Tax Insider

HOW TO BEAT THE TAXMAN AND BOOST YOUR INCOME!

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HMRC Inheritance Tax (IHT)

IHT may be payable on an estate when someone dies, or when assets are transferred into a discretionary trust or to a company.

For the majority of estates there will be no IHT to pay because they fall within the nil-rate band.

If you are dealing with an estate and do not know whether or not inheritance tax will be due our Customer guide to IHT will help you to decide.

A grant of representation will be required in most except the very smallest of estates. Advice on whether or not a grant of probate is necessary can be found on the Probate Service website in their leaflet PA2 - How to obtain probate (PDF 237K). For advice about applications in Scotland and Northern Ireland, use the probate link below.

Inheritance tax is once again in the political spotlight with the recent announcement by shadow chancellor George Osborne that the Conservatives, if elected, would raise the inheritance tax threshold to £1m. Whether this becomes a reality remains to be seen, but in the meantime HMRC have announced changes to the processes for making the initial payment of inheritance tax where payment is made by cheque. The new processes apply from 5 November 2007.

The new processes have been introduced as a result of HMRC moving advance IHT payments from Nottingham to Accounts Office, Shipley. This move has necessitated the need for bank-approved payslip. The new processes will also improve security as regards registering IHT processes before an account is delivered.

IHT 200 and New IHT Reference

Where someone dies and it is expected that inheritance tax will be due, it is necessary to deliver a full account on the form 'IHT 200' to HMRC.

From 5 November 2007, an IHT reference number must be obtained before submitting IHT 200. The IHT reference number should be written in the top right-hand corner of the IHT 200. The new IHT reference is not needed if the IHT 200 is to be delivered before 5 November 2007.

HMRC recommend that the IHT reference is applied for as soon as possible, but in any event, at least three weeks before the expected delivery date of the IHT 200. It is necessary to apply for the form in writing, either online via the HMRC website or by post using form D21.

The online option will be available on the HMRC website from 22 October. The IHT reference can be requested by using the `do it online' link on the far side of the IHT home page (www.hmrc.gov.uk/cto/iht.htm). If the online option is used, an email acknowledgment will be sent confirming that HMRC have received the IHT reference request.

If the postal route is taken, form D21 is required. This can either be downloaded from the HMRC website or ordered by telephone from the forms orderline (0845 30 20 900; option1).

An IHT reference will then be allocated to the estate and HMRC will send details of the reference, together with a payslip and a pre-addressed envelope, by post. HMRC have stated that they will aim to respond to requests for an IHT reference within 5 days

where the request is made on-line, and within 15 days where the request is made by post.

The new IHT reference is not required if there is no inheritance tax to pay, but the form IHT 200 is required. In this situation, the completed IHT 200 should be sent to HMRC in the normal way.

Due Date for Payment of Inheritance Tax

Inheritance tax is due six months after the end of the month in which the person died. This means that if someone dies on 2 October 2007, any inheritance tax in respect of their estate is due on 30th April 2008. If the tax is not paid by that date, interest is charged on the unpaid tax.

However, it is not necessary to pay all the tax that is due in order to apply for a grant, although a minimum amount of tax must be paid. This is the tax that is due on assets included in section F of the IHT 200. This is inheritance tax on assets where the option to pay in instalments in not available and includes items such as cash, bank and building society accounts, premium bonds, quoted shares, dividends and interest, personal assets and household goods.

The inheritance tax due on items included within section G of the IHT 200 can be paid in instalments. The instalment payment option applies predominantly to land and buildings, business interests and assets, and certain shareholdings. The tax in respect of such assets may either be paid in a lump sum before the six month due date in order to avoid interest, or in ten instalments. Where payment is made by instalment, normally interest is payable on the tax that remains unpaid at the time each instalment falls due. However, where tax is paid by instalments in respect of some businesses, certain quoted shares or land that qualifies for agricultural relief, some interest relief may be available such that interest is only charged as each instalment becomes due.

It is important to note that if any of the assets on which tax is being paid by instalments is sold, HMRC should be notified. The instalment payment option comes to an end if the associated asset is sold and any remaining tax is due immediately.

