

“ Plain speaking legal advice ”

## Tax planning Wills for Couples.

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It used to be the case that the conventional Will for a married couple provided that everything passed to the survivor, the problem with this was that in effect the Nil Rate Band (NBR) of the first party to die was thrown away. Since about 1992 the focus of most tax planning in Wills has been to find a way to preserve the NRB of the first party to a marriage so that when the second party dies there would be two NRBs available rather than one. The main vehicle for this sort of tax saving was the Nil Rate Band Discretionary Will Trust (NRBWT) usually coupled with a loan facility for the surviving spouse. At a stroke the TNRB has in effect removed the need for such complicated tax planning.

In these circumstances what should people be doing and should those with existing NRBWTs contained in their Wills be reviewing their Wills?

Up to now we have been extremely cautious about advising any action as there was always the fear that until the effect of the Pre-Budget Report was put into law the Government might change its mind. The Budget Speech on 13 March and accompanying press releases seem to make it clear that the Government is not going to renege and is not going to introduce any new anti-avoidance provisions. Accordingly, we now feel more confident to advise although at this stage the hyper-cautious might want to wait until the Finance Act is finally passed into law around about the first or second week in July.

That said here are our current thoughts on Wills. Very broadly speaking there are three options available to the average married couple. These are as follows:

- A Nil Rate Band Discretionary Will Trust
- A Will incorporating a Life Interest Trust
- An absolute gift of property to each other

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**Nil Rate Band Discretionary Will Trust** - the main objective of this is always to preserve the NRB of the first spouse to die so that when the second spouse dies there is two NRBs. For most couples this sort of Trust was effected via a loan back arrangement to the second spouse secured on the matrimonial home. Relatively few of these Trusts were created using cash or investments held by the first spouse. Our current view is that for a couple whose principal asset is their house there is probably little or no benefit in the use of the NRBWT with the loan back facility. However, if you are lucky enough to have substantial cash or investment assets available separate from the matrimonial home, then there are still considerable attractions in the use of the NRBWT.

- Firstly, and for reasons which we won't attempt to explain in this article, investments held in a well managed NRBWT portfolio can increase substantially in excess of inflation and in excess of the NRB threshold but can still pass free of tax when the second spouse dies.
- Secondly, Discretionary Trusts are very flexible and this can be extremely useful to a family.
- Thirdly, the use of Trusts serves to protect property if a surviving spouse remarries, goes into a nursing home or simply becomes incapable of managing his or her affairs. Property in the Trust is protected and will
- ultimately pass to the intended beneficiary

Interestingly, the NRBWT can be put to good use for couples who are unmarried or same sex partners who have not entered into a civil partnership. The problem for some couples is that when the first partner dies his or her NRB is lost if the estate is to be used for the benefit of the survivor. Using a NRBDS can preserve that NRB in almost exactly the same way as married couples.

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For those with an existing NRBWT included in their Wills the question arises whether or not this should be reviewed. The nature of a Discretionary Trust is that it can easily be amended after the first spouse has died and therefore it is arguable that no action needs to be taken. However this does leave you with a complicated Will that many people dislike. There are also costs associated with amending the Trusts at a later date. More importantly most of these Wills are in a format that would at a later date preclude the introduction of a Life interest Trust in the form that is suggested below.

**Wills incorporating a Life Interest** – a Life Interest is a right to benefit from property during your lifetime while not having ownership of that property. What this means is that the surviving spouse has a right to receive income derived from an asset or in the case of a house has the right to use the asset but does not have the freedom to dispose of that asset. Where a life interest arises under the Will of someone who has just died it is also called an Immediate Post Death Interest (IPDI), a title taken from the Finance Act 2006.

For the purposes of Inheritance Tax property contained in IPDI is treated as if it belonged to the person having the benefit of the life interest. In other words, if one spouse gives his or her estate to the survivor on an IPDI then it passes completely free of Inheritance Tax on the first death and is subject to tax on the second death. Prior to the October 2007 Pre-Budget Report this would throw away the NRB of the first spouse. However, post October 2007 this no longer applies and when the second spouse dies he or she would have two NRBs available.

The existence of the Trust structure provides protection for the property. As the surviving spouse is not the owner of that property he or she cannot dissipate the assets, nor should the assets be vulnerable to a second spouse or to nursing home fees. Inevitably this gives a little bit less flexibility to the surviving spouse but with modern trust structures this is much less of a problem than it might have been a generation ago.

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Life interest trusts can be structured in a number of ways. On one hand they can be highly prescriptive with the surviving spouse being entitled during his/her lifetime and then on death everything passing to the children of the marriage in proportions specified in the Will. On the other hand these trusts can be highly flexible with the Trustees given great power to vary the rights of both the spouse and or the children. This maximises the opportunity for tax savings and ensures that the needs of the family are properly looked after. There does have to be a high degree of trust between the surviving spouse and the Trustees, and in some cases this flexibility is not always welcomed by the surviving spouse.

**A simple Will giving everything to the surviving spouse** – this is in effect a reversion to what everybody used to do before the NRBWT was invented. It is by far and away the simplest of solutions, it preserves the NRB of the first spouse for use when the second dies. The disadvantage of this arrangement is simply that it fails to protect property, particularly against means testing or avaricious second spouses.

This article can only very briefly outline the principal options that are available and in very simple terms outline the pros and cons of each. For further advice please contact a member of our Private Clients team via [plainspeaking@herrington-carmichael.com](mailto:plainspeaking@herrington-carmichael.com)

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