The Charity Law & Practice Review

TAXATION NEWS

Robert Venables QC[1]

Review of Charity Taxation

Publication of the long overdue review of charity taxation was eventually made on 9th March 1999. One is reminded of Horace's *Ars Poetica* line 139:

"Parturiunt montes, nascetur ridiculus mus."[2]

Inheritance Tax

A thorny question which often arises when the residue of a deceased's estate is shared between charities and non-charities is whether the division into the stated shares should be made before or after the payment of inheritance tax. As gifts to charities are in general exempt from inheritance tax but other gifts are not, it is in the interests of charities that the division be made before the payment of tax. The question in every case is one of construction of the particular will. No doubt, most testators wish the charity to have the benefit of the exemption and do not wish to give a greater gross share to the non-exempt beneficiaries, so that they take the same net shares as the charities' gross and net shares. One of the problems is that inheritance tax is a testamentary expense[3] and that the residue is often defined in terms of what remains after payment of testamentary expenses. The position is further complicated by Inheritance Tax Act 1984 section 41, which provides: "Notwithstanding the terms of any disposition—... (b) none of the tax attributable to the value of the property comprised in residue shall fall on any gift of a share of

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2 "Mountains will labour and give birth to - one pathetic little mouse".

3 Inheritance Tax Act 1984 section 211.

residue if or to the extent that the transfer is exempt with respect to the gift."

In *Re Ratcliffe (deceased); Holmes and another v McMullan* [1999] STC 262, the testatrix's will provided:

> "I give devise and bequeath all my ... estate unto my Trustees upon trust ... after payment thereout of my debts and funeral and testamentary expenses to stand possessed of the residue as to one-half part thereof for John ... and Edward ... in equal shares absolutely ... and as to the remainder of my estate upon trust for the following Charities in equal shares ..."

The charities contended that the two half shares of residue were to be calculated after providing for the debts and funeral and testamentary expenses but before payment of the inheritance tax due in respect of the individuals' half share. Hence, the net benefit received by the individuals would be less than the net benefit received by the charities, on account of the deduction for inheritance tax. The individuals contended that there were to be equal half shares of net residue after payment of the appropriate amount of inheritance tax, which was to be treated as a testamentary expense by virtue of section 211 of the 1984 Act.

Blackburne J held that the charities' contentions were correct. He refused to follow an earlier decision of the Chancery Division, *Re Benham's Will Trusts, Lockhart v Harker, Read and the Royal National Lifeboat Institution* [1995] STC 210. He was clearly persuaded by the commonsense approach to what the testatrix intended, rather than to the literal wording of the will, which in my view clearly directed a division of a net fund, after deduction of inheritance tax.

If a testator wishes to ensure that the division between (a) charitable and other exempt beneficiaries and (b) non-exempt beneficiaries is on a net basis, very clear words to that effect will now be needed.