



Preparing an Islamic Inheritance Strategy in light of the Inheritance Taxation laws of England & Wales.

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All praise be to Allah, Creator of the Heavens and the Earth. Owner of the Day of Judgement. I bear witness that there is none worthy of worship other than Allah and that Mohammed (SAW) is his last and final Messenger.

This paper has the following sections;

- **Introduction – Why bother making a will?**
- **Priorities on the estate – Burial costs, Debts and the 1/3**
- **The Fixed shares and the Residue**
- **Practical Examples**
- **U.K Inheritance Law**
- **Lifetime Taxation Planning**
- **Incorporating Shariah within the U.K Taxation framework**
- **Taxation and Trusts on Death**

A. INTRODUCTION

Many can speculate as to why Islam has placed such emphasis on both the laws of inheritance and making a will. One could argue it prevents family conflicts on death, others may feel it represents a means via which needy relatives can benefit from a wealthy family member. Whatever Allah (SWT)'s wisdom is, it has been praised internationally from various quarters. Consider the following analysis of the inheritance laws by a leading British University Professor:-

“The Muslim law of inheritance comprises beyond question the most refined and elaborate set of rules for the devolution of property that is known to the civilised world”

Professor Almaric Rumsey, King's College, London

The Shariah of course states in no uncertain terms the importance of making a will. In the Muwatta of Imam Malik, we find what is arguably the most commonly quoted Hadith on this subject;

*"It is the duty of a Muslim who has anything to bequeath no to let **2 nights** pass without writing a will"*

Narrated by Ibn Umar (contained in Muwatta)

Ibn Umar then noted that 'not one night has passed without me having my will with me'.

We also find the following compelling Hadith purporting the importance of making a will:-

"A man may do good deeds for seventy years but if he acts unjustly when he leaves his last testament, the wickedness of his deed will be sealed upon him, and he will enter the Fire. If, (on the other hand), a man acts wickedly for seventy years but is just in his last will and testament, the goodness of his deed will be sealed upon him, and he will enter the Garden."

(Ahmad and Ibn Majah)

With such compelling instruction in Shariah, one would expect every adult Muslim to give priority to ensuring he/she makes a will. Unfortunately though as with so much in our faith these days, Muslims have largely neglected the *Sunnah* of making a will. I will relay to you 2 real-life experiences I recently faced when talking to Muslims about this subject.

ISLAM – AS ONLY MUSLIMS KNOW HOW

I met a Muslim Businessman in the NorthWest of England. Alhamdulillah the brother is one of the wealthiest Businessmen in the area. When I mentioned making a will to him, he replied '*Is it allowed in Islam to make a will?*'. He clearly had not heard the above hadith like many more of us.

My second experience was with an accountant whose clients I had been advising on Inheritance Tax. The clients were Muslim and consisted of a father with 3 mature sons. The accountant posed me the following concerning question, he said "*I can understand you wanting to make a will for the father due to his estate size and potential taxation burden, but the sons do not have any major assets*"

This attitude sadly reflects the approach taken by most Muslim professionals of this subject. Only making wills to avoid inheritance tax. Do we not realise that Allah (SWT) has covered few subjects in the Qur'an in such precise detail as the laws of inheritance (principally in Surah An'Nisa).

A GENUINE NEED

On the subject of taxation, I feel this is one of my main motivations for presenting this article. Whilst there exists a wealth of Islamic material on how to distribute the estate, and solving complications arising therein, I feel in contrast there is a complete lack of material on more preliminary aspects such as how to make a will. Furthermore, how to make a will and ensure the estate escapes inheritance tax under the English taxation system, yet still ensuring that the estate is distributed in accordance with Shariah, is a subject which has never been formally addressed. Quite often when Muslims are adopting the Quranic provisions, they find that they are facing an excessive tax burden. This is because Inheritance Tax (IHT), is levied at 40% on assets above the Nil rate Band Threshold (Currently £263,000). The aim here is to present an approach which seamlessly ensures that the theory of Surah An Nisa intertwines with the taxation laws of the land.

THE LAWS OF INTESTACY

Before moving further, it make worthwhile mentioning what happens if somebody dies without having made a will. In such a case, the laws of Intestacy apply. These say that the first £125,000 plus chattels are given to the wife and half the remainder of the estate is placed in Trust giving the wife a right to income for life. On death the assets pass to children if they are above 18. If not then assets are still held under Trust. The remaining half of the estate is held in Trust for the children until they are 18.

