JOHN LAMB
FINANCIAL PLANNING

Insights

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In this issue

OTS REVIEW OF INHERITANCE TAX

The Chancellor of the Exchequer has requested that the Office for Tax Simplification (OTS) carry out a review of inheritance tax.

The main directed focus appears to be on ensuring that the administration and payment system of the tax is fit for purpose and as simple as possible. It is thought that the experience of taxpayers should be as smooth and clear as possible. All laudable aims.

It also seems that the OTS is to consider how the current rules for gifting interact with the inheritance tax system generally, and whether the rules as they stand cause any distortions to taxpayer decision making in relation to transactions connected with estate planning.

ON-TIME SELF-ASSESSMENT RETURNS BREAK THE RECORD AGAIN

In another record breaking year for the number of self-assessment returns submitted on time, HMRC has revealed that 10.7 million customers submitted their self-assessment return before the 31 January 2018 deadline.

Proving increasingly popular with its handy tips and helpful advice, HMRC's online service was used by 9.9 million customers – meaning more than 92.5% of total returns were completed online.

There were 758,707 people who completed their return on the last day before the deadline. The most popular hour for customers to hit 'submit' was from 4pm to 5pm on 31 January with 60,596 returns received, and thousands of customers avoided any penalties at the last minute as 30,348 customers completed their returns from 11pm to 11:59pm.

SCOTLAND TWEAKS ITS INCOME TAX REVAMP

The Scottish government announced a radical change to the structure of income tax in its Budget on 14 December 2017. At the time we noted that "The Scottish National Party does not have a majority in the Scottish government, so the proposals could change. This happened last year, when the Greens forced a freezing of the higher rate threshold". And, to no great surprise, that is what has happened again this time around.

Instead of increasing the 2018/19 higher rate threshold in line with inflation, the Scottish government has now announced a 1% increase. The threshold (which applies to earnings and National Insurance) will thus be £43,430 instead of the £44,273 previously proposed and the £46,350 applicable in the rest of the UK (and to the dividend and savings income of Scots).

The 2018/19 income tax system for Scotland now has the tax bands shown below, which should receive enough votes to pass into legislation.

Taxable Income £	Band Name	Tax Rate %
0-2,000	Starter	19
2,001-12,150	Basic	20
20 12,151-31,580	Intermediate	21
31,581-150,000*	Higher	41
Over 150,000*	Top	46

* Those with more than £100,000 income will see their personal allowance reduced by £1 for every £2 of income over £100,000

The £843 shrinkage in the intermediate band adds at most another £168.60 to tax bills and raises an extra £56m revenue. It also expands by £2,920 (£43,430 - £46,350) the band in which a Scottish taxpayer faces both higher rate tax (41%) and full NICs (12% for employees), a maximum total marginal rate of 53%.

COMMENT

At what point do high earners in Scotland decide to leave for pastures less taxing? Someone with earnings at the higher rate threshold in England (£46,350) will pay £787.50 less in tax than their Scottish counterpart.

POWERS OF ATTORNEY – MAKING GIFTS ON BEHALF OF THE DONOR

In the light of some recent judgments by the Court of Protection, the Office of the Public Guardian for England and Wales has updated its legal guidance for professional deputies and attorneys on making gifts of a protected person's property.

The new guidance in included in Public Guardian practice note PN7 updated on 18 January 2018. It does not make any new rules but clarifies the position in the light of a number of recent decisions from the Court of Protection (CoP). As most advisers will be aware, the power to make gifts by an attorney (acting under a Lasting Power or an Enduring Power) or a deputy is very limited.

From now on we refer to attorneys and donors but the same rules apply to deputies.

The basic rule

Attorneys can only make gifts on behalf of the donor:
- in some limited situations, and
- if it's in the person's best interests.

Donor's capacity

Before making a gift, an attorney must consider whether the donor:
- has the mental capacity to understand the decision to make a gift, and
- if they can take part in the decision.

If the donor has the capacity to make a gift, then they should normally make the gift themselves, rather than instruct the attorney to make it on their behalf. If the attorney considers that the donor has capacity to make a gifting decision, they should keep a record of the steps they took to make sure they did. However, the guidance goes on to state that even if the donor apparently has the capacity to make a gift, the attorney must still use care and caution when the donor expresses a desire to make one. If a substantial gift is involved, the attorney may need to seek advice or arrange for a mental capacity assessment, or both. If the donor lacks capacity then, as with all decisions an attorney makes, the main test is whether it is in the donor's best interests.

