

Inheritance Tax Planning – Prevention better than cure!

Planning to mitigate the IHT bill that your estate might have to pay on your death is a complex procedure requiring expert independent help. IHT is not a tax that everyone need pay and, by taking sensible steps, you need not share your assets with the Inland Revenue.

Have you left your heirs or beneficiaries with the headache of having to sell off assets to pay your tax bill?

| | Estate A | Estate B | Estate C | Estate D |
|--|----------|----------|------------|------------|
| Estate Value | £500,000 | £750,000 | £1,000,000 | £2,000,000 |
| First £250,000 taxed at 'nil rate' | £250,000 | £250,000 | £250,000 | £250,000 |
| Amount of estate liable to IHT | £250,000 | £500,000 | £750,000 | £1,750,000 |
| Tax bill (IHT) payable at a flat rate of 40% | £100,000 | £200,000 | £300,000 | £700,000 |

A widespread lack of understanding of the tax rules means that many of us could end up in the future leaving more to the taxman than to our family or to good causes. Inheritance tax (IHT) payments to the Inland Revenue coffers are likely to increase in the years ahead, due partly to increasing house prices. So how can you plan for eventuality? Follow our guide;

Who will pay your tax bill?

Keeping it simple, there is no IHT to pay on the first £250,000 (the 'nil' - rate band) you leave, but assets over this level are currently taxed at 40 per cent unless they pass to your surviving spouse. The table shows various sizes of estate and the tax bills they could generate.

If you have currently made no IHT provision, and you are single, a widow or a widower, these could be the bills your beneficiaries will have to face on your death. Fortunately there are ways to keep the Inland Revenue's slice of your assets to a minimum or, with careful planning, to nothing at all.

Prevention is better than cure

If you think that you could have a potential IHT liability, the first step is to talk to us - you are probably far wealthier than you imagine. Remember, an estate worth just £500,000, which could include your family home, a second property, life assurance

policies not written in trust and other investments you hold, could generate an IHT bill of £100,000.

Here are some of the ways in which we can help you plan for IHT.

Making a will. Proper wills are the cornerstone of inheritance tax planning, yet far too many people die without having made one. If you don't have a will, you cannot guarantee how your assets will be distributed on your death.

Arranging a will trust. This allows married couples to arrange in their wills that, on the death of the first spouse, the trustees can advance or lend up to the £250,000 nil-rate portion to the surviving spouse. This enables the surviving spouse to inherit all the deceased spouse's assets but have access to the assets in the trust via the trustees. On the second death any loan must be repaid to the trust and any outstanding loan normally is deductible from the value of the estate before IHT is calculated. The remaining assets then pass to the children net of the loan, giving a tax saving of up to £100,000, assuming the loan has been spent.

Distributing your assets. No tax is due when assets are passed between a UK domiciled husband and wife, whatever the size of the estate. Unfortunately, as the sole owner of all the assets, a surviving spouse will almost certainly trigger a bigger IHT liability on his or her death. One solution is for a husband or wife to leave a slice of assets to others, including their children, as well as to their spouse. Assets could be left in a discretionary trust, written into your will. Your spouse can be a beneficiary of this as well as your children, and you can request that the trustees pay her income - and even capital - out of the trust as required.

Using insurance policies. The Inland Revenue won't always wait long for settlement of a tax bill, which can be far more than many people have in liquid assets. You could solve this problem for your heirs through insurance policies that pay out on death. These should be written in trust, so that the proceeds do not form part of your estate and trigger an even bigger tax bill.

Reducing the value of your estate. If you reduce the value of your estate while you are alive, less inheritance tax will ultimately be due. For example, up to £3,000 a year can be given away in lifetime gifts, with no tax due at the time or on death. Parents can give up to £5,000 each on a child's marriage. And transfers out of income that do not affect the donor's normal standard of living can also be tax-free. Any number of small gifts of up to £250 per person per year can be made with no IHT liability.

Making lifetime gifts. If you potentially face a large inheritance tax bill, you can give assets to a relative or other party with no immediate tax liability. Known as potentially exempt transfers (PETs), these gifts are subject to a relatively complex seven-year rule. Say you give away assets worth £40,000. If you live for another seven years, that £40,000 will not be taken into account when your estate is valued for IHT purposes. If you die within seven years, a sliding scale of tax is due if the PET causes you to exceed your allowable nil-rate band.

What about your business? Different rules apply to business assets, which could reduce the amount of tax that your heirs may have to pay. Reliefs can reduce the value of a business asset by up to 100 per cent before a person's chargeable estate is calculated. If you require more information please contact us.

Moving assets. A deed of variation (deed of family arrangement) could be used if you are faced with a big inheritance tax bill after the death of a spouse. This is particularly useful if the way in which assets have been distributed means that the spouse inherits all of the assets. Within two years of death, the surviving spouse can apply to re-allocate some of her share of the assets in a more favourable way. This way up to £250,000 of assets can be re-directed to say, the children to use the nil-rate band of the first spouse to die.