As is evident, the above approach is neither Islamic nor logical. The assets will certainly not be distributed by Shariah and worse still the children's shares may be trapped under Trust until certain time in the future. This aspect quite often involves the Court of Protection's consent when administering any of the child's assets.

B. PRIORITIES ON THE ESTATE

Before even the heirs mentioned in Shariah can receive their shares, Islam clearly stipulates that Funeral Expenses and Debts (of the deceased) should be paid.

Allah says in the qur'an 'After payment of any bequest that has been made, or debts'

An Nisa 4:12

Shariah allows the deceased to bequeath upto **1/3** of his/her estate to whomever he wishes, as long as the beneficiaries are not from amongst those who will benefit from the the remaining 2/3 as a result of their entitlement under Surah An Nisa. This may be the perfect opportunity to assist a poor relative who otherwise would not qualify for a share. It may even be a good opportunity to benefit a close non-Muslim relative. **Non Muslims cannot** inherit from the 2/3 estate. Usamah reported that the Prophet (SAW) said

'The followers from 2 different religions may not inherit from each other'

Recorded by Abu Dawud

As for the principle of 1/3, it is derived from the occasion where Sa'd Bin Abi Waqqas was struck by severe illness in Makkah. With death on his mind, he asked the Prophet (SAW) how much of his vast wealth to bequeath as a gift. Sa'd only had one daughter who could be an heir in accordance with Shariah principles. The Prophet (SAW) agreed on 1/3 sighting the following as reasoning – *'You had better leave your inheritors rich after you than leave them as a burden, begging people'* The Hadith is found in Bukhari.

On the basis of this hadith the scholarly consensus is a maximum of 1/3. (Some scholars hold that ¼ is more preferable, but agree that 1/3 is the maximum)

Gifts can be given to Muslim charities either as outright donations of *Waqf*. These funds can be used as a form of Sadaqa Jariyya for the deceased in years to come. There are many charities who operate this principle in the U.K, including Islamic Relief, Human Appeal, Muslim Aid etc. Contact details for these can be found in the Muslim Directory.

C. FIXED SHARES AND THE RESIDUE

HEIRS TO THE ESTATE

The heirs to a Muslim's estate as defined in Shariah can take 2 forms.

- 1) **Fixed Share Inheritors** – These are heirs for whom Surah Nisa has made an explicit percentage provision eg wife (1/4 or 1/8, dependent upon children), Husband (1/2 or ¼ dependent upon children) etc.
- 2) **Residuary Inheritors** – These are heirs whose exact percentage is not fixed, but rather receive the balance of an estate once the fixed shares have been calculated. Examples of these are sons and daughters (usually).

The above 2 types of heirs and their respective percentages are meticulously dealt with in the following quran ayah:-

Fixed share Inheritors

Allah has decreed the shares of a deceased's offspring and parents in the following *ayah* (Surah Nisa v11):

Allah instructs you concerning your children's (inheritance): a male receives a share equal to that of two females. But if they (the children) are only women, and are more than (or equal to) two, their share is two thirds of that which he (the deceased) had left. And if there is only one

woman, her share is half (of the estate). And for his parents, each one's share is a sixth of that which he left if he had children. But if he had no children, and the parents inherit from him, the mother's share is one third. And if he had siblings, the mother's share is a sixth. (These distributions should be done) after the payment of any bequeathals that he may have made or debts (that he may have had). Your parents and offspring – you do not know which among them are nearest to you in benefit. (These shares are) an ordainment imposed by Allah. Indeed, Allah is Knowing and Wise.

The *ulama* derive many important instructions from this *ayah*, the most relevant of which to our discussion are the following:

1. The debts and bequests are taken out of the estate before dividing the rest among the heirs.
2. A deceased's offspring share in his estate, a son receiving twice as much as a daughter. This is done after taking out any ordained shares.
3. If the deceased's offspring are only females (two or more), they receive two-thirds of the estate, which is then equally divided among them.
4. If the deceased is survived by only one daughter, she receives one half of the estate.
5. In the presence of children, the parents receive one-sixth each.
6. In the absence of children, if the deceased leaves brothers or sisters – full paternal, or maternal, then the mother receives one-sixth.
7. In the absence of children and siblings, the mother receives one-third.

