LAW

THE TIMES

September 18, 2007 ■ "We are not monks and recluses" — Lord Kenyon, 1800, on judges

TUESDAY

Why inheritance tax is an unjust burden

David Semmens explains how to avoid handing your treasure to the Treasury

The legality of inheritance tax is under challenge. Last week Joyce Burden, 89, and her sister, Sybil, 81, lodged a last-ditch appeal in Strasbourg over the rule that each will have to pay inheritance tax on the home they jointly own near Marlborough, Wiltshire, because they cannot have the same exemptions given to married or gay couples in civil partnerships.

The move is just the latest challenge to a tax decried as hitting the moderately well off and punishing the thrifty. If you die worth £750,000 after repaying debts and leaving no spouse or civil partner, then at current rates, 40 per cent of an estate above £300,000 goes to the Treasury — namely £180,000.

This penalty comes after people have paid income tax on earnings and the interest on savings. Not to mention capital gains tax if stocks and shares are sold; or on the net profit of the sale of any investment property; or the stamp duty land tax paid when you bought that investment; or your main home.

Taxed at every turn when alive, good housekeeping is duly rewarded at death with a raid by the Chancellor of the Exchequer on hard-earned assets. Other countries seem to manage without — or at least on a less punishing scale. Italy and Sweden have no death tax. The US has a far more realistic threshold of $1.5 million and in Germany non-spouse relatives are taxed at only 12 per cent.

If geography offers no comfort, then history is little better. When introduced at the end of the 18th century, the legacy tax did not affect surviving wives or children. In the second decade of the 19th century death duties were extended to all relatives except spouses, but the rates were only 1 per cent for children and 3 per cent for siblings up to a maximum of 10 per cent for non-family beneficiaries.

It was, of course, estate duty introduced in 1894 that over time punished and even destroyed large wealthy landed estates — through a top rate, by 1939, of 50 per cent on everything above £2 million and by 1969, 80 per cent on estates worth more than £1 million. So it was certainly a "wealth" tax in the true sense. But at the lower end the rates were kinder.

Even IHT proper, introduced in 1985, did not seem too bad.

For legal gossip this week read The Water Cooler
timesonline.co.uk/business/law

Between 1987 and 1992 the nil-rate band (NRB), on which no tax was paid, duly doubled from £71,000 to £140,000 to keep pace with inflation. However, while the NRB has risen by 16 per cent in the past five years, house prices have gone up by 60 per cent.

Many believe that IHT has become fundamentally wrong. So what can be done? Radically increase the NRB — or lower the rate to, say, 10 per cent? What about exemption or a better rate for children and close relatives? Or exempt the family home? Or scrap IHT for a small wealth tax? Surely any would be fairer. History has seen many an unfair or immoral tax. But they have tended to end up being ceremoniously or unceremoniously dumped. So, short of successful IHT riots, people should do what they can to lessen its impact.

Anyone in a lasting relationship could perhaps consider marriage or a civil partnership: no tax on what is passed to a surviving spouse or civil partner. But ensure that you use your NRB in your will, either through a discretionary trust or, if you can afford it, an appropriate gift to children or others rather than your spouse. At current rates this will save at least £120,000 IHT. And, if you can afford it, use your annual gift allowance of £3,000 (more if the gifts are paid out of normal income). Don't forget insurance: second-death life insurance written in trust can go a long way to reducing the impact of IHT when a spouse or civil partner dies.

And, despite the 2006 Budget, trusts are still useful for the married, healthy and wealthy. How about an immediate transfer of £600,000 to two new discretionary trusts? But you must live for another seven years. Even with periodic and exit charges, that could mean an extra £240,000 to your children rather than the Treasury.

Finally, see a qualified specialist in IHT planning — not someone trying to sell an insurance-backed product but a solicitor or accountant specialising in succession planning. People still make home-made wills to save a few hundred pounds when they may end up paying thousands in IHT for lack of professional advice.

Alternatively — and pending a ruling on the Burden sisters' anomaly — you can just wait for the IHT protest marches along Piccadilly. I fear it may be quite a long wait.

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SOUTH WEST NEWS SERVICE

Sybil and Joyce Burden will both pay IHT on their joint home

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