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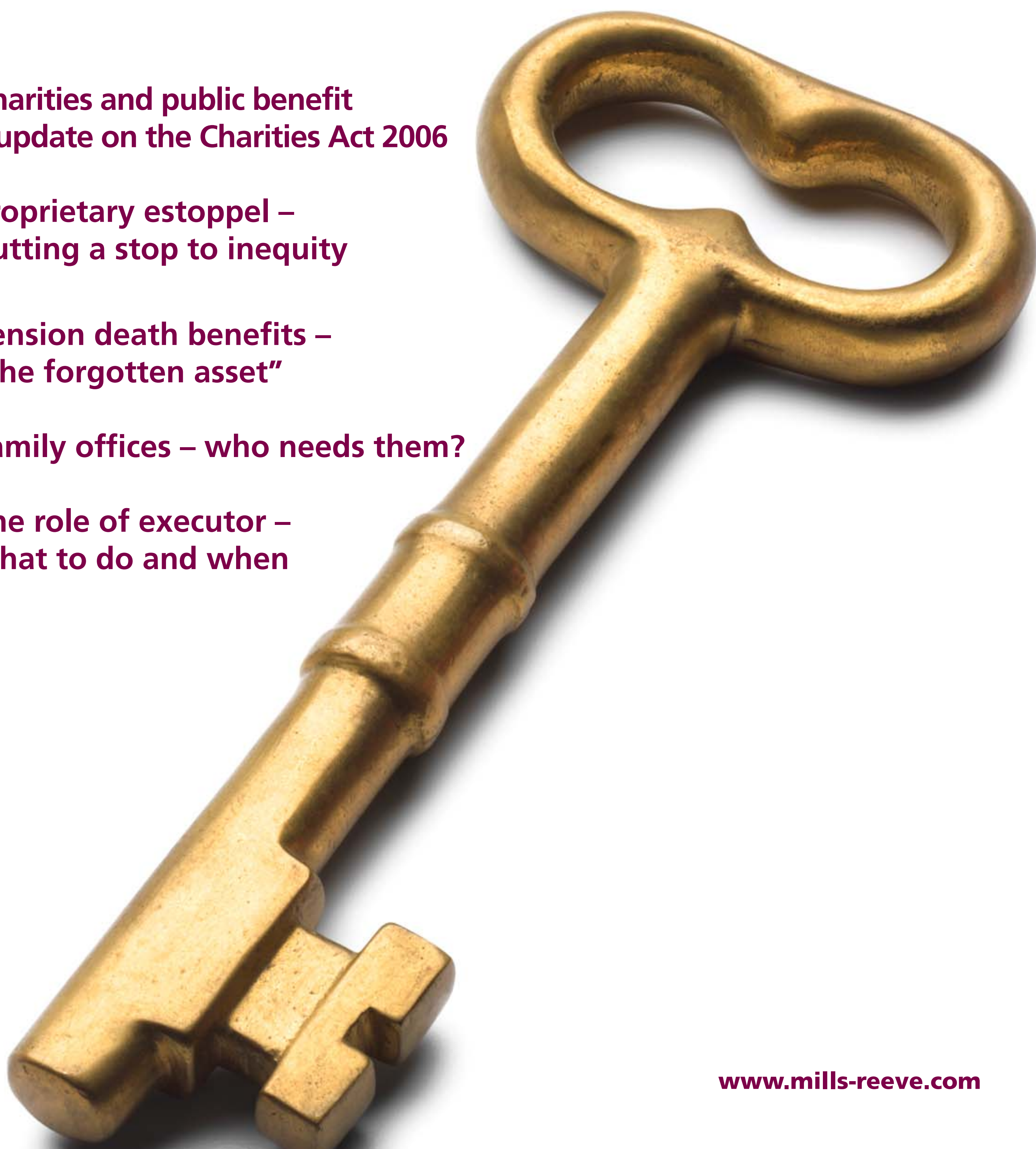
Spring 2008



Charities and public benefit – update on the Charities Act 2006

Proprietary estoppel – putting a stop to inequity

Pension death benefits – "the forgotten asset"

Family offices – who needs them?

The role of executor – what to do and when

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Welcome to the spring 2008 edition of *Private Affairs.*

Following the recent changes in the taxation of individuals and trusts, tax planning has been made more challenging in some areas. However, one relatively simple but often overlooked area of planning relates to death benefits arising under pensions and policies. We have included an article on this topic to give you some idea of the opportunities and pitfalls. On another subject, individuals are often daunted to find themselves appointed as executor of an estate. Our article will give you a brief overview of what this important role involves.