Spouses and Maternal Siblings

The following *ayah* (*Surah Nisa v 12*) deals with the share in the inheritance of the spouses and maternal siblings:

You receive one half of that which your wives leave if they have no child. If they have a child, you receive one fourth of what they leave – after payment of any bequeathals that they had made or debts (that they had). And they receive one fourth of that which you leave if you have no child. If you have a child, they receive one eighth of what you leave – after payment of any bequeathals that you had made or debts (that you had). If the man or woman whose inheritance is in question has neither ascendants nor descendants, but has a (maternal) brother or sister,

each one of them two receives a sixth; and if they were more than two, they share a third – after payment of any bequeathals that had been made or debts (that are owed), and that are not intended to cause harm (to the legal inheritors). This is a commandment from Allah; and Allah is ever Knowing and Tolerant.

Amongst the instructions that we derive from this *ayah* are the following:

1. A husband receives one-half of his wife's estate if she does not have any offspring. Otherwise, he receives one-fourth.
2. A wife is a woman who was married to the deceased when he dies, or that was divorced by him a non-final (third) time and had not completed her *'iddah* (waiting period). If there is more than one wife (maximum four) for a deceased, their share is divided equally among them.
3. The wives receive one-fourth of their husband's estate if he does not have any offspring – from them or other women, immediate or grandchildren, otherwise, they receive one-eighth.
4. There is a consensus among the *ulama* that the brothers and sisters mentioned in this *ayah* are the maternal siblings, because the shares of the other siblings are mentioned in the *ayah* at the end of *Surat an-Nisa* (4:176).
5. The shares of males and females of the same rank (brother and sisters, uncles and aunts, sons and daughters, etc.) are such that a male receives twice as much as a female.
6. The maternal siblings are the only exception to the above rule. If there is only one maternal sibling, he (or she) receives one-sixth. If there are two or more, they share one third.

Inheritance rules can get incredibly complex, once we go beyond the scope of most scenarios and delve into half brothers and agnate relatives. It is beyond the scope of this paper to delve into such complexities. As stated initially, the intention here is to provide an impetus to the Muslim community to ensure they write their wills in intention.

RULES SUMMARY

There are 6 simple rules which if borne in mind will allow any adviser to calculate shares probably 90% of the cases that occur. The rules are as follows:-

1. Wife receives $\frac{1}{8}$ or $\frac{1}{4}$ of husband's estate, with or without children respectively.
2. Husband receives $\frac{1}{4}$ or $\frac{1}{2}$ of wife's estate, with or without children respectively.

3. Mother and father receive 1/6 each if client has children. If client has no children, then mother get 1/3
4. Sons get twice what daughters receive of the residual estate after fixed share inheritors receive their shares.
5. If 2 or more daughters exist, they receive 2/3 of the estate. One daughter alone receives 1/2 the estate.

The following link accesses a computer package which will instantly work out your heir's entitlement – www.islamicsoftware.org/irth.html

SUFFICE TO SAY, WHERE THERE'S A WILL, THERE'S RELATIVES

D. PRACTICAL EXAMPLES

Try the following example to confirm your knowledge of the basic principles.

1. Imran married to Rehana, Imran passes away with his Mother still living and 1 child, a boy. Estate divided into 24 parts, 3 to wife (1/8), 4 to mother (1/6) and 17 parts to Son.
2. Jameel married to Rizwana, Jameel passes away with no mother but 2 children, a boy and girl. Estate again divided into 24 parts with Wife receiving 3/24 (1/8) whilst children share in ration of 2:1. Boy receives 14/24 parts and girl gets 7/24 parts.
3. Try your own scenario and then double-check it with the above link.

E. INCORPORATING SHARIAH WITHIN THE U.K TAXATION FRAMEWORK

WHAT IS INHERITANCE TAX

Inheritance tax (IHT) is payable at a rate of 40% on certain assets within a deceased person's estate in excess of £263,000. This individual allowance is revised annually and known as the '**Nil Rate Band**' (NRB). There are a number of relatively straight-forward steps which can substantially reduce or even eliminate any IHT liability, if arranged prior to death. Whilst there are many exemptions and reliefs available, the following is a summary of the most relevant principles.

GIFTS

Gifts of any value, made by the deceased to the surviving spouse, before or on death, are exempt from IHT. However, these gifts may be liable to IHT on death of the surviving spouse. It is important to note that English law does not recognise the Islamic Nikkah ceremony as having legal force, if undertaken in the United Kingdom, except where those performing the ceremony have been granted a license to issue marriage certificates. Consequently, it is important for clients wishing to use this exemption to possess a civil marriage certificate. If required, these can be obtained by attending a

marriage ceremony at a local registry office. If the surviving spouse is not UK domiciled, the inter-spouse exemption is limited to £55,000.