Payment Methods

Inheritance tax can be paid in various ways:

- Cheque
- Electronic transfer
- Bank giro credit
- National Savings Investment owned by the deceased.

Each payment method is examined further below.

Cheque

The processes governing the initial payment of inheritance tax by cheque are changing from 5 November 2007. From that date, a bank approved payslip carrying an IHT reference must be sent with the cheque. As noted above, the payslip is sent out together with the IHT reference and a pre-addressed envelope once the IHT reference has been requested either online or by post.

When making the payment by cheque, the payslip should be completed and put with the cheque (and nothing else) in the pre-addressed envelope sent out by the HMRC with the reference and payslip. The cheque should not be folded, nor should the cheque and payslip be stapled together.

Cheques should be made payable to `Her Majesty's Revenue & Customs'

The payment and the IHT 200 should not be sent together. The cheque and payment need to be sent to the HMRC cashiers at Nottingham, whereas the IHT and supporting papers should be sent to either Nottingham or Edinburgh, depending on where the application for probate or confirmation is to be made.

Electronic Transfer

Payment of inheritance tax can also be made by electronic transfer using CHAPS or BACS payments. When making payments in this way, details should be given of the full name of the deceased, transferor or settlement, where appropriate, the date of death or settlement and the capital taxes reference number, if known.

Bank Giro Credit

Inheritance tax can also be paid via bank giro credit. If this option is chosen, a pre-printed giro slip is required. This should be obtained from HMRC and can be requested by telephone (0115 974 2463).

National Savings

It is also possible to pay some, or all of the tax and interest that is due prior to application for a grant by using National Savings owned by the deceased. However, where this route is taken, it can take up to four weeks for the payment to be processed.

Transferring Assets to the Crown

Perhaps not an option for the average person, but all or part of an inheritance tax bill and associated interest can be settled by transferring national heritage property to the Crown. The rules are complicated and property cannot be accepted in lieu of payment of inheritance tax before a grant of representation can be taken out. Further details of meeting inheritance tax liabilities in the way can be obtained direct from HMRC.

Final Thoughts

It is important that the correct processes are followed to ensure that payments are allocated to the account promptly, and that interest in not incurred unnecessarily. Further details on the procedures governing the delivery of an inheritance tax account and the payment of the tax are available on the inheritance tax pages of the HMRC website (www.hmrc.gov.uk/cto/iht.htm).

Just When You Thought it was Safe to Have a Family Business... The Chancellor's Revenge for Arctic Systems

By James Bailey

There was a chilling announcement in the Pre Budget Report, warning us that legislation would be introduced in the next Finance Act to counter "income splitting", with effect from April 2008.

This was not exactly unexpected. Ever since HMRC's humiliation in the House of Lords in the summer, when the Arctic Systems case was decided in favour of the taxpayers, we have been waiting for the backlash from the taxman.

The Arctic Systems case involved a standard type of tax planning that has been used for many years by family businesses. Mr Jones was an IT consultant and he set up Arctic Systems Ltd as the vehicle to run his business. He and his wife owned 50% of the share capital each and most of the business profits were extracted by way of dividends.

This makes sense, because for a 40% taxpayer the effective rate of income tax on a dividend is 25%, compared to the 41% tax (that is 40% income tax and 1% NIC) payable on a salary from the company, and the 12.8% employers NIC the company has to pay. For a company with profits of less than £300,000, significant tax savings could be made.

HMRC decided in 2003 that what had previously been regarded as normal tax planning was in fact unacceptably sophisticated tax avoidance, and tried to use the "settlements" legislation to charge Mr Jones to tax on the dividends paid to his wife (she was a basic rate taxpayer and so had no income tax to pay on her dividends).

After a battle through the courts, the Joneses were finally victorious in the House of Lords and the very next day the Treasury announced that they were going to look at ways of changing the law to nullify that victory. If you can't win, change the rules!

