

Settling affairs

Lynne Bradey and Oliver Hallam explain how a loss of mental capacity is not the end of the road for clients' estate planning

The onset of mental incapacity does not have to mark the end of effective estate planning for clients. The Court of Protection (CoP) has a wide range of powers available to it, and this article intends to highlight some common estate planning issues which can be resolved by an application to the CoP for directions. Following the recent case of *Re P* [2009] EWHC 163 (Ch), we will also look at the guidelines that the CoP will now follow when assessing the execution of a statutory will. Finally, we will provide a checklist of information that will be needed on an application to the CoP.

It is difficult to predict the onset of mental incapacity. Some clients will have put their affairs in order and some will not. Even if a client has executed a will and done some estate planning, their circumstances and the circumstances of their family will often change over time. If family circumstances do not change, it is possible that the introduction of new legislation will mean that an individual's tax planning becomes outdated.

While this article deals with statutory wills, it should also be noted that an application to make lifetime gifts can also be made under the Mental Capacity Act 2005 (MCA 2005). These applications are often made to mitigate inheritance tax (IHT) liability which may be payable in the event of the incapacitated client's death.

CASE STUDY: STATUTORY WILLS

Take as an example John, who was diagnosed with early onset dementia at the age of 60. The dementia progressed slowly and, while John still had mental capacity, he and his wife, Sue, quickly took legal advice and created some nil-rate band discretionary trust wills with a loan / charge mechanism leaving their residuary estate to each other outright, then down to their children in equal shares on second death. They also created lasting powers of attorney (LPAs), and registered them at the Office of the Public Guardian. John then lost his mental capacity.

John and Sue's affairs are well-organised but, as the years go by, the following events take place:

1. The government introduces the transferable nil-rate band. This might be an opportunity to simplify John and Sue's wills by removing the loan / charge mechanism which in some, but not all, cases may be obsolete.
2. Sue is diagnosed with cancer and the prognosis for them both becomes uncertain. If John and Sue leave their residuary estate to each other outright, there is little asset protection from likely future care fee assessments or financial difficulties. A life interest for the survivor, incorporating overriding powers of capital appointment, might be advisable in the circumstances.

3. John and Sue's son, Luke, has a nervous breakdown and his siblings, James and Emily, start to look after his finances and affairs for him. John and Sue's current wills leave their residuary estates to the children in equal shares outright on second death. Given that there is now a vulnerable beneficiary, it might be advisable for them to leave part or all the estates on discretionary trusts instead.

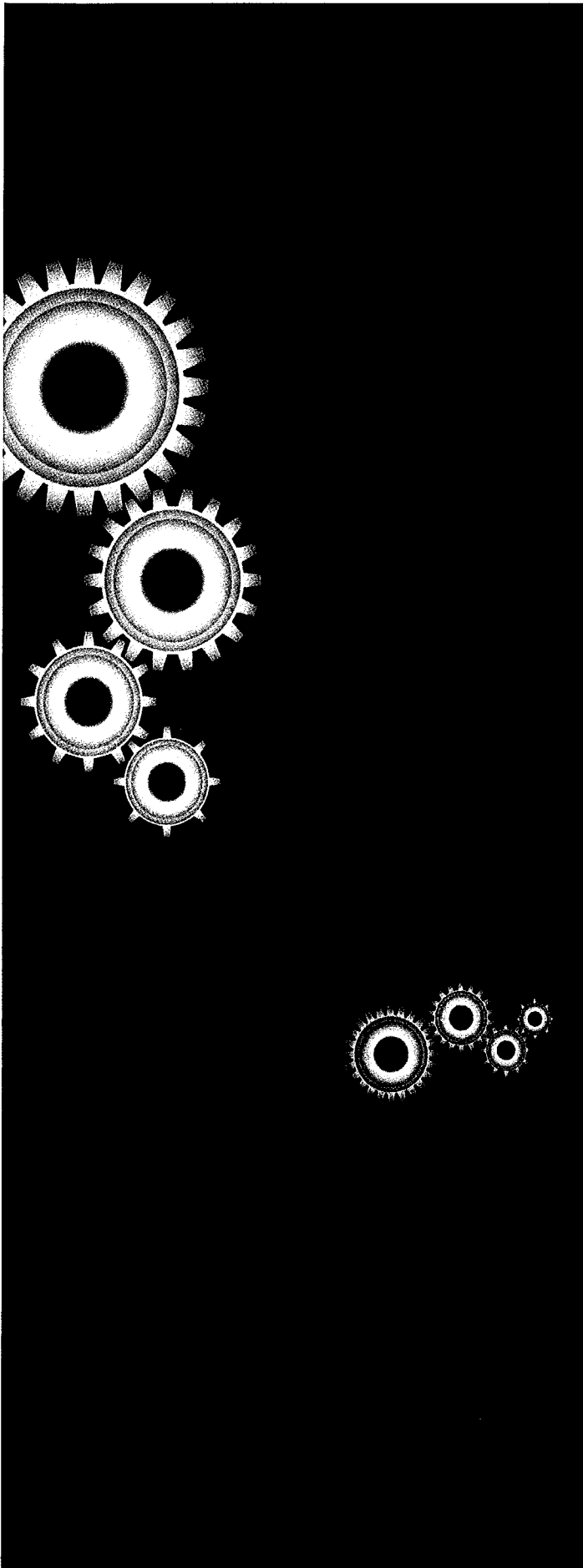
4. Sue finds some old insurance policies on John's life and hears from a friend that they will mean that a lot of IHT will be payable on John's death if he survives her, or ultimately on Sue's estate if she

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dies shortly after John. Assigning the death benefits from the life policies to the trustees of a pilot discretionary trust would normally be advisable, particularly given the changes in family circumstances described above.