A popular use of this exemption is to ensure on death all assets in excess of the NRB are passed to the surviving spouse.

Gifts with reservation.

LIFETIME TRANSFERS

Gifts of any value are deemed to be exempt from IHT, if made seven or more years prior to death. IHT is payable in full on gifts made less than three years prior to death, and on a sliding scale, on gifts made between three and seven years prior to death. Gifts in which the donor retains some beneficial interest (e.g. a house in which the donor continues to reside rent free) are considered to be 'Gifts with Reservation'. They are liable to pay IHT in full, irrespective of when the gift was made.

BUSINESS PROPERTY RELIEF

The transfer of shares in an on going business concern are exempt from IHT, if the shares have been owned for two or more years by the deceased. This relief is of crucial importance to business owners, as the vast majority of trading companies and partnerships will qualify for this relief. Investment companies, or properties, both commercial and residential, generating rental income normally do not qualify for Business Property Relief.

ANNUAL EXEMPTION

A single gift of £3,000 per annum can be made which is exempt from IHT. Any unused annual exemption can be carried forward one tax year enabling a maximum £6,000 to be gifted.

GIFTS

Gifts of any value made to a U.K. registered charity are exempt from inheritance tax (IHT).

DEEDS OF VARIATION

The Beneficiaries of an estate are able to retrospectively revise a Will after death usually for religious, family or tax reasons. In order for a Deed of Variation to be accepted by the Inland Revenue, all Beneficiaries must be over 18 and sane, and give their written consent within two years of death. Deeds of Variations are typically very costly and time-consuming.

Now that the basic principles of inheritance law have been covered, please complete '1st Ethical's Wealth Calculator' (overleaf) in order to ascertain the value of your estate and potential inheritance tax liability.

F. Lifetime Planning

There are a variety of taxation tools which can be used during life to allow reduction in a client's estate. Quite often these methods involve some form of

capital gains tax planning. The commonly used ones, their benefits and costs are as follows:-

1. Transfers into a DT – This allows for assets to be transferred into a discretionary trust during life. The allowance is of course only available every 7 years. With a Husband and wife this increases to 2 NRB's (currently £526,000).

Key Benefits

- 1) Non Business Assets (equity up to NRB) can be transferred in without triggering a CGT (Capital Gains Tax) charge. This currently allows £526k per couple. The debt (mortgaged) element of the transfer will usually attract Stamp Duty (This though may still be more attractive than paying the Inheritance Tax)
- 2) Under section 260 of the Taxation of chargeable gains Act 1992, the trustees of the DT are allowed to holdover the CGT gain on assets transferred in. When the asset is transferred back out, the beneficiaries are able to hold out the gain.
- 3) Asset protection of course, ie protection against lawsuits filed against the potential heir.

Restrictions

- 1) Only assets up to NRB can be deposited.
- 2) The settlor can never be a beneficiary of the DT, otherwise a GWR will be triggered.
- 3) Also, when asset is held-out, beneficiaries will inherit base cost, this means that if they sell the asset during life then they will pay CGT based on base cost. To fully avoid CGT, one will have to wait till death, when CGT base is uplifted to IHT base cost and then asset distributed via Will D/T or FLIT (Flexible Lifetime Trust).

Practical Issues – An election to holdover needs to be made via form IR295. This only requires settler to sign. It is subsequently lodged with the Inland Revenue's Nottingham trust District.

Key Rule: A trust needs to be registered with Inland Revenue if income is being generated in it.

Costs – No charges are levied on entry for assets up to the NRB. However assets above NRB trigger lifetime charge of 20%. Note the following:-

- 1) If asset is within NRB on entry there is no exit charge to pay.
- 2) If asset is above the NRB on entry and above prevailing NRB at time of exit then quarterly charge is due on excess. This would be a maximum of 6%. *(eg Client puts in residential property at £250k today. Currently no tax charge, if this is within NRB. In 10 years asset is worth £500k, with a NRB at that time of £400k, still no charge. However if NRB today is £200k, and asset being placed in trust is worth £250k, then lifetime charge will be levied on £50k. On exit, the periodic 6% charge will also be levied.)*. The actual calculation is very complex, and very

few super-geeks can actually do it. Most people get Revenue to do it on self-assessment. 10 yearly charge and exit charge are calculated on similar basis, (a quarterly basis).

