CLARENCE TRUSTEES

WILLS, TRUSTS, & PROBATE

7 Great Ways to Minimise IHT

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7 GREAT WAYS TO MINIMISE IHT

With the Inheritance Tax (IHT) Nil Rate Band (NRB) at £325,000 per person and the new Main Residence Nil Rate Band (MRNRB) starting at £100,000 in 2017/18 and rising to £175,000 in 2020/21, a married couple will be able to have a joint estate of £1m without paying any IHT – so long as they make the best use of all their exemptions and allowances.

Therefore, the first six points in this guide relate to making best use of exemptions and allowances up to £1m and the final idea relates to saving IHT for estates in excess of £1m.

So here are the first six of our seven great ways to minimise IHT . . .

1. YOUR WILL & YOUR SPOUSE

A vital element of effective estate planning is to make a will. Unfortunately 60 per cent of adults with children under 18 fail to do so.

Making a will ensures your assets are distributed in accordance with your wishes.

This is particularly important if you have a spouse or civil partner because there is no IHT payable between spouses and civil partners - but there could be IHT payable if you die intestate (i.e. without a will) and assets end up going to other relatives.

With a correctly drafted will you can ensure that, on first death, the assets of the estate pass to the surviving spouse or civil partner (which at that point will be free of IHT) and ensure that the full available NRB and MRNRB will be transferred to the survivor.

To find out more about why you should have a correctly drafted will, please refer to our separate guide entitled "Why Do I Need a Will?".

2. MAKE ALLOWABLE GIFTS

You can give cash or gifts worth up to £3,000 in total each tax year and these will be exempt from IHT when you die. Please note this is one lot of £3,000 per annum, not £3,000 per annum per recipient.

You can carry forward any unused part of the £3,000 exemption to the following year but then you must use it or lose it.

When a child gets married, parents can give cash or gifts worth up to £5,000, grandparents can give cash or gifts up to £2,500, and anyone else up to £1,000.

Small gifts of up to £250 a year can also be made to as many people as you like.

3. LEAVE SOMETHING TO CHARITY

Anything you leave to charity is free of IHT, so it can be a useful way of reducing your IHT bill, while benefiting a good cause.

If you leave at least 10% of your estate to charity, it will cut the rate at which IHT is due on the rest. The rate at which IHT will be calculated will be 36% rather than 40%. This rate is applied to the balance of the estate to the extent that it exceeds the available NRB.

This may not be a huge saving, but it can mean that family and friends will receive more than they would do otherwise – while your favourite charities also benefit.

A Word of Caution:

Charities can sometimes be very aggressive in pursuing the executors of an estate for their share of the estate and, if the will is not properly drafted, such bequests to charities can sometimes leave the family beneficiaries worse off than the testator intended.

4. USING TRUSTS

If you put some of your assets into a trust (from which you, your spouse and your children under 18 years do NOT have an absolute right to benefit), such assets are no longer part of your estate for IHT purposes.

You can set up a trust right away or you can establish one in your will. There may be Capital Gains Tax consequences if you transfer certain assets into a trust in your lifetime, but there will be no liability to Capital Gains Tax if you establish a trust in your will.

Keep in mind that some types of trusts are subject to their own tax regimes and if the wrong type of trust is used it might have to pay IHT itself.

Also, trustees are likely to be liable for Income Tax at a rate of 45% on the trust income and Capital Gains tax at 28% on any capital gains in the trust.

The rules around trusts are complicated so you must take advice from an expert, such as Clarence Trustees.

Trusts can be used:

- *To provide for vulnerable/disabled beneficiaries (Disabled Persons Trust)*
- *To "skip" a generation when passing assets (Spousal Bypass Trust)*
- *To simulate (for unmarried couples) the transfer of the NRB that is possible for married couples*

To read about some of the trusts that can be used for IHT planning, please refer to our separate guide entitled "Trusts (an Introduction)".

5. INCOME OVER EXPENDITURE

As well as putting lump sums into a trust you can also make monthly contributions into certain savings or insurance policies (not ISAs) and put them in trust.

The monthly contributions are potentially subject to IHT - but if you can prove that these payments are not compromising your standard of living (i.e. that you can afford the payments out of income and not out of capital) then they are exempt.

Likewise, any gifts of cash you make out of income are also exempt.

6. LIFE INSURANCE

If you are not in a position to take avoiding action, an alternative approach is to make provision for paying IHT when it is due.

IHT must be paid within six months of death (otherwise interest will be charged by HMRC). The difficulty is that probate will not be granted until the IHT has been paid. Until probate has been granted, no money can be released from the estate to the executor.

This means the executor – usually a son or daughter – will often have to borrow money or use their own funds to pay the IHT bill!

This is where life assurance policies written in trust can be very useful.

A life assurance policy can be taken out on both a husband's life and a wife's life with the policy paying out only on the second death.

The amount of cover should be equal to the expected IHT liability.

If the policy is put in trust it means that it does not form part of the estate.

The proceeds can then be used to pay any IHT bill straightaway without the need for the executors to borrow.

But better than that, the premiums for such a policy will be paid by the individuals whose lives are being insured – which reduces the value of their estate and means the IHT liability is reduced too!

Premiums for this type of life insurance are not expensive. For example, at the time of writing (Feb 2017) the monthly contribution required for a sum assured of £120,000 on a middle aged husband and wife is around £70. The premiums are usually guaranteed - so if the policy lasts for 50 years, £42,000 will have been paid in premiums for a guaranteed tax free pay out of £120,000.

If you need advice on this type of life insurance, Clarence Trustees is part of the Antony J. Holdsworth & Co group of businesses and our Independent Financial Advice arm (Alexa Financial) will work hand in hand with us to provide whatever advice you require.

If your joint estate with your spouse or civil partner is up to £1m then the above will enable you to plan your estate so that no IHT becomes payable. However, if your joint estate is in excess of £1m then you may need to consider something extra . . . .

7. FAMILY INVESTMENT VEHICLE

For estates over £1m with substantial investments, a Family Investment Vehicle (FIV) may well be appropriate – but in addition to (not instead of) the preceding ideas.

An FIV is either a limited company or a limited liability partnership (LLP) combined (in some cases) with a family trust to provide a tax efficient vehicle in which to make long term investments where the assets can grow and/or earn income in a lower tax environment.

FIVs (if structured correctly) also enable significant amounts of IHT to be saved.

These structures are usually created to protect "family wealth" and allow such wealth to be used to provide long term benefits to children and grandchildren.

Control can be retained by the individual(s) over the family wealth until they pass away – at which point the next generation can take control.

If your estate is of this magnitude, please contact Clarence Trustees for advice on a FIV.

8. HOW WE CAN HELP

Clarence Trustees can provide a complete estate planning service.

We can:

- Draft your will to ensure you make use of all your available exemptions and allowances
- Advise on and implement any trusts that may be necessary
- Assist with the protection of your assets; and
- Provide extended IHT planning (such as FIVs) for higher value estates.

Please contact us now to plan your estate and protect your wealth.

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