This is not the place to look at the technicalities of the Arctic Systems case, particularly as they are presumably going to become irrelevant as a result of the proposed legislation. It is also not the time to look at that new legislation because it has not yet been published. I want to focus on the injustice and inconsistency of this attack on the family business, and I want to make four simple points:

- The use of dividends as in Arctic Systems was not "tax avoidance". It was normal routine tax planning and was encouraged by Gordon Brown in 2002 when he slashed the rates of corporation tax for small companies.

- The House of Lords in their judgement described the way the current "settlement" rules work as "workable and fair". I very much fear that whatever anti-avoidance legislation is introduced will be so complex as to be unworkable - I already know it will be unfair!

- We are told there will be "consultation" on the new legislation. If that is the case, why has it not been published yet? It is over three months since the Treasury made the threat and if they can rewrite the rules for IHT in a week in response to the Conservative Party's announcement, then surely they can draft this legislation in time for the Pre-Budget Report? I fear that any "consultation" will be meaningless, given the short time available before the Budget in March

- It is vital to remember that this will be an attack on small family businesses - the use of dividends does not benefit a company or its shareholders if the company's profits are over £300,000, because then a salary is (just) more tax efficient than a dividend. Big business gets its corporation tax rate cut to 28% and the small family company is going to get hammered.

If there are two words that send a chill down my neck when used by a Chancellor, they are "simplicity" and "fairness".

"Simplicity" (as you will see in my article about capital gains tax) is another word for taking away tax reliefs, and "fairness" usually means creating an unworkably complex set of rules to counter something that used to be tax planning, but which the spin doctors have decided is now tax avoidance.

The Chancellor is desperate for more money, but it is politically impossible to do the obvious and increase rates of tax. Instead, as with pensions in the late nineties, he hides a tax increase behind a smokescreen of "reform".

You Only Want Me for My Nil Rate Band... A New Perk for Married Couples

By James Bailey

The Chancellor's announcement of radical changes to Inheritance Tax (IHT) in the Pre Budget Report means that yet again everyone is going to have to review their IHT planning in order to take account of the new rules.

The changes announced on 9th October 2007 only affect married couples (and civil partnerships), and those who were widows or widowers on 9th October 2007. If you have never been married, you might as well stop reading - except that you may feel that getting married might not be a bad idea once you have read this article!

In order to understand where we are now, we need to look at where we were before 9 October 2007.

IHT is charged on the value of your estate when you die, plus the value of any gifts made in the seven years preceding your death. Everyone has a "nil rate band" of £300,000. That is the current figure but it is increased each 6th April. The first £300,000 of your estate is charged at 0% and the balance is charged at 40%.

A legacy to your spouse or civil partner is exempt from IHT. Before 9 October 2007, much IHT planning focussed on how to make sure the nil rate band of the first spouse to die was not wasted. If you simply left everything to your spouse, there was no IHT payable on your death, but when it was their turn to die, they would only be able to set their own nil rate band against the value of their estate, so yours would have been wasted.

The planning strategy to get round this problem was known as "second death planning" and it generally took the form of a "nil rate band discretionary trust". The first spouse to die left £300,000 (or whatever the nil rate band was when they died) to a discretionary trust, with the surviving spouse and (typically) the children as beneficiaries. The rest of the estate was left to the spouse absolutely. There was no IHT to pay because the legacy to the spouse was exempt from IHT, and the legacy to the trust was within the nil rate band so IHT was payable on it at 0%.

When the second spouse died, their nil rate band could be set against their estate and the assets in the discretionary trust did not form part of their estate, so their heirs benefited from both the couple's nil rate bands.

There were problems with nil rate band discretionary trusts, particularly where, as in so many cases, the major asset was the family home. It was still possible to use a trust but there were complications for capital gains tax, and if the trust was not set up by an expert, there could also be IHT problems.

As from 9 October 2007, the rules have changed. From now on, if the first spouse to die does not use their nil rate band - because, for example, they leave everything to the surviving spouse - then the survivor "inherits" the nil rate band and can use it against their estate when they die.

For example, if Mr Brown (to pick a name at random) dies today and leaves everything to his wife, there will be no IHT to pay because of the exemption for legacies to spouses. If his wife dies in January 2008, her executors can use her nil rate band of £300,000 AND Mr Brown's unused nil rate band of £300,000, so there is no IHT to pay on the first £600,000 of her estate.