- 3) Solicitors typically charge between £1000 – £2000 for this service.

2) IIP Transfer – This is where assets are transferred into a Trust conferring an Interest in possession to a specified individual and a defined range of beneficiaries.

Key Benefits

- 1) No limit on level of transfer allowed in.
- 2) Asset Protection
- 3) Minimal Paperwork and administration, no lodging with revenue.

Key Restrictions

- 1) No holdover relief available, and hence only suitable for client whose allowances mean that property being transferred should have little or no CGT charge attached.

Practical Issues – Simply drafting of paperwork by solicitor and signing by client. Again this is then lodged with revenue if income is generated from asset.

Costs – Typical charge - £750 - £2000.

3 - Declaration of Trust – This allows for ownership of an asset to be deemed as shared by a group of individuals rather than just the legal owner (or indeed just one individual other than the legal owner). It is allowed by the revenue, as there are genuine reasons for its existence eg

- 1) Poor Credit rating - If A has poor credit rating and cannot get a mortgage, then B can apply for it and hold it on trust for A until mortgage is paid and deed transferred. The revenue would no doubt expect to see evidence of A paying the mortgage repayments if investigated.
- 2) Secrecy – If A wants to buy the building B is leasing currently, without B knowing. The building can be bought by C and held on Trust for A.
- 3) Control – If father lends son £100k to buy house, and wants to ensure son cannot remortgage house for a Ferrari etc, then Dad can hold house on trust for son. Mortgage provider may have to consent to this.

Of course the abuse of this tool can be extraordinary, and experts feel that the revenue is poor at clamping down on potential abuse.

Key Benefits

- 1) Can help a client in a tricky credit situation.

- 2) Can substantially reduce CGT and other taxes if sufficient proof can be provided to back trust claims. Bear in mind that revenue does not watch this really closely.

Restrictions

- 1) Can incentivise clients, to abuse this.
- 2) If challenged by the revenue, costs of losing the case could be huge, including penalties and interest.

Charges – This a simple document which some solicitors will not even charge for it. Those who charge will probably charge around £300. Some solicitors charge a much higher price eg £1500 for it, claiming that they are incorporating charges for liaising with the revenue should things go wrong. However, if you are pulled up by the revenue on this, I think your primary defence would lie via a specialist tax accountant or tax barrister, not a ‘cut & paste’ solicitor.

4) Direct Gifts – This is where a parent gifts an asset to a son/daughter as an outright gift without any Trusts involved.

Benefits

- 1) Little admin, no real cost beyond registering with HM Land Registry.

Restrictions

- 1) No asset protection, then again maybe this is not a priority for such a client.
- 2) No holdover available on Non-Business assets.

5) A&M Trusts – Known commonly as the grandparent’s Trust. This is essentially a discretionary trust into which the settlor deposits funds to be used for the education and maintenance of his grandkids.

Key Benefits

- 1) On death, bearing in mind 7 year rule, assets in Trust will not be part of settlor’s estate.
- 2) The personal allowances of the grandchildren can be used to offset the tax burden on income generating assets within the Trust.
- 3) Asset Protection.

Restrictions

- 1) Settlor cannot benefit.
- 2) Law prevents parents doing this for kids.

Practical Issues – It is essentially a lifetime DT with a small twist. Solicitors will charge around £1000 - £2500 for doing it. It also needs to be registered with the Inland Revenue.

6) Splitting asset ownership – As there is no CGT between Husband and Wife just like IHT), there is scope here to equalise assets and reduce tax liabilities. The most common form of planning here is severing a joint tenancy to a tenancy in common, or even a sole tenancy into a tenancy in common. Beyond the residential home this can also be applied in business to assets owned jointly or solely by husband and wife.

Key benefits

- 1) Helps equalisation of estates and hence may reduce CGT tax liabilities in life and also ensure NRB not wasted on death.

Restrictions

- 1) Loss of partial asset control will be experienced by one party.

Practical Issues – This is a simple document which is signed by the husband and wife, it is then forwarded to HM land registry. Solicitors should really not be charging more than £100 for it.

7) Manipulating PPR Relief – Covered this in detail last time. Key benefit is to be able to backdate residence in a property for 3 years and hence reduce CGT. Supporting documentation eg electoral roll is probably advisable.

