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GUIDE TO

THE NEW INHERITANCE TAX RULES

SAFEGUARD YOUR WEALTH FOR FUTURE GENERATIONS

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Safeguard your wealth for future generations

Unforeseen life events and circumstances can potentially impact your finances in a number of ways. We can help you to safeguard your wealth for future generations. But, for many of us, there can be a remarkable gap between our intentions and our actions.

Although often in the news, Inheritance Tax (IHT) is still not widely understood. That's worrying, because it affects thousands of families every year. If you thought IHT was just for extremely wealthy people to worry about, think again. The amount of IHT collected has doubled over the last five years[1].

The Government is introducing a new IHT allowance, adding an extra tax-free amount when you own a property. But, without the right advice and careful financial planning, HM Revenue & Customs could become the single largest beneficiary of your estate following your death.

MONEY AND POSSESSIONS

If your estate has an IHT liability, your beneficiaries will have to pay the IHT bill. This may not be the kind of legacy most people think of leaving behind. IHT is payable on assets such as property, money and possessions that are passed on when you die. IHT is payable at 40% on assets that exceed the threshold 'nil-rate band', which is currently at £325,000.

The good news is that there are things you can do – in your lifetime – to take care of a potential IHT problem. But finding the right options for you will depend on your personal circumstances and receiving appropriate advice.

NEW IHT RULES

Under the new IHT rules, more estates are likely to pass free of IHT post–5 April 2017. By 5 April 2021, some estates worth £1 million will pass free of IHT. This is the good news, but is far from the whole picture. For many, in particular the childless, the IHT could in fact (with the effect of inflation) be higher post–5 April 2017.

For deaths from 6 April 2017, an additional IHT-free 'residence nil rate band' will be available. This will begin at £100,000 in the tax year 2017/18 and will increase by £25,000 each tax year, reaching £175,000 by 6 April 2020. This 'residence nil rate band' is available where the deceased leaves a property (or the proceeds of sale of a property if sold on or after 8 July 2015), in which they have lived at some point, to their direct descendents (their spouses and children).

RESIDENCE NIL RATE BAND

The residence nil rate band is available on top of the existing IHT nil rate band of £325,000, so that in 2020/21 an individual will potentially be able to leave £500,000 free of IHT. As is now the case with the standard nil rate band, where the first of a married couple to die leaves their estate to their spouse, the residence nil rate band can effectively be 'passed on' to the surviving spouse.

For those with a conventional family, a modest home and savings (and subject to the rate of house price increases in the coming years), it is therefore likely that no IHT will be payable on their estate.

DOWNSCALED OR SOLD UP

The new rules are designed to ensure that the elderly are not encouraged to retain family homes they would otherwise have sold. Where the deceased has downscaled or sold up on or after 8 July 2015, it will still be possible to pass on the proceeds of the family home and make use of the residence nil rate band. The rules provide only that the deceased must have lived in the property in question at some point, and that assets of an equivalent value are passed on to direct descendents.

The additional residence nil rate band will not be available to the most valuable estates. The amount of residence nil rate band available will be tapered for estates worth more than £2 million.

Additional nil rate band to be phased in as follows:

- 2017/18 – £100,000
- 2018/19 – £125,000
- 2019/20 – £150,000
- 2020/21 – £175,000

In subsequent tax years, the residence nil rate band will increase in line with the Consumer Price Index.

For estates worth in excess of £2 million the additional nil rate band will be tapered at a withdrawal rate of £1 for every £2 over the threshold. In 2020/21, there will be no residence nil rate band available on the first death if the net value of the deceased's estate exceeds £2.35 million. This figure will be £2.7 million in 2020/21 on the death of the second spouse, assuming their own and their deceased spouse's residence nil rate band are both available.

INDIVIDUALS WITH A RESIDENTIAL PROPERTY

An additional nil rate band of £175,000 will be available for individuals when a residential property, which has been their residence at some point, is passed on death to a direct descendant. Direct descendants include children (including stepchildren, adopted children or foster children) or grandchildren. This extra nil rate band will be in addition to the existing nil rate band of £325,000 (which will remain at this level until 2020/21). As with the existing nil rate band, any unused additional nil rate band can be transferred to a surviving spouse or registered civil partner, resulting in an effective inheritance threshold of £1 million for a couple with children that they wish to inherit the property (a property worth at least £350,000 and total estate over £1 million, but not over £2 million from 2020/21, i.e. the £1 million only applies to people meeting these criteria).

This additional nil rate band is available for individuals who have downsized or sold their home on or after 8 July 2015, as long as they pass assets of an equivalent value on to direct descendants on death. For example, an individual who sells their £300,000 home and purchases a £150,000 home could benefit from the maximum allowance of £175,000 in 2020/21 if they leave their home and assets of £25,000 to direct descendants on death. They will be liable to IHT only if their total estate exceeds £500,000.

ERODED BY INFLATION

The nil rate band of £325,000 is now frozen until at least April 2021 (the Government has said it will increase with the Consumer Price Index from 2021 onwards). This means that for the unmarried, and for those who leave no children or grandchildren, the IHT-free band will continue to be eroded by inflation. A single person owning property in London, for example, is highly likely to leave an estate subject to IHT. The number of single and childless persons of even modest means who will fall within the IHT bracket will inevitably continue to increase.

The actions you need to take depend on your family's needs for capital and income, as well as your current assets and your intended beneficiaries. So it's important to speak with us for expert advice on the best options for your circumstances.

Source data:

[1] HM Revenue & Customs (HMRC) collected £4.7 billion from thousands of bereaved families in 2015/16. Source: Office for National Statistics, 2016

BURDEN OF INHERITANCE TAX

The increase in the IHT threshold from 6 April 2017 will allow more individuals to pass on the family home to their direct descendants without the burden of IHT, but each individual's situation will be different. To review your plans and to consider the options, please contact us.

INFORMATION IS BASED ON OUR CURRENT UNDERSTANDING OF TAXATION LEGISLATION AND REGULATIONS. ANY LEVELS AND BASES OF, AND RELIEFS FROM, TAXATION ARE SUBJECT TO CHANGE.

THE VALUE OF INVESTMENTS AND INCOME FROM THEM MAY GO DOWN. YOU MAY NOT GET BACK THE ORIGINAL AMOUNT INVESTED.

PAST PERFORMANCE IS NOT A RELIABLE INDICATOR OF FUTURE PERFORMANCE.

> "This additional nil rate band is available for individuals who have downsized or sold their home on or after 8 July 2015, as long as they pass assets of an equivalent value onto direct descendants on death."

UNPREPARED, UNSUPPORTED AND UNINFORMED

Your loved ones may find receiving an inheritance a challenging time. Some inheritors are largely unprepared, unsupported and uninformed about inheritance. We can help you review your options and ensure your intentions to transfer wealth are achieved.

To discuss your particular situation, please contact us.

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