The change in the rules is also retrospective. If Mr Brown had died in, say, 2002/03 (when the nil rate band was £250,000), and he had left £125,000 to his brother and the rest to his wife, he would have used up 50% of his nil rate band on the legacy to his brother. His wife's executors can therefore use the other 50% of the current nil rate band (£150,000) together with Mrs Brown's own £300,000, so the first £450,000 of her estate is free of IHT. Notice that the amount of the unused nil rate band is expressed as a percentage, so that Mr Brown's unused 50% gets more valuable each year as the nil rate band is increased for the new tax year.

Even if Mr Brown died 20 years ago, if his wife was alive on 9th October of this year (2007), then when she dies, any unused percentage of Mr Brown's nil rate band can be added to her nil rate band.

This of course produces administrative nightmares - already in my firm we are desperately rooting through old files to find out how much of the nil rate band was used up when the spouses of our client widows or widowers died some years ago.

There are three vital planning points for anyone who is married or whose spouse has died:

- Check your will - if it includes a "nil rate band discretionary trust" take advice on whether this is still the best choice for you. In many cases, the best strategy will be to leave everything to your spouse, even if they then immediately make gifts to other people you wish to benefit.

- If your spouse has died, check how much, if any, of the nil rate band was unused on their death and keep a record of it - as time goes by, it will become harder and harder to find the correct figures as the documents get lost or eaten by mice.

- If your spouse died less than two years ago and left a "nil rate band discretionary trust", you must urgently consider whether you need to use a "Deed of Variation" to redirect their entire estate to you and thus take advantage of the new rules

There are still some circumstances where a nil rate band trust will still be the best choice, but in the majority of cases, a simple will leaving everything to the spouse is likely to be the new strategy.

I am seriously considering giving up tax consultancy and opening a marriage bureau. I will specialise in very poor, very old people. I will introduce them to widowed millionaires whose dead spouses (possibly because of my advice under the old rules!) used up their nil rate bands on a discretionary trust when they died. If the millionaire marries my elderly client (and thus acquires their nil rate band when they die) I will charge a fee of 10% of the current nil rate band. I will soon be a millionaire myself!

A Nice Simple Tax - the "reform" of Capital Gains Tax

By James Bailey

Of all the changes announced in the Pre-Budget Report, probably the most far reaching, illogical, and unfair are the changes to Capital Gains Tax (CGT).

CGT was described to me years ago when I was a trainee inspector as a "simple" tax. At that time, I suppose it was. You could work out the CGT on a transaction in your head, whereas for income tax or inheritance tax, or any of the other Treasury fundraisers, you needed a pen and paper, a calculator, and some reference books.

Of course, like all simple taxes, CGT was unfair - think of the Poll Tax which could not have been simpler!

One of the main objections was that it was effectively a tax on inflation. In cash terms, during the 1970s assets were increasing in value at a huge rate, but still you paid 30% of the difference between their cost and the sale proceeds you received.

The indexation allowance was introduced to deal with this, allowing you to increase the cost of the asset in line with inflation, so you only paid CGT on the real increase in value.

In 1998, indexation was "frozen" for individuals and trusts (it still applies to companies). In its place was put Taper Relief. Given that the Chancellor at the time was Gordon Brown, this was amended and amended and reformed and revised until it became extremely complicated, but the basic proposition remained simple - taper relief rewarded those who invested for the long term and it rewarded traders more than investors.

Any investor could look forward to a reduction of up to 40% in the gain that was chargeable to CGT after he had owned the asset for ten years, and the owner of a trading company (or a partner or sole trader) could have 75% of his capital gains exempted from tax if he had owned the business for two years or more.

The rate of CGT charged depended on your other income and gains for the year - 20% if you were a basic rate taxpayer and 40% if you paid higher rate income tax.

All that is being swept away for individuals and trustees, because the old indexation rules will still apply to gains made by companies. From 6 April 2008, all gains will be taxed at 18% no matter what the asset, how long you have owned it, and what other income you have.

