



Inheritance tax Wills for married couples

When is inheritance tax payable?

Your family pays inheritance tax (IHT) on the value of the assets you own when you die and on any gifts made in the previous seven years.

Either you or your family may also have to pay IHT on other lifetime gifts.

How much is IHT?

The basic rate of IHT on death and gifts in the previous seven years is 40%.

IHT on gifts more than three but less than seven years before death can be less than 40%.

There is 20% IHT on lifetime gifts to most trusts, where these exceed the available nil rate band which is currently £312,000.

Are there any reliefs?

Yes, the following are normally free of IHT:

- Most gifts more than seven years before you die.
- The first £312,000 (known as the nil-rate band or NRB) given away in the seven years before you die or which you leave on your death.
- Any assets transferred between husband and wife.
- All gifts to UK charities.
- Small lifetime gifts, for example the first £3,000 in each tax year.
- Regular lifetime gifts you make out of income.
- Some categories of business and agricultural property.

Has the nil rate band for married couples been increased?

- Despite recent press coverage, the amount of the NRB has not been increased. Instead the government have introduced the concept of a “transferable nil-rate band” between married couples. This will not apply to couples who simply live together or are divorced.

- For the “transferability” to apply, the couple must have been married on the death of the first of them to die. In some circumstances this will increase the nil-rate band to £624,000 if the NRB of the first to die is completely unused.
- There is a complicated calculation for working this out but it means that the amount of the NRB potentially available for transfer will be based on the proportion of the NRB that was unused when the first spouse died.

With the transferable nil-rate band do we still need to plan for IHT?

Yes - if your assets exceed £624,000 and you have other circumstances which may make this attractive.

What is a will with a nil rate band discretionary trust?

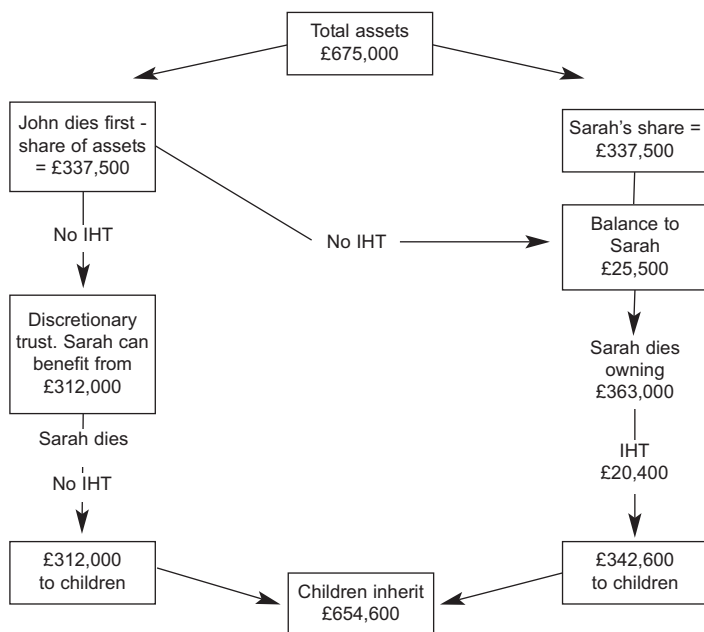
This is best explained by use of an example:

John and Sarah are married and own their own home (worth £400,000) a share portfolio (£225,000) and cash (£50,000).

By his will, John leaves the first £312,000 worth of his assets to a NRB discretionary trust, and any surplus to Sarah.

There is no IHT on John's death.

Sarah can benefit from the NRB trust during her lifetime but the £312,000 is free of IHT when Sarah dies. IHT on Sarah's estate is £20,400. (£363,000 worth of assets is taxed. The first £312,000 is free of tax and £51,000 is taxable at 40%).



I've heard that wills with nil rate band discretionary trusts no longer work. Is this true?

Before the introduction of the transferable NRB, the NRB of the first to die was often wasted. Many of our clients planned for this by including in their wills NRB discretionary trusts so as to make use of the NRB on the first death.

Because the NRB is now automatically transferable between spouses, this type of planning may no longer be appropriate for everyone.

