types would suit you, or the complicating factors apply, meaning you need a more bespoke service, we should be happy to advise you, so that the process of making a Will is as easy as possible.

# Abatement Lizzie King

Quite often some considerable time can pass between someone's Will being executed and their death. This article looks at the implications this may have for the beneficiaries of a Will and the importance of regular reviews of your Will.

Between executing a Will and death you could acquire or dispose of your property. Your estate could increase or decrease in value leading to a difference between an estate at probate and the property considered when the

Will was written. Should this happen, your estate may not pass as you had intended.

### What is Abatement?

In respect of a Will, abatement is the reduction of the Executor's payment obligation to the beneficiaries in satisfaction of their legacies.

### When can Abatement be applied?

- when an asset bequeathed in a Will must be sold to settle an Estate's liabilities.

- when the settlement of an Estate's liabilities reduces the value of the net estate to less than the sums bequeathed.
- when a Will bequeaths more property than the testator had at the time of death.

The above are examples of when abatement can be applied are not an exhaustive list.

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**How is it applied?**

Liabilities (including administration costs and IHT) must always be settled in full before the net estate can be calculated and beneficiaries paid.

After the net estate has been calculated, the general rule to determine how property is distributed is to reduce residuary gifts first, then general gifts, and then specific gifts.

Each class of gift must fully abate before applying the rules to the next class. Where there is more than one gift in the same class, these will abate rateably, on the principle that 'equality is equity' (*Miller v Huddleston* (1851) 3 Mac & G).

**Types of gift**

- Residuary gifts are given to the residuary beneficiaries of the estate. They consist of everything not specifically disposed of by the Will. A common phrase used in a Will is "I give the rest, residue, and remainder of my estate to..." although no specific wording.
- A general gift is a gift of a specific value, such as £100, but it is general because only the value of the property has been specified, not its identity.
- Demonstrative gifts are general gifts from a specified source, such as "£100 from my savings account with X bank." These only abate if the source out of which it is expressed to be paid is exhausted

- A specific gift is a specific item that is given to a specific person, such as "I bequeath my wedding ring to my daughter."

**The all too common problem...**

...is that there is insufficient residue property to pay liabilities, costs and IHT. This deficit in residue causes the legacies to abate...

**The solution..**

..is to make sure that when you are drafting and/or reviewing your Will, the residue of your estate will be sufficient to pay liabilities, estate administration costs and IHT.

# When I'm sixty-four...

**Rosamond McDowell****From property and finances to health and welfare**

*"When you were young, you girded yourself and walked where you would; but when you are old, you will stretch out your hands, and another will gird you and carry you where you do not wish to go."* For many people, old age and incapacity is almost more daunting than mortality. Thankfully, our legal system enables us to put a framework in place to govern how decisions will be made.

**Lasting Powers of Attorney (LPA)**

- An LPA is a document by which you may appoint another person or persons (the "attorney") to act on your behalf if and when you are unable to do so yourself.

- The LPA may appoint more than one attorney, and set out in what circumstances they must act together (jointly) or may act separately (jointly and severally). A joint appointment will cease automatically if one of the attorneys is unable or unwilling to act.
- You may also appoint a replacement attorney, to act if the first-named attorney cannot.
- It is possible to include restrictions which will bind an attorney absolutely, e.g. a prohibition on the attorney dealing with a particular property or making certain medical decisions, and/or guidance to your attorney as to how he/she should act in particular circumstances.

- Once appointed, your attorney is obliged to act in accordance with statutory principles, the most important of which is that any act or decision on your behalf must be done, or made, in your best interests.
- There are two LPA forms. The first relates to property and financial affairs, and the second relates to health and welfare. You may make either or both of these.

**Will you still need me?**

- Decisions made under an LPA for property and financial affairs would include, for example, operating a bank account, making investment decisions, signing tax returns and buying and selling property.

