

DEATH, PERSONAL REPRESENTATIVES AND LEGATEES

This Help Sheet gives you information to help you complete the Capital Gains Pages of your Tax Return.

It is only an introduction. If you are in any doubt about your tax circumstances you should ask your tax adviser.

Your Inland Revenue office will also be pleased to help. You can ask to see the Inland Revenue Capital Gains Manual which explains in detail the rules for particular situations.

If you need information regarding Inheritance Tax, please contact the Capital Taxes Office.

MEANING OF EXPRESSIONS USED

In general these notes refer to the legal terms used in England and Wales. In most respects the taxation principles are the same where the law in Scotland or Northern Ireland applies. However, the general law background may differ slightly. Because of the differences in general law some of the terms used for cases outside England and Wales may be different from those used in these notes.

Personal representatives is the term used for the persons who are responsible for settling the affairs of a deceased person. It includes both executors and administrators (in Scotland, executors nominate and executors dative).

The administration period is the period when the personal representatives are settling the estate. It starts on the death of the deceased person and usually ends when the residue of the estate has been ascertained.

The residue of the estate is ascertained when the net balance of the estate has been identified and sufficient funds have been provided to enable any liabilities to be paid.

A legatee is defined for Capital Gains Tax purposes as including any person benefiting from a testamentary disposition (that is, normally a Will), or on an intestacy or a partial intestacy.

GENERAL POSITION

When a person dies leaving assets which will be passed to his or her legatees under the terms of a Will, or under the rules where there is no Will, there will be no Capital Gains Tax charge. Instead there are special rules.

In broad terms, the assets which were owned by the deceased at the date of death are treated as though they had passed to the personal representatives at the date of death at their market value on that date. When the administration of the estate has been completed and the assets remaining in the estate are passed to the legatees, they are treated as though they had passed to the legatees at the date of death at their market value on that date.

Example 1

Mr Andrews dies on 10.10.98. At the time of his death he owns a house, value £75,000, some shares, value £25,000 and money in a bank account, £20,000. All of these are treated as passing to his personal representatives at those values.

The administration of the estate is completed on 31.1.2000. At that date the house is worth £80,000 and the shares £35,000. Those assets are passed to Mr Andrews' legatees but are treated as having been acquired by the legatees on 10.10.98 at values of £75,000 and £25,000.

CAPITAL GAINS TAX LIABILITY FOR PERIODS UP TO THE DATE OF DEATH

Before death the deceased may have disposed of assets. There may be Capital Gains Tax arising. Returns of the gains may not have been sent to the Inland Revenue, or the correct amount of tax may not have been agreed. The personal representatives must agree the liability of the deceased up to the date of death with the Inspector. This will include:

- settling any points that are open for those years in which Tax Returns have already been made
- completing a Tax Return for the period from the previous 6 April to the date of death, plus Tax Returns for any years where a return is outstanding, **and**
- agreeing the liability for those years and making appropriate payments.

Annual exemption

There is no restriction imposed on the amount of the annual exemption for a year in which an individual dies. The whole of the exemption is available to set against gains arising in that year, however short the period from 6 April to the date of death.

— Losses in year of death

If the deceased disposed of assets in the part of the tax year before death, there may have been losses on some assets rather than gains. If so, those losses must first be set against any chargeable gains made in that period. The losses must be set against all gains, even if this reduces the net chargeable gains to below the amount of the annual exemption.

If any allowable losses remain after this has been done, those excess losses may be carried back. The losses can be set off against gains:

- arising in the three tax years prior to the tax year in which death occurs, **but**
- the losses must be set off against gains in a later year before making set offs against gains of an earlier year.

Losses carried back in this way are only set off so that the net chargeable gains are reduced to the amount of the annual exemption. The full benefit of the annual exemption is still enjoyed for those years.

Any losses which are not required to be set against gains of:

- the part of the tax year before death
- the three previous tax years

cannot be used.

Such losses cannot be used by:

- the personal representatives, **or**
- the legatees

against gains from disposals of assets acquired from the deceased.

Example 2 (Losses carried back)

Mrs Gee died on 30.9.99. In the period 6.4.99 to 30.9.99 she had chargeable gains of £1,000 and allowable losses of £10,000. In the three previous tax years her net chargeable gains were:

1996-97	£20,000
1997-98	£3,000
1998-99	£8,000

1. First set the 1999-2000 losses against her gains of that year.

1999-2000

Chargeable gains		£1,000
Allowable losses	£10,000	
Set off	£1,000	<u>£1,000</u>
Net chargeable gains		zero
Excess losses available to carry back	£9,000	

2. Set off excess losses against gains of earlier years, taking into account later years before earlier years. Therefore consider 1998-99 first.

1998-99

Chargeable gains	£8,000
Covered by annual exemption	<u>£6,800</u>
Limit set off to	£1,200

Therefore reducing Capital Gains Tax to zero.