5. Each year John's attorneys have been using John's £3,000 annual gift allowance for IHT by making gifts to John's godson. Without an order for gifting, attorneys cannot make more than the normal customary gifts out of the donor's estate. Although the gifting powers appear to have been widened by the MCA 2005, the general consensus is still that attorneys cannot use the £3,000 annual IHT exemption, although it is surprising how many think they can, and indeed have been doing so. Any gifts which have been made outside the attorneys' authority will be treated, for IHT purposes at least, as if they have never left the donor's estate. If John's attorneys have been making the annual gift out of John's excess income, then the CoP may sanction the gifts if the income can be proven to be excess in accordance with the rules set down by HM Revenue and Customs (HMRC).

6. John receives letters from some trustees explaining that he is a life tenant under a family trust. The remaindermen are John's children. John does not need the income, and Sue has been advised that the value of the money in this trust will count as John's for IHT purposes, further increasing his tax bill. John's attorneys and Sue see no reason why the trust cannot be wound up and the capital distributed. This will require consideration of the most appropriate way of dealing with Luke's share, in light of his problems, but the family feel that accelerating the benefit to Luke



will allow him to move to more suitable accommodation, away from the triggers for his breakdown.

7. The trustees explain that John is due to receive the residue of the estate of a deceased relative. John's attorneys and Sue think that, were it not for John's incapacity, it would have been possible to execute a deed of variation within two years of the date of death, to pass John's share down to his children, and, again, this could assist Luke's move.

John's attorneys and Sue are concerned by these events and see going to their solicitor as a last resort. They are convinced that there is nothing that can be done because John has lost his mental capacity. However, a solicitor will be able to advise that this is not the case, and that an application can be made to the CoP to take these estate planning steps.

All of these issues can be dealt with. Events 1 to 3 above suggest an application be made to the CoP to execute a statutory will on behalf of John. Dealing with events 4 to 7 will require an application to the CoP to exercise its gifting powers under the MCA 2005.

The recent case of *Re P* provides clarification of the overriding principles that will guide the CoP when exercising its power to make statutory wills under the MCA 2005. The CoP can no longer apply the principles laid down by the CoP in exercise of its powers under the Mental Health acts of 1959 and 1983.

Prior to the case of *Re P*, when assessing an application for a statutory will, the CoP followed the principles established in the case of *Re D (J)* [1982] Ch 237. In brief, the court tried to decide what the testator would have wanted if they were not mentally incapable. The will was deemed to be made during a brief lucid interval, during which the testator had a full awareness of his situation, was properly advised and knew that, following the execution of the will, he would again become incapable.

The CoP, in the case of *Re P*, found that, under the MCA 2005, the overriding principle is that any decisions must be made in the person's best interests. This follows section 4 of the MCA 2005, which applies in equal measure both to attorneys in making day-to-day decisions and to the CoP. The MCA 2005 directs the CoP to follow a number of steps in its decision-making, which include encouraging the person to participate in decisions, considering the person's past and present wishes, beliefs and values, and taking into account the views of third parties as to what would be in the person's best interests. Justice Lewison also held that the CoP was entitled to take into account how the person would be remembered after his death. He made it clear that the statutory rules can also cover all immovable property in England and Wales.

In the case of John, his attorneys will be able to apply to the CoP, and it will take into account the views of not only the attorneys, but also of Sue and their children, and of other third parties, as to whether the proposals are in John's best interests.

HOW TO APPLY TO THE COURT

Applications of this type need to be made to the CoP, asking it to exercise its powers under sections 16 and 18 of the MCA 2005. The application would normally be made by the deputy or attorney(s) under a registered enduring power of attorney (EPA) or LPA, and the incapacitated person is referred to as 'P'. If, as in John's case, the application is to be made by attorneys, the most practical way to deal with the paperwork is often for one attorney

