

2010 | Helping Families Secure Their Future

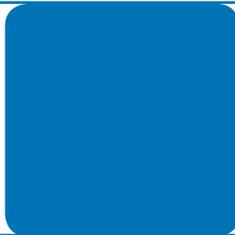
- an agenda for policymakers



Helping Families Secure Their Future

- an agenda for policymakers

- **Protecting the vulnerable**
- **Modernising our inheritance laws**
- **Building financial security**
- **Building a better tax system**



Foreword

The next few months in the UK are clearly going to be closely fought politically. Whatever the political claim and counterclaim, the reality is that the financial crisis means that whoever wins the approaching election will need both to repair the public finances and ensure that families are well placed to support themselves as much as possible through what could remain difficult times in the broader economy.

Helping families from every walk of life secure their financial future, in both good times and bad, is what STEP members do. We have therefore drawn together our memberships' practical knowledge of the real problems confronting many families, often at times of great personal difficulty, emotional challenge and complexity, to draw up an agenda for policymakers, of whatever political persuasion, over the lifetime of the next parliament.

Many of our suggestions are unlikely to count as 'headline grabbing.' Issues such as making it easier for families to use powers of attorney or improving consumer protection in the area of will writing are never likely to be at the top of the national political agenda. We would nevertheless argue that any incoming government prepared to invest policy time in such initiatives could do a lot to help families of all backgrounds across the country – at little or no cost to the public purse.

When working with families to draw up their long term plans, STEP members also develop a good

understanding of the issues that matter to families working to build their savings and assets to achieve long term security for the current generation and a solid start for the next generation. Too often the current arrangements surrounding pensions and savings have been left behind by changes in the economy and broader society. We have therefore also put forward a range of suggestions in this area - some radical, some less so – which we believe deserve careful study by government.

STEP members are drawn from a range of professional backgrounds. In consequence many of our proposals will touch on issues that are also important for other professional bodies. We would welcome the opportunity to work with both fellow professional bodies and policymakers alike over the coming months to refine an agenda that we believe could deliver a real change for the better in many people's lives.



**David Harvey, CEO
STEP Worldwide**



**Julia Abrey, Chair of STEP
England & Wales**

Helping Families Secure Their Future

STEP members work with families helping them to draw up long term plans for their savings and property and also helping them to protect the interests of vulnerable family members. The issues our members are asked to advise on are a good reflection of the issues that are of real concern to ordinary people. Increasingly, however, our members report that the tax, legal and institutional framework they work with has not adapted to the rapid changes in society over recent years.

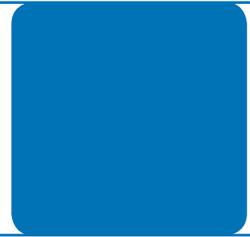
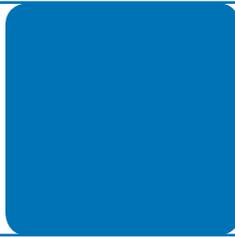
The past generation has seen rapidly rising prosperity alongside a major expansion in home ownership. Household net wealth per head now averages over GBP100,000¹. Already more than 175,000 estates over GBP100,000 go to probate each year² and STEP expects this figure to grow strongly as the boom in home ownership over recent decades works its way through. Given these figures, families increasingly recognise the need to think carefully about how they want the assets they have accumulated over their lives to be used.

Alongside the rise in prosperity, social trends increasingly require families and advisors to make

sure that family assets are used to the best effect. A range of issues, such as rising divorce rates, improved longevity, increased geographic mobility within families and the shift to caring for vulnerable adults in the community all have major implications for how families need to arrange their affairs if they are going to help support relatives. Unfortunately too often the so-called 'sandwich generation', struggling to simultaneously care for children and elderly parents while holding down full time jobs, find themselves working 'against the grain' of rules and regulations that were drawn up before such issues became commonplace and with differing priorities in mind.

This pamphlet therefore looks at a range of issues that have been raised by STEP members from their professional practice. Most of our recommendations to tackle these issues would involve minimal or no net cost to the tax system. Quite often all that is required is sensitivity to the needs and concerns of older citizens, alongside greater awareness from officialdom of what, for example, powers of attorney are used for. In other areas, such as those where significant changes to primary legislation may be required, STEP would welcome the opportunity to work with all interested parties to refine the recommendations we have put forward.

The Society of Trust and Estate Practitioners (STEP) is the worldwide professional body for practitioners in the fields of trusts and estates, executorship and related issues. STEP members help families secure their financial future and protect the interests of vulnerable relatives. With almost 6,000 members in the UK (and over 15,000 members around the world), STEP promotes the highest professional standards through education and training leading to widely respected professional qualifications.



STEP's Recommendations

Delivering dignity for the vulnerable

Recommendation 1: Helping those diagnosed with degenerative diseases or mental health problems

The current rules often impose tax penalties on families setting up trust arrangements to protect the interests of those diagnosed with degenerative diseases or suffering mental illness. Government should extend the relief, which currently applies to trusts for a very narrowly defined group of 'disabled persons', to trusts established for persons who have partial, fluctuating or progressive illness or conditions, which do or will have the effect of significantly reducing their ability to administer their property or manage their affairs.

Recommendation 2: Making it easier for families to use powers of attorney

In the face of an ageing population it is unacceptable that basic tools to help the elderly, such as powers of attorney, are still poorly recognised by many organisations. It should be a regulatory requirement that staff in areas such as financial services should undergo basic training in issues such as how powers of attorney work. This would sit alongside the basic training they are already required to receive in areas such as anti-money laundering procedures.

Recommendation 3: Taking fraud seriously

The BBC has reported a ten-fold increase in some

types of attempted fraud against estates, a statistic which matches the experience of many STEP members. This problem needs tackling urgently by making such fraud a priority in police targets commensurate with the distress it causes families.