For the guest article, Alexander Scott of Sand Aire informs us about the advantages of using family offices. For those of you whose circumstances make this an appropriate solution, it will give some interesting ideas.

We also have an article on the doctrine of proprietary estoppel, which seeks to hold individuals to their promises when others have relied on their word and acted to their detriment as a result. The article focuses on a particularly interesting case of a nephew who worked unpaid for a number of years on the basis of an understanding relating to an inheritance. There is also an article on the recent overhaul and increased regulation of the charity sector, which may prove to have an impact on some private schools that have charitable status.

Finally, we are very excited to announce our recent expansion into Manchester and Leeds. Please turn to the back page for more details.

As always, we would be pleased to receive your comments and ideas about *Private Affairs*. Please contact your local office to give us your views.

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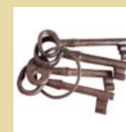

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Charities and public benefit – update on the Charities Act 2006

The aim of the new Act is to clarify certain aspects of the law relating to charities and to introduce more effective regulation of the sector.

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- **There are now thirteen charitable "purposes"**
- **There is a new public benefit test**
- **The Charity Commission has issued guidance**
- **There are new reporting requirements**

There is a new list of charitable purposes – thirteen in total – which includes the relief of poverty, the advancement of education, religion, the arts, culture, heritage or science, amateur sport and, by way of a "sweep-up", other purposes that are currently recognised as charitable.

The Act removes the presumption that charities set up for the relief of poverty, the advancement of education or the advancement of religion are automatically for the public benefit. This means that all charities must now actively demonstrate that this is the case.

Public benefit

Guidance relating to what constitutes a public benefit has been published by the Charity Commission (the CC) and this is supplemented by further sector-specific guidance for charities operating in the following arenas:

- the prevention and relief of poverty;
- the advancement of education;
- the advancement of religion; and
- fee-charging charities.

Although charity trustees are not legally required to follow the guidance, they should be able to show that they have paid due attention to it where appropriate and they must comply with the reporting requirements (see later).

The charitable organisation must be able to show the following:

- there must be an identifiable benefit that is clear, related to the aims of the charity and balanced against the detriment; and
- the benefit must be to the public, which means that the beneficiaries must be appropriate, the opportunity to benefit must not be unreasonably restricted, people in poverty must not be excluded and any private benefits must be incidental.

Private schools

Much of the press comment on the guidance has focused on the impact on independent fee-charging schools. There have been suggestions that such schools may struggle to pass the public benefit "test". However, the comments in the guidance are relatively reassuring. The guidance states that "the fact that the charitable facilities or services will be charged for and will be provided mainly to people who can afford to pay the charges, does not necessarily mean that the organisation does not have aims that are for the public benefit". It also makes it quite clear that benefits provided to those who are unable to pay the fees charged must be material – token or nominal benefits will not suffice.

So, charging fees per se is not a bar to passing the public benefit test but a private fee-charging school must ensure that its activities extend beyond simply providing an education for children whose parents can afford to pay the fees. Issues that should be looked at include bursaries and sharing facilities/expertise with schools in the state sector.

Reporting requirements

With effect from 1 April 2008, charity trustees will have a duty to report in their annual report on their charity's public benefit. The level of detail required will depend on whether the charity is above or below the audit threshold (gross income in excess of £500,000 per annum or income in excess of £100,000 per annum and asset value in excess of £2.8 million). For those below the threshold, a brief summary of main activities undertaken to carry out the charity's aims for the public benefit will suffice. For those above the threshold, a fuller explanation will be required.

Action points

Charities, particularly those in the education sector, should look carefully at the benefits that they provide and the extent to which those benefits are available to the wider public. In addition, charity trustees should ensure that they have read the CC's guidance on public benefit.

Proprietary estoppel – putting a stop to inequity

Recent case law has highlighted the fact that family disputes often arise where, for example, parents assure their children that they will inherit the family home or business and the children rely on such assurances to their detriment. The doctrine of proprietary estoppel seeks to redress the balance in such circumstances. This article considers the doctrine and the recent decision in *Thorner v Curtis & Others*.

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The legal principles

In its modern form, there are three elements to the doctrine of proprietary estoppel:

- A makes assurances or promises to B;
- B relies on those assurances or promises; and
- B suffers a detriment as a result of his reliance on the assurances or promises of A.