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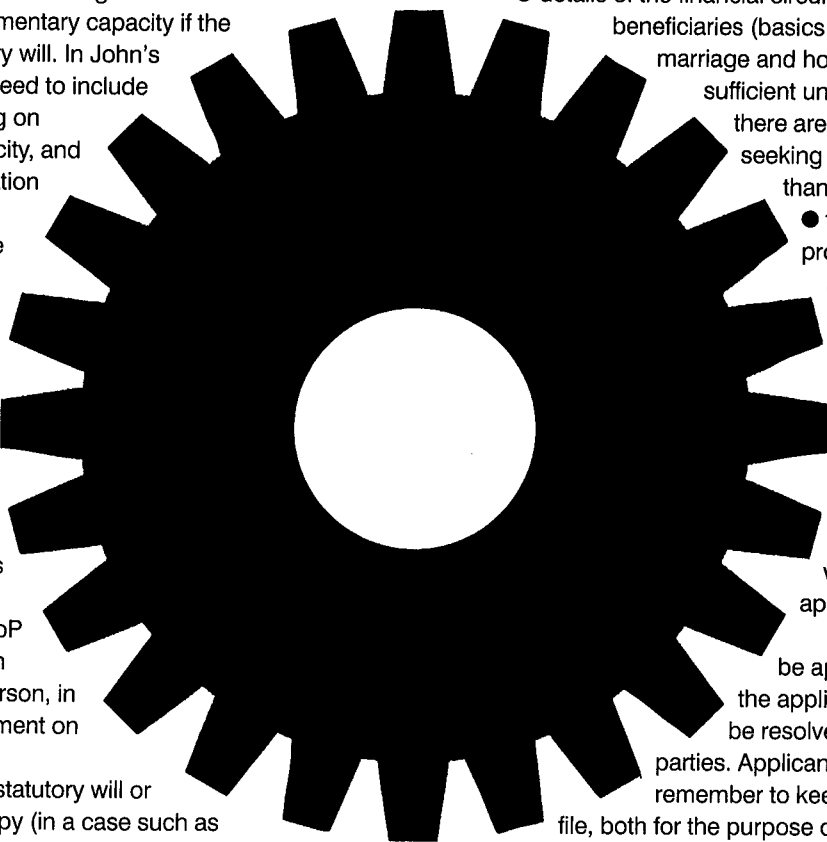
(perhaps Sue or one of the children) to take the lead and make the application, and prepare statements from the others indicating their agreement. This can save quite a lot of time and paper.

The application needs to be made on the CoP's application form COP1, with supporting financial evidence in form COP1A. The CoP is also likely to require a medical report on form COP3, unless there is a very recent one on exactly the same point, so applicants should assume one will be necessary. Applicants should also remember that the COP3 will need to set out the specific test for the application being made – for example, the test for testamentary capacity if the application is for a statutory will. In John's case, the application will need to include John's doctor commenting on John's testamentary capacity, and also on his capacity in relation to the proposed gifts. The doctor should generally be asked to give an opinion on life expectancy at the same time, particularly where this is thought to be very short, or gifting is contemplated.

The court fee will be £400, with a hearing fee of £500 if one is needed, although most applications which are not contentious will not require one. The CoP will also require information about the incapacitated person, in the form of a witness statement on form COP24 including:

- a copy of the proposed statutory will or trust deed, plus a spare copy (in a case such as John's, if any of the gifts are to be directed into a trust – in John's case, perhaps for Luke – a copy of the proposed deed will need to be included);
- a copy of any existing will or codicil (obviously important in statutory will applications, but in other applications, the CoP will want to check that a lifetime gift or variation is not adversely affecting people who will benefit under P's will, or those who may benefit under the intestacy rules);
- consents to act by the proposed executors (sometimes requested even where they are the additional applicants, so it is best for applicants to provide them just in case);
- details of the family background including a family tree, with full names and dates of birth where possible;
- a schedule of P's current assets (to the extent that these are not clear from COP1A);
- income and outgoings schedule;
- details of P's current and future needs;
- full information on P's health, currently and as prognosticated for the future;
- if P is cared for by the NHS, whether they are likely to be discharged and to where, and the likely change this would make to the financial picture;

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- details of the financial circumstances of proposed beneficiaries (basics, such as employment, marriage and home ownership should be sufficient unless the CoP asks for more, or there are circumstances where you are seeking to benefit one person more than another);
 - the tax implications of the proposed action (IHT, income tax, and capital gains tax);
 - details of how the proposed action will affect P's resources, preferably with a 'before and after' schedule;
 - details of P's domicile and any effects of that on the application;
 - details of any land which will be affected by the application.
- The official solicitor will usually be appointed to act on P's behalf in the application, and most issues can be resolved by negotiations between the parties. Applicants and their solicitors should remember to keep copies of the application on file, both for the purpose of serving the official solicitor, and to refer to. Apparently, applicants quite often send their only copy in, and then have to ask for a copy back.

The costs of the application are subject to assessment and are usually met from P's estate. The CoP does not have to order that costs are met from the estate, and where a party has objected unreasonably or brought an application that was not appropriate, they may have to bear their own costs.

CONCLUSION

With more clients living longer and unfortunately losing capacity, it is vital that private client practitioners realise that there are still ways in which they can assist. The case of *Re P* has clarified the CoP's approach in statutory will applications, and will have relevance to gifting and other applications, too. We hope that this article has highlighted some of the ways in which private client practitioners can benefit our clients by putting appropriate estate planning measures in place, even after the onset of incapacity. ■

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