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INHERITANCE TAX PLANNING IN 2021 - INFORMATION FOR CLIENTS
Walsh West Private Client Legal 2021

12 ways to minimise inheritance tax

What is inheritance tax?

Inheritance tax (IHT) is a tax you must pay when you die. Whether you have to pay it, and how much you pay, is based on the value of your estate. Estates are essentially the value of all your cash, belongings, and property.

Your estate's value is the value of the whole entirety of your assets. An asset is anything of value that is owned, for example cash, investments, businesses, cars, payouts from life assurance etc.

What is the threshold for inheritance tax?

- ✓ The current rule is that IHT is paid on anything valued above £325,000.
- ✓ The current market rate is 40% on anything over this nil rate band. The nil rate band is currently fixed, but since property prices continue to rise with inflation, more and more people are finding they need to pay IHT.
- ✓ The standard 40% rate is reduced to 36% if you transfer 10% or more of your estate to a charity in your will.
- ✓ If you are in a couple, you can also leave everything to your other half. Whether you leave all of your legacy or just some to your partner, the remaining sum of your nil rate balance will be transferred to them on record.
- ✓ For example, if you leave everything to your other half the impact is that the nil rate allowance for their estate doubles to £650,000.

Who pays the inheritance tax?

The person responsible for paying your inheritance tax depends on if you have a will in place. If you have a will, taxes on your inheritance are paid by the executor named in writing in your will. The executor normally needs to apply for probate before they can pay inheritance tax.

Many people do not have wills set up when they die. In this instance the administrator of your estate will be the one paying your taxes on inheritance. The administrator will need to get the correct letters of administration beforehand.

HMRC normally demands that heritage tax is paid off in the first 6 months after death. The inheritance tax bill in either situation will likely be paid using the funds from your estate.

When is the deadline for paying the inheritance tax?

HMRC generally require payment of tax on inheritance in the first 6 months after death. After this point, interest will begin to build up on the debt.

The exception is if some of the value of the estate is caught up in a property or business. Then you have the option to pay annual instalments for a maximum of 10 years. Whilst this exemption has its benefits, interest will be charged until the final payment is made.

How can I pay off the inheritance tax (IHT) bill?

If you are the executor of a will, you must pay the debts on behalf of the deceased.
You first need to value the assets of the deceased. You must then tell HMRC, or the 'taxman', what their estate value is.

Probate cannot be granted until the inheritance tax bill has been paid. This means that your loved ones assets cannot be shared out amongst family and friends until the inheritance tax is paid.

What is inheritance tax planning?

Unfortunately, if your estate is valued above the inheritance tax threshold, you cannot get out of paying your inheritance tax. However, there are things you can do before you die, to help reduce the likelihood of the thresholds being exceeded.

This is known as inheritance planning. Essentially, it helps you strategically manage your wealth to maximise the amount your beneficiary's gain.

Once someone has passed away, you might be able to minimise their tax liabilities to some extent. Reducing such losses will leave more for each beneficiary. Speak to an expert to see what your options might be.

Gifts are not subject to inheritance tax, unless they exceed the threshold limits. In the UK, you can give away gifts up to the value of £3000 each year. Individuals that are given gifts with a value greater than £3000 might have to pay inheritance tax on the gift.

Do I pay inheritance tax on gifts?

What is a 'gift'?

A gift is something with a tangible value. Cash, possessions, and even property can all be considered gifts. A gift is also anything that experiences a loss in value when it is transferred to a new owner.

What is the inheritance tax on gifts?

Gifts are not subject to inheritance tax, unless they exceed the threshold limits. In the UK, you can give away gifts up to the value of £3000 each year. Individuals that are given gifts with a value greater than £3000 might have to pay inheritance tax on the gift.

You should also consider the impact of Capital Gains Tax (CGT). Even if you have gift exemption, if your gift has risen in value since you bought it, you might have tax to pay.

Gifting to charities and your spouse or civil partner are potentially exempt transfers when it comes to CGT.

What is the residence nil rate band?

The residence nil rate is an additional allowance for those whose estate is above the threshold but are giving their home to direct descendants.

Residence allowance gives you an additional amount of value your estate can reach before inheritance tax is due on it.

The exact allowance will change each tax year, for example it was £125,000 in the 2018/2019 tax year, £150,000 in 2019/2020, and £175,000 in 2020/2021.

Will foreign assets be included in inheritance tax?

This depends on where your main residence is. If your main home is in England and Wales then you have inheritance tax liability for foreign assets.

If your permanent home is abroad then foreign asset exemptions might apply. However, if your main home is abroad but you have been living in England and Wales for a substantial period of time you might be considered a 'domicile' for the purpose of IHT.

12 ways to avoid inheritance tax

1 – Be clear on the different allowances and rules

Often, people leave inheritance planning too late. On average over 30% of people do not start planning until they are 55, many waiting until retirement.

By understanding each allowance and how to reduce your assets you can maximise what you leave in your legacy. The sooner you do this, the more provisions you can put in place during the course of your lifetime.

If you have a complex estate it can be hard to understand how the different rates and reliefs apply to all your different assets. In such cases, a financial advisor can be of great benefit.