8) Business Assets Holdover – Holdover relief is available on the disposal of a business asset which is used for the purposes of a trade, profession or vocation. There is no restriction on the amount of holdover however issues may arise if only part of the asset was used for trade. If shares of a personal company (one where you own more than 5% of the voting shares) are being held over, then the relief is restricted by reference to those non-business assets of the company which give rise to a chargeable gain if sold.

Key Benefits

- 1) Can reduce the IHT estate of a client if he can pass business assets to his children. (bear in mind that he probably would have got BPR on death anyway)

Restrictions

- 1) Loss of asset control.
- 2) Asset must be a business asset.

9) Offshore Planning – this is principally the ability to keep assets out of the clutches of the revenue by ensuring they are owned by an offshore company or Trust. These strategies are generally only for the very wealthy. If your assets are above the £5 million mark. Then contact us and we will look into this.

Real Live Case

The following is a real life case study of a client with wealth exceeding £526,000 (2 Nil Rate Bands). The solution documents both the potential

tax liability and then a step-by-step approach to reducing the liability and distributing the estate Islamically.

G. DT AND FLIT PRACTICAL EXAMPLE

Estate Value exceeds £526,000 but not £1.5 Million (Excluding Business Property and Pension Benefits)

1. **Scenario** - Yusuf and Aisha are married with 1 son and two daughters. Yusuf's Estate value is £920,000. This does not include Business property (Yusuf's Telecom's Firm which he founded and still owns) valued at £1 Million. Aisha has an estate worth £263,000. Yusuf's Personal Pension fund is worth £200,000.

Questions :

1. What is their potential IHT liability
2. How can this liability be reduced
3. How can they distribute their estate Islamically via their wills?

1. Potential IHT Liability

Estate Value = £920,000

Less NRB = (£263,000)

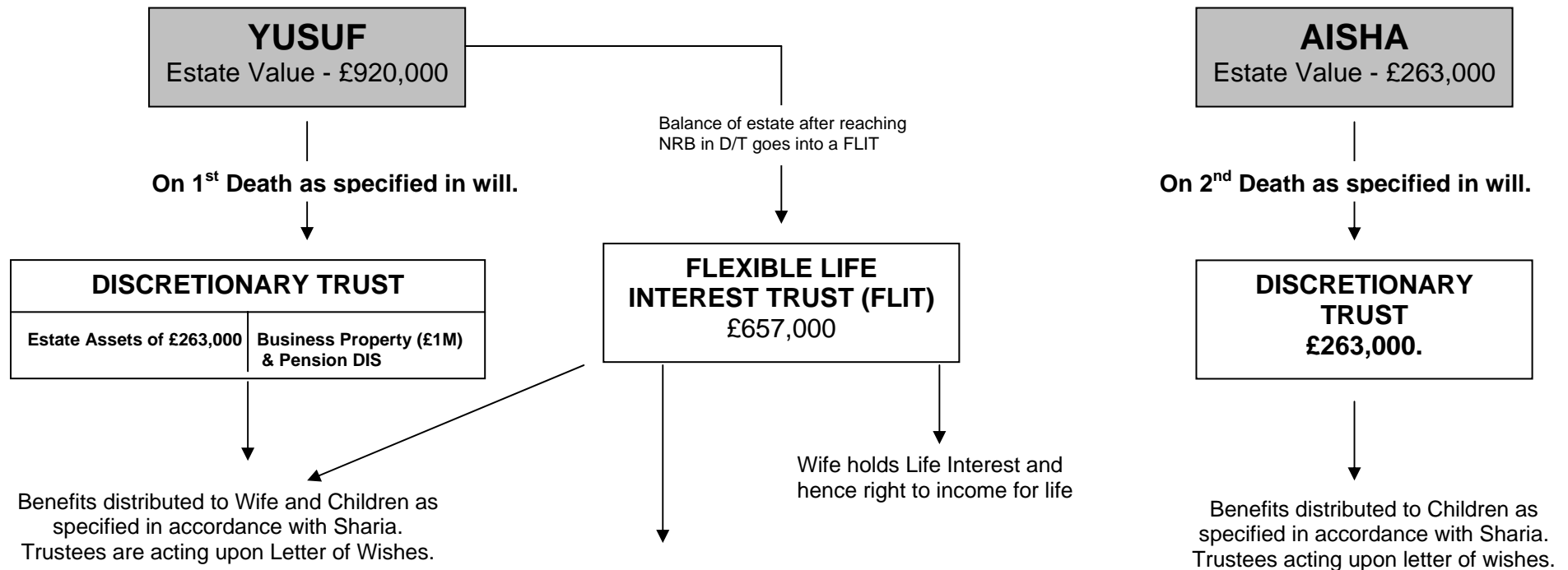
Taxable Estate = £657,000

IHT Liability = £657,000 * 40% = £262,800.

