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CONTENTS

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MIRROR WILLS AND MUTUAL WILLS

In a recent case the High Court held, on the basis of witness evidence, that a married couple had made mutual wills, despite apparently express wording to the contrary in each will.

There are not many mutual wills and there is even less case law on the subject so when a case like this comes along it is bound to be interesting.

Married couples often execute wills which are identical in their provisions, frequently giving the estate to the surviving spouse or, if the spouse does not survive, to the children. These are commonly referred to as "mirror wills". However, not every mirror will is a "mutual will", indeed very few mirror wills are mutual wills.

In both types of will the terms of the will of one person will mirror the other person's will. However, with an ordinary mirror will the survivor can make a new will after the death of the first to die without any constraints and without having to have regard to the will of the first to die. A mutual will, on the other hand, is a will which is also a mirror will but where the two testators enter into an agreement that they will not revoke their will without the consent of the other testator. The consequence of this is that if the first individual dies without having altered the mutual will, the surviving testator is not able to alter their own will. Indeed, if there is any later will made, it would be ineffective to the extent that its provisions are different from those in the mutual will.

The main reason why individuals make mutual wills is where both testators wish to ensure that specific intended beneficiaries benefit from their estate after the death of the second testator to die. This is often what the testators will be adamant about despite the fact that the arrangement is totally inflexible after the first of them dies. It would be usual to have something in writing confirming that the will is intended to be mutual. Conversely, very often in a mirror will there will be a provision confirming that the will is not intended to be a mutual will.

In the recent case of *Legg and Others v Burton and Others* [2017] EWHC 2088 (Ch) the Court found the wills to be mutual despite an apparent contrary wording in them. The Judge also stated that mutual wills might not require a contract and that they could be based on proprietary estoppel. *Estoppel* is an equitable rule which applies in English law whereby a Court may prevent, or "estop", a person from going back on a promise they have made. The result was therefore somewhat surprising and is perhaps a warning that a will may be considered to be mutual when this may not have actually been intended.

The facts of the case were as follows:-

Mr and Mrs Clark had each made mirror wills in July 2000, each giving their estate to the surviving spouse or, if the spouse did not survive, then to their two daughters in equal shares. The wills were professionally drafted by a solicitor who attested the execution. Both wills included the following clause:

‘My trustees shall pay my residuary estate to my spouse absolutely and beneficially and without any sort of trust or obligation’.

The wills also appointed the two daughters as executors and trustees. Mr Clark died in 2001 and his estate passed to his widow without the need for probate. Between 2004 and her death in 2016 Mrs Clark had made 13 separate wills, the last one being in December 2014 which left only small legacies to her two daughters with the remainder going to other beneficiaries. In that will Mrs Clark appointed one of her grandsons as the executor and he duly obtained probate.

The daughters challenged the 2014 will asserting that the original will executed in 2000 was one of a pair of mutual wills which therefore could not have been revoked by the later wills. The grandson executor defended the case on the basis that the 2000 will expressly provided that the estate was passing to the surviving spouse absolutely and beneficially without any sort of trust or obligation; therefore it could not have been a mutual will.

The two daughters claimed that the parents had made an agreement not to change their wills and this was explained to both of them as well as to the rest of the family at the time the wills were made. The Judge listened to the evidence from witnesses and clearly was more impressed by the evidence from the two daughters. He also examined the will carefully and concluded that the additional words about the assets passing to the surviving spouse absolutely and beneficially did not exclude the possibility of mutual wills, rather that this was a standard form of clause which is regularly found in wills of this kind.

In conclusion, despite there being no direct evidence that an agreement for mutual wills was entered into, the Judge decided, based on the witness statements, that an agreement had been made and that a promise not to change the wills, given orally to the daughters, was binding. The outcome of the case was that the two daughters inherited the entire estate and the beneficiaries named in the later will received nothing.

Comment

It may be of concern that even if wills do not expressly state that they are mutual wills, and there is an apparent provision that the survivor is to take absolutely and beneficially, this may not be enough to ensure it is not a mutual will. If there is a dispute, the Court is entitled to take into account extrinsic evidence and the reliability or otherwise of any witnesses will be of paramount importance.

When discussing wills with your clients, it is therefore important to explain that what is said about the will provisions may be just as important as what is written.