Modernising our inheritance laws and institutions

Recommendation 4: Protecting consumers by regulating will writers

There is growing evidence that due to poor drafting a significant number of wills are failing or being contested in the courts, often at considerable expense. Those who write wills professionally should be regulated to ensure minimum standards of competence and behaviour and to give the public protection in the form of negligence insurance and continuity arrangements.

Recommendation 5: Meeting the challenges facing cross-border families.

With 5.5 million Britons living abroad, including 1 in 12 pensioners, and 6.5 million UK residents born overseas, including a third of all Londoners, it is important that the UK legal and tax system acknowledges the issues faced by cross-border families. The UK should engage positively with EU initiatives such as 'Brussels IV', which are aimed at

simplifying the rules and procedures related to cross-border inheritance and which also look closely at how the risk of double taxation can be minimised.

Recommendation 6: Embedding a culture of giving and volunteering

Trust and estate planning plays a key role in supporting charity and philanthropy, with legacies providing around 10 per cent of charities' total income and a further GBP3.3 billion a year flowing from trusts and foundations. Much more can nevertheless be done to both encourage civil involvement and embed a culture of giving by individuals and families. Government should establish a permanent framework to co-ordinate the work of family advisors, charitable bodies and the public sector to promote education and training on philanthropy and remove bureaucratic barriers to giving.

Creating the capital to support the elderly and the vulnerable

Recommendation 7: Shifting the focus from 'savings' to 'capital accumulation'

In spite of huge tax subsidies, half of all UK adults are saving nothing for their pension and around a third have no savings at all. It is time to think afresh, breaking down the barriers between 'savings', 'pensions' and 'assets' and focusing on encouraging 'capital accumulation' and making it easier for families to use their capital resources to support

themselves in times of need. The relative success of ISAs highlights the importance of flexibility and transparency in schemes to help people build their resources, as does the success of several overseas long term savings schemes.

Recommendation 8: Helping the young

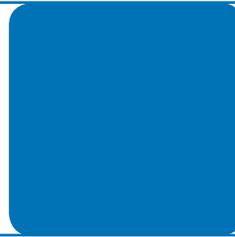
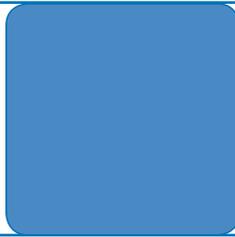
For many people the help they receive from grandparents and others in the family when they are young can be a crucial factor in allowing them to ultimately build enough assets to fund retirement. Consideration should be given to either removing the tax barriers to A&M Trusts for children or developing new means for families to give long term support to children, perhaps by lowering the age at which ISAs can be opened for children (currently 16 for cash ISAs, 18 for share ISAs).

Recommendation 9: Encouraging lump sum savings

Paying for university, buying a first house and starting a family typically impose a heavy strain on personal finances, which in many cases is only lifted when someone receives a lump sum representing their share from their parents' estate. Better provision should be made for savers to be able to save such lump sums, perhaps allowing them to aggregate the current ISA annual limits over several years.

Recommendation 10: Making better use of non-financial assets

Almost 65 per cent of household net wealth is held in non-financial assets. Consideration should be given as to how families can best use these assets, alongside their savings in financial assets, to support



them through retirement and other key life events. STEP has developed preliminary proposals for Lifetime Trusts, which would allow financial and non-financial assets to be pooled. Lifetime Trusts would significantly boost the funds available at retirement for the typical household while allowing much more flexibility than most current pension savings schemes. They would also allow savers to pass the residue of their Lifetime Trust on to future generations, adding significantly to the incentive to save.

Building a better tax system

Recommendation 11: Establishing a tax law review body

The UK is increasingly at a competitive disadvantage because of complex and uncertain tax laws. STEP strongly supports the consensus among professional bodies and others that a new body is needed with the specific remit of simplifying and improving our tax laws. This body could be either in the form of a Tax Law Commission or a Joint Parliamentary Committee, but its remit should be drawn widely and it should be empowered to consult freely with the professional bodies and others. It should also be resourced to allow rapid progress.

Recommendation 12: Recognising the legitimacy of tax planning

Certainty has been undermined for both taxpayers and advisors by repeated government assaults on the legitimacy of tax planning advice previously considered entirely acceptable. An independent review

should be launched to establish a clear distinction between 'acceptable' and 'unacceptable' tax planning. This review should give due regard to both the need to defend the public purse and the importance of people being able to plan their affairs in ways that are both tax efficient - for example avoiding being subject to multiple taxes on the same stream of income - and legally certain.

Recommendation 13: Ensuring adequate consultation

Consultation can play a vital role in avoiding unintended consequences, as well as accurately assessing likely costs and benefits from proposed legislation. Welcome progress has been made in opening up proposed tax law changes to consultation, but there are still too many instances of policy announcements without adequate prior consultation. It should be the norm that changes to tax laws (as opposed to changes in tax rates) should be made after public consultation and after a rigorous cost benefit assessment.

Recommendation 14: Improving non-legislative rule making

In practice changes in HMRC 'Guidance' and 'Explanatory Notes' can have as much impact on taxpayers as changes in legislation contained in the *Finance Bill*. Even so, such changes are typically announced without any opportunity for parliamentary scrutiny and often without any formal external consultation. Changes to HMRC 'Guidance' and 'Practice Notes' should be subject to the same consultation processes as changes to tax law.

