

Inheritance Tax: What are the rules and what can I do about it?

This guide is to help you understand the main points of how Inheritance Tax (IHT) is charged on death and highlight some options that can help you minimise your exposure to this.

What is Inheritance Tax?

IHT will be due if your estate exceeds your available allowances and reliefs. The rate of tax is 40% on the excess amount. Your taxable estate includes property, land, jewellery, possessions, money, and life insurance. If property or bank accounts are owned jointly with others, generally half the value is also included. Pensions, death in service benefits and life insurance written into trust are not included in your estate.

Any liabilities such as mortgages, credit cards and loans would be deducted from the assets to calculate your estate value.

What are the current allowances?

The current allowance for inheritance tax is £325,000, known as 'The Nil Rate Band'.

The amount of Nil Rate Band you have available on death depends on whether you have given away money (above exempt amounts) or made a gift into a trust in the seven years before your death.

No IHT is payable if your estate is below the available Nil Rate Band.

There is an additional relief of up to £175,000 known as 'The Residence Nil Rate Band' (RNRB). Several conditions apply to the availability of this relief, including:

- It only applies if the property (or proceeds) go to qualifying beneficiaries e.g. children, grandchildren, stepchildren etc. It does not include nieces or nephews.
- Applies only to property that has been a residence of the deceased. It excludes buy-to-let.
- The RNRB is available if the estate is less than £2million. At £2.35 million (£2.7m couples), no RNRB is available. Between these amounts, tapering rules apply.

- The value of the RNRB is a maximum of £175,000 (or £350,000 for a married couple). If the value of the property is less, the relief is limited to the property value.
- The property does not need to be owned at death to qualify for the RNRB. The RNRB is still available if you have downsized or sold your property to move into residential care or with a relative. You should keep records of any sale.

The Nil Rate Band and the Residence Nil Rate Band rates apply until 2026. Other reliefs such as Business Property Relief and Agricultural Property Relief may also be available to your estate.

Spouse (Civil Partner) Exemption

You can leave an unlimited amount to your spouse. There is no IHT due to the spouse exemption. Giving assets to a spouse or civil partner during life or death does not use up your nil-rate band. Different rules apply for married couples where one spouse is UK domiciled and the other is not.

Unused IHT allowances between married couples and civil partners are transferable. A married couple can have a combined allowance of £650,000 plus the RNRB if applicable. This is a maximum of £1,000,000.

When the surviving spouse dies, the unused allowance needs to be claimed by the executor. Your choice of executor is important so that the right reliefs are claimed and the correct tax is paid.

If you leave any of your estate to someone other than your spouse or civil partner, any amounts exceeding available allowances will be subject to IHT at 40%.

By making a will you can ensure your estate benefits from using the spousal exemption and other reliefs.

If you are married with children, for example, the division of your estate through the rules of intestacy could result in your family being caught out and potentially hit twice with an IHT bill.

Making a will can help you to avoid this problem and much more.

| Basic Overview | Married Couple | Married couple | Single Person | Single Person |
|---------------------|---|---|---------------|---|
| | Home Owners | Home Owners | Home Owner | Home Owner |
| | With children or other qualifying beneficiaries | No children or other qualifying beneficiaries | With children | No children or other qualifying beneficiaries |
| Max. NRB available | £650,000 | £650,000 | £325,000 | £325,000 |
| Max. RNRB available | £350,000 | Nil | £175,000 | Nil |
| Total | £1,000,000 | £650,000 | £500,000 | £325,000 |

Unmarried couples do not have transferable allowances and are treated as a single person regardless of how long they have been together or if they have children. Unmarried couples are also not provided for by the rules of intestacy so it is **important that unmarried couples make a will and consider IHT planning options early** so IHT on first death can be minimised.

Options to minimise IHT on death

- **Do nothing.** For some people IHT is not a concern and they do not wish to take any action.
- **Spend it.** Going on holiday, for example.
- **Leave a gift to a charity in your Will.** Leaving 10% or more of your estate to charity reduces the IHT rate from 40% to 36%.
- **Tax efficient investments.** Some investments can be exempt from IHT. They are often high risk investments and there will be specific qualifying criteria.
- **Life Insurance.** A 'whole of life' insurance policy could be put in place to cover any IHT liability on death. This should be written into trust.
- **Gifts made during your lifetime.**
 - Annual Exemption of £3000
 - Gifts out of regular income
 - Gifts on marriage (limits apply)
 - £250 unlimited gifts to different people
 - Lump sum gifts to an individual or trust – if you live for 7 yrs, the gift is exempt (unless you continue to receive a benefit from it).
- **Pensions.** Money within a pension usually sits outside of your estate. Depending on the type of pension you have, it may be more tax efficient to take income from other sources to reduce the size of your estate below the IHT allowance.



Points to consider:

- There is not a one size fits all approach to IHT planning.
- Make sure you have an up-to-date will and regularly review this.
- Talk to us about how trusts (set up in your lifetime and by will) can help with planning.
- Seek independent financial advice early so that more options are available to you.
- Tax rules and allowances can change so you should keep your planning under review.
- Make gifts early to maximise the chance of your gift being exempt after 7 years.
- Use annual allowances and other exemptions.
- Be aware that if making a gift, you do not retain a benefit from it, e.g. gifting a holiday home to a child and using it regularly without paying market rent. It could be classed as a gift with reservation of benefit and included in your taxable estate.

Disclaimer

We hope this provides a useful introduction. It is not tax or legal advice and you should always seek advice relevant to your own situation. Tax rules and allowances do change so you should keep your planning under review.