There will be some winners. In particular, this is good news for buy to let residential landlords as currently the lowest rate of CGT they can ever hope for (as a higher rate taxpayer) is 24%. It is also good news for people who play the stock market, who will pay 18% on their gains instead of (typically) 40%.

It is bad news for family trading businesses, entrepreneurs, and (ironically, given the chancellor's stated purposes) people on low incomes making gains just over the annual exempt amount (currently £9,200). For example:

Mr Jones owns a few shares his father left him 10 years ago. He is short of cash and has little income so he sells the shares and makes a gain of £20,000. Taper relief reduces this gain to £12,000, and after his annual exempt amount he pays CGT on £2,800. As he has little other income his CGT is charged at 20%, so he pays £560 in tax.

If Mr Jones waits until 6 April 2008 to sell his shares, he will be taxed at 18% on the gain above the annual exempt amount. £20,000 less £9,200 is £10,800, so his tax bill will be £1,944.

You will have noticed that the second sum is much simpler to do, but I suspect Mr Jones would rather have had a slightly more complicated system that took account of how long he had owned the shares, and the fact that he has a low income.

If you have assets you may want to sell in the next year or so, you need to work out if you are going to be a winner or a loser as a result of the changes.

If you will be worse off on a disposal after 5th April 2008, you should consider taking steps to "crystalise" the gain before 5th April so that you pay less tax. CGT on a gain "crystallised" before 5th April 2008 is payable on 31 January 2009, so as long as you actually sell the asset before then, you will have the cash to pay the tax.

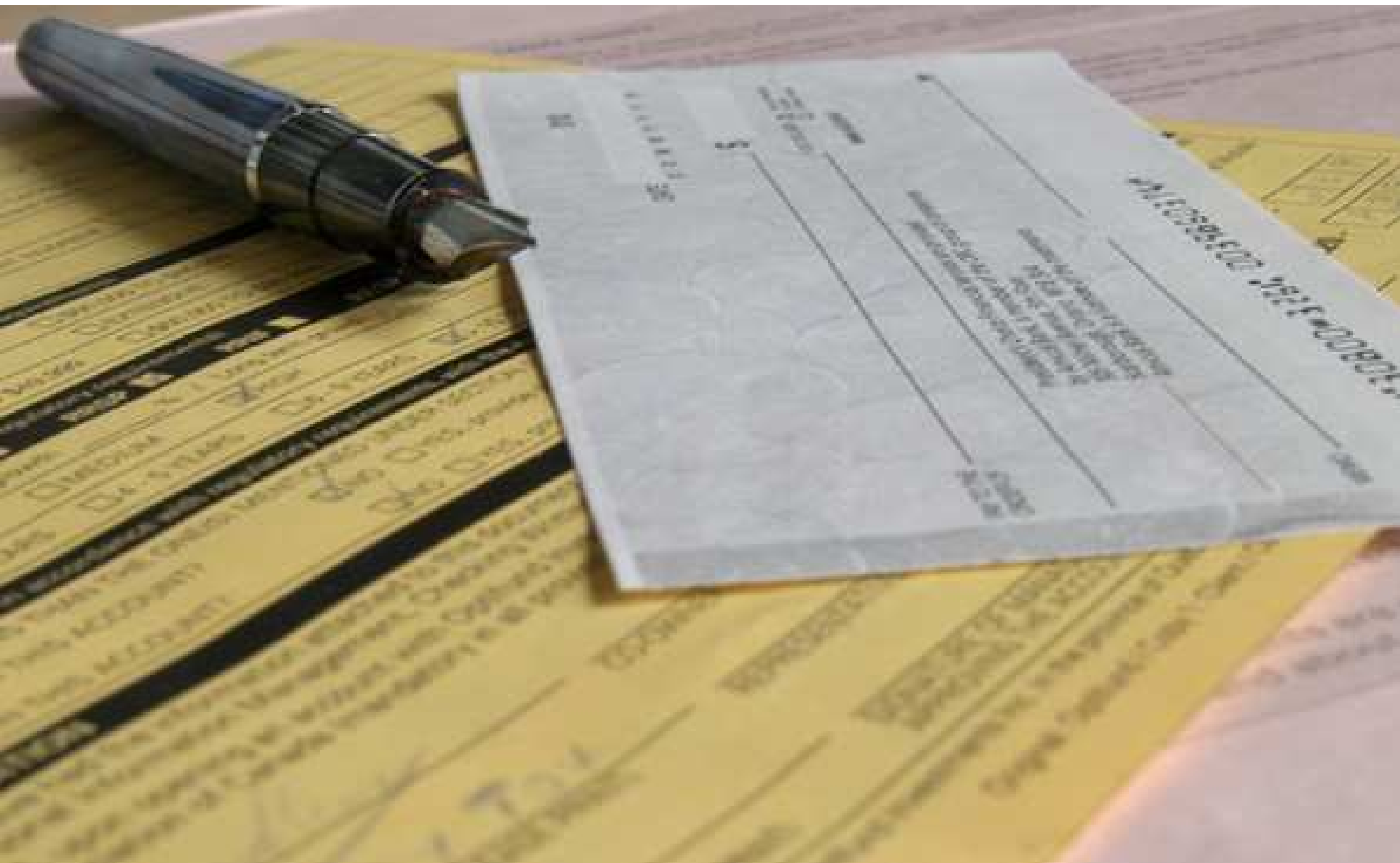
Gains can be "crystallised" by several different methods (such as transferring the asset to a "settlor interested trust"), but this is a job for a tax specialist.