Dignity for the Vulnerable

Helping those diagnosed with degenerative diseases or mental health problems

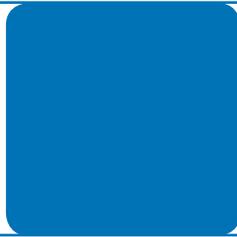
While recent years have seen good progress in creating wide public acceptance of the need to build a strong culture of protecting the interests of children, the problems surrounding protecting the interests of vulnerable adults remain less widely recognised. Many families, for example, have to grapple with the issue of how they can best support and manage the affairs of a family member who is unable to manage his or her own affairs. Often this occurs when an elderly family member begins to suffer dementia; one side effect of us living longer is that more and more families have a relative with dementia. There are currently 700,000 people with dementia in the UK, a figure widely expected to rise to over 1 million by 2025.³ But the need for family support for a vulnerable relative is not just an issue confined to the elderly. One in six of the population has mental health problems at any one time and such problems affect young and old alike.⁴

All sides in such situations would often prefer, if at all possible, for care and support to come from within the family and STEP members are often asked to help draw up long term plans to help this process, protecting the dignity of vulnerable family members. A trust should always be one of the options considered in these circumstances. Put simply, trusts are a safe way of holding and managing money or property for

people who may not be ready or able to manage it for themselves.⁵ Trusts are therefore well suited to helping people support vulnerable family members. Trusts are nevertheless widely misunderstood and often seen as something just the rich need be concerned with. In reality, the great majority of people, often without realising it, will come into contact at some point of their lives with a trust in one form or another. Most company pension schemes, for example, are structured as trusts, with the employer giving cash to a fund overseen by trustees to invest for the benefit of employees when they retire. Similarly, many life insurance policies are 'written in trust', so that when the person insured dies the policy pays out to a trust run by the insurer, which can pay the cash out quickly in line with the insured person's wishes.

As well as being the outcome the family wants, support from within the family can provide substantial savings to the public purse. Caring for those with dementia costs around GBP17 billion a year⁶, but those cared for by their families save the community around GBP6 billion a year. Similarly the overall costs of mental illness have been estimated at GBP48.6 billion in 2007⁷ and improving support within the family could deliver huge savings here. Yet families and their advisors trying to help a relative often encounter a string of practical problems, which are both frustrating and costly.

One major obstacle is the impact of the changes to trust taxation in the 2006 *Finance Bill*. These had the effect of introducing significant tax penalties on



many of the most common types of trusts, although reliefs continued for trusts for the benefit of 'disabled persons.' The problem is that the definition of 'disabled persons' is based on the definition used for access to certain benefits (such as the attendance allowance) and is drawn very narrowly. In practice it excludes those with degenerative diseases (such as Alzheimer's) whose mental capacities are currently moderately impaired but who are bound to deteriorate over time. It also excludes those with fluctuating mental capacity (as found in many mental illnesses, such as depression) and those with drug or alcohol dependency. In many of these cases it would clearly be appropriate to set up arrangements now to help

the vulnerable relative in the future, but any family establishing a trust to provide funding under the control of trustees faces significant tax penalties. Such penalties seem particularly inappropriate given that quite often the situation is one in which a family of relatively modest means is simply trying to do what is best for a relative with a degenerative illness or mental health problem.

Recommendation: The current rules often impose tax penalties on families setting up trust arrangements to protect the interests of those diagnosed with degenerative diseases or suffering mental illness. Government should extend the relief, which currently applies to trusts for a very narrowly defined group of 'disabled persons', to trusts established for persons who have partial, fluctuating or progressive illnesses or conditions which do or will have the effect of significantly reducing their ability to administer their property or manage their affairs.

Making it easier for families to use powers of attorney

Families who want to help a vulnerable relative manage their day to day affairs will often wish to set up a lasting power of attorney so that they can run a bank account and pay bills on behalf of their relative. These powers of attorney need to be registered with

the Office of the Public Guardian. STEP, alongside other professional bodies, campaigned to resolve the initial problems of excessive bureaucracy in this process and we welcome recent improvements in the registration system.

Nevertheless, many families still encounter significant problems when they try to use lasting powers of attorney. Staff in financial institutions, utilities and other organisations will frequently not accept perfectly valid powers of attorney, variously citing 'money laundering rules', 'data protection' or just 'company policy' for not dealing with anyone other than the named account holder. This can cause immense frustration and further expense to families. It also creates fresh dangers of abuse. In practice the current system often leads to 'informal arrangements' where friends or neighbours are given PIN numbers or internet passwords - arrangements which can create significant risks of financial abuse of the elderly and vulnerable.

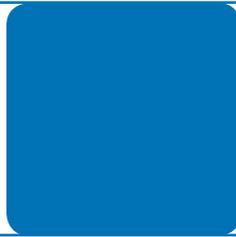
Recommendation: In the face of an ageing population it is unacceptable that basic tools to help the elderly, such as powers of attorney, are still poorly recognised by many organisations. It should be a regulatory requirement that staff in areas such as financial services should undergo basic training in issues such as how powers of attorney work. This would sit alongside the basic training they already receive in areas such as anti-money laundering procedures.

Taking fraud seriously

STEP members report a strong rise in the number of attempted frauds and thefts from the elderly and vulnerable, as well as attempted probate fraud on the estates of the recently deceased. Such attempted frauds can be particularly distressing for the family and the problem is in danger of becoming endemic. Some time ago the RNIB estimated that such fraud was now equivalent to over GBP150 million a year, but more recently the BBC has reported a ten-fold increase in some types of attempted fraud against estates.⁸

In spite of the growing scale of this problem, many STEP members also report that too often such crimes appear to attract very little interest from the police. The City of London Police has echoed the view that 'fraud is not seen as a priority for most forces', because it is generally not part of the target system set down for the police.⁹ To try and defraud a grieving family is a particularly heartless crime that is becoming increasingly common. Tackling such crimes should be given a priority that reflects the distress such attempted frauds can create.

Recommendation: The BBC has reported a ten-fold increase in some types of attempted fraud against estates, a statistic which matches the experience of many STEP members. This problem urgently needs tackling by making such frauds a priority in police targets commensurate with the distress they cause families.