2 & 3. Reducing IHT liability and distributing estate Islamically

Answer – In this instance, the clients need to prepare wills in accordance with sharia and ensure 2 key trusts are inserted into the will. Firstly, a discretionary trust (see definition above) into which assets equivalent to the Nil Rate Band will pass on death (Referred to as a Nil Rate Band Discretionary Trust) .

- Secondly a Flexible Life Interest Trust (FLIT).
- **KEY TERM** - This is a Trust in which the surviving spouse has a life tenancy. A life tenancy simply means a right to income for life. As the wife holds a life tenancy in the FLIT, all transfers to the FLIT are free of inheritance tax on death. A transfer to a FLIT is essentially the same as an inter-spouse exemption for taxation purposes. Naturally then, the balance above the Nil rate band on 1st death will be passed into the FLIT to avoid any taxation. Our detailed guide is as follows:-



Trustees distribute trust assets in accordance with Sharia. If wife dies within 7 years of these gifts, then they are considered PET's and as such will be taxed on a Sliding scale basis. As the Wife held the life tenancy, she is deemed to have made the gifts. A life policy may be effected to mitigate this taxation, should it arise (A fatwa from Mufti Taqi Usmani has been approved permitting this). *For added tax-planning, the trustees may choose to put assets from this trust into another discretionary trust up to the value of the prevailing NRB. (See point 12 below)*

Step By step guide

1. Complete the factfind available at www.1stethical.com/ihtfactfind. Feel free to make as many copies of this factfind as desired. The factfind records all your assets, liabilities, family members, business interests and even any gifts you may have made in the last 7 years. It is critically important to fill this in with as much detail as possible. The strength of 1st Ethical's proposed solution will largely be based upon the detail in this document. On completion of the factfind, post it without delay back to 1st Ethical.
2. 1st Ethical will arrange for a draft will to be prepared for each spouse member based upon the factfind. The law firm used will be one of utmost credibility registered with the Law Society.
3. The Solicitor will ask you for an executor to be nominated in your will. This is the person(s) who is overall in charge of distributing your estate on death. This can be a relative or even a respected member of the community. **Great care must be taken in selecting executors. It is fair to say that if a client cannot rely on his/her executor to distribute the estate fairly, then no amount of legal and tax planning will do the job effectively.**
4. At this stage, there is no need to worry about the exact Islamic percentages into which the estate should be distributed. These percentages are only relevant on death and as such should be worked out then. A clause will be inserted in the will which explicitly states that the executor must distribute the estate in accordance with Sharia. It may be worthwhile stipulating in the will the authority responsible for calculating the percentages on death. (eg Local Scholar, 1st Ethical etc).
5. Once all details of the will are finalised eg 'name spellings' etc, then each spouse will sign their will and it will be independently witnessed and counter-signed. This is now legally binding.

6. On death of the first spouse, the executor may need to complete form IHT 200/IHT 205/IHT 206 etc.. (1st Ethical can help you with this). This is submitted to the Inland Revenue who will then issue the relevant documentation to show the IHT liability has been paid. This document is then presented to the court which grants probate to the executor who distributes the assets in accordance with Sharia (as stipulated in the will/Letter of wishes).
7. As the estate does not exceed the Nil Rate Band (tax-free allowance), no tax will be payable to the Inland Revenue.
8. On death of the 1st spouse, all assets will pass into the discretionary trust. As the value of the Trust will be below or equal to the Nil rate Band, there will be no tax levied on this transfer.
9. If any Business Property was present in the estate, then it too will pass into the discretionary trust. Its value is immaterial for taxation purposes as it is all exempt, regardless of size. This is also true for any lump sum pension benefits.
10. Once probate has been ascertained, the Trustees of the discretionary trust will at this point normally distribute the assets in accordance with the Letter of Wishes (This is why the selection of Trustees is so important). As the letter of wishes will clearly stipulate a distribution of assets in accordance with Sharia, the Trustees should oblige thereby alleviating the final burden of responsibility off the shoulders of the deceased.
11. Any remaining assets in the estate, after the disposals in the discretionary trust will pass into the Flexible Life Interest Trust (FLIT) (See above definition). All the assets passing across into the FLIT will be exempt from taxation, due to the wife possessing the life interest. The Trustees of the FLIT have the power to distribute assets however they see fit. It is therefore imperative to ensure that Trustees are appointed who will distribute the estate in accordance with Sharia.
12. The Trustees of the FLIT should promptly start making sharia-compliant distributions out of the FLIT. As the Trustees make distributions out of the FLIT to their rightful beneficiaries, each distribution is considered to be a gift by the surviving spouse. This is due to her life interest in the FLIT. This causes a potential problem as her death within 7 years of these distribution will trigger an inheritance tax liability on all assets above the Nil rate band, due to PET's. Tax is payable on a sliding scale, based upon how many years the spouse survives post-distribution. This is illustrated in table XX.

