

Changes to Inheritance Tax

Transferable Nil-Rate Band

The big change to Inheritance Tax this year has been the introduction of the “transferable Nil-Rate Band”. It affects spouses and registered civil partners wishing to leave assets to the survivor on the death of the first.

It used to be best practice on the first death to leave the Inheritance Tax allowance (the Nil-Rate Band) to a Discretionary Trust – a trust for the benefit of the whole family but of which the survivor was treated as the principal beneficiary - or to those who were to benefit on the death of the survivor, typically the children. This ensured that the Nil-Rate Band of the first to die was used and not wasted.

Use now, or use later

It is now possible for a couple to use both Nil-Rate Bands on the death of the survivor even where the first spouse has already died. Instead of Wills containing discretionary trusts of the Nil-Rate Band, the much simpler “all to each other and then equally between the children” is now just as effective Inheritance Tax planning.

Existing arrangements where one spouse has already died

The change will not affect Nil-Rate Band Will provisions which have already been put into effect following the first death. Existing Discretionary Trusts are still effective to avoid Inheritance Tax on the death of the

survivor and they should be left undisturbed. Outright gifts of the Nil-Rate Band will have used up the Nil-Rate Band of the first to die. In both cases the survivor will have just one Nil-Rate Band to use on his or her death, and the assets put into trust or given outright on the first death will not be taxable on the death of the survivor.

Is it necessary to change your Will?

Provided your Will has been properly drafted it will not be necessary to change it. The trust it contains should include a power to distribute capital at any time, and the trustees could use this to distribute the trust assets to the surviving spouse. Provided this is done within two years of the first death, both Nil-Rate Bands will be available to use on the death of the survivor.

Many clients will be happy to leave their Wills unchanged until they next review them – we generally recommend a review every 5 to 10 years. But for those who would like to make the change now, it is a relatively simple and inexpensive exercise.

In Summary

This is a good simplifying measure, which will make Will and estate planning much more straightforward. There will still be instances where a Nil-Rate Band discretionary trust is useful to include in a Will, but it is now unlikely to be for tax reasons.

Example

Mr & Mrs PG’s estates comprise a house worth £800,000 which they hold as joint tenants and chattels, cash and stocks and shares of £500,000, £200,000 in Mr PG’s name and £300,000 is Mrs PG’s name.

Mr PG dies in July 2007 leaving his entire estate to Mrs PG. Mrs PG dies in July 2008.

IHT on Mr PG’s death

Assets: Half share of house	£400,000
Other assets	£200,000
Taxable Estate	£600,000
Spouse exemption:	(£600,000)
Subject to IHT	Nil
IHT on Mr PG’s death	Nil

IHT on Mrs PG’s death

Assets: Full value of house	£800,000
Other assets	£500,000
Taxable Estate	£1,300,000
Mrs PG’s Nil-Rate Band	(£312,000)
Mr PG’s unused NRB	(£312,000)
Subject to IHT	£676,000
IHT on Mrs PG’s death	£270,400

If you have any questions about these changes, please get in contact with us.

A reminder about existing A&M Trusts

With effect from 5th April all existing Accumulation & Maintenance trusts (most commonly grandchildren settlements) will enter a different tax regime: they will be taxed on an ongoing basis at the rate of up to 6% every ten years.

Prior to that date, and provided the trust deed allows, the terms of the trust can be changed so as to minimise the effect of this new regime. If you have trusts which have not been reviewed, then it is important to review them now.



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