However, there are good reasons why many couples will still want to include this arrangement in their wills. We have set out the advantages and disadvantages below to assist you in deciding whether you would like to consider this arrangement.

The advantages of making wills with a nil rate band discretionary trust

- If the first spouse to die has assets which are likely to qualify for business or agricultural property relief, then a will with a NRB trust offers significant planning opportunities. Having a discretionary trust which will capture, not only the NRB, but also business and agricultural property, may shelter a much more significant sum from inheritance tax on the second death.
- If the assets in the NRB discretionary trust grow and exceed the top of the NRB applicable on the second death. Although the Chancellor indicated the upper limit of the NRB might be increased in line with property prices, governments in need of tax revenues are not noted for sticking to their word.

Take the example of Nathan and Natasha:

Nathan died in 2002, having made no previous transfers and with an estate worth £250,000 (equal to the then NRB). The only asset in Nathan's estate was an investment portfolio.

Natasha then dies in 2009, also with no previous transfers, and with an estate (excluding Nathan's investment portfolio) of exactly £325,000 (equal to the then NRB). The investment portfolio is now worth £400,000.

If Nathan's estate had passed to Natasha outright, IHT on Natasha's death will be £30,000 (40% on £75,000 – the excess over £650,000 – the combined NRBs at that time).

If Nathan's investment portfolio had passed to a NRB discretionary trust under his will and the portfolio is distributed at Natasha's death then there would be only a small IHT 'exit' charge of £3,150, saving £26,850.

- The NRB trustees will have their own allowance for capital gains tax purposes (presently £4,800). This is in addition to the survivor's annual allowance, currently £9,600.
- The NRB discretionary trust offers a great deal of flexibility. The trustees can exercise their discretion and make distributions to children and grandchildren as well as the survivor. If income is paid to or for the benefit of younger children and grandchildren, this will generally attract lower rates of income tax on the distributions.
- If the surviving spouse remarries, the NRB trust can save further IHT while ensuring that the assets of the first spouse eventually pass to his or her children.
- The NRB trust should shelter the trust assets from any possibility of means-testing for the purposes of nursing home fees.
- This trust will also shelter assets from various unfortunate events such as bankruptcy and claims on the divorce of your children.
- Our wills are drafted so that if the NRB trust proves to be unattractive after the first death, then the trustees may make an absolute advance to the surviving spouse. The transferability of the NRB to the survivor is therefore preserved.

The disadvantages of having a will with a NRB discretionary trust

- It is more expensive to put these wills in place. There will also be set up and trust administration expenses following the first death. It is important that these matters are dealt with and proper advice sought, as otherwise the advantages of the NRB trust may not be achieved.

- The value of the assets in the NRB trust may not exceed the growth in the value of the NRB amount.
- A future government might increase the level of the NRB significantly.

The solution

Whether this arrangement will be suitable for you and your family will very much depend on your own circumstances. It is not possible in this leaflet to give advice that will apply to all scenarios. The law in this area is constantly changing and there is no substitute for well informed professional advice. Please do discuss your own aims and objectives with one of our lawyers.

Other methods of planning for IHT

- Always place any insurance on your life (including death benefits from pension plans) in trust for your family. A policy not in trust risks 40% IHT, when it will be worth only 60% of its value. The same policy, in a trust, may

be free of IHT and will certainly pay much less than 40%. Our leaflet *Inheritance tax - trusts of insurance and pension benefits* gives more details.

- Consider whether you can afford to give away assets during your lifetime. Can you afford to make small or regular gifts?
- Consider the use of a two year deed of variation for any assets you inherit. These can be put into trust in a way that allows you to benefit without the assets being treated as yours for IHT.

We will be pleased to advise you in more detail on other opportunities for saving IHT.

Are there any other complexities?

This guide can only provide a brief summary of some of the main features of IHT. As with other taxes, there are many complicated and detailed rules laid down by Parliament.

For further information, or to discuss your estate planning needs, please contact Barry Glazier, David Parkhouse, Richard Fairbairn, Jeremy Mills, Ann Corke, Michael Norton, Dorothy Burton, Emily Copping, Natalie Gamble, Paula Shea or Mahendree Naidoo of our Tax Trusts and Wills team who will be pleased to help you.