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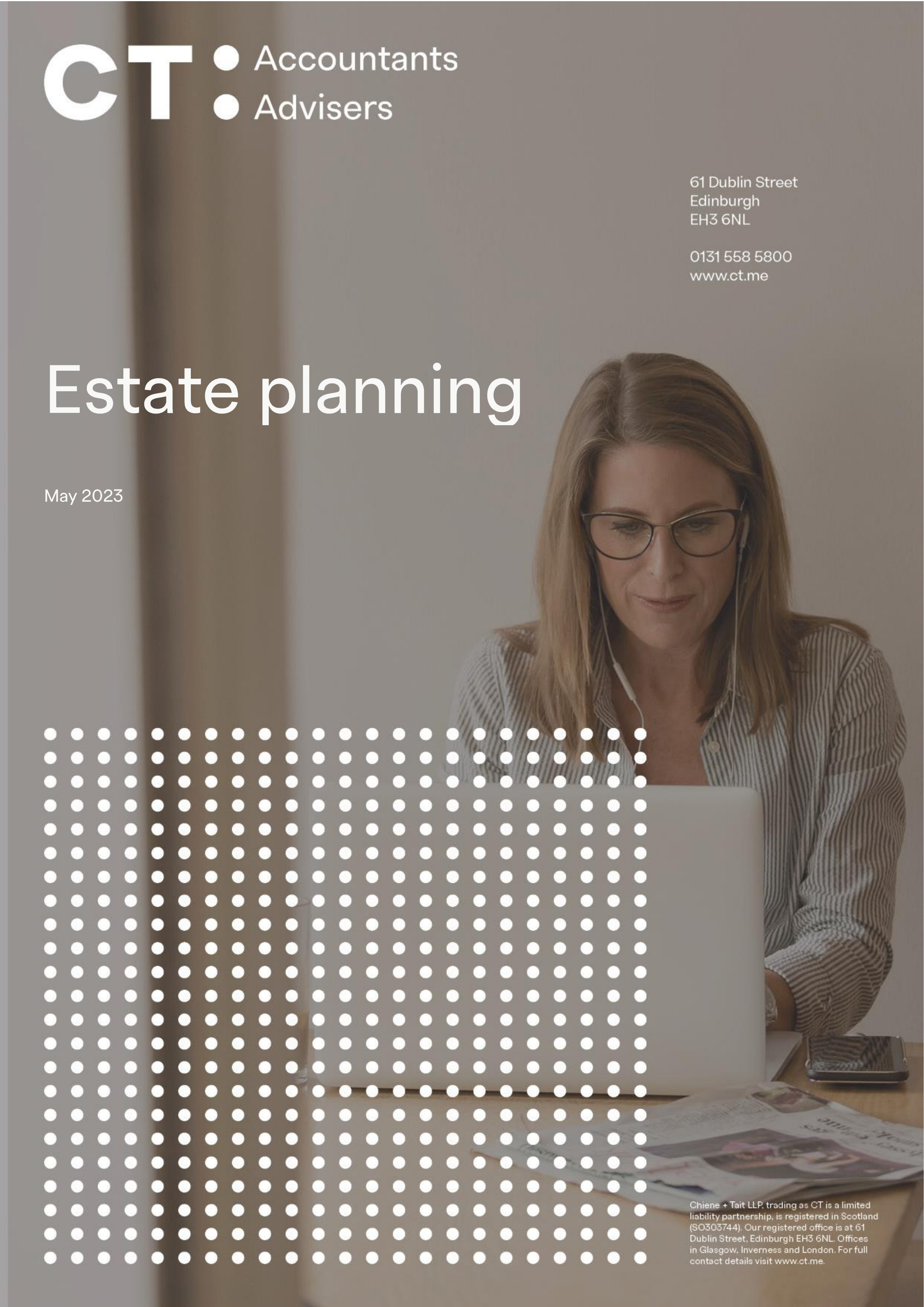
Estate planning

May 2023



Estate planning

You can’t take it with you...

It is often said that Inheritance Tax (IHT) is not a tax for the rich – it is a tax for the unprepared. If you plan in advance, you can significantly reduce its impact.

IHT is charged on:

- Lifetime gifts of capital into trust
- Most gifts of capital within seven years of death
- Assets passing on death.

The following do not attract IHT:

- The ‘nil rate band’ – the first £325,000 of gifts
- Gifts to a husband, wife, or civil partner (but see special cases below)
- Gifts to charity
- The value of certain business and farming assets
- The first £3,000 given away each year
- ‘Normal expenditure out of income’ – gifts which are made regularly and do not affect the donor’s capital
- Wedding gifts up to a set value
- Small gifts of up to £250 to a particular recipient in a year (but this is not deducted from a larger gift).

Key planning questions

The first step towards IHT planning is to establish what your exposure to the tax is. You need a realistic assessment of the current value of all your assets, less your liabilities (such as a mortgage). Bear in mind, insurance policies that are payable to your estate on your death are included in the chargeable total. The excess of your net assets over £325,000 is potentially liable to IHT at 40%.

If you are a widow or widower and your former spouse left you their estate, you may benefit from an increased nil rate band. It’s important to work out how much this might be and factor it into your calculations. If you received the whole of their estate, you could have a double nil rate band of £650,000.

Certain couples will ultimately have a double nil rate band of £1,000,000, if the estate qualifies for the residence nil rate band (RNRB) for the family home. The RNRB stands at £175,000 per person and applies to individuals who pass on their main residence to their direct descendants.

It’s important to note that estates worth over £2 million will have their RNRB reduced by £1 for every £2 over the threshold. This means that the RNRB will be zero if the estate’s value exceeds £2.35 million.

The second step is to identify any assets that you can give away, and to consider who you want to benefit from them. If you don't think the ultimate beneficiary is ready to own them outright, you can move those assets out of your chargeable estate by transferring them to a trust.

Key planning points

If you can give assets away in your lifetime, you can substantially reduce the IHT charge on death. It's worth considering all the above exemptions. If you have insurance policies on your life, make sure they are not payable to your estate on your death. Transfer the benefit of the policy to a trust, or make sure that someone else is the beneficiary from the outset.

Make sure your Will is written with IHT in mind and regularly reviewed. If you're considering making charitable donations in your Will, take advantage of the 36% reduced rate of IHT, where at least 10% of the net estate chargeable on death is left to charity.

Catches

Gifts must be made outright to be effective for IHT purposes. For example:

- If you continue to enjoy the use of the property that you've given away, the value of that asset is likely to remain part of your estate for IHT purposes.

- If you own a business or an agricultural property that's eligible for 100% IHT relief, it can be left in your estate without an IHT charge. However, if you sell the property, you'll suddenly become exposed to IHT on the full value.

- Farmers retiring from farming activity may lose the benefit of the agricultural property relief on the farmhouse they live in. If you have assets that might qualify for an IHT exemption, it's essential to keep them under review to make sure they continue to qualify. If they don't, consider what action to take in respect of the increased IHT exposure.

Need more help?

For more information, please contact the Personal Tax team at PersonalTaxAdvisory@ct.me

- Information correct at May 2023.

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