The "best interests" test

A best interests decision is not the same as asking what the person would decide if they had capacity. You have to think about:

- whether the person was in the habit of making gifts or loans of a particular size before they lost capacity
- the person's life expectancy
- the possibility that the person will have to pay for care costs or care home fees in future
- the amount of the gift – it should be affordable and no more than would be normal on a customary occasion or for a charitable donation
- the extent to which any gifts might interfere with the inheritance of the person's estate under their Will, or without a Will if one has to be created
- the impact of inheritance tax on the person's death.

Gifts which are permitted

The general rule for attorneys in relation to making gifts on behalf of the donor is simple: apart from some exceptions (set out below), the law states you must not make gifts from the person's estate.

To count as an exception, the gift must be:

1. given on a customary occasion for making gifts within families or among friends and associates (for example, births, birthdays, weddings or civil partnerships, Christmas, Eid, Diwali, Hanukkah and Chinese new year);
2. to someone related or connected to the person or (if not a person) to a charity the person supported or might have supported; and
3. of reasonable value, taking into account the circumstances in each case and, in particular, the size of the person's estate.

If an attorney wants to make a gift that falls outside the exceptions they must apply to the Court of Protection for approval.

Often the most difficult point will be the last one, i.e. whether the gifts are reasonable. This will, of course, depend on the circumstances. However, the Office of the Public Guardian (OPG) gives the following guidelines:-

To work out whether or not a gift is reasonable, you must consider:

1. The impact of the gift on the person's financial situation. You must consider not only their current and future income, assets, capital and savings but also their present and future needs. Consider whether their income covers their usual spending and will continue to do so in the future – and whether the gift would affect that.
2. Whether making the gift would be in the person's best interests (see above).

In deciding whether gifts are reasonable, the following should also be considered:

- are all members of the family being treated equally – if not, is there a good reason?
- is the attorney taking advantage of their position by making gifts only to himself or their family and not considering making gifts to others?
- is the proposed gift for someone who is not a relative of the person or closely connected to them? If so, the gift may be beyond the attorney's authority
- has the donor made gifts to someone before they lost capacity, and so would it be reasonable to give gifts to them now?

The guidance also states that the contents of a person's Will may be taken into account when making gifting decisions, as it is an indication of the donor's wishes.

What is a gift?

It is also important to remember that a gift is when you move ownership of money, property or possessions from the person whose affairs you manage to yourself or to other people, without full payment in return.

A gift can include:

- making an interest-free loan from the person's funds, as the waived (lost) interest counts as a gift
- creating a trust of the person's property
- selling a property for less than its value
- changing the Will of someone who has died by using a deed of variation to redirect or redistribute the person's share in the estate (meaning someone's property and money)

For any gifts which are not covered by the "exceptions", the attorney needs to apply to the CoP before they go ahead. The CoP has the power to either approve or refuse an application.

The guidance also states that any gift or transfer of real property (for example, land or a house) – either the whole property or a part share – is almost certainly outside of the attorney's powers despite what the donor might have said when they had mental capacity. To make such a gift, they are likely to have to apply to the CoP for permission.

Attorney accepting/taking gifts for themselves

The guidance suggests that particular care should be taken if an attorney is thinking of accepting a gift for themselves from the person's estate. The conflict of interests is obvious and an attorney must not take advantage of their position to benefit himself.

‘De minimis exceptions’ and inheritance tax planning.

The CoP has recognised that there are exceptions to the rule that an application to the CoP will always be required if the gift is not covered by the "exceptions" mentioned above. Those exceptions from the rule are when an attorney would go beyond their authority to make a gift but in such a minor way that it doesn’t justify a Court application – as long as the person’s estate is worth more than £325,000. These exceptions are often called ‘de minimis exceptions’.

Specifically, the exceptions can be taken as covering the annual inheritance tax exemption of £3,000 and the annual small gifts exemption of £250 per person, up to a maximum of, say, 10 people when:

a) the person has a life expectancy of less than 5 years;
b) their estate is worth more than the nil rate band for IHT purposes (currently £325,000);
c) the gifts are affordable, taking into account the person’s care costs, and won’t adversely (negatively) affect their standard of care and quality of life; and
d) there is no evidence that the person would be opposed to gifts of this value being made on their behalf

However, being able to gift small amounts up to the £3,000 annual and small gifts exemptions without the permission of the CoP doesn’t mean that an attorney can carry out any IHT planning without the CoP’s permission.

Neither can an attorney rely on other IHT exemptions to avoid applying to the CoP for permission to make a gift.

In one recent case, the Senior Judge at the CoP specifically stated that attorneys who want to make larger gifts for IHT planning purposes – such as setting up monthly standing orders to themselves – should apply to the CoP for permission.

All of the above is based on English law, as different rules apply in Scotland and in Northern Ireland.