13. If the spouse dies within 7 years of assets being distributed by the FLIT, then the potential IHT liability can be paid by a 7 year Term Assurance. This is essentially a 7 year life Insurance policy. Life Insurance is a controversial subject with most scholars. 1st Ethical's IHT solution has been granted a fatwa by the Centre for Islamic Economics (CIE) in Karachi, Pakistan. The Principal of the Centre is the Esteem Mufti Taqi Usmani (Retd Former Judge in the Supreme Court of Pakistan). The fatwa explicitly allows for the use of a life assurance policy in such circumstances. The fatwa is based upon the principle of the **lesser of 2 evils** – this being to either pay the tax to the Inland Revenue and hitherto deprive the heirs of their rightful inheritance; or to alternatively effect a simple life policy which would pay the liability on death and allow for the entire estate to be distributed Islamically to the rightful heirs. Any seasoned IHT practitioner will attest to the above IHT solution being one which has used every means of trust planning possible to mitigate the tax liability, and ultimately only resorting to a life policy to mitigate the residual liability.
14. The Trustees of the FLIT may decide to place assets to the value of the prevailing NRB into a discretionary trust rather than gifting them directly to the beneficiaries. The wisdom here is to extricate assets from the spouse's estate as soon as possible thus exempting them from tax on the spouse's death (Any assets still in the FLIT on death are considered the spouse's for IHT purposes). In addition, beneficiaries can have their assets protected from divorce settlements or creditors.
15. Ideally on the death of the surviving spouse she should have less than the Nil Rate Band in her estate. This will allow her executor to distribute her estate tax-free via a simple will or a will with a NRB Discretionary Trust built in. If her estate exceeds the Nil Rate Band, then she will probably have to effect a life assurance policy to cover the tax liability on the balance.

KEY POINT: Whenever Life assurances are effected, it is critically important to place them in trust. This means that on death the life assurance proceeds will pay out in their entirety in a trust with pre-determined trustees. The trustees can then use the entire proceeds to pay any IHT liability. If no Trust is created, the life policy will pay out directly into the estate of the deceased thereby resulting in 40% of the policy's proceeds being chargeable to taxation.

Points 6-10 inclusive will be repeated on the wife's death.

Remember to update your will at time of death of an heir, remarriage or birth.

No doubt scenarios vary based upon individual client circumstances and the above is just an example. Sometimes significant lifetime planning may be required, sometime none whatsoever.

H. Summary

It is clearly very important for a Muslim to plan adequately for his financial affairs prior to death. The Shariah strongly supports this view. The Islamic philosophy however must be accompanied by sophisticated Trust based Tax planning in line with U.K Taxation Laws. Failure to achieve this may render the entire Islamic Planning void. 1st Ethical has thoroughly researched this field of Islamic Inheritance Planning and has a variety of solutions appropriate for your needs. You can log on to our website, and in the inheritance section you will find a factfind to be filled in. On completion of the factfind, post it to our offices and we will take it from there. Jazakallah Khairan for listening. All that is good in this paper is from Allah, whilst errors are directly attributable to myself. We end where we begun

Sources:

- 1. The Islamic will – Ahmad Thomson**
- 2. Will writing and Islamic Inheritance Planning – 1st Ethical**
- 3. The Islamic Laws of Inheritance – Dr Abid Hussain**
- 4. The final Bequest – Mohammed Al-Jibaly**
- 5. The A-Z Guide to Inheritance – 1st Ethical Ltd.**

