

## Inheritance Tax

### Managing Inheritance Tax (IHT)

Inheritance tax is charged at 40% on estates that exceed £325,000 (2010/11) and the value of many houses now exceeds this limit and IHT is payable.

IHT is called the voluntary tax, since much of it is avoidable. Specialist advice is always advisable when tax planning for inheritance tax.

In his Pre-Budget Report, the Chancellor of the Exchequer announced that for deaths on or after 9 October 2007 it will be possible for spouses and civil partners to transfer their unused Inheritance Tax nil rate band allowances. This means that any part of the nil rate band that was not used when the first spouse or civil partner died can be transferred to the surviving spouse or civil partner for use on their death.

The following are a number of areas to legitimately manage an estate to prevent large amounts of IHT being payable.

- Gift exemptions [Inheritance Tax Gifts](#)
- Potentially exempt transfers
  - Assets given away during the lifetime of the deceased have to be transferred within seven years before death, otherwise IHT is charged in a sliding scale from 40% to 8% in the last year. This relief only applies to gifts that fall outside the £325,000 allowance.
- Spouse's Exemption
  - All transfers between spouses are exempt of IHT but if the spouse is non-UK domiciled the exemption is only to £55,000.
- Business and Agricultural reliefs
- Back to Back Schemes
  - This involves buying a life annuity and using the income to pay a whole life assurance policy which is then written in trust to pay the IHT bill on death
- Equity Release Schemes
- Family Trusts
  - Recent changes to this scheme must be noted. Transferring the property(ies) into a trust fund managed by the beneficiaries whilst the original owners retain the rights to live in the property until death has been very popular. The pre-owned assets tax legislation came into effect on 6<sup>th</sup> April 2005, and this means that the occupiers must pay a market rental or tax on the annual market rental value. Children who move in with a parent to care

for them are exempt when the property is transferred to them.

- Discretionary Will Trusts
  - This scheme allows for the first spouse to die and bequeath assets equal to the nil rate bands into trust for their beneficiaries. The surviving spouse becomes a discretionary beneficiary of the trust and can draw funds from the trust up to £325,000. On the death of the surviving spouse the £325,000 is deducted from their estate and repaid to the trust of the first spouse.
  - For example - the total value of the combined estate is worth £650,000 (married couple) spouse 1 dies and leaves £325,000 in a trust. Spouse 2 borrows £325,000 from the trust, and continues to receive interest and/or benefits from the trust. When spouse 2 dies then
    - Spouse1 trust is refunded the £325,000 and the other living beneficiaries then inherit that trust fund.
    - Spouse 2 estate is passed onto their beneficiaries.

The original £650,000 is used by each spouse at £325,000 each and no IHT has been paid.

- Loan Trusts
  - The loan trust receives an interest free loan from the deceased's estate, which is then invested for capital growth in an investment bond. Assets held in trust do not come within IHT calculation. Repayment of the loan is made over time, and as long as the repayments made are spent, there is no tax to pay on that, whilst the bond grows and is protected from IHT.

There is an excellent glossary of terms on the HMRC website that can help further.

<http://www.hmrc.gov.uk/cto/glossary.htm>

In addition please find below the link to the section on the HMRC website

<http://www.hmrc.gov.uk/inheritancetax/intro/basics.htm>