FREE GUIDE

HOW TO MINIMISE INHERITANCE TAX & PROTECT YOUR ASSETS

Produced by Sedulo. For more information visit www.sedulo.co.uk

IN THIS GUIDE

PAGE 2	Contents
PAGE 3	Expert view
PAGE 4	IHT & Residence NIL rate band
PAGE 5	Spouses and IHT
PAGE 6	Estate value
PAGE 7	Paying and reducing IHT - Make lifetime gifts
PAGE 8	Reducing IHT- Make regular gifts
PAGE 9	Reducing IHT - Business property relief
PAGE 10	Reducing IHT- Agricultural property relief Trusts
PAGE 11	Reducing IHT- Pensions Insurance policy
PAGE 12	Expert view
PAGE 13	Any questions?

The information provided in this guide is of a general nature and is not a substitute for specific advice in your own circumstances.

We would recommend that you obtain specific advice from a professional adviser before you take or refrain from any action. Whilst we endeavour to use reasonable efforts to provide accurate, complete, reliable, error free and up-to-date information, we do not warrant that it is such. The information can only provide an overview of the law in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice.

EXPERT VIEW

Recent years have seen an increase in the amount of Inheritance Tax paid in the UK. There are a few reasons for this, firstly due to the increased value of estates which has largely been driven by increased house prices, secondly due to the recent "bull" stock market with growth in portfolios of c20% over the last year and finally due to the thresholds and allowances remaining the same.

However, Inheritance Tax remains somewhat of a minority tax, with less than 10% of all estates paying it. Around £4.1 billion was collected by HMRC during the 2015/16 tax year which represents roughly 1% of the total tax take in the UK.

This guide gives an overview of the Inheritance Tax rules and provides a few tips on how it might be mitigated.

DAVID EVANS - TAX PARTNER

IHT AND RESIDENCE NIL RATE BAND

WHAT IS INHERITANCE TAX?

!

Inheritance Tax or "IHT" is a tax which is paid on the value of someone's estate after they have died. It is also pa on certain gifts made during someone's lifetime.

The estate includes their **property**, **money** and **possessions**.

There is normally no IHT paid if:
• The value of your estate is less than the nil rate band (currently £325,000), or
• You leave everything to your spouse or civil partner, or
• You leave everything to charity

Example: If the value of your estate is above £325,000, IHT will be chargeable on the excess. The current rate of IHT is 40%, so if your estate was valued at £425,000, the IHT would be £40,000 (40% of the £100,000 excess over £325,000).

The nil rate band is fixed at £325,000 until 2021.

RESIDENCE NIL RATE BAND

!

From April 2017, there is an additional nil rate band, called the "residence nil rate band" or "home allowance". This is on top of the regular nil rate band of £325,000. To qualify for the residence nil rate band, you must pass on your home (or your share of it) to your children or grandchildren. This includes step-children, adopted children, foster children but it doesn't include nieces, nephews or siblings.

The residence nil rate band is currently £100,000 but is scheduled to increase to £175,000 by the 2020/21 tax year.

The table opposite shows the combined nil rate band:

	Nil Rate Band	Residence Nil Rate Band	Combined Allowance
2017/18	£325,000	£100,000	£425,000
2018/19	£325,000	£125,000	£450,000
2019/20	£325,000	£150,000	£475,000
2020/21	£325,000	£175,000	£500,000

Note that the residence nil rate band starts to be withdrawn if the value of your estate exceeds £2 million.

SPOUSES AND IHT

SPOUSES

If you leave everything you own to your spouse, then there will be no IHT due and you will not have used any of your nil rate band.

In this case, the surviving spouse can use the unused nil rate band of the deceased spouse, which means the surviving spouse may have a double nil rate band. This also applies to the residence nil rate band.