Interestingly, the Judge quoted a suggestion from an earlier case that it is inherently improbable that in this day and age a testator should be prepared to give up the possibility of changing his or her will in the future whatever the change of circumstances. It has to be said that, generally speaking, it would be unusual to recommend that clients should make mutual wills, given that changing circumstances in families these days are so wide-ranging and frequent. Surely, when drafting any will flexibility is likely to be an important factor. However, the Judge in the above case disagreed with this assertion, quoting an example of a testator who knows he is dying and therefore will have little interest in preserving his freedom to change his will in the future but every interest in ensuring that his wishes are carried out even after the death of the beneficiaries of his own will.

In short, every testator's circumstances will be different and all will depend on their wishes. Clearly it is important, though, that those making wills are aware of the consequences of their words, both written and spoken.

OFFSHORE TRUSTS AND NON-DOMICILED SETTLORS – THE NEW RULES

In this article we provide an overview of the complex new income and capital gains tax rules that apply to offshore trusts created by non-domiciled settlors and highlight some of the traps to watch out for.

Background

Trust income and gains can be attributed to settlors in certain circumstances under:

- The Settlements Code (ITTOIA 2005, Pt 5, Ch 5)
- The Transfer of Assets Abroad rules (ITA 2007, Pt 13, Ch 2)
- The Taxation of Chargeable Gains Act (TCGA) 1992, s86

Where the rules apply, a UK domiciled settlor will be subject to tax on income and gains as they arise; while a non-UK domiciled settlor can choose to be taxed on the remittance basis on overseas income/gains.

The Transfer of Assets Abroad rules and TCGA 1992, s87 can also create tax liabilities for UK resident beneficiaries who receive capital payments or other benefits from offshore trusts (although non-UK domiciled beneficiaries who elect for the remittance basis will only be subject to tax if the payment or benefit is remitted to the UK).

The new deemed domicile rules that apply for income and CGT purposes mean that, without protections, UK resident settlors with a foreign domicile of origin lose access to the remittance basis of taxation, and will thus be treated in the same way as UK domiciled settlors, once they have become deemed domiciled because they have been resident in the UK for 15 out of the preceding 20 tax years. In other words, they will be subject to tax on trust gains and foreign income on an arising basis.

The ‘protected settlement’ rules introduced in Finance (No.2) Act 2017 and Finance Act 2018 address this and ensure that settlors with a foreign domicile of origin will be treated more favourably than UK domiciled settlors (or settlors who are classed as Formerly Domiciled Residents – see ‘traps and anti-avoidance measures’ below) in relation to offshore trusts they create prior to becoming deemed UK domiciled under the new 15-year rule.

The new trust protections

The protections apply to settlors with a foreign domicile of origin both before and after deemed domiciled status is acquired under the 15 out of 20 tax years rule; and regardless of whether the trust was created before or after 6 April 2017. The criteria are simply that:

- The trust is a non-resident trust (i.e. with offshore trustees);
- It was created prior to the settlor becoming deemed domiciled under the 15 out of 20 tax years rule;
- No additions are made to the settlement, directly or indirectly, by the settlor (or by another trust either established by the settlor or of which the settlor is a beneficiary) after deemed domicile status has been acquired. What constitutes an addition for these purposes is widely defined and includes adding value to property held by the trustees; as well as a non-commercial loan made from the settlor to the trustees.

For as long as the trust meets the criteria for a ‘protected settlement’, ‘protected foreign source income’ will be allowed to roll up tax free, even if the trust is settlor-interested. UK source income of a settlor-interested offshore trust will continue to be attributed to the settlor in the usual way and taxed on the arising basis.

S86, TCGA 1992 is also disapplied so that trust gains (even if they arise in respect of disposals of UK assets) are not attributed to deemed domiciled settlors.

This makes non-resident trusts very attractive for non-domiciliaries – including those currently paying the remittance basis charge – as it means that most foreign income and gains can be rolled up in such trusts without the need to claim the remittance basis and pay the remittance basis charge.

When can tax charges arise?

(i) Income tax

UK resident, non-domiciled settlors will be subject to income tax by reference to benefits they receive from the trust that can be matched to foreign income. A UK resident settlor may also be taxed on income matched to benefits received by ‘close family members’ if the beneficiary is not themselves liable to tax (i.e. because he or she is either non-resident or a remittance basis user).

The term ‘close family member’ includes a spouse or civil partner, a cohabiting partner and the minor children of anyone in those categories.

