



Although often in the news, inheritance tax is still not widely understood. That's worrying, because it affects thousands of families every year.

If you thought inheritance tax (IHT) was just for extremely wealthy people to worry about, think again. Rising property prices have meant more estates than ever are likely to face an inheritance tax bill. In fact, the amount of inheritance tax collected is expected to reach £6.9 billion by 2023-24, an increase of £1.5 billion in just five years.

If your estate has an inheritance tax liability, your beneficiaries will have to pay the inheritance tax bill. This may not be the kind of legacy most people think of leaving behind. The good news is that there are plenty of things you can do – in your lifetime – to take care of a potential inheritance tax problem. But finding the right options for you will depend on your personal circumstances. In this guide, we set out some of your options in more detail to help you make an informed choice.

Helping to untangle Inheritance Tax

Key Features

- IHT is charged on a person's estate when they die and on certain gifts made during their lifetime,
- the rate of tax on death is 40% and 20% on lifetime chargeable transfers. The first £325,000 is not chargeable
- many lifetime gifts are treated as 'potentially exempt transfers' (PETs). So long as the individual lives for at least seven years after making the PET there will be no possibility of an IHT charge whatever the size of the gift

Mitigating liability

There are exemptions and reliefs that you may be able to make use of:

- an annual allowance of £3,000 per year. This can be carried forward for one year only if unused
- small gifts not exceeding £250 in total per individual per tax year
- gifts made out of income that are typical and habitual
- gifts made in consideration of marriage up to £5,000 if made by a parent, £2,500 by grandparents and £1,000 by others
- gifts to charities whether made during lifetime or death, gifts between spouses and registered civil partners, whether made during lifetime or on death

Planning in your lifetime

If possible you should make absolute gifts in your lifetime. A gift to an individual will be a Potentially Exempt Transfer (PET) so **there** will be no liability if the individual survives seven years. Even if the individual fails to survive **for** all of that period there may be a tax saving because the charge which will arise on the **PET will** be based on the value of the asset when it was originally gifted and not on the value at the date of death. If the value of the **gift** is below the threshold there will be no charge on the PET but the gift will use up some of the nil rate band on death. This means that there may be more tax to pay on the assets still in the estate on death.

Using available reliefs

Important reliefs of up to 100% are available on business assets such as shares in a family trading company or on agricultural property. It is important that these reliefs are utilised because once the asset concerned is sold the relief will be lost. They can only be used in connection with transfers that are chargeable to IHT.

In lifetime it may be worth considering transfers **of** such assets into trusts for members of the **family**. On death such assets should not automatically be left to the surviving spouse because that transfer will be exempt and, if the survivor subsequently sells the asset, the relief will have been wasted.

Consider using trusts

As stated previously, many lifetime gifts are PETs. So if the individual lives for at least seven years after making the gift the PET is removed from any charge to IHT on death. However, the individual ceases to have any control over what the beneficiary does with the gift. This is where trusts can be useful. Most transfers into trust are immediately chargeable to IHT but if the value of the assets transferred into trust within a seven year period is below the nil rate band, there is no charge. The assets (and their subsequent growth in value) are removed from the donor's estate. The rules are complex but significant tax savings can be achieved with careful planning. Trusts can also be an effective way of using important reliefs on businesses and agricultural properties.

Tax Planning

Each spouse/civil partner can take advantage of the IHT nil rate band. Furthermore, gifts between them are exempt (but with special rules for non-UK domiciles). Therefore it pays to use this exemption to broadly equalise estates so that both partners can make full use of exemptions and the nil rate band

Remember that you cannot continue to benefit in any way from the asset gifted because this will render the gift ineffective for IHT purposes. You cannot, for example, give away your home to your children but continue to live in it rent free.

Tax Planning

Using trusts can provide an effective means of removing assets from an estate but still allow flexibility in their ultimate destination and allow the donor to retain some control.



The nil rate band

On death, assuming the nil rate band has not already been utilised in the last seven years, it pays to ensure that it is not wasted. This gave rise to practical problems in that if assets equal to the nil rate band were bequeathed to children in the Will, the surviving partner may be left short of funds. The rules were therefore altered several years ago to allow any unused nil rate band on the death of the first spouse to be transferred to the estate of the surviving spouse.

Use the main residence nil rate band

An additional nil rate band may be available where a residence is passed on death to direct descendants such as a child or a grandchild. This band is £150,000 in 2019/20, rising to £175,000 in 2020/21. The additional band can only be used in respect of one residential property which has, at some point, been a residence of the deceased. Any unused nil rate band may be transferred to a surviving spouse or civil partner. The additional nil rate band is also available when a person downsizes or ceases to own a home on or after 8 July 2015 and assets of an equivalent value, up to the value of the additional nil rate band, are passed on death to direct descendants. There is also a tapered withdrawal of the additional nil rate band for estates with a net value (after deducting any liabilities but before reliefs and exemptions) of more than £2 million. The withdrawal rate is £1 for every £2 over this threshold.

Charitable giving

Legacies to registered charities will reduce the value of the chargeable estate and thus save 40% IHT. In addition the legacies may result in a lower IHT liability on the estate which remains chargeable.

A reduced rate of IHT applies where 10% or more of a deceased's net estate (after deducting IHT exemptions, reliefs and the nil rate band) is left to charity. In those cases the 40% rate will be reduced to 36%.

Make a Will

If you die without a Will, the intestacy provisions will apply and may result in your estate being distributed in a way you would not have chosen. Keep your Will up-to-date to reflect changes in the family situation. In particular, Wills need to be reviewed and amended as necessary on marriage or on divorce. The precise position depends on whether English or Scottish law applies.

Use life assurance

Life assurance arrangements can be used as a means of removing value from an estate and also as a method of funding IHT liabilities. A policy can be arranged to cover IHT due on death. It is particularly useful in providing funds to meet an IHT liability where the assets are not easily realised, eg family company shares.

Tax Planning

- Do you have a Will?
- Where is it kept - do you and your family know?
- Is it up-to-date?
- Does your Will make full use of IHT exemptions and reliefs - in particular does it take account of the new main residence nil rate band?
- Do you have adequate life assurance?

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