withersworldwide

Incentives for charitable legacies: new precedent clause from STEP

16 NOVEMBER 2011

Alana Petraske
PARTNER | US

CATEGORY:
ARTICLE

The Chancellor's March 2011 Budget announced that a reduced rate of inheritance tax (IHT) will be introduced for those who donate 10% or more of their net estate to charity. HM Revenue and Customs held a consultation on the proposal which closed on 31 August 2011, and draft legislation for further consultation is expected early in December.

For deaths on or after 6 April 2012, it is now proposed that individuals who include charitable legacies in their will of at least 10% of their net taxable estate will benefit from a 36% rate of IHT, a 10% reduction from the usual IHT rate of 40%.
The purpose of this relief is to incentivise giving generally. It should be of particular interest for potential benefactors who are already considering leaving legacies and who may find under the proposed relief that they can leave more to charity without taking away from the amount left to their non-charitable beneficiaries.

Four – the magic number?

As can be seen from the example below, an individual who would have left a 4% legacy to charity under the current regime could, under the proposed regime, leave the same amount to his or her non-charitable beneficiaries after tax even if the charitable gift is increased to 10% of the net taxable estate.

Current regime	
Gross estate	£1,325,000
Nil rate band	£325,000
Taxable estate	£1,000,000
Legacy to charity (4%)	£40,000
Taxable estate	£960,000
IHT at 40%	£384,000
Net estate after tax	£576,000

Proposed regime

Gross estate

£1,325,000

Nil rate band

£325,000

Taxable estate

£1,000,000

Legacy to charity (10%)

£100,000

Taxable estate

£900,000

IHT at 36%

£324,000

Net estate after tax

£576,000

In other words, depending on the value of the originally intended legacy, a donor may be able to ‘top up’ the legacy to 10% without taking away from the amount ultimately enjoyed by the non-charitable beneficiaries. A 10% gift on death under the proposed regime will also be more tax-efficient than making a comparable lifetime gift via the gift aid scheme.

That a donor may **more than double** the intended legacy amount without taking away from the non-charitable beneficiaries of the estate is a fairly compelling ‘ask’. Perhaps even more compelling is that if a donor is planning a legacy of between 4% and 10% of the taxable estate, by increasing the legacy to 10% the taxable residuary beneficiaries actually receive more than they would have done. Any charity that seeks legacy income or engages in major donor fundraising will want to ensure that its fundraisers are able to explain this to interested donors.

Legacy10, a campaign to promote legacy giving in the UK was launched at the start of November and is intended to be constituted as an independent registered charity.

It is difficult to know whether the proposal, once enacted in its final form, will encourage legacy giving. As many have pointed out, the number of estates within the scope of IHT in the first place is relatively low and the complexity of the reduction may discourage some testators. There has also been concern expressed about the potential impact the reduction may have on lifetime giving, particularly at a time when charities have such great need of income to meet present demands.

Nevertheless, charities seeking legacy income will want to ensure their fundraising teams are familiar with the reduction and that materials are up to date since any legacy successfully solicited under this regime will by definition be a significant gift.
STEP has produced a draft model clause to be adopted in the wills of persons wishing to leave a legacy qualifying for the new relief.

“Click here to read the draft clause”: which will be reviewed and updated once the draft and then final legislation are available.

Authors

Alana Petraske

PARTNER | NEW YORK

Charities

+1 212 848 9849

alana.petraske@withersworldwide.com