Inheritance Tax

Getting to grips with the basics:

- Are you considering IHT planning?
- What's the threshold and how can I reduce my liability?
- The main residence nil-rate band
- I've heard about the 7-year rule but how does it work?
- Making gifts which are exempt from IHT

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Inheritance Tax (IHT) has come under the spotlight over the past few years, due largely to the continued rise in house prices. These days, you don't have to be hugely wealthy to be affected by IHT. More people than ever before are calculating the value of their estates and finding they have a greater liability to IHT than they'd first thought. IHT can cost your estate thousands of pounds when you die; however, the good news is that expert planning can legitimately mitigate this tax, meaning you can pass on assets to your family as you'd intended.

What is IHT?

IHT is a tax payable on money, savings or any other assets you pass on when you die, and potentially on some gifts you make during your lifetime. The amount payable is calculated after debts and funeral expenses have been deducted.

Who pays IHT?

When someone dies, the administration of their estate will fall to their executors, or administrators if they die intestate. If the estate is liable for IHT, it is usually payable at 40%. Your executor will be responsible for paying the tax, which can only come from the deceased person's estate with the prior agreement of HM Revenue & Customs. Once the tax has been paid, then the Grant of Probate can be made, allowing the assets or their proceeds to be distributed to beneficiaries.

What is the current Inheritance Tax threshold?

The current threshold is £325,000 for an individual and £650,000 for a married couple or civil partners. The unused nil-rate band can be passed to the surviving spouse or civil partner on death.

If one partner has already died, the allowance could be £650,000, but will depend on how much of the allowance was used on that partner's death.

In response to the continuing rise in house prices, the government introduced an additional nil-rate band when a residence is passed on death to a direct descendant. This was introduced in April 2017.

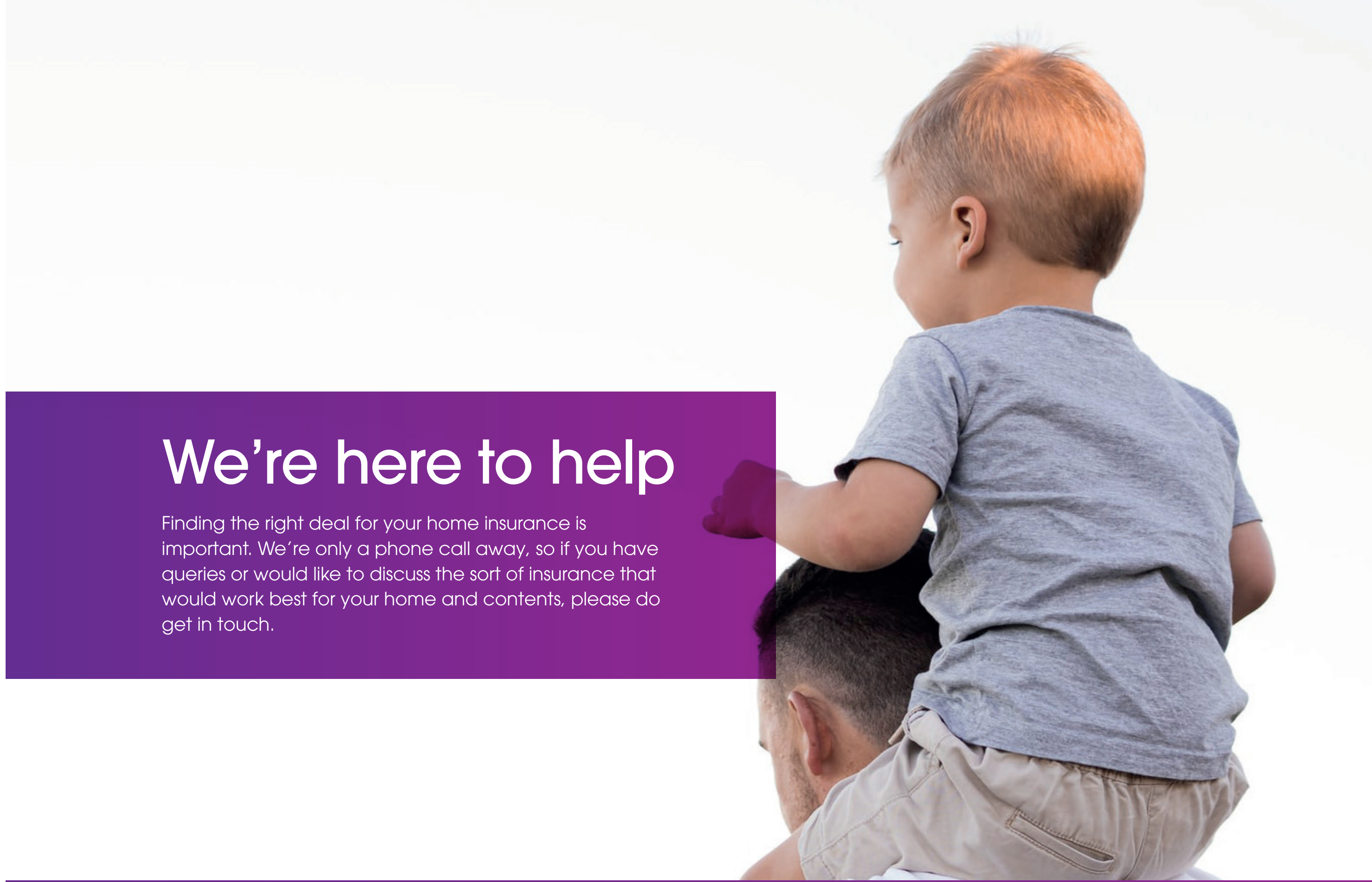
How does the main residence nil-rate band work?