Modernising Our Inheritance Laws

Protecting consumers by regulating will writers

STEP believes that everyone should be encouraged to have a will. A will helps ensure that someone's estate will be used as they would wish after their death. Passing on an estate is also probably the biggest financial transaction anyone will ever plan for. Those with relatively simple affairs can often draft a usable will themselves with the help of some research. Those with more complex affairs, however, are usually best advised to seek professional advice. The cost of such advice will normally be very modest relative to the potential cost and family distress that can be caused if, for example, a badly drafted will fails to do what was intended or is contested.

Recent survey evidence suggests that 12 per cent of families suffer disputes or disagreements over inheritance and possibly as many as 3 per cent of wills currently fail.¹⁰ Indeed some charities, such as the National Trust, now suggest that as many as 1 in 10 wills leaving bequests to them are challenged.¹¹ There is also a consensus among professionals that the number of wills being contested is on a strongly rising trend. Quite often these disputes relate to poor drafting and can result in legal costs that swallow up much of the estate under dispute.

The problem consumers currently face is that the business of offering professional advice to those wanting to make a will is totally unregulated. As Lord

Hunt, in his recent 'Review of the Regulation of Legal Services' noted, most people 'would surely be taken aback to learn that anyone can currently set himself or herself up as a will writer.'¹² They need have no technical qualifications, negligence insurance or continuity arrangements to protect clients should they cease trading for whatever reason. Will writing is totally unregulated and there is no requirement for will writers to be subject to any professional body's code of conduct or disciplinary proceedings. A survey conducted for the Institute of Professional Will Writers found that 78 per cent of the public thought that these issues should be remedied via regulation of will writers.¹³

Recommendation: There is growing evidence that due to poor drafting a significant number of wills are failing or being contested in the courts, often at considerable expense. Those who write wills professionally should be regulated to ensure minimum standards of competence and behaviour and to give the public protection in form of negligence insurance and continuity arrangements.

Meeting the challenges facing cross-border families

The UK legal and tax systems have failed to keep pace with the increasing mobility of the population. 5.5 million Britons live abroad and 1 in 12 UK pensioners have retired overseas. Moving the other

way, 6.5 million (one in nine) UK residents were born abroad and in London alone a third of residents (2.4 million) come from overseas.¹⁴

One of the many challenges that can flow from modern cross-border families is what happens in terms of wills and their estate when someone lives in one country but has property in another. The EU has drafted proposals aimed at simplifying rules and procedures related to cross-border inheritance (Brussels IV) and STEP argues strongly that the UK should engage positively in the discussions around these proposals. Many families, however, will have strong links outside the EU, in areas such as Asia or the Caribbean. The UK authorities should launch a review to consider the increasingly frequent problems they encounter, not only with respect to inheritance laws, but also with issues such as cross-border recognition of trusts and powers of attorney. The UK tax system also needs to adapt to the growth in cross-border families. For many such families double taxation is a major issue that requires careful planning and advice to avoid.

Recommendation: With 5.5 million Britons living abroad, including 1 in 12 pensioners, and 6.5 million UK residents born overseas, including a third of all Londoners, it is important that the UK legal and tax system acknowledges the issues faced by cross-border families. The UK should engage positively with EU initiatives, such as Brussels IV, which are aimed at simplifying rules and procedures related to cross-border inheritance and also look closely at how the risk of double taxation can be minimised.

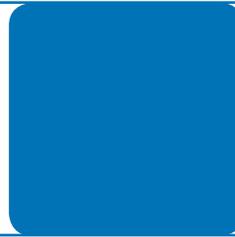
Embedding a culture of giving and volunteering

Trust and estate planning has a key role to play in

supporting UK charities. Survey evidence suggests that over 20 per cent of people intend to leave money to a charity in their will.¹⁵ Indeed legacies provide about GBP2 billion a year to charities, 10 per cent of their total income.¹⁶ In addition, GBP3.3 billion flowed from trusts and foundations into UK charitable activities in 2005/6.¹⁷ STEP members are trusted advisors to many families and a natural first port of call for a client wanting help on giving. They form part of a network comprising: solicitors, accountants, investment advisors and others, all of whom can play a part in helping their clients structure charitable and philanthropic donations to best effect.

The practical problem is that while the majority of advisors offer philanthropy advice to clients, often that advice is little beyond tax advice and advice on the structuring of foundations or trusts. With better co-ordination between advisors, charities and government much more could be done to encourage a culture of giving in the UK by better informing trustees, advisors and their clients of the opportunities available, ensuring the tax system works as effectively as possible to support charity and philanthropy and ensuring that charitable organisations promote themselves in the most effective manner to prospective donors.

Recommendation: Trust and estate planning plays a key role in supporting charity and philanthropy, with legacies providing around 10 per cent of charities' total income and a further GBP3.3 billion a year flowing from trusts and foundations. Nevertheless, much more can be done to both encourage civil involvement and embed a culture of giving by individuals and families. Government should establish a permanent framework to co-ordinate the work of family advisors, charitable bodies and the public sector to promote education and training on philanthropy and remove bureaucratic barriers to giving.