Allowable losses brought back	£9,000
Set off 1998-99	<u>£1,200</u>
Excess loss to carry back	£7,800

3. Consider next **1997-98**. Net chargeable gains of £3,000 are already wholly covered by annual exemption. Therefore none of the losses brought back should be set against these gains.

4. Consider next 1996-97.

1996-97

Chargeable gains	£20,000
Covered by annual exemption	<u>£6,500</u>
Available to set loss against	£13,500

As this exceeds the losses brought back of £7,800, all those losses can be set against the 1996-97 assessment.

Net chargeable gains before set off	£20,000
Minus losses brought back	<u>£7,800</u>
Revised net chargeable gains for 1995-96	£12,200
Minus annual exemption	<u>£6,500</u>
Gains chargeable to tax	£5,700

CAPITAL GAINS TAX LIABILITY FOR THE PERIOD OF ADMINISTRATION

During the period of administration, the personal representatives may be liable to Capital Gains Tax if they sell or otherwise dispose of any of the assets in the estate. This does not apply when assets are passed to legatees under the terms of the Will, etc.

During this period the personal representatives have absolute control over the assets. They are **not** bare trustees or nominees for the legatees.

Where:

- an asset has not been formally transferred to a legatee (usually at the completion of the period of administration), **and**
- the asset is sold, **and**
- a gain arises,

that gain is chargeable on the personal representatives and not the legatee.

Residence status of deceased

In general terms, only individuals who are treated for tax purposes as resident or ordinarily resident in the UK are liable to Capital Gains Tax.

The personal representatives of a deceased individual are treated as having the same residence status as the deceased. So, if the deceased was not resident and not ordinarily resident in the UK before death, then the personal representatives will not be liable on any disposals even if they are themselves resident in the UK.

Where, despite being not resident, the deceased would still have been liable to Capital Gains Tax on the disposal of particular assets (for example, where the assets had been used in a trade carried on in the UK through a branch or agency), then the personal representatives will also be liable on any disposal of those assets.

If you want further information on residence and ordinary residence, ask the Orderline for the Non-residence etc. Pages.

Calculating gains and losses

In calculating gains and losses, most of the normal Capital Gains Tax rules apply to personal representatives as to individuals, but there are some differences. These are explained in this section.

The assets that were owned by the deceased at the date of death are treated as though they had passed to the personal representatives at the date of death at their market value at the date of death. This value is the 'cost' or acquisition value.

Where the personal representatives acquire assets during the course of administering the estate, the actual cost or value of those assets is used in calculating gains or losses on their disposal.

Annual exemption

The full amount of the annual exemption is allowed to personal representatives:

- for the period from the date of death to the following 5 April (no matter how short this period is), **and**
- for the two tax years following the year of death.

Where gains arise in a later year, no annual exemption is due.

Rate of tax

The chargeable gains, after deducting any annual exemption due, of the personal representatives are taxable wholly at the rate applicable to trusts. For 1999-2000 the rate is 34%. The lower rate and higher rate charges which apply to individuals do not apply to personal representatives.

For years to 1997-98 chargeable gains of the personal representatives are taxable wholly at the basic rate.

Expenses incurred by personal representatives

Personal representatives incur legal and other expenses in the administration of the estate, for instance, in obtaining a grant of probate. If they sell or dispose of some of the assets of the estate, then some of that expenditure may be allowable in calculating the gains or losses. Because of the way solicitors charge for their services, it is often difficult to isolate the allowable expenditure from other expenditure which is not allowable.

The Inland Revenue will accept calculations which include deductions for costs of establishing title which are based on a published scale. The scale is published as Statement of Practice SP8/94 (for deaths after 5 April 1993). SP7/81 deals with deaths from 1981 to 1993. (These statements are published in Inland Revenue booklet *IR131: Inland Revenue Statements of Practice*. A copy of the booklet can be obtained from the Orderline.)

Personal representatives are entitled to claim the actual expenditure where this is known.

This expenditure is only available where the personal representatives dispose of assets.

Transfer of assets to legatees

When the personal representatives have completed the administration of the estate, they will pass the assets to the legatees in accordance with the wishes of the deceased in the Will, or under rules laid down where there is no Will. The administration is usually completed when the residue of the estate has been ascertained.

When the personal representatives pass the assets to the legatees, no Capital Gains Tax is charged. Under the special rules the assets which were owned by the deceased at the date of death are

treated as though they had been acquired by the legatees at the date of death at their market value on that date (see Example 1).

Sometimes the personal representatives will themselves acquire assets during the course of the administration and these assets may be passed to legatees under the terms of the Will, etc. In that case those assets are treated as though they had been acquired by the legatees on the date the personal representatives acquired them, at the cost they were to the personal representatives or the value at which the personal representatives acquired them.

TREATMENT OF LEGATEES

All assets acquired by a legatee following a death, and which were assets owned by the deceased at the date of death, are treated as though acquired by the legatee:

- at the date of death
- at their market value on the date of death.