COMMENT

The subject of powers of attorney, as well as Wills, is often a good starting point for discussing clients’ estate planning. Where the client acts as an attorney, making gifts as part of IHT planning for a donor will frequently come up in any such discussions and so all advisers should be familiar with the legal rules for such planning.

PENSIONS MISCELLANY

- The Pensions Regulator (TPR) has published a report on its decision to approve a major restructuring of the British Steel Pension Scheme by Tata Steel UK last year.

The report covers:

- key stages in the case; - how TPR assessed the application from Tata Steel UK for a Regulated Apportionment Arrangement (RAA); and
- - the proposal for a new pension scheme.

- The DWP has updated guidance to personal pension providers, trustees and managers of occupational schemes whose members hold safeguarded-flexible benefits and those charged with delivering information requirements on their behalf.

- This update includes a new section on valuation - paragraphs 1-11 - and some updates to the transitional provisions section.

- A further newsletter on relief at source for Scottish income tax is planned in mid-February 2018.

- HMRC has received questions about their information powers for pension schemes. Paragraphs 34B and 34C of Schedule 36 Finance Act 2008 allow HMRC to issue third parties with an information notice about pension matters in specific circumstances. Approval from the tribunal or taxpayer isn't needed.

THE CONTRACT (THIRD PARTY RIGHTS) (SCOTLAND) ACT 2017

The Contract (Third Party Rights) (Scotland) Act 2017 ("the Act") will come into force on 26 February 2018.

The Act implements the recommendations of the Scottish Law Commission to replace the old case law on the subject with a new statutory set of rules.

The new Scottish regime is similar to, but differs in certain important respects from its English equivalent, namely the provisions of the Contracts (Rights of Third Parties) Act 1999.

Under the new provisions in Scotland it will be easier for businesses to make contracts on a group wide basis, simplifying contracts and reducing uncertainty. For example, one company will be able to enter into a contract that will benefit other companies within its group.

In relation to financial services, and particularly insurance, it will be possible to make contracts for the benefit of third parties. For example, a travel insurance policy can be taken out by a parent for the whole family. Under the Act, beneficiaries should be able to make a claim even if they are not the contracting party.

In relation to life assurance contracts and, in particular, to certain employee benefit schemes, the ability to make contracts for third parties should be attractive in some circumstances. For example, employer-funded health insurance can be set up on the basis that an employee himself can make a claim rather than relying on the employer making a claim.

There are, of course, other possibilities including, for example, utilising methods favoured in certain European countries of writing life assurance policies for the benefit of family members or other named individuals. In the UK, typically, life policies are written subject to trust, which brings with it the complex and misunderstood law of trusts into play. If, instead of using a trust, the intended beneficiary can be given a contractual right as a third party under the policy, the objective of a speedy claim payment to the intended recipient could be achieved without a trust.

COMMENT

Although the English Contracts (Rights of Third Parties) Act mentioned above has been in force since 1999, no life office, to our knowledge, has yet ventured into writing insurance contracts for the benefit of third parties. Indeed, it is typical in any insurance contract under English law for this particular Act to be excluded. It remains to be seen whether companies and practitioners in Scotland will take up the challenge of exploring a new way of writing insurance contracts under the new Scottish legislation.

FEE REFUNDS AND POWERS OF ATTORNEY

The Ministry of Justice is offering partial refunds to those who registered a lasting power of attorney or an enduring power of attorney between 1 April 2013 and 31 March 2017.

Last year, the Office of the Public Guardian cut fees for registering a lasting power of attorney or an enduring power of attorney from £110 to £82 on 1 April 2017. The reason for the reduction was that the increasing volume of applications meant the registration fee income the Office received exceeded the cost of the service, which is meant to be on a not-for-profit basis.

The Ministry of Justice has now taken a further step and is offering to make partial refunds of fees paid between 1 April 2013 and 31 March 2017. These only apply if the power of attorney (enduring or lasting) was made in England or Wales and the claim must be made by either the donor (the person who made the power of attorney) or the attorney. The level of refund (including an alleged 0.5% interest) is based on when the fee (£110, or £55 for the reduced fee) was paid:

When the fee was paid	**Refund for each power of attorney***
April 2013 to September 2013	£54
October 2013 to March 2014	£34
April 2014 to March 2015	£37
April 2015 to March 2016	£38
April 2016 to March 2017	£45

* The refund is halved if a reduced fee was paid.

Claims can be made online or by phone (0300 456 0300 choose Option 6). Unfortunately, if the donor is dead, a claim can only be made by phone.

INCOME WITHDRAWAL RATE FOR FEBRUARY 2018

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in February 2018 is 1.5%.