Creating the Capital to Support the Elderly and Vulnerable

Shifting the focus from 'savings' to 'capital accumulation'

STEP members spend much of their working lives advising families on how best to arrange their affairs to fund the long-term support of family members. Inevitably professional planning can only go so far in helping people with such issues. People need a certain level of funds if they are to live without state support. Clearly in many cases the real answer is that we need to make it easier for people to save for different stages of their life. This is recognised in government and the Treasury has itself argued that building a framework that encourages families to save can play a key role in both providing 'people with independence throughout their lives, security if things go wrong, and comfort in old age.'¹⁸

Successive governments have therefore launched initiatives to encourage savings, with the main emphasis being on encouraging pension provision. We now spend over GBP27 billion (almost 2 per cent of GDP) on tax breaks for private pensions¹⁹, compared with GBP2 billion on tax breaks for ISAs.²⁰ The problem is that in spite of this huge support from taxpayers, the UK long term savings market is not working. Over the past decade the proportion of income being saved (the saving ratio) has tested record lows, even if it has recently begun to rebound a

little. Indeed half of UK adults are saving nothing for their pension²¹ and 30 per cent have no savings at all.²²

In the face of these statistics it seems appropriate to think afresh about the factors that give people confidence to put assets aside for the longer term. The normal barriers between 'savings', 'pensions' and 'assets' raised by government policies need to be broken down. What is needed are policies that will both encourage broadly based 'capital accumulation' and, just as importantly, make it easier for families to use their capital to support themselves in times of need.

Individual Savings Accounts (ISAs) are widely seen as one of the more successful government initiatives aimed at encouraging savings. HMRC research shows that 37 per cent of people have an ISA, around a third of people say they have been encouraged to save by ISAs and around one in four people say ISAs are the main reason they save.²³ As well as their tax advantages, ISAs can adapt through people's lives. While younger people typically use ISAs for 'rainy day/emergencies savings', most people in the 45-64 age group use ISAs 'specifically for retirement.' Saving for retirement is given as the main reason for saving in an ISA by 10 per cent of people overall.²⁴ Another attraction of ISAs is the ability to withdraw savings easily if needed, but perhaps because of the flexibility to suit differing needs at differing periods of peoples' lives, in practice savings in ISAs are relatively 'sticky.' HMRC research found that 61 per cent of ISA savers had never made a withdrawal.²⁵



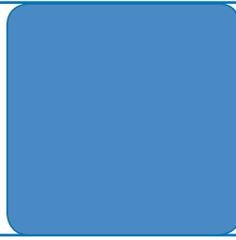
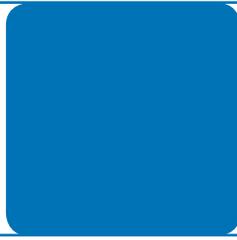
Other countries have successfully developed simple, flexible and transparent schemes analogous to ISAs, but more broadly focused on building long term savings, particularly pensions. Examples range from the Kiwisaver in New Zealand to 401(k) schemes and Life Time Savings Accounts in the US. Looking at the lessons learnt from such schemes, there have been a variety of suggestions²⁶ as to how the UK should build on the success of ISAs, preserving their simplicity, flexibility and cheapness, but developing them into one of the main platforms for pension savings. STEP welcomes any proposal that might help people build resources for retirement or to help support family members.

Recommendation: In spite of huge tax subsidies, half of UK adults are saving nothing for their pension and around a third have no savings at all. It is time to think afresh, breaking down the barriers between 'savings', 'pensions' and 'assets' and focusing on encouraging 'capital accumulation' and making it

easier for families to use their capital resources to support themselves in times of need. The relative success of ISAs highlights the importance of flexibility and transparency in schemes to help people build their resources, as does the success of several overseas long term savings schemes.

Helping the young

For many people the key to accumulating the sort of capital that will permit a reasonable lifestyle in retirement is avoiding going into excessive debt while they are younger. The help and support they receive from grandparents and other family members when they are young can be crucial here. Survey evidence suggests that 48 per cent of families have, or plan to, help family members financially while they are alive, rather than leave money to them in their will.²⁷ Accumulation & Maintenance (A&M) Trusts were a popular route to give children financial help, while at the same time safeguarding against young people spending their savings frivolously. Unfortunately, tax changes introduced without consultation in the 2006 *Finance Bill* effectively penalised the setting up of A&M Trusts and the options for helping children are now limited. Child Trusts Funds, for example, allow only very limited annual contributions (which, even if used to the full, are unlikely even to cover the costs of going to university). Consideration should be given to either removing the tax barriers to A&M Trusts for children or developing new means for families



to support children, perhaps by lowering the age at which ISAs can be opened for children (currently 16 for cash ISAs, 18 for share ISAs).

Recommendation: For many people the help they receive from grandparents and others in the family when they are young can be a crucial factor in allowing them to ultimately build enough capital to fund retirement. Consideration should be given to either removing the tax barriers to A&M Trusts for children or developing new means for families to give long term support to children, perhaps by lowering the age at which ISAs can be opened for children (currently 16 for cash ISAs, 18 for share ISAs).

Encouraging lump sum savings

The years in which someone leaves university (often these days with substantial debt), buys a first house and starts a family are often a period of huge financial strain. For many, balance is only restored when they receive a lump sum in later life, often their share from their parents' estate. Many wish to save this lump sum, but the annual limits on ISA savings mean that one of the most popular forms of savings account is often not suitable. Similar problems arise when grandparents leave bequests to their grandchildren. Better provision should be made for savers to be able

to save such lump sums into ISAs, perhaps allowing them to aggregate the current annual limits over several years (analogous to corporate tax reliefs), possibly with restrictions on the circumstances in which such lump sums can be withdrawn.

Recommendation: Paying for university, buying a first house and starting a family typically impose a heavy strain on personal finances which is often only relieved when someone receives a lump sum representing their share from their parents' estate. Better provision should be made for savers to be able to save such lump sums, perhaps allowing them to aggregate the current ISA annual limits over several years.