The table below shows a few examples of IHT liabilities at different estate values:

	INHERITANCE TAX DUE			
Estate value	**Single person with no residence NRB**	**With max residence NRB**	**Widow(er) with no residence NRB**	**Widow(er) with max residence NRB**
£325,000	£0	£0	£0	£0
£375,000	£20,000	£0	£0	£0
£425,000	£40,000	£0	£0	£0
£500,000	£70,000	£0	£0	£0
£650,000	£130,000	£60,000	£0	£0
£750,000	£170,000	£100,000	£40,000	£0
£1,000,000	£270,000	£200,000	£140,000	£0
£1,500,000	£470,000	£400,000	£340,000	£200,000
£2,000,000	£670,000	£600,000	£540,000	£400,000
£2,300,000	£790,000	£780,000	£660,000	£580,000
£3,000,000	£1,070,000	£1,070,000	£940,000	£940,000

ESTATE VALUE

HOW TO VALUE THE ESTATE

To value an estate for IHT purposes you need to list out all the assets and work out their value at the date of death.

Common assets include the following:
(This is not a full list)
- **Money**
- **Property & land**
- **Jewellery**
- **Cars**
- **Shares**
- **Household goods**
- **Works of art**
- **Investments / ISAs**

You can deduct the value of any debts and liabilities, such as mortgages, credit card debts, household bills and funeral expenses. **It is important to keep records of how you have arrived at the values as HMRC can ask to see records up to 20 years after the IHT is paid!**

Gifts also need to be included if they were made within the 7 years before the date of death. You'll also need to include any earlier gifts if the person who died continued to benefit from the gift, for example if they gave away their house but continued to live in it rent free. **These are known as gifts with reservation of benefit.**

PAYING AND REDUCING IHT

PAYING IHT

Where there is a will it is normally the executors that work out and pay any IHT due. If there isn't a will, the administrator will deal with the IHT.

The IHT should be paid within 6 months of the date of death and it is usually paid out of the funds in the estate. This means that assets may need to be sold to realise the cash to pay the IHT. Once the IHT has been paid, the remaining funds can be distributed to the beneficiaries. Note that good executors can make interim distributions.

REDUCING IHT - MAKE LIFETIME GIFTS

If you give assets away and survive 7 years then there will be no IHT on these assets. These are called either Potentially Exempt Transfers or "PET's". If you die before the 7 years are up, then the value of these gifts will be brought back into the estate for IHT purposes.

Gifts made within 3 years of death are taxed at the normal 40% rate, however earlier gifts attract reduced rates. This is shown in the table below:

Gift made within	Value of Gift Brought Into Estate	Effective IHT Rate
Less than 3 years of death	100%	40%
3 to 4 years of death	80%	32%
4 to 5 years of death	60%	24%
5 to 6 years of death	40%	16%
6 to 7 years of death	20%	8%

Planning point - If you think IHT will apply then it makes sense to give away assets earlier as you are more likely to survive 7 years. For example, if you are in your eighties, surviving 7 years might be trickier than if you were in your fifties!

REDUCING IHT

REDUCING IHT - MAKE REGULAR GIFTS

Each year an individual can give away a certain amount (known as an annual exemption) which is exempt from IHT, even if you die within 7 years of making the gift. The current exempt amount is £3,000 per person per year. You can also use the prior year's £3,000 exemption if you made no gifts in that year.

Planning point – the annual exemption lends itself to assets which can be handed down gradually over time, such as cash or shares in quoted and unquoted companies.

You can also give away small gifts under £250 each to any number of people and these will be exempt from IHT. Note that this can not be the same person you give £3,000.

You can also make regular gifts out of your income, as long as they do not affect your normal standard of living. This is known as "normal expenditure out of income". No specific limit is placed on this; what is important is that the gift is made from income, for example; you gift some of your pension income and that you can maintain your usual standard of living after the gift. If you have a large amount of income each year, then this gives scope to make some large gifts free of IHT.

If you are considering this, you should take specific advice as these rules are complex.

WEDDING GIFTS

Certain gifts you make to people on their wedding day may be exempt from IHT. This wedding allowance is in addition to the £3,000 annual exemption. See example below.

Amount you can give to each of your children	**£5,000**
Amount you can give to each of your grandchildren	**£2,500**
Amount you can give to anyone	**£1,000**

REDUCING IHT

REDUCING IHT - BUSINESS PROPERTY RELIEF

Business property relief (BPR) allows a business (irrespective of its value) to be passed on to the next generation free of IHT.