Assets acquired by the personal representatives during the course of the administration are treated as though they had been acquired by the legatee:

- at the date of acquisition by the personal representatives
- at the cost to the personal representatives or the value at which they were acquired by the personal representatives.

If the legatee subsequently sells or otherwise disposes of those assets, the normal rules of Capital Gains Tax will apply.

The legatee is not entitled to claim unused losses of the deceased or personal representatives or any of the expenses incurred by the personal representatives in establishing title to the estate.

VALUATION OF ASSETS OF DECEASED AT DATE OF DEATH

A legatee is treated as though assets acquired from an estate were acquired at their market value.

A legatee may sometimes acquire only part of an asset. For instance, a holding of shares may be divided between a number of legatees, or several legatees may become joint owners of an indivisible asset such as land. Where this happens, the acquisition cost of each legatee's share is an appropriate fraction of the market value of the holding or asset acquired by the personal representatives.

Example 3

On 31.12.99 personal representatives acquire the deceased's shareholding of 600 shares in a company. This represents a 60% holding in that company and is valued at £60,000 or £100 per share. On the date of death a holding of 200 shares or 20% of the company would have been valued at £2,000 or £10 per share.

When residue is ascertained, each of the three legatees receives 200 shares from the personal representatives. They are each treated as having an acquisition cost of one-third of £60,000 (the personal representatives' acquisition value). Their acquisition cost is thus £20,000, not the value of £2,000 that would have been placed on a 20% shareholding.

The value of an asset at the date of death may be needed in order to calculate the Inheritance Tax liability of the estate. It may also be required for Capital Gains Tax purposes as an acquisition cost if either the personal representatives or the legatee subsequently disposes of the asset. Because the valuation is used in arriving at the liability under both taxes, there are special rules to ensure that the same value is used in dealing with each tax.

Where:

- the value of an asset is required for the purposes of both taxes, **and**
- that value has been 'ascertained' for the purposes of Inheritance Tax,

that value is also to be used as the acquisition cost for Capital Gains Tax purposes.

In the course of their duties, the personal representatives will usually prepare a statement setting out the proposed values of all the assets in the estate. This may then be sent to the Capital Taxes Office for Inheritance Tax purposes. Such values are sometimes known as 'probate values'.

Where a value is used by the Capital Taxes Office to arrive at a final charge to Inheritance Tax, and the amount of the liability is dependent on the valuation, the value has been 'ascertained'.

In some cases the Capital Taxes Office may not need to accurately assess the values of some or all of the assets. This can happen, for example, where all the assets pass to a surviving spouse and the entire estate is exempt, or where the estimated value of the estate is well below the threshold on which tax is payable.

In such cases, the values will either not have been considered in any detail or not considered at all and are not 'ascertained' under the special rules mentioned above.

If the asset is disposed of either by the personal representatives or legatees, the acquisition value will have to be agreed or determined.

VARIATION OF THE TERMS OF THE WILL OR INTESTACY

Sometimes, the legatees of an estate decide that they want to change the way in which the estate is to be distributed. This can be done by a deed of variation, or a similar legal document.

Where the document is legally valid, and if certain conditions are met, then:

- the variation will be treated for Capital Gains Tax purposes as not being a disposal, **and**
- the rules outlined in this Help Sheet will apply as they would if the variation had in fact been included in the Will.

In other words, the rules outlined in this Help Sheet apply as they would if the terms of the deed had been included in the Will, etc.

The conditions, all of which must be satisfied, are that:

- the variation must be effected by an instrument in writing made within two years of the person's death
- the persons who wish to give up all or part of their entitlement under the Will or intestacy provisions must be parties to the instrument
- there must be no consideration in money or money's worth for the variation other than consideration in the form of a disclaimer or variation of other dispositions of the same estate
- written notice must be given to the Board of Inland Revenue by the parties making the variation within six months of the date of the deed, or such longer period as the Board may allow.

Sometimes proceedings are brought under the Inheritance (Provision for Family and Dependants) Act 1975. Where the Court makes an order under Section 2 of that Act, the terms of that order are deemed to have applied from the date of death for all purposes. There are therefore no capital gains disposals on the making of the order and the special rules outlined in this Help Sheet apply.

Where the conditions are not met, and the terms of the deed are not treated as though included in the Will, the variations will involve disposals by some of the parties which may have Capital Gains Tax consequences. This is a complex area and in such cases you may wish to seek professional advice.

Sometimes a trust is declared in the deed of variation. If this trust replaces an absolute gift of residence or assets under the Will, then the person who gave up his or her entitlement under the Will in favour of the trust is the settlor of that Trust for Capital Gains Tax purposes. If the trust replaces in whole, or in part another trust declared in the Will, then the position is not straightforward and you should ask the Inland Revenue Office dealing with the estate or your tax adviser for help.

These notes are for guidance only, and reflect the position at the time of writing. They do not affect any rights of appeal.