As mentioned above, where the close family member is not themselves liable to tax on a benefit that they receive, the benefit is treated as received by the settlor. As a result of this a non-domiciled, remittance basis-using settlor will therefore only be liable to tax on the benefit if it is remitted to the UK by the close family member at a time when he or she is a ‘relevant person’ in relation to the settlor. The term ‘relevant person’ is defined more widely than ‘close family member’ and additionally includes minor grandchildren and the trustees of a settlement under which any other category of relevant person is a beneficiary. This means, for example, that if a distribution is made to a 16-year old child who does not remit the distribution to the UK until after attaining age 18, the settlor will not be taxable on the remittance (and nor will the child).

(ii) CGT

UK resident beneficiaries (including settlors who are beneficiaries) will continue to be taxed on trust gains to the extent that they can be matched with capital benefits they receive from the trust, with deemed domiciled settlors and beneficiaries taxed on benefits wherever paid (i.e. not on the remittance basis).

UK resident settlors will also be treated as having received capital payments made to close family members. However, one difference between this and the corresponding income tax rule is that, as far as capital gains tax is concerned, the gains are attributable to the UK resident settlor irrespective of whether or not the close family member would have otherwise been taxable on the benefit received. For example, if a distribution which is matched against gains is made to a UK resident and domiciled spouse of the settlor, those gains will be attributed to the settlor even though the spouse would, in the absence of the close family member rule, have been taxed on the distribution. If the settlor is a remittance basis-user, tax will only have to be paid if the distribution is received in the UK or if it is remitted to the UK.

Traps and anti-avoidance rules

- The protections do not apply to formerly domiciled residents (broadly, settlors with a UK domicile of origin who have changed their legal domicile to a domicile of choice elsewhere but who have then returned to the UK); or to settlors who become UK domiciled under the general law;

- Life policy gains have never been taxed on the remittance basis and so, like UK source income, are immediately taxable on a UK resident settlor, regardless of domicile status;

- Due to a defect in the legislation, offshore income gains that are made in respect of non-reporting funds owned by the trust, will currently be attributed to a non-UK domiciled settlor on an arising basis once they have acquired deemed domicile status. It is hoped that HMRC will amend the legislation shortly to correct this anomaly;

- If the trustees receive overseas income which they use in the UK (for example to make a UK investment) and then subsequently confer a benefit outside the UK on a remittance basis-beneficiary, the remittance basis-beneficiary will have an immediate tax charge if the benefit is matched against the income which has been remitted to the UK by the trustees. This would be the case even though the benefit itself is received outside the UK and remains outside the UK. If, therefore, trustees think that they are likely to confer benefits on remittance basis-beneficiaries, overseas income received by them should not be used in the UK;

- New "conduit" rules exist that ensure that if a distribution is made from the trust to somebody who is not taxable but that person then makes an onward gift to somebody resident in the UK, the ultimate recipient in the UK is treated as if they had received the distribution directly from the trustees.

Comment

The tax treatment of offshore trusts created by non-domiciled settlors is now an extremely complicated area. This article provides an overview of the rules but it is important to consider the precise facts in each case. Bespoke advice from a professional with expertise in this area will be essential.

FIVE THINGS YOU SHOULD KNOW ABOUT EIS AND RISK

Mark Brownridge, CEO of the Enterprise Investment Scheme Association (EISA), has recently outlined his thoughts on the Enterprise Investment Scheme (EIS) and risk in the following article:

‘The Treasury is keen to encourage investors to support enterprise in Britain. But, equally, it recognises that an investment in a start-up or SME business carries significant risk to the point where potentially an investor could lose all their initial capital. To compensate for this risk, the Treasury offers investors generous tax reliefs.

HMRC recently amended rules that enabled investors to benefit from these tax reliefs while investing in low-risk, asset-backed schemes. These schemes were not without risk - if one investment failed it was possible that the returns from the others would not outweigh losses.

So, is what we are left with too risky to contemplate?

Risk is something that always makes a sensible investor nervous. But with risk should come reward and our members can offer plenty of examples of exits that have delivered handsome rewards for investors. Don’t forget risk builds trust, not vice versa!

If you understand risks you can mitigate them and improve your chances of success. Below we have outlined the five key points you should consider when assessing risk in relation to EIS and SEIS investments. We hope it will encourage informed and helpful discussions between advisers, investors and fund managers so that investments in EIS are made in knowledge and confidence, but for more information please read our guide.

1. **Systemic risk -** Systemic risk is the risk of the collapse of a whole market or sector (as in the financial crisis of 2008/9). Companies within EIS portfolios tend to have reduced systemic risk. The long-term nature of the investment and the fact that most are unlisted mean they are often less buffeted by the emotional highs and lows of markets.

