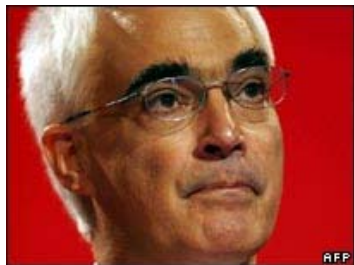




October 2007 Pre-Budget Report



Inheritance Tax

The existing Nil Rate Band (NRB) of £300,000 remains the same with phasing to £350,000 by 2010.

In the case of a married couple/civil partners the NRB can be transferred to the survivor IF NOT used up by the first to die. The survivor inherits the tax free band at the level it is when the surviving spouse dies and **not** at the level it was when the first spouse died.

Example 1: Husband and wife both make Wills leaving everything to the other. Husband dies 1 May 2007 (when NRB is £300,000). Wife dies in 2010 when NRB is £350,000. Wife has a nil rate band of £700,000.

Example 2: Husband's and wife's Wills leave £150,000 to children on first death. Husband dies 1 May 2007 (when NRB is £300,000). The gift to children uses half of his NRB – the other half is transferred to wife. Wife dies in 2010 when NRB is £350,000. Wife has a nil rate band of £525,000 (£350,000 + £175,000).

This applies to all existing widows/widowers/civil partners where their spouse/civil partner has already died irrespective of the date of death. It would seem that there can only be **one** carry-forward in the case of those who marry more than once.

Impact on IOU DWTs

This would mean that anyone leaving their entire estate to the surviving spouse direct **WOULD NOT** need an IOU DWT if their joint estate is below the threshold, but it equally means that anyone wishing to actually direct assets on second death whilst leaving flexibility to the surviving spouse to benefit from such assets during his or her lifetime **WOULD** continue to need a discretionary will trust or a property trust in their Wills.

One of the side benefits of the IOU DWT is that it locked the nil rate band for the children and it could not be passed on to a new spouse and, further, it protected the amount within the nil rate band from care home charges which, after all, can decimate an estate more than IHT.

These proposals are to have immediate effect though it will no doubt be some time before the necessary legislation is effected, and it has often been

the case that what is proposed in a pre-budget report is not subsequently enacted into law in exactly the same specification as had been originally proposed.

Where the joint estate is above the threshold (i.e. over £600,000) there could still be an advantage in using a NRB DWT as any increase in value due to investment performance will also be outside the survivor's estate. Where the value of half the house is used (by means of the IOU) the loan can be index linked with the result that the debt on the surviving spouse's estate is far greater than the carried forward nil rate band. Clearly, however, tax planning Wills may become a slightly harder sell as will deeds of variation (although the increase in value argument could similarly apply).

In the case of existing Wills with DWTs there is no immediate need to rewrite them, there may be just **less** point in setting up the trust on the first death. The caveat to that, of course, is that few of us have the crystal ball that can predict the overall estate value and our individual needs at the point of death some years in the future.

The proposals do not reduce the need for couples or individuals to make a Will. Only through making a Will are



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couples (married, civil partnership, living together) able to pass on their assets to those that they would wish, provide for guardians for young children and ensure that proper trusts are written for children to inherit at an age more sensible than 18. And of course anyone with qualifying business assets would benefit from a business property trust.

The Intestacy laws remain unchanged.

Married couples owning property

Married couples may now face considerable unforeseen risks. They may not need to undertake any IHT planning if their joint estate is likely to be worth less than £600K, (£700K by 2010). But, this may leave the main home, and any other properties at risk of being lost in the future., for example:

1. If the surviving spouse remarries after first death, any existing children may lose their inheritance if the surviving spouse then dies and the new spouse inherits.
2. If the remarriage ends in

divorce then this also puts the estate at risk of any divorce settlement not in favour of the children from the first marriage.

3. If the surviving spouse needs long term care after first death, Social Services are likely to demand that any property be sold to pay for the costs of that care.

In other words, Estate Preservation/Property Trusts now assume much greater significance for many people without any current tax planning in their Wills.

An updated Briefing Note on Estate Preservation will be issued shortly.

Unmarried couples

Unmarried couples, whose joint estate is worth more than £300k, and who *do not intend to marry*, are in the same situation as married couples were in before the Pre-Budget report. IHT will be charged on second death on all amounts above £300k, at 40%.

Unmarried couples may still benefit from using the IOU DWT to reduce their potential IHT liability. This would prevent 'bunching' of assets on the second death i.e. if £300,000 was put into a DWT on first death it is not aggregated with the survivor's estate when they die.

Remarriage

If you were to remarry then the inclusion of the IOU DWT in the Will of your first spouse would give you the opportunity to **treble-up** on the NRB! If you stuck with simple double Wills you would lose the NRB of your first spouse as you would only be able to carry-forward the NRB of your second spouse.

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