The overriding aim of the doctrine is to prevent unconscionable conduct. It is necessary to look at the matter in the round to decide whether the three elements are satisfied and, if so, the level of award necessary to do justice to the claimant while avoiding a disproportionate result.

Assurances

The case of *Thorner* reiterated that an assurance need not amount to an express promise. While an assurance can be made expressly by spoken or written words, it can also be made by implication from spoken or written words or from conduct.

David Thorner had worked on his cousin, Peter's farm in Somerset since 1976 without receiving any payment. He undertook a wide range of tasks and worked long hours. Peter made various hints and remarks over the years, which led David to hope and then expect that he would inherit the farm. Peter had also made a will leaving his estate of £3.6 million (including the farm) to David. Although Peter subsequently destroyed his will and died without making another, there was no reason to believe his intentions in relation to David had changed.

Where there is no express promise to rely on, it is crucial for the claimant to support their case with clear and substantial detrimental reliance. Much weight was given to evidence from witnesses able to corroborate the meaning and intention that David had imputed to Peter's words and actions. The court concluded that Peter's words and conduct had brought the doctrine into play.

Detrimental reliance

Reliance and detriment are often intertwined to the extent that they cannot be considered separately. The assurances made do not need to be the sole inducement for the claimant to take a decision that is detrimental to him. In *Thorner*, Peter's assurances were a significant (although not necessarily the sole) factor in David's decision to remain in Somerset and work on the farm. Detriment need not consist of the expenditure of money or other quantifiable financial loss, so long as it is something substantial. It must be judged at the moment when the person who has given the assurance seeks to go back on it. Whether the detriment is sufficiently substantial is tested by whether it would be unjust to allow the assurance to be disregarded – the essential test of unconscionability.

In *Thorner*, David's reliance on Peter's assurances strongly influenced his decision to refuse opportunities that would have provided him with an income and independence from his parents.

Satisfying equity and proportionality

Provided the claimant can satisfy all three elements of proprietary estoppel, the court will consider the minimum award necessary to do justice to the claimant and to avoid an unconscionable or disproportionate result. It is often virtually impossible to quantify detriment in terms of monetary value.

In many cases, it can be as difficult to put a financial figure on the value of the claimant's detriment as to measure their expectations. Detriment can be quantified with reasonable precision if it consists

solely of expenditure on improvements to another's property. By contrast, the detriment of an ever-increasing burden of care for an elderly person is very difficult to quantify in monetary terms. The court has to exercise a wide judgmental discretion and consider a number of factors, including the competing claims of other beneficiaries or potential beneficiaries, the extent of the claimant's expectation, the level of detriment suffered and the value of the assets in question.

In *Thorner*, the court held that it would not be disproportionate for David to receive the farmhouse, land and farming assets, valued at approximately £3 million. Peter and David were fully aware of the extent of the farm, if not its open market value. However, David was not aware of the extent or value of Peter's other assets, valued at £620,000.

On intestacy, Peter's estate would have devolved to his surviving siblings, none of whom he enjoyed a close relationship with. Peter's words and conduct created more than an expectation in David; there was a mutual understanding that he would inherit the farm. In reliance, David was extraordinarily committed to the farm, making significant contributions to its state and condition, thereby increasing its value. It would have been unconscionable to deny him the farm.

- **All three elements of proprietary estoppel must be established**
- **An assurance may be express or implied, written or unwritten**
- **Where there is no evidence of an express promise, witness evidence will be key**
- **The minimum equity necessary to do justice to the claimant will depend on all the circumstances of a case**

Pension death benefits – "the forgotten asset"

Many people understand the importance of estate planning to reduce inheritance tax (IHT) and to ensure that their assets reach the intended beneficiaries. However, it is easy to overlook lump sum death benefits that they may receive under pension policies.

These can be insured death benefits (eg, a set lump sum or multiple of salary) and/or a return of the current fund value or policyholder contributions on death before taking benefits. The value of these benefits can often rival or exceed the value of the more visible assets, even the family home!

This article looks at some of the potential pitfalls regarding lump sum death benefits under registered pension schemes and how these can be addressed.

Pension policies: issues to consider

1. IHT on the policyholder's death
Broadly pension death benefits are subject to IHT if paid to the policyholder's estate and if the estate was entitled to these "as of right" on the policyholder's death. Many policies avoid this by giving the scheme trustee or administrator discretion over who receives the benefits from a class of potential beneficiaries and the policyholder can make a non-binding nomination of who they would like to benefit.