Making better use of non-financial assets

STEP practitioners have also been considering more radical reforms to our current pensions and savings arrangements. The current debate about pensions and savings focuses almost exclusively on encouraging people to build up their financial assets. Realistically, particularly in the context of low annuity rates, many families will find it impossible to build up a pool of financial assets large enough to provide an income to support them adequately in retirement. Financial assets are nevertheless only a part of the typical household's net wealth. The OECD estimates

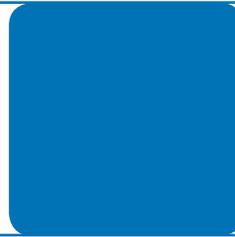
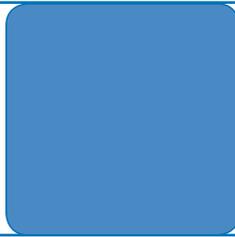
that non-financial assets, dominated by housing, comprise around 65 per cent of UK household wealth.²⁸ Over two thirds of households own their own home, with the median value of homes being put at GBP190,000.²⁹ In the light of such figures, it clearly makes sense to take account of the way in which families build up their overall wealth, not just savings in financial assets, and how they can then use them to support themselves when needed. Around 40 per cent of individuals say that property and other non-financial assets already form part of their retirement planning and over 10 per cent of people see property as their sole or largest source of income.³⁰

To reflect these realities, we would recommend that the government should consider establishing a much more broadly based long term savings scheme than we have seen previously. STEP has drawn up preliminary proposals for one such broadly based scheme, which we have labelled 'Lifetime Trusts.' Like ISAs, Lifetime Trusts would offer savers transparency, easy control of where their savings are invested and the ability to withdraw funds on occasions other than just retirement. Unlike ISAs and most other current savings and pension arrangements, savers would be able to transfer non-financial assets, including the equity in their house, into the Lifetime Trust. They and their employer could also agree that pension contributions, which would normally go to a DC pension scheme, could go to their Lifetime Trust instead.

When it came to retirement the saver could use the value of either all or part of the Lifetime Trust to buy an annuity, as with current personal pension schemes. Alternatively they could use the value of either all or part of the trust as security, with the trustee's permission, to borrow against (mimicking current UK equity release schemes, but providing additional safeguards). This might be particularly useful in allowing people to respond to particular pre-defined life events, such as redundancy. In the US the popular 401k savings schemes see around

15 per cent of savers³¹ use the equivalent facility at some point. Alternatively, after retirement or in certain circumstances, such as redundancy, savers could opt to take an investment income from their Lifetime Trust, while leaving the capital preserved.

Around 20 per cent of savers say the main reason they save is to provide for other family members³² and many people have also told us that they would be likely to save more if they could be confident that their family would enjoy the full benefits of their savings if they die. This is currently a particular problem with many pension arrangements, where savers are forced to take an annuity by age 75, often with very low returns, and surrender the opportunity to leave any excess in the fund over and above their pension needs to their children. A key attraction of Lifetime Trusts for some, therefore, would be that if they opted to take an income from the Trust on retirement, rather than an annuity, the capital value of the trust would form part



of their estate and go to their heirs after death. Indeed, there may be an argument to allow the residue in someone's Lifetime Trust, perhaps subject to an upper limit, to pass on favourable IHT terms directly to the Lifetime Trusts of their heirs, if this has the effect of allowing successive generations to build up funds for retirement and avoid being reliant on state provision.

Recommendation: Almost 65 per cent of household net wealth is held in non-financial assets. Consideration should be given as to how families can best use these assets, alongside their savings in financial assets, to support them through retirement and other key life events. STEP has developed preliminary proposals for Lifetime Trusts, which would allow financial and non-financial assets to be pooled. Lifetime Trusts would significantly boost the funds available at retirement for the typical household, while allowing much more flexibility than most current pension savings schemes. They would also allow savers to pass the residue of their Lifetime Trust on to future generations, adding significantly to the incentive to save.

Lifetime Trusts could provide a radical new approach to long term savings in the UK. The main features of Lifetime Trusts would be:

- The saver could place a wide-range of both financial and non-financial assets in their Lifetime Trust, including cash, shares and property (including their own residence). They and their employer could also agree that pension contributions, which would normally go to a DC pension scheme, could go to their Lifetime Trust instead.
- Tax relief on income accumulated within the trust. Free of capital gains tax within the trust. Tax at savers marginal rate on income taken from the trust.
- At retirement, saver would have choice of either converting trust into annuity or taking income from trust and preserving all or part of the capital. They would also be able to borrow against the value of the property in the trust to help fund an annuity.
- Savers would be allowed limited early access to their Lifetime Trust (or the income from the trust) in certain pre-defined circumstances: e.g. redundancy, ill health, or to fund a deposit for a first home.
- On death, the capital value of the Lifetime Trust would form part of the estate of the saver. Possibility of favourable IHT treatment if it passes straight to the Lifetime Trust of heirs.
- Written under trust law with a trustee acting for the benefit of the saver and controlling the assets.

Building a Better Tax System

Establishing a tax law review body

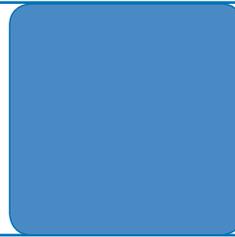
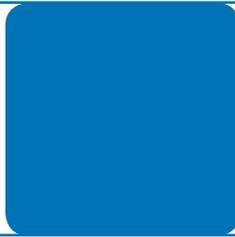
The respected Institute for Fiscal Studies recently concluded that for the UK to remain competitive, 'it needs a tax system that is sufficiently clear for business to be able to operate with confidence, that is stable so that long term decisions can be made without significant risk of tax change and that is fiscally comparable to its competitors' tax systems.'³³ Few are confident that the UK tax system currently meets these criteria for competitive success.

We have what is widely reported to be the longest tax code in the world.³⁴ In this context it is hardly surprising that increasingly taxpayers and their advisors complain about the complexity of the UK tax system and the costs of ensuring compliance. A recent National Audit Office report on HMRC's dealings with older people recommended: 'The Department should explore with HM Treasury the cost effectiveness of the current structure ... and the scope to simplify the arrangements.'³⁵ Many will feel that this recommendation could be usefully applied well beyond HMRC's dealings with the elderly.

