Inheritance Tax

Inheritance Tax (IHT) has been a growing concern for many families. As property prices and asset values continue to rise, more estates are being subjected to IHT, reaching record levels year on year. The increasing burden of IHT can significantly reduce the wealth passed on to your beneficiaries, making it crucial to understand and address this issue effectively. This factsheet explains the rules and various types of planning available to you.

Simple Guide to Fundamental Rules of IHT

1. **IHT Threshold:** The current IHT threshold, also known as the nil-rate band, is £325,000. Estates valued above this amount are subject to a 40% tax rate on the excess.
2. **Residence Nil-Rate Band:** An additional allowance, the residence nil-rate band (RNRB), applies if you pass your home to your direct descendants. For the 2023/24 tax year, this is set at £175,000.
3. **Transferable Allowances:** Unused portions of the nil-rate band and RNRB can be transferred to a surviving spouse or civil partner, potentially doubling the threshold.
4. **Gifting Rules:** Gifts made more than seven years before death are generally exempt from IHT. Taper relief may apply to gifts made between three and seven years before death.

It's important to note that IHT is essentially a voluntary tax; with proper planning, you can take significant steps to reduce or even eliminate the amount of tax payable on your estate. By engaging in proactive planning during your lifetime, you can ensure that more of your hard-earned assets are preserved for your loved ones.

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Inheritance tax planning options

1. Will

A well-drafted will is the cornerstone of IHT planning. It ensures your wishes are followed and can help minimise IHT by making full use of available allowances and reliefs. Consult a professional to draft a Will that reflects your intentions and optimises your estate for tax purposes.

2. Gifts

- **Lifetime Gifts**: Regular gifts from surplus income are exempt from IHT, as are smaller annual gifts up to £3,000. Consider making larger gifts early to benefit from the seven-year rule.
- **Charitable Gifts**: Donations to registered charities (and clubs) are exempt from IHT. If you leave 10% or more of your net estate to charity, the IHT rate on the remaining estate reduces to 36%.
- **LPAs**: LPAs enable trusted individuals to manage your financial affairs if you become incapacitated, ensuring your IHT planning remains effective.

3. Trusts

Trusts can be a powerful tool for managing IHT liability. By placing assets in a trust, you can control how they are used and potentially reduce the taxable value of your estate. Various types of trusts serve different purposes, so seek advice to choose the best option for your circumstances.

4. Whole of Life Insurance

A whole of life insurance policy can provide a lump sum to cover IHT liabilities, ensuring that your beneficiaries do not have to sell assets to pay the tax. Make sure the policy is written in trust to avoid increasing the value of your estate.

5. Pensions

Pension funds are typically outside the scope of IHT. By maximising pension contributions and drawing down other assets first, you can reduce the taxable value of your estate.

Review your pension nominations to ensure they align with your estate planning goals.

6. Business Relief / IHT Free ISAs

Some ISAs offer the potential for IHT exemption if invested in qualifying AIM (Alternative Investment Market) shares, which can benefit from business relief after two years.

Contact Us

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