In general, you must have held the business property for at least two years prior to death to qualify for the relief. BPR is not available in the following circumstances:

- Where the business consists of dealing in securities, holding investments or dealing in land
- Where the property transferred is subject to a binding contract for sale
- Where the shares are in a company in liquidation
- Where the assets are not used wholly or mainly for business purposes.

Planning point – given that business property is largely exempt from IHT, it is normally recommended that you hold onto it until death so that you benefit from the relief. For example, if you sold your business during your lifetime, the cash you receive will not be covered by BPR and will be subject to IHT.

There are six types of business property which qualify for BPR:

Type	Relief
A business or interest in a business	100%
A controlling shareholding in an unquoted company	100%
A minority shareholding in an unquoted company	100%
A controlling shareholding in a quoted company	50%
Land, buildings, machinery or plant used in a business carried on by a company controlled by you or a partnership in which you are a partner	50%
Land, buildings, machinery or plant which you have an interest in possession & used in your business	100% (If transfered with the business, 50% if not)

REDUCING IHT

REDUCING IHT - AGRICULTURAL PROPERTY RELIEF

Agricultural Property Relief (APR) works a bit like BPR in that it grants either a 100% or a 50% exemption to agricultural property (buildings and land only) from IHT. However, APR only applies on the agricultural value of the asset which is often lower than the market value.

You can generally qualify for APR via two routes:

1. By personally using land for agriculture for the two years prior to death, or

2. By owning land used for agriculture by somebody else for seven years prior to death.

The APR rules are complicated, so if you own agricultural property you should obtain further specific advice.

REDUCING IHT - TRUSTS

Wealthy families have used trusts to avoid IHT for years. The basic principle with trusts is that assets are transferred into a trust which, for tax purposes, is a separate legal entity, i.e. you no longer own the assets.

Trust planning is bespoke to each case and as such we have not gone into detail in this guide. If you would like advice on trust planning, you should contact our Tax department.

REDUCING IHT

REDUCING IHT - PENSIONS

2015 saw a major change to IHT rules around pensions. In summary, if you die before the age of 75, your beneficiaries can get the money in the pension fund free of IHT. If you die over the age of 75, your beneficiaries can transfer the money into their own pension fund. If they take the cash or draw it out as an income they will pay income tax on it at their marginal rate(s) of income tax.

If you would like more advice about the IHT treatment of your pension fund then you should contact our Wealth Management team.

REDUCING IHT - INSURANCE POLICY

It is possible to take out an insurance policy to cover some or all of the IHT on an estate. This means that your family will not have to sell the assets (such as the family home) to pay the tax.

In summary, there are two types of insurance policy which can be used for this purpose:

1. Whole of life policy
This type of insurance lasts for your whole life, irrespective of how long you live. We would recommend that you take out this kind of policy as early as possible, as the premiums are cheaper the younger you are.

2. Term insurance policy
This type of insurance lasts for a predetermined period and only pays out if you die within this period.

Planning point – it is important that the insurance policy is written into trust. You should take professional advice in this regard to ensure that this is done correctly. If you are interested in insurance for IHT, you should contact our Wealth Management team for more information.

EXPERT VIEW

Inheritance Tax is often a voluntary tax in that it can be planned for and potentially mitigated.

Put simply, you can either do nothing, plan to have the funds set aside to pay the tax bill or you can plan to reduce your taxable estate.

The problem with reducing your taxable estate is that it involves giving money away, either directly to beneficiaries such as your children or to a trust.

Giving money away to your beneficiaries is perhaps the easiest way to reduce IHT but this means that they are free to do with the funds what they want. It is also their money should they get into financial difficulty or divorce.

The use of a trust means you retain control over the funds, as a trustee, and can decide who benefits from the funds and when. However, for the planning to be effective you cannot benefit from the funds in the future.

PAUL LINDFIELD - WEALTH MANAGEMENT PARTNER

ANY QUESTIONS?

Got a question about this IHT guide or need to speak to us? Get in touch about popping in for a coffee using any of the details below...

TEL 0161 236 9077
EMAIL david.evans@sedulo.co.uk
ADDRESS Sedulo, Regency Court, 62 - 66 Deansgate, Manchester, M3 2EN