Provided genuine discretion can be exercised, this should prevent such benefits from a registered pension scheme falling into the policyholder's estate for IHT. However, not all policies include these provisions and there can be problems where no genuine discretion is or can be exercised.

2. IHT on the recipient
After the benefit has left the pension scheme it will be included in the estate of the recipient(s) for IHT, which can have significant tax consequences.

Example:
A policyholder dies with a pension fund of £200,000, having not taken retirement

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- **Death benefits may be overlooked in IHT planning**
- **There are advantages to ensuring discretion over payment**
- **The use of a family trust can be advantageous**
- **The retirement market can offer flexible solutions**

benefits. He nominates his wife as the recipient and the benefits are paid to her. The wife then keeps the fund and, when she dies some years later, it has grown to £300,000. This amount will then form part of her estate along with her other assets and potentially be subject to IHT at 40 per cent on £300,000 – totalling £120,000.

3. Asset protection
Nominating the spouse or children to receive benefits outright may not result in the death benefits passing down the family in the longer term.

Example:
A policyholder dies with a pension fund of £1 million, having not taken benefits. He nominates his wife as the beneficiary of a third with the remaining two-thirds shared between his daughter (aged 21) and his son (aged 18). Payment is made in accordance with his wishes.

The wife subsequently remarries and leaves the bulk of her estate (including her late husband's pension fund) to her new husband.

The daughter marries and is divorced at age 35. Depending on the circumstances, her ex-husband may get a share of the pension funds if this is included in the assets to be shared between the couple.

The son develops a gambling addiction following the loss of his father and fritters away the money left to him.

The solution: a family trust
Instead of nominating individual beneficiaries, the benefits could be made payable into a separate family trust, providing the scheme documents are flexible enough to cater for this (and many modern pension schemes are).

Typically the trust would be discretionary, giving the trustees flexibility to adjust to changing circumstances (eg, a divorce, means assessment issues or an irresponsible beneficiary) when considering who should benefit and when.

A trust keeps the assets out of the surviving spouse's and children's estates while allowing them to benefit from the trust fund where necessary. For instance (if the trust allowed this) the fund could be loaned to the surviving spouse in such a way that the loan (plus interest) could be a debt on their estate, hence ensuring that the bulk of the pension death benefits do not get charged to IHT on the surviving spouse’s death.

How do recent developments affect things?
Following the Finance Act 2004, there is significant flexibility over funding of pension funds, enabling large funds to be built up quickly, for which careful tax and asset protection planning will be important.

Also, the retirement market has become more flexible with many policyholders opting for alternatives to traditional annuity purchase (eg, income drawdown). These alternatives generally involve keeping some or all of the retirement fund intact into retirement (usually up to a maximum age of 75) meaning that the issues identified in this article remain relevant.

When is the best time to consider the structure of pension death benefits?
Anyone with significant pension death benefits (including insured pension death benefits) should ensure that they are comfortable with their current arrangements.

It is also useful to consider this when reviewing one's will (which should be done regularly!). Decisions such as who to appoint as trustee and what instructions to give them involve similar considerations to those necessary in making a will.

Another important time to consider this is when considering a transfer of benefits between schemes (eg, transferring at retirement to a scheme offering income drawdown). NB – pension transfers are an area where expert financial advice is important.

When is the best time to consider the structure of pension death benefits?
1. Many individuals have significant pension funds justifying careful thought as to what would happen were they to die before taking benefits.

2. Pension death benefits can be very valuable, even where the pension fund is small (because of insured death benefits).

3. Modern flexible retirement options mean that significant lump sum death benefits may be payable into retirement.

4. Ensure that the payment of any death benefit would not trigger an IHT charge.

5. Where death benefits are paid to individual beneficiaries there is the risk of IHT when that person dies and also that the assets may not pass down the family as the policyholder would have wished.

6. Family trusts can avoid IHT issues on the death of the intended beneficiaries and ensure that the assets pass down the family appropriately.

Family offices – who needs them?

Having created and developed a family office for my own family in 1996, it is fascinating to see how the sector has evolved. Ten years ago, the term "family office" was known to only a few in this country, whereas a Google search restricted to the UK now delivers over 250,000 references. The first couple of pages of the search show links to two stockbrokers, two legal firms, two accountants and two specialists, all offering family offices, together with four conferences on the subject. Clearly, professional service businesses are fulfilling a need among their clients and it is instructive to review their own descriptions of the services they provide.