In practice many of the problems encountered regarding the tax system reflect the fact that it is struggling to keep pace with rapid changes in both society and the economy. This core issue is compounded by the fact that when changes to



the tax system are proposed, it is often without consultation and with limited parliamentary scrutiny and discussion. These problems are widely recognised and several organisations, including the IFS Tax Law Review Committee, the Hansard Society and a variety of professional bodies have called for the establishment of a body with an overall remit to simplify and improve our tax laws, either in the form of a Tax Commission analogous to the Law Commission or in the form of a Joint Parliamentary Committee on Taxation. STEP strongly supports these calls.



Recommendation: The UK is increasingly at a competitive disadvantage because of complex and uncertain tax laws. STEP strongly supports the consensus among professional bodies and others that a new body is needed with the specific remit of simplifying and improving our tax laws. This body could be either in the form of a Tax Law Commission or a Joint Parliamentary Committee, but its remit should be drawn widely, it should be empowered to consult freely with the professional bodies and others and it should be resourced to allow rapid progress.

Recognising the legitimacy of tax planning

Tax planning plays a key role in our economy and society. People expect their tax advisors to ensure they pay the right amount of tax and to give them clear guidance as to when that tax will need to be paid, so that they can draw up their financial plans accordingly. For example, family businesses account for over 30 per cent of GDP and employ 9.5 million people³⁶ and the long term future of such businesses rests crucially on careful trust and estate planning. Without such planning few family businesses would survive passing from one generation to another.

The traditional legal position around tax planning has been clear. Tax evasion was illegal, tax

avoidance – arranging your affairs within the law to minimise tax liabilities – has in contrast long been considered entirely legitimate. In recent years, however, government has sought to blur this distinction between evasion and avoidance, making frequent criticism of what it calls ‘unacceptable’ or ‘aggressive’ tax avoidance techniques. Indeed the government has recently sought to attempt to impose fresh requirements on taxpayers and their advisors. The HMRC consultation on a ‘Code of Conduct on Taxation for Banks’ suggested that banks should ‘not undertake tax planning that aims to achieve a tax result that is contrary to the intentions of Parliament.’³⁷ HMRC’s own code of practice appears to go further, reportedly suggesting that unacceptable avoidance is a situation where more tax would have been paid ‘if Parliament turned its mind to the specific issue in question.’³⁸

There is a clear danger that taxpayers and their advisors will be left in a situation where not only do they have to interpret long and often complex laws, they also have to interpret ‘the intentions of Parliament’ where this differs from the laws parliament passed and perhaps even take into account what parliament would have intended if it had considered a particular issue that in fact it had not considered. This is contrary to any concept of natural justice. STEP recommends that an independent review should be launched to establish a clear distinction between ‘acceptable’ and ‘unacceptable’ tax planning. This review should give due regard to both the need to

defend the public purse and the importance of people being able to plan their affairs in ways that are both tax efficient and legally certain.

Recommendation: Certainty for both taxpayers and advisors has been undermined by repeated government assaults on the legitimacy of tax planning advice previously considered acceptable. An independent review should be launched to establish a clear distinction between ‘acceptable’ and ‘unacceptable’ tax planning. This review should give due regard to both the need to defend the public purse and the importance of people being able to plan their affairs in ways that are both tax efficient and legally certain.

Ensuring adequate consultation

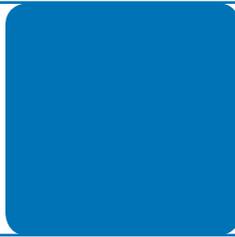
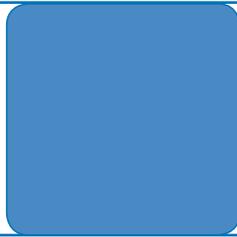
STEP endorses the view of the IFS Tax Law Committee that ‘consultation is not and should not become a substitute for Parliamentary scrutiny.’³⁹ Consultation can nevertheless play a vital role in avoiding unintended consequences and accurately assessing likely costs and benefits from proposed legislation.

For example, the 2006 Finance Bill introduced significant changes to the tax treatment of commonly used trusts without any consultation with the professional bodies. This legislation was in practice



retrospective and forced many families to unwind long standing arrangements to help and protect younger family members, incurring substantial costs. On most estimates these costs substantially outweighed any potential revenue gain to the government. It seems likely that the government may have been able to achieve its end objectives much less disruptively had it instead consulted in advance with the professional bodies.

In other cases, such as recent changes to the residence and domicile rules, consultations were launched, but either after it was clear that most of the key decisions had already been made, or without any clear indication of what the strategic aims of the proposed policy change were. This made it very hard for outside commentators to suggest more effective ways of achieving those aims. STEP would very much endorse the views of the House of Lords Economic Affairs



Committee, which has noted: 'We are firmly in favour of consultation...If clarity and certainty are to be achieved, consultation should in principle take place as early as possible whenever there is any significant technical content.'⁴⁰

Recommendation: Consultation can play a vital role in avoiding unintended consequences and accurately assessing likely costs and benefits from proposed legislation. Welcome progress has been made in opening up proposed tax law changes to consultation, but there are still too many instances of policy announcements without adequate prior consultation. It should be the norm that changes to tax laws (as opposed to changes in tax rates) should be made after public consultation and after a rigorous cost benefit assessment.

Improving non-legislative rule making

For taxpayers and advisors alike, changes to HMRC 'Guidance' and 'Explanatory Notes' can in practice have just as big an impact as changes to tax legislation in the *Finance Bill*. Such changes from HMRC are equivalent to non-legislative rule making and they can fundamentally alter taxpayers' understanding of the tax rules and require significant restructuring of their affairs. Such changes are nevertheless typically announced without any

opportunity for parliamentary scrutiny and often without any formal external consultation. STEP believes that the same good governance arguments that support consultation before legislative changes also apply to changes in non-legislative rules in the form of HMRC 'Guidance' and 'Explanatory Notes.'