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- The attorney is not permitted to make gifts (other than those usually made by you for birthdays or to charity), execute your Will or act as a trustee or executor in your place.
- This must be an independent person (not your attorney) who has known you for at least two years, or has the relevant professional skills to enable him/her to make the assessment, eg your solicitor or doctor.

#### Will you still feed me?

- Decisions made under an LPA for health and welfare would cover issues such as where you will live, your care and medical treatment, diet and dress and dealing with personal correspondence, information and papers.
- Importantly, your attorney cannot refuse life-sustaining treatment unless your LPA expressly says so. The form requires you to decide whether this decision should lie ultimately with your doctor or your attorney.

#### The Certificate

- The LPA must be executed by a “certificate provider”, who is able to confirm that you have capacity and understand the significance of making the LPA.
- An LPA may be cancelled at any point, before or after it is registered, so long as you have the capacity to do so.

#### Registration

- An LPA does not need to be registered as soon as it is made. However, it cannot be used until registered, and registration may take up to 6 weeks. In most cases, it makes sense to register the LPA immediately. Once registered, an LPA for property and financial affairs may be used immediately, unless it specifies otherwise. LPA for health and welfare may not be used until you have lost capacity.
- You will need to nominate at least one person who must be notified before the LPA is registered.

#### Advance Decisions (AD)

- You may also decide to make an Advance Decision (also known as a Living Will).
- This is a decision made to refuse medical treatment in the future if and when you lack capacity to consent to such treatment.
- An Advance Decision is not applicable to life-sustaining treatment unless it is specific, made in writing and signed, using the correct form of words, and witnessed properly.
- An Advance Decision may be withdrawn or amended, and if you make a later LPA which authorises your attorneys to make decisions in relation to the same situation, then it will be overridden automatically. Conversely an Advance Decision made after an LPA will bind your attorneys.
- It is important in practice that you notify all relevant people of having made an Advance Decision, and that your medical records are updated accordingly.

# VAT: Connection to gas or electricity mains supply HMRC

The current concessionary arrangement which allows first time connection to utilities to be treated as zero rated for VAT will be withdrawn with effect from 1 January 2012.

#### Background

The concession allows zero rating for the first time connection to the gas or electricity mains supply of dwellings, communal residential and non-business

charitable buildings, residential caravans and houseboats. Under the terms of Notice 701/20 Caravans and houseboats, HM Revenue and Customs (HMRC) additionally allows concessionary zero rating for first time

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## Bits and pieces...

### Powers

Standard Life carried out a survey in 2006. It showed that 74 percent of people asked did not have a Power of Attorney.

connection of non-residential caravans to the gas or mains supply and for first time connection of caravans and houseboats to water and sewerage, where the relevant charge is made by the caravan site owner or moorings provider.

There are no legal vices in EU law which would permit this Extra-Statutory Concession to be introduced

in UK legislation. After the concession is withdrawn, first time connection to electricity or gas will be subject to the reduced rate of VAT if the utility is for domestic or non-business charity use and the connection charge is made by a person who supplies the fuel.

Charges made by caravan site owners and houseboat mooring providers for first time connection to electricity, gas, water and sewerage will be subject to the same VAT liability as the caravan pitch or mooring (standard rated or exempt, depending on the circumstances) unless the site owner or mooring provider can identify the

actual consumption of users (ie through metering), in which case, the connection charge will be subject to the same VAT liability as the supply of the utility (reduced rated for electricity and gas, zero rated for water and sewerage).

For further information about domestic or non-business charity use, see HMRC Notice 701/19 Fuel and power.

## your feedback...

We would like to know if there are any particular issues which are important to you and that you feel we should cover. Please do get in touch.

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### landtax

**Mitre House, Lodge Road, Long Hanborough Business Park, Long Hanborough, Oxfordshire, OX29 8SS**  
**Email: [info@landtax.co.uk](mailto:info@landtax.co.uk) Web: [www.landtax.co.uk](http://www.landtax.co.uk)**