2 – Have a plan in place

Once you understand the different rules and regulations you should start estate planning. The benefit of this is huge, especially since the government has frozen the inheritance tax rate. Due to inflation, more people are losing out to IHT each year.

Planning can be a confusing process, and you want to make sure you get it right. This is why we recommend seeking guidance from an advisor. In fact, there are companies out there that do pretty much all the work for you.

An adviser will consider your individual circumstances and wishes, for example what you want to leave to family members. They can use this information and their experience to help make plans for your finances.

Inheritance tax planning can help reduce the value of your estate, so that you have less tax to pay. In some cases, it could even bring you below the iht-paying threshold. Then you won't have to pay any tax.

3 – Give a gift to your partner/spouse

If you are in a civil partnership you can gift assets to your partners. The total financial value of your gift will not be considered part of your estate.

However, if the gift is something that increases in value it might be subject to Capital Gains Tax. The process can also be complex for couples where the recipient wasn't born in the UK.

4 – Give gifts to other members of your family or friends

Every year you can give gifts up to the value of £3,000. You can gift to anyone: your children, grandchildren, spouses, and even friends.

Gifts given within the 7 year period before you die, however, might still be considered part of your estate. If you die in the first seven years after making the donation, it may not be tax free. The size of the tax relief given then is determined by the 'Taper relief' scale.

These terms do not apply to gifts given to a civil partner.

The other exemption is if you give a gift to old relatives such as grandparents for health and maintenance purposes. Then there is no limit on your tax free payout.

Other types of expenditure that are exempt from inheritance tax are those for weddings and education. Up until age 18, families can gift their child for education or training purposes. Parents can also gift children up to £5,000 tax free for their weddings.

5 – Give a gift to a charity of your choice

In terms of the size of a lump sum, you can choose to gift a charity anything you want. There are a number of benefits that result from doing this.

Firstly, if you do not have any heirs or a descendant to leave your estate income to a charitable investment can be a nice way to help out. Some people have specific charities that they want to offer support to, especially if they have personally benefited from the service.

Secondly, leaving a gift deed to a charity will is one method of reducing the IHT you pay. If you leave 10% or more of your assets to a charity then the IHT on your remaining estate in turn falls to 36%.

We recommend seeking tax advice from experts before signing any forms agreeing to gift to charity. The expert advisers can guide you through the process, giving answers to any questions. Their tips can help optimise your inheritance tax planning.

6 – Get a life insurance policy

Life insurance policies pay out to eligible parties either a regular income or a one off lump sum. Some examples are term insurance, family income benefit policies, and whole of life insurance. A solicitor will explain the difference to you.

Essentially, these policies are solutions because no inheritance tax is paid on the amount given by the bank, so long as the policy is written in trust.
The only variation to this is when the policyholder has asked for the transfer of shares to be delayed. In this case, tax may be demanded if the budget accrues interest.

To ensure protection of your assets, speak with the accountants that handle your lifetime mortgage. As part of tax planning, you can ask them to have your policy publication written in trust.

7 – Set up a trust

Putting parts of your estate into a trust can be a good way of getting your estate below the nil rate band. There are different types to consider, two being a gift trust and a loan trust.

Trusts allow you to give control of parts of your estate to trustees. Trustees are chosen people that act as a representative for the individual you leave things to in your trust. Trustees are then in charge of any matter or affairs regarding your trust.

If you wish to set up a trust, you should first speak with a financial adviser. Ensure you do your research to check your financial adviser is on the financial services register. This will protect you from risk.

8 -Business owner exemptions

If you have business owner status, or have shares of a business, this will be reflected in the value of your estate.

Business relief is either 50% or 100% on an estates business assets. You can pass on business assets whilst alive/during your business career, or by including it in the relevant section of your will.

The exact relief amount depends on the nature of the assets. There are a number of guides online that can help you figure out what exemptions you might be eligible for.

You should also take steps to seek professional advice.

9 – Wedding gifts

A wedding gift is a form of gift, but it is not considered in line with the other annual gifts you make. An extra £5,000 is available annually for wedding gifts to your children.

On top of this, you can make a gift of £2500 to grandchildren and £1000 to anyone else.

10 – Spend more

If you are in excess of the threshold of the nil rate band, why not benefit from your estate in your own lifetime? A financial advisor can help you make a plan so that you spend more, but do not run out of money.

11 – Give away agricultural land or buildings

Another form of inheritance tax planning is to take advantage of agricultural relief. This applies to agricultural property, such as a farm or short rotation woodland area.

The inheritance tax exemption received will be either 50% or 100%. You should speak with a financial adviser to discuss your specific case.

12 – Consider Equity Release Schemes

Equity release schemes are other actions that can help reduce inheritance tax. With lifetime mortgages and home reversion schemes you can keep living in your family home, release money, and reduce IHT.

Once you have released equity from your house you can gift the equity to your descendants. Provided this is done at least seven years before you die there will be no IHT to pay on it.

For initial advice about Estate Planning including Lasting Powers of Attorney, Wills, Trusts and Probate; call our team on 0203 488 7503, 01992 236 110 or contact us by email at welcome@walshwestcca.com or via our website www.walshwestcca.com.