Recommendation: In practice changes in HMRC 'Guidance' and 'Explanatory Notes' can have as much impact on taxpayers as changes in legislation contained in the *Finance Bill*. Even so, such changes are typically announced without any opportunity for parliamentary scrutiny and often without any formal external consultation. Changes to HMRC 'Guidance' and 'Practice Notes' should be subject to the same consultation processes as changes to tax law.



References

¹ Source: Social Trends 2009, ONS, pg 63

² Source: HMRC

³ Source: *The Times*, 6 October 2009

⁴ Source: 'Psychiatric morbidity among adults living in private households in Great Britain,' ONS 2000

⁵ For more details on trust and their uses, see 'Trusts Explained', available (for free) at:<http://www.step.org/publications/leaflets>

⁶ Source: The Alzheimer's Society

⁷ Source: 'Paying the Price, the Cost of Mental Health Care in England and Wales to 2026', Kings Fund

⁸ Source: 'You and Yours' report, BBC Radio 4, 24 March 2008

⁹ Source: 'Policing in the 21st Century', House of Commons, Home Affairs Select Committee, HC 364-I, para 34

¹⁰ Source: Will Aid research survey, 7 October 2009

¹¹ Source: *Third Sector*, 29 October 2009

¹² 'The Hunt Review of Legal Services', October 2009, The Law Society

¹³ Institute of Professional Will Writers, June 2007.

¹⁴ Source: ONS, February 2009

¹⁵ Source: 'Wills and Trusts Research Report 2009', Standard Life

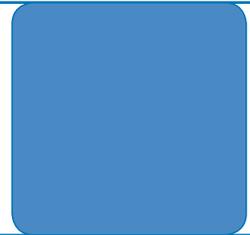
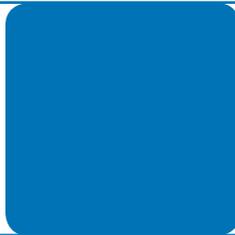
¹⁶ Source: NCVO

¹⁷ Source: 'Charity Trends', Charities Aid Foundation

¹⁸ Source: Economic Secretary to the Treasury, speech to the ABI Savings Conference, November 2008

¹⁹ Source: Pensions Policy Institute: <http://www.pensionspolicyinstitute.org.uk/default.asp?p=92>

²⁰ Source: HMRC: http://www.hmrc.gov.uk/stats/tax_expenditures/table1-5.pdf



²¹ Source: BBC survey: <http://news.bbc.co.uk/1/hi/business/8068728.stm>

²² Source: 'Wealth and Assets Survey, 2008', ONS

²³ Source: <http://www.hmrc.gov.uk/research/working-paper-isa.pdf>

²⁴ Source: <http://www.hmrc.gov.uk/research/working-paper-isa.pdf>

²⁵ Source: <http://www.hmrc.gov.uk/research/working-paper-isa.pdf>

²⁶ See for example the suggestion for 'Life Time Savings' account by Dr Ros Altman (http://www.rosaltmann.com/pdf/Lifetime_Savings_Account_Framework2001.pdf), as well as the 2007 proposals by The Conservative Party: 'Economic Competitiveness Policy Group'

²⁷ Source: 'Wills and Trusts Research Report 2009', Standard Life

²⁸ Source; 'Households' Wealth Composition Across OECD Countries and Financial Risk Borne By Households', OECD, 2008

²⁹ Source: 'Wealth in Great Britain', ONS, December 2009

³⁰ Source: 'Wealth in Great Britain', ONS, December 2009

³¹ Source: *Financial Times*, 29 October 2009

³² Source: 'Wealth in Great Britain', ONS, December 2009

³³ Source: 'Countering Tax Avoidance in the UK: Which Way Forward?' IFS, February 2009

³⁴ Source: LexisNexis, quoted in *The Daily Telegraph*, 6 September 2009

³⁵ Source: 'HMRC – Dealing with the tax obligation of older people', NAO, October 2009

³⁶ Source: 'The UK Family Business Sector', Institute for Family Business, February 2008

³⁷ Source: 'Code of Conduct on Taxation for Banks', HMRC, 29 June 2009

³⁸ Source: *The Daily Telegraph*, 21 October 2009

³⁹ Source: 'Making Tax Law', IFS Tax Law Committee, March 2003.

⁴⁰ Source: House of Lords Select Committee on Economic Affairs, Second Report, *Finance Bill* 2008

2010 | Helping Families Secure Their Future

- an agenda for policymakers

The Society of Trust and Estate Practitioners (STEP) is a unique professional body providing members with a local, national and international learning business network. STEP provides education, training, representation and networking for its members, who are professionals specialising in trusts and estates, executorship, administration and related taxes.

Full members of STEP are the most experienced and senior practitioners in the field of trusts and estates.

Visit [www.step.org/
findapractitioner](http://www.step.org/findapractitioner)
for further details

STEP Worldwide

Artillery House (South)
11-19 Artillery Row
London SW1P 1RT
England, UK
Tel: +44 (0)20 7340 0500
Fax: +44 (0)20 7340 0501
Email: step@step.org
Website: www.step.org

STEP Canada

2225 Sheppard Ave
East Suite 1001 Toronto
Ontario M2J 5C2
Canada
Tel: 416 491 4949
Fax: 416 491 9499
Email: stepcanada@step.ca
Website: www.step.ca

The Society of Trust and Estate Practitioners is a company limited by guarantee and incorporated in England and Wales under the Companies Act 1985.
Registered No: 2632423.
Registered Office:
Artillery House (South)
11-19 Artillery Row
London SW1P 1RT

