

Inheritance Tax was introduced on 18th March 1986 and replaced Capital Transfer tax. This tax applies to nearly all transfers of capital made at or within 7 years of death and is calculated on a cumulating basis. The current rate of Inheritance Tax is 40%.

## Nil Rate Band

Currently the Nil-Rate Band for Inheritance Tax is set at £325,000. Any part of the estate in excess of this after death will be charged to tax at a rate of 40%. Each individual has their own Nil-Rate Band allowance.

Nil-Rate Band planning is a method whereby upon the first death, that partner leaves to trust the value of their estate up to the Nil-Rate Band. However, the need to do this has been greatly diminished by the ability to transfer the unused Nil-Rate Band to the surviving spouse.

Nil-Rate Band planning still has a place in financial planning where monies are to be left to a child from a former relationship for example.

Transfer of the unused Nil-Rate Band is done on a pro-rata basis. For example, if a husband placed £162,500 in trust during the tax year 2023/24 after all other reliefs had been used he would be deemed to have used 50% of his nil-rate band.

## Residence Nil Rate Band

The Residence Nil-Rate Band (RNRB) is an additional allowance for Inheritance Tax for deaths occurring after 6 April 2017.

In order to qualify, you must own a property or a share in a property that you have lived in at some stage, and that you leave to your direct descendants (including children, grandchildren or step-children). For estates over £2 million, the RNRB is reduced at the rate of £1 for every £2 over £2 million. In addition, it only applies on death and not on gifts or any other lifetime transfers.

The Residence Nil-Rate Band remains at £175,000 for 2023/24. These figures are per person, so a couple may benefit from double the allowance. The RNRB value is limited to the lower of the value of the property left to direct descendants or the total RNRB available. The RNRB is applied to the estate first and then the Nil-Rate Band (currently £325,000) is applied. Both the Nil-Rate Band (NRB) and the RNRB will be frozen until 5 April 2026.



## Lifetime Gifts

Gifts made prior to but within 7 years of death are brought into the charge at a tapered rate. Such gifts are taxed on the value of the date of gift using the death rate scale applicable to the date of death.

## Tapering Scale

Years between gift and death	% of full charge at death
0-3	100%
3-4	80%
4-5	60%
5-6	40%
6-7	20%

For the purposes of calculating liability to Inheritance Tax certain business and agricultural assets are deemed to be less than their actual value.

Any gift made, whether into trust or directly to a person, should be unconditional. This means that you should derive no benefit from the gift, otherwise it would be considered for Inheritance Tax purposes to be a "Gift With Reservation" (GWR) and it will fall back into your estate for the purposes of calculating the tax.

There are other ways of mitigating Inheritance Tax:

- Spend all your money before you die
- Give away your capital using the exemptions where possible. (see below)
- Gift money directly into trust although normally you cannot have access to capital

## Exemptions:

### Wedding/Civil Partnership Ceremony Gifts

Wedding or civil partnership ceremony gifts (to either of the couple) are exempt from Inheritance Tax up to certain amounts:

- Parents can each give £5,000
- Grandparents and other relatives can each give £2,500
- Anyone else can give £1,000

You have to make the gift on or shortly before the date of the wedding or civil partnership ceremony. If the wedding is called off and you still make the gift, this exemption will not apply.

### Small Gifts

You can make small gifts up to the value of £250, to as many people as you like in any one tax year (6th April to the following 5th April) without them being liable for Inheritance Tax. This is known as your small gifts exemption.

However, you cannot give a larger sum, £500 for example, and claim exemption for the first £250, and you cannot use this exemption with any other exemption when gifting to the same person. In other words, as an example, you can't combine a "small gifts exemption" and a "wedding/civil partnerships exemption" and give one of your children £5,250 when they get married or form a civil partnership.

### Annual Gift Allowance

You can give away £3,000 in each tax year (your annual allowance) without paying Inheritance Tax. You can carry forward all or any part of the £3,000 exemption you do not use to the next year but no further.

This means you could give away up to £6,000 in any one year if you had not used any of your exemption from the year before.

You cannot use your annual exemption and your small gifts exemption together to give someone £3,250 but you can use your annual exemption with any other exemption such as the wedding/civil partnership ceremony gift exemption.

So, if one of your children marries or forms a civil partnership you can give them £5,000 under the wedding/civil partnership exemption and £3,000 under the annual exemption – a total of £8,000.

We would recommend that any gifts are documented so that an audit trail is established.



## Gifts paid out of your normal expenditure

Any gifts you make out of your net income (but not your capital) are exempt from Inheritance Tax if they are part of your regular expenditure. This includes:

- Monthly or other regular payments to someone, including gifts for Christmas, birthdays or wedding/civil partnership anniversaries
- Regular premiums on a life insurance policy (for you or someone else)

It is a good idea to keep a record of your net income and normal expenditure including gifts you make regularly. This will show that the gifts are regular and that you have enough income to cover them and your usual day-to-day expenditure without having to draw on your capital.

## Maintenance Gifts

You can also make Inheritance Tax free maintenance payments to:

- Your husband or wife
- Your ex-spouse or former civil partner
- Relatives who are dependant on you because of age or infirmity
- Your children (including adopted children and step-children) who are under 18 or in full-time education.

## Potentially Exempt Transfers (PETs)

If you, as an individual, make a gift in any of the situations described below and it is not covered by one of the exemptions already described, it is known as a “Potentially Exempt Transfer” (PET). A PET is only free of Inheritance Tax 7 years after you make the gift.

Gifts that count as a PET are gifts that you, as an individual, make to:

- Another individual
- A trust for someone who is disabled
- A bereaved minor’s trust where, as the beneficiary of and Interest in Possession (IIP) trust (with an immediate entitlement following the death of the person who set up the trust), you decide to give up the right to receive anything from that trust or the right comes to an end for any other reason during your lifetime – see example below

## Example:

A wife is the beneficiary of assets in an IIP trust under her husband's will and the minor child a beneficiary of income, but the wife decides to give up any interest in the assets and these also become held in trust for the bereaved minor child.

Changes introduced by the Finance Act 2006 mean that lifetime transfers into other types of trust since 22nd March 2006 no longer count as PETs.

## Only "outright gifts" count as PETs

If you make a gift with strings attached (technically known as a "gift with reservation of benefit"), it will still count as part of your estate no matter how long you live after making it.

For example, if you give your house to your children and carry on living there without paying them a full commercial rent, the value of your house will still be liable for Inheritance Tax.

In some circumstances, a gift with strings attached might give rise to an Income Tax charge on the donor based on the value of the benefit they retain. In this case, the donor can choose whether to pay the Income Tax or have the gift treated as a gift with reservation.

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