The websites proclaim that the organisations are able to address the complex requirements of their clients and are concerned with long-term wealth preservation and growth. There is much talk about multi-disciplined control, co-ordination and delivery of services. None of the sites reviewed talk about the wealth levels required to qualify for such services, although one lawyer suggests that they tend to be of interest to families with assets of some £125 million and above. Nevertheless, it is clear that they are of relevance to only the wealthiest of clients. It would seem that family ambition and administrative complexity are two key characteristics of those seeking a family office solution.

We all know the phrase "shirtsleeves to shirtsleeves in three generations". Whether or not one is sympathetic to families who experience such a fall in financial and associated status, some wealth creators have the ambition to see their wealth endure beyond its natural life-expectancy of three generations. Family offices promote themselves as being capable of assisting in tackling the forces of dissipation. They do so by primarily addressing the three central characteristics of successful wealthy families: family unity and effective governance, efficiency and control in administrative matters and strategic coherence in investment of both illiquid and liquid assets. Such a combination tends to facilitate enduring wealth.

Websites do not reflect the total extent of family offices delivering all or some of these services. The full range can be described as being a continuum from:

- the person who decides to deliver all the services themselves (DIY);
- the family that creates a single family office dedicated to their own family (single family office or SFO);
- the independent multi-family office (specialists in the field who serve multiple families – MFOs); and
- MFOs embedded within either professional firms (such as lawyers and accountants) or banks.

There is no perfect solution for any family and there are advantages and disadvantages to each one of these models, but the emergence of each of these variations of the family office provides a choice to wealthy families considering a family office, which did not exist a decade ago.

Cost versus performance drives most purchasing decisions in the service sector and the family office sector is no different. The DIY approach will be cheap, but the governance, administration and investment responsibility will all fall to one person – and if this person has proved to be a wealth creator in another sector of the economy, they may struggle to be both content and successful in the financial services sector. Creating a full-service SFO is an option that has been pursued by many families for decades and is an option available to only the wealthiest. Estimates of the minimum net worth required to follow this route vary, but tend to suggest that a liquid fortune of £250 million is the minimum level that begins to make this approach cost effective if the family has the time, experience and energy to oversee what they have created.

The independent MFO is a more recent arrival and is designed to allow wealthy families to access all the professional services provided by an SFO on the basis of sharing. This allows families with significant wealth to access specialist skills and expertise that would otherwise be available only if they established their own SFO. The minimum wealth required to become a client is rarely stated publicly and will depend upon a number of factors, but the minimum tends to be well in excess of £10 million. The embedded MFO will tend to specialise in the area of expertise provided by its creator (tax, law or investment) and, because of the nature of its creator, provide a deep organisational resource as part of its service. Equally, the economies of scale resulting from the size of the parent means that such MFOs can offer a service to families in a wealth bracket below that of their independent competitors.

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In all but very few of the family office offerings outlined above, services will be based upon the principle of being a focus for, and meeting the needs of, one or more of the three key requirements of families (governance, control and administration, and investment) while engaging multiple external providers to deliver those skills not available in-house to their client families.

A decade ago, I searched for these services myself and couldn't find a coherent response to my family's own needs in the UK. The intervening years have seen the emergence of the family office as a sector of wealth management in its own right, and wealthy families have a wider, richer choice of options if they possess the combination of ambition and complexity that suggests a family office solution is appropriate to their needs.

- **The number of "family offices" is growing**
- **Key characteristics are family ambition and administrative complexity**
- **There are different types of family office to suit different circumstances**
- **Considerations of cost versus performance**

The role of executor – what to do and when

The role of executor will fall to most people at some point in their lives, whether they are appointed by the will of a parent or a friend. This role can seem overwhelming, particularly during emotional times. It is quite common therefore for executors to enlist professional help and to instruct solicitors to act for them in administering an estate. If you find yourself so appointed, even if you choose to instruct solicitors to act on your behalf, it is helpful to understand the work involved and the legal burden resting ultimately on your shoulders as the executor.

Much of what an executor must do when called upon to act is common sense and a first-time executor may already have personal experience of registering a death and arranging a funeral. From an executor's point of view, it is helpful to obtain several copies of the death certificate from the registrar and to keep careful records of all funeral expenses. These will be a liability of the estate and are paid in priority to other debts.