If you will be better off selling after 5th April 2008, it is tempting to hang on until then, but if you already have an eager buyer who has made you a good offer, this may be commercially unwise. Once again, a good tax consultant can come to the rescue and arrange to defer the point at which the capital gain "crystallises" until after 5th April, even though for practical purposes the sale takes place before then.

There is only one way to be sure whether you will be smiling or frowning after 5th April - and whether you therefore need to indulge in a little time travel for tax purposes - get out the calculator and do the sums!

VAT Recovery on Business Assets That Have Private Use

By Andrew Needham



Over the past few years, there have been a number of changes in the legislation and HMRC policy relating to the recovery of VAT on goods and services with both business and private use.

Lennartz

The most important changes have come in the wake of the ECJ case of Lennartz v Finanzamt Munchen III in 1991. Initially, HMRC ignored the decision and maintained its policy that input tax should be apportioned on the purchase of an asset.

In 2003, the ECJ reconfirmed this principle in a case concerned with the construction costs of a building used partly as a private residence. The decision conflicted with legislation that HMRC had just proposed preventing the use of the Lennartz principle for buildings and civil engineering works. HMRC considered the case concerned, but stated that there was a derogation in Article 6(2) of the EU 6th Directive that allowed Member States to withdraw the Lennartz mechanism altogether for certain assets. However, they did make some minor amendments to their legislation, stating "the Lennartz mechanism is not available for land, buildings or civil engineering works (or services related to them such as construction services) where no entitlement for any qualifying input tax arose prior to 9 April 2003".

In 2005, HMRC grudgingly agreed that the Lennartz mechanism could be extended to land and buildings, following the Charles & Charles-Tijmens case which, in effect, prevents EU Member States from legislating against the use of Lennartz accounting.

In the 2007 Budget, it was announced that there would be a number of changes to the use of the Lennartz mechanism.

The measures enable the UK to implement the ECJ decision in Wollny, and, for land and buildings, to reduce the period over which VAT charges on non-business use are paid. Currently, HMRC's policy is that, for land and buildings, the maximum adjustment period is 20 years. The new regulations will introduce a shorter 10-year adjustment period for land and buildings. In practice, this will mean that 10% of the full cost of the building will be taken into account in calculating non-business use charges each year. It will also specify the period for non-business use charges on other assets.

The second part of the measure will affect assets where Lennartz accounting has already been applied. Non-business use charges accounting for use of assets after the introduction of the new regulations will need to be calculated on the new basis.

On 14 August 2007, HMRC issued Revenue & Customs Brief 56/07 regarding the implementation of these measures. The proposed implementation date of 1 September 2007 has now been delayed to 1 November 2007, because HMRC received some very helpful comments on the draft Regulations during consultation, and, for once, decided to listen to them.