2. **Specific risk -** Specific risk is the risk facing an individual company (like its technology being overtaken or failing to find a market). EIS-qualifying investments have heightened specific risk. Much of this guide will be focused on how to help mitigate these risks.

3. **Liquidity -** To enjoy the tax benefits associated with EIS you need to be invested for three years. It may take much longer than that for some of your investments to reach a successful exit. As most EIS companies are not listed, it will usually be impossible for you to liquidate your investments in the event of you needing cash rapidly. So before investing, you should consider carefully the likelihood of you needing the cash before the investments mature.

4. **Eligibility -** In most cases, before considering a company for investment, an investment manager will want evidence that the company is likely to be EIS-qualifying. An investee company may apply to HMRC for 'advance assurance', which is an indication that it appears to meet EIS-qualifying criteria, based on the information provided to HMRC.

5. **Diversification -** Predicting which companies will succeed and which will fail when making investment decisions is extremely difficult. Diversification is one of the best ways to reduce specific risk. An investment in an individual EIS company offers two outcomes – the company will either succeed or fail. You could make a good return if the company achieves a successful exit or lose everything, apart from loss relief and the initial income tax relief, if it fails.

   Investing across a portfolio of EIS funds or companies allows you to spread your risk and improves your chance of good overall returns. Diversification can help to reduce risk and is particularly important when investing in higher-risk opportunities. But over-diversification can reduce your chance of a high overall return — the more companies you invest in, the more likely your return is to be close to the median as any super-performers will be averaged out by poor performers.

Following EISA's constant dialogue with HM Treasury we have been informed that the European Commission has now approved the Autumn Budget 2017 changes to the EIS and VCT schemes without objection.

A detailed decision letter will be published in due course. For now, the Treasury is proceeding with the process of laying commencement provisions. As with all parliamentary processes, the Treasury cannot be sure of an exact date when this will occur, but it should be soon.

THE DISGUISED REMUNERATION LOAN CHARGE: THE LATEST HMRC GUIDANCE

Broadly, disguised remuneration schemes involve using a loan, or other payment, which is unlikely to ever be repaid, to reward employees, directors or contractors, via a third party, such as a trust or other vehicle, instead of salary or other taxable income or benefits. Legislation applies to tax transactions entered into on or after 9 December 2010.

Now, such loans made on or after 6 April 1999, and which remain outstanding at 5 April 2019, will attract a tax and National Insurance charge – a loan charge. The amount subject to tax and National Insurance will be the outstanding loan amount on that date. Loan amounts repaid before that date will not be subject to the new loan charge, subject to certain anti-avoidance provisions which are designed to ensure that a genuine repayment has been made.

To avoid, or mitigate, the loan charge, it's necessary to register an interest with HMRC and provide all required information by 30 September 2018.

This settlement opportunity is open to employees, employers and self-employed contractors who have used disguised remuneration schemes.

HMRC has now issued a Policy Paper reminding users of disguised remuneration schemes about the 30 September 2018 deadline. It has also issued new Guidance on settling their tax affairs.

If they are already speaking to someone in HMRC about their use of a disguised remuneration scheme, or have a customer compliance manager, they should register their interest with them. Otherwise they will need to register by email.

According to the Financial Secretary to the Treasury, the charge on disguised remuneration loans is estimated to raise £3.2 billion for the Exchequer by 2021, so some hefty bills are anticipated.

Flexible payment arrangements are available to anybody who ‘has genuine difficulty paying what they owe’. By this, HMRC means that it will allow scheme users to spread their payments over five years if their taxable income in 2018/2019 is estimated to be less than £50,000, and as long as they are no longer in avoidance.

Those with higher incomes and those who need to pay over a longer period can also request for extended payment periods, which HMRC will consider based on individual circumstances.

Comment

Concerns continue to be raised by MPs and the Loan Charge Action Group around the potential size of the loan charge and effects on the wellbeing of individuals where HMRC pursues employees and contractors for payment, rather than the employer, or the promoter of the scheme.

An 'early day motion', which calls on the Government to revise the legislation to avoid significant damage to independent contractors and freelancers in the UK, now has 79 signatures; and for the charge to apply only to disguised remuneration loans entered into after Finance Act 2017 received Royal Assent.

INCOME WITHDRAWAL RATE FOR AUGUST 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 August 2018 is 1.5%.