If the original will has not already been found, this is the next task – a copy will not suffice to obtain a grant of probate, unless you can show the original was lost or destroyed without an intention to revoke the will. Originals are often kept by a solicitor or a bank for safekeeping. If no will is found, an intestacy arises that is outside the scope of this article. Essentially, the administration of an intestate estate is similar up to the point of distribution, when the statutory rules will apply.

When the original will is located, non-professional executors often turn to solicitors for help in the rest of the administration. The establishment of the exact assets and debts of the estate is a thorough and detailed process, which is surprisingly time-consuming. It is usual to remove all paperwork from the deceased's home and to retain all original documents such as title deeds, share and National Savings Certificates, bank and building society passbooks and insurance policies. Every lead must be followed to ensure that all assets are quantified and secured. Often valuables must be removed from an unoccupied property, property insurers notified and independent valuations of non-cash assets obtained. All payments outstanding at the time of death must also be ascertained. Any passports, driving licences, copies of tax returns and pension statements should be kept as these will be needed. Additionally, income tax returns must be prepared for the tax year up until the date of death. This may result in a refund to the estate, which must be entered into the estate accounts.

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A detailed inventory of all assets and liabilities must then be submitted to the Capital Taxes Office. If the estate exceeds the statutory limit – currently £300,000 – and is not left to a spouse or charity, the excess will usually be charged to inheritance tax at 40 per cent. The proportion of the tax bill that relates to broadly non-land assets must be paid before the grant of probate can be obtained to realise the cash in the estate. This can present the need for a bridging loan, which usually incurs high rates of interest.

Once the grant is issued, the executor can claim cash balances and life policy proceeds and sell shareholdings and other assets unless these are specifically gifted in the will. It is usual to open an executor's bank account to hold the cash until it is distributed. All debts and inheritance tax must be paid before the legacies and the remaining estate are distributed. It is inadvisable to distribute all funds until after six months from the date of the grant. Claims by dependents can be made against the estate in this time period and the executor could be personally liable if a challenge is upheld.

The administration of an estate may take a year or more and involves a great deal of time and paperwork. Non-professional executors are not entitled to payment but will be able to recover reasonable expenses incurred in performing their role.

Although appointed as executor, you need not act if unable or unwilling to do so. Another executor may have been appointed who can take on the role solely or, failing which, one of the beneficiaries of the will can be appointed.

If you appoint a solicitor to act for you in the estate as executor, you will be kept up to date on the progress of the administration and will still be required to approve and sign the key documentation such as the application for the grant of probate and the oath for executors. However, you can leave the detailed preparation of the estate accounts and tax returns and other day-to-day work to an experienced probate manager.

- **An executor's role can be more complicated than most people realise**
- **Many lay executors appoint solicitors to assist them**
- **Administration of an estate can take a considerable amount of time**

Mills & Reeve celebrates launch of largest family practice in Europe

February brought the exciting news that we have launched two new offices in Leeds and Manchester, following the announcement in November last year of the transfer of Addleshaw Goddard's entire family team to Mills & Reeve.

The new office openings take our national family law team to more than 40 lawyers, making it the largest dedicated family team in Europe. We now have a national network of six offices, 84 partners and a total staff of more than 800.

Our private client practice contributed 20 per cent to the firm's total work last year, and this latest expansion aims to ensure that the hugely successful national division maintains this high level of contribution.

Our new team in Leeds is headed by senior lawyers, David Salter and Philip Way, and in Manchester by Nigel Shepherd – each individuals with outstanding reputations and experience of handling complex cases involving multimillion-pound assets. David is cited by *Chambers* as "truly excellent", Philip is someone who "draws a great deal of praise" and Nigel is "a top practitioner with a solid approach".

Commenting on the office launches, David Salter said: "Our aim in the northern offices is to continue to offer a high quality service to a wide range of clients within a competitive pricing structure, which will benefit from the strength and depth that Mills & Reeve as a top 50 UK law firm is able to offer across a wide range of practice areas".

Nigel Shepherd said: "We are delighted to be part of the largest team of dedicated family law and divorce specialists in Europe. The move sees Mills & Reeve building on its solid reputation of providing unrivalled quality legal expertise in the North West region and beyond".

At Mills & Reeve, we're recognised for pioneering developments in mediation and collaborative law. Roger Bamber, joint head of our family practice, was one of the original group who initiated the new alternative dispute resolution initiative from America. October saw the much publicised re-launch of our website, Divorce.co.uk – the UK's premier online information resource, which provides comprehensive advice and guidance for individuals going through a separation, divorce or dissolution of a civil partnership.

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