Home Computers

In another change announced on 14 August 2007, HMRC issued Revenue & Customs Brief 55/07 notifying businesses of a change in policy regarding VAT recovery on computers made available by employers to their staff for use at home. The gist of the Brief is that, whilst the Home Computers Initiative remained in place, HMRC effectively disregarded the VAT consequences of any private use, but now that the HCI has come to an end, HMRC will expect employers to identify private use and account for VAT accordingly.

Businesses will only be able to claim full VAT recovery without any requirement to account for VAT on any private use, where the provision of a computer is necessary for the employee to carry out the duties of his employment. In these circumstances, HMRC's view is that it is unlikely that any private use will be significant when compared with the business need for providing the computer in the first place.

Where a business cannot demonstrate that it is necessary to provide an employee with a computer in order to carry out the duties of his employment, then only a portion of the VAT incurred can be reclaimed. HMRC will accept any method of apportioning the VAT incurred, as long as the result fairly and reasonably reflects the extent of business use.

Where a business continues to provide a computer under an existing HCI agreement, full VAT recovery can continue until the agreement (normally 3 years) has expired.

Mobile Phones

Most employers provide their employees with mobile telephones to enable them to contact them for business reasons. In some cases, the employers allow staff to make private calls, whilst in others, they do not.

In all cases, the expenditure on the purchase and line rental for mobile phones is seen as being incurred for business purposes, and so the VAT on this element of the bill can be reclaimed.

If the company has a policy prohibiting private use, then the tax incurred on the calls can also be recovered in full.

If a business allows its employees to make private calls on their mobile phones, and no charge is made for this use, the VAT on the bill should be apportioned using any "fair and reasonable" method. It would be best to get this method agreed in writing by HMRC. Any internal controls on private use of mobile phones or accounting for output VAT should be documented, so that HMRC can see that they are being enforced.

If a business charges employees for private use of the phone, it can recover the VAT in full but must then account for the output tax on the call charges.

TAX TIPS

• Moving to new premises? Make sure you tell HMRC beforehand!

When we move premises, we remember to tell the telephone, gas and electricity companies about it. However, forgetting to tell HMRC could lead to a lot of unnecessary hassle. Legally, a business is required to tell HMRC of a change of address within 30 days.

• Missing traders!

Lord Lucan Ltd registered itself for VAT and was quickly visited by a VAT Officer to check some of the registration details. After two months, it moved premises and HMRC came out to see the business again, only to find it wasn't there. Not surprisingly, the VAT Officer quickly decided that he may be dealing with a bogus business, such is the high incidence of 'missing traders' in relation to 'carousel fraud'. He promptly deregistered the business on 'revenue protection' grounds.

• Do you want the good news or bad news first…?

Good and bad news for property developers - the ludicrously complicated Planning Gain Supplement that has been hovering over you has been scrapped, but the bad news is that as a consolation prize, Local Planning Authorities are to be empowered to charge "Supplementary Business Rates" and a "Local Planning Charge".

• Renovating empty residential property

If you are renovating residential property that has been empty for the appropriate period, your builder need only charge you 5% VAT and the required period is to be reduced from three years to two.

• Bad news for "Non Doms"

Bad news for "Non Doms" - that is, people who are resident in the UK but have their roots elsewhere. From April 2008, the "remittance basis" (which exempts Non Doms from tax on income arising outside the UK if they do not bring it into the country) will no longer apply once you have been UK resident for seven years, unless you pay an annual bribe (sorry, tax charge) of £30,000.

• A change in the rules for determining UK residence.

Those who are not resident here but make regular visits should beware of another change in the rules for determining UK residence on the basis of the number of days spent in the UK in a tax year. Until now, days of arrival and departure were not treated as days spent in the UK, but from next April (2008) they will be.

• Stamp Duty Land Tax threshold raised for land transactions.

The threshold for notifying HMRC of a land transaction for Stamp Duty Land Tax has been raised to £40,000. What land transaction could be for less than £40,000? Well, for example, if you gift a share in a property to your spouse and there is a mortgage of £80,000 on the property - your spouse is deemed to have paid you £40,000 for it.