This new nil-rate band will apply if you want to pass your main residence to a direct descendant like a child or grandchild (including step, adopted or foster children).

It's important to note that as only direct descendants can benefit, not everyone will be able to rely on it for IHT planning purposes.

The new nil-rate band will increase from £150,000 in 2019-20 to £175,000 in 2020-21. When added to the existing threshold of £325,000 this could potentially give rise to an overall allowance of £500,000 for those who are single or divorced, or £1m for those who are married or in civil partnerships.

However, it's important to be aware that larger estates will find that residence relief is tapered. It will reduce by £1 for every £2 of value for estates valued over £2 million.



We're here to help

Finding the right deal for your home insurance is important. We're only a phone call away, so if you have queries or would like to discuss the sort of insurance that would work best for your home and contents, please do get in touch.

What is the 7-year rule, and how does it work?

To reduce the amount of IHT payable, many families consider giving their assets away during their lifetime. These are called 'potentially exempt transfers'. The catch is that for these gifts not to be counted as part of your estate on your death, you must outlive the gift by 7 years. If you die within 7 years and the gifts are worth more than the nil-rate band, taper relief applies so that if you die say within 6 years, the tax will be less than if you were to die a year after making the gift. Gifts must be outright, and you can no longer benefit from them. So, if you were to gift your home, but continue to reside there without paying a commercial rent, HMRC would consider this to be a 'gift with reservation' and include the value as part of your estate.

Can I make gifts that are automatically free from IHT?

Yes, you can. Each financial year you can make gifts of up £3,000 (in total, not per recipient) and if you don't use this in one tax year, you can carry over any leftover allowance to the next year. If you do this, you have to use up all your allowance in that tax year, you can't accumulate several years' worth of allowance and use it up in a single gift. Gifts of up to £250 per person per financial year to any number of people are exempt. Each parent of a bride or groom can give up to £5,000; grandparents or other relatives can give up to £2,500 and any well-wisher can give £1,000. Gifts to registered charities and political parties are also exempt from IHT. There is another simple way of passing money to the next generation which allows for gifts to be made from surplus income. Conditions apply, and advice would be needed to ensure that the gifts are made in the right way.

How are assets held abroad treated for IHT?

