

Today, concerns over Inheritance Tax are shared by more and more people. No longer are issues of Inheritance Tax and Estate Planning concerns of the extremely wealthy.

Indeed, many people who view themselves simply as "comfortably well off", or "of reasonable means" may need to think seriously about the implications of Inheritance Tax when making their Will.

Although it is illegal to evade paying Inheritance Tax, it is perfectly acceptable and indeed responsible to reduce your Inheritance Tax payments that your Estate might need to pay.

Everyone is allowed to leave up to the stipulated threshold. This amount changes frequently and the current rate for 2009 – 2010 is £325,000 without any inheritance tax becoming applicable, this is known as and 'nil rate band'. After this amount tax is levied at 40%. You can keep up to date in relation to the relevant threshold on the Inland Revenue website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

Since October 2007 a new concept was introduced the 'transferable nil rate', which allows spouses and registered civil partners the ability to utilise their partners nil rate band, should this not have already been used upon the death of the first spouse / civil partner. Essentially, this means the surviving spouse / civil partner is able to leave an estate up to a value of £650,000 (using 2009 – 2010 figures) without any inheritance tax liability.

### **What the law allows:**

#### **Individuals**

The law allows you to leave an Estate worth up to £325,000 without having to pay any tax upon it. This £325,000 is called the 'Nil Rate Band'. After the first £325,000, or the Nil Rate Band, your Estate will be charged 40% Inheritance Tax for everything else.

Thus, should you leave an Estate worth £500,000 you would be allowed the first £325,000, without having to pay any Inheritance Tax, and then you would be charged 40% on the remaining £175,000. A total of £70,000 Inheritance Tax.

However, there are several exceptions to Inheritance Tax which can and should be considered if your Estate is worth more than £325,000. These amounts can be taken out of the Inheritance Tax calculation before the tax man looks at your Nil Rate Band.

Gifts up to £3,000 per tax year. If this allowance is not used up in any one year, the unused portion can be carried forward to the next tax year, but not to subsequent years. Thus, in the first year, a gift of up to £6,000 can be made.

Wedding Gifts; parents can give up to £5,000 to a child as a wedding gift, each grandparent can give £2,500 and all other persons can give £1,000.

Gifts up to £250 per person per year. This can be used for as many persons as you wish. Therefore, it would be quite legitimate, theoretically, to portion your whole estate up into £250 portions if you were to know so many people.

All assets given, or left, to a spouse are exempt, unless the spouse is foreign domiciled.

All gifts to registered charities are exempt.

Additionally, Inheritance Tax can also be claimed on gifts that a person has made during the last seven years of their lifetime. The following sliding scale applies to gifts made in the seven years before death, this is the example given on the Inland Revenue website for 2009 – 2010:

Years between transfer and death & Taper relief % Proportion of tax payable

3 to 4	20	80
4 to 5	40	60
5 to 6	60	40
6 to 7	80	20

#### Example

Henry made a gift of £300,000 on 1 February 2002. He died on 20 June 2005.

The inheritance tax threshold at the date of death was £275,000.

The gift exceeds the threshold by £25,000

Full rate of tax on the gift:  $40\% \times £25,000 = £10,000$

The gift is within 3 to 4 years of the death, so taper relief at 20% is due.

Taper relief:  $£10,000 \times 20\% = £2,000$

Revised tax charge:  $£10,000 - £2,000 = £8,000$ .

#### Married Couples and Civil Partnerships

Traditionally, if you were a married couple, or in a civil partnership one of the simplest and most effective ways of avoiding some Inheritance Tax, was simply to take advantage of two Nil Rate Bands, upon the death of each partner as follows:

If Mr. & Mrs. Smith have a joint Estate worth £800,000, upon the death of the first spouse /partner they give away to their beneficiaries £325,000 without having to pay Inheritance Tax, thereby utilizing a Nil Rate Band. Then upon the death of the second partner they also gave away £325,00 without paying tax, so that the remaining £100,000 was taxable leaving a liability of £40,000.

Prior to October 2007, if a couple had not approached the inheritance tax as outlined above and failed to use both nil rate bands, then they could end up paying much more tax as in the following example, Mr. & Mrs. Smith have £800,000. Upon the death of first spouse, all the money is left to the remaining spouse without using the Nil Rate Band. Upon the death of the remaining spouse, only the one Nil Rate Band of £325,000 was be allowed, leaving an Estate of £475,000 liable to Inheritance Tax at 40%, resulting in an Inheritance Tax of £190,000.

However, due to the changes in October 2007, married couples and those in a civil partnership are allowed to take advantage of both nil rate bands without the need to leave money upon the death of the first spouse/partner.

The new rules allow a surviving spouse/partner to use any nil rate band that their spouse, or partner did not use against their inheritance tax estate in addition to their own.

The new rules also apply retrospectively, so that any unused nil rate bands on deaths before the 9<sup>th</sup> October 2007, can be added to the nil rate bands of surviving spouses/ partners.

For example:

Mr Smith died in January 2005 having made no chargeable transfers. He left his entire estate to Mrs Smith. Mrs Jones dies in April 2008 and can set £650,000 of nil rate bands against her inheritance tax estate.

There are other ways to avoid some Inheritance Tax which are not as effective. The individual will have to carefully think about how they wish to implement some of the other exceptions mentioned above when making their Will.

Another simple example could be a grandparent making use of the £250 exception. They may have four children, who each have two children. If he or she wished to avoid some Inheritance Tax, they could make direct gifts to the grandchildren up to the £250 limit mentioned above, rather than giving the money to the parents. They would still be able to request that the money was kept in trust for the grandchildren by the parent, but they would thus be able to pass £2,000 to the grandchildren, without having to pay Inheritance Tax upon it.

All that you need to do is understand what exceptions are available, and make it clear in your Will that these gifts are to be given before Inheritance Tax is considered.

If you are an individual and believe your estate is worth up to about £325,000, or a married couple/civil partnership and believe the joint estate to be worth up to £650,00, we would recommend implementing one of our standard Wills, bearing in mind the information in this Help sheet.

However, if you believe your estate to be worth in excess of £325,000 for individuals or £650,000 for married couples/civil partners, please indicate this on your form, and we can pass on your details to our associates who specialise in Estate Planning and the Reduction of Taxes, for large Estates through Trusts.

## Contact Us

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