• Penalties for late returns.

If you are a "contractor" for the purposes of the Construction Industry Scheme, watch out! From this month the gloves are off as regards penalties for late returns. These will be automatic for returns submitted late after 19 October 2007.

The Tax Insider Gurus Answer Your Questions

Q.1 My mother bought a flat in my name in 1995 for £155k. We lived there until 2005 when I got married and moved out. She still lives there and would like me transfer half the property to her. There is a small mortgage of £85k and the property is now worth about £500k. She is a 64 year old pensioner. Will she have to pay stamp duty on the transfer and will I have to pay CGT? No money will change hands.

A.1 If you gift the property to her, she will be deemed to take over half the mortgage, but as the value of that is below the SDLT threshold, there will be no SDLT to pay. There will also be no CGT because the property was your main residence until 2005 and the last three years of your ownership will always be exempt in such a case.

I do, however, question the wisdom of transferring part ownership to your mother. The value of the property will be part of her estate for Inheritance Tax and £250K (half of the value of the flat) means she only needs other assets of £50K to use up her "nil rate band" and be taxable at 40% when she dies. Depending on the detailed facts, it is also possible that her share of the mortgage would not be allowed as a deduction from the value of her estate.

If you insist on going ahead, remember you will need to get the consent of the mortgage provider to the transfer.

Q.2 My partner and I (not married) are moving into a rented property while renting out our current property that is in my name. I'm in the higher rate tax band and my girlfriend is in the base rate tax band. Can I put her name as landlord on the contract so she receives all rental income and avoid paying the higher rate income tax, or do I have to transfer the deeds into her name first?

A.2 Joint owners of a property who are not married can agree to divide the rental income in any proportion they like, provided they actually receive that proportion of the rent (so don't go paying it into a joint account and have a written agreement as to the division of the rent). This only applies to joint owners, however, so unless you transfer an interest in the property to her, all the rent will be taxable on you. If there is a mortgage on the property, beware of SDLT - see the answer to question 1.

Send your questions to: questions@taxinsider.co.uk for consideration in future editions.

Tax advice and help to solve your challenges at an affordable price!

The contributors to this e-zine are current practising specialists. They have made available an advice and helpline service to help resolve any UK and international tax matters.

Please visit www.taxinsider.co.uk for more information about this affordable service.

Q.3 I am presently buying a property which I intend to let. However, a certain degree of work will be required to be carried out as follows:

New central heating system	£3,500
Decorating etc	£ 500
Fridge, cookers	£ 450

My question is, how will each of the above pre-letting expenses be treated for tax purposes?

My understanding is that the new central heating system and decorating will be treated as capital items, and relief will be obtained when I sell the property through CGT. Also, that no capital allowance (Plant & Machinery) will be able to be claimed in respect of them. I am not sure of the treatment of the fridge etc.

A.3 Central Heating - you say a "new" system. If the old system was working and the place was fit for letting before it was replaced, and the new system is merely a more modern version of the old system rather than a real improvement on it, then this is a repair and can be deducted from the rent.

Decorating - at £500, it sounds as if this is just regular maintenance of the property, and if so, it's another repair and deductible.

Fridge, cooker - You have a choice. If the property is being let furnished (see next question), you can either claim 10% of the rent each year as a "wear and tear" allowance, or you can claim the cost of renewing appliances and soft furnishings, but not the initial cost of the first ones you put in. Think carefully, because you can't chop and change methods from year to year on the same property.

Q.4 I have recently rented my house as 'part furnished' - i.e. carpets, blinds, curtains and white goods - dishwasher, fridge freezer, washer dryer. Am I able to claim the wear and tear allowance or is this only for fully furnished houses? If I am able to, I am assuming it wouldn't be the usual 10%.

A.4 This is right on the borderline - you don't have to be fully furnished to get the 10% allowance, but in this case, with no beds, tables or chairs, I would expect HMRC to challenge the 10% allowance. You should either put in a bit more furniture or claim the cost of renewals as described in the answer to question 3.

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