The UK's tax system takes into consideration assets located in the UK and abroad, so IHT is levied on all your worldwide assets. This is a complex area of tax law and so advice is recommended.

Top Tips

Make a gift every year

Don't forget to maximise the use of your annual allowances; doing so can reduce the ultimate tax liability substantially.

Put things into trust

It's worth considering putting some of your cash, investments or property into a trust, as there is then the potential for this to no longer form part of your estate for IHT purposes. So, for example, you could put money into a trust to pay for your grandchildren's education, or to provide support for a relative, to ensure that these are provided for after your death.

Leave something to charity

If the size of your estate means that IHT is likely to be payable, you can reduce the rate at which it is payable by leaving at least 10% of your estate to charity. This would mean that the rate of tax payable on the balance of the estate could be reduced from 40% to 36%.

Take out life assurance

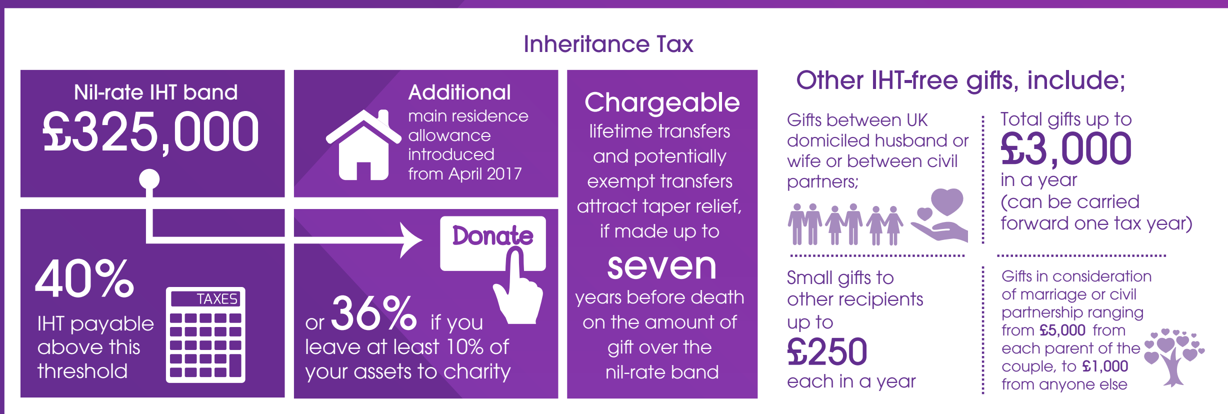
If you are concerned about the amount of IHT that may be payable on your estate, you could consider taking out a suitable life policy. Whilst it won't reduce the amount of IHT that will be due on your estate, the payment from the policy could make it easier for your beneficiaries to pay the bill. You would need to have the policy written under trust to ensure that it doesn't form part of your estate on your death. Payments of premiums are considered gifts for IHT unless they can be covered by one of the IHT exemptions.

Take professional advice

These days, many more estates are likely to be subject to IHT, so taking expert advice could save your beneficiaries substantial amounts of tax. There are simple steps you can take to reduce the amount of tax due. For instance, it's vital to have a valid Will in place; assets left to a surviving spouse or civil partner are free from IHT, but if you die without making a Will, not all of the estate will necessarily pass to the surviving spouse/civil partner.

One thing is certain, if you feel that your estate is likely to be subject to IHT you should obtain in-depth professional advice that looks at all aspects of your requirements, lifestyle and goals and develops a financial strategy that meets your needs.

If you could use some practical, no-nonsense advice, then please do get in touch.



Warning statement

Premium loading is the amount an insurance company adds to the basic premium to cover their business costs; knock-on effects to homeowners include increased premiums and excesses. Particularly relevant to those living in flood-risk areas where insurers may increase premiums for properties deemed at risk, to protect their balance sheets in the likelihood of a claim. Exclusions in insurance are clauses inserted into the terms of a policy which detail what items/events, are not included in the cover provided. It is vital to check the finer detail of the policy to avoid any unexpected exclusions.

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