

Inheritance Tax



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Inheritance Tax

From April 2022 to March 2023, HM Revenue & Customs accumulated £7.1 billion in inheritance tax. This marks a £1 billion increase from the previous tax year.



Are your loved ones going to be faced with immensely high rates of tax after they inherit your assets?

The IHT threshold currently stands at £325,000. So, if the value of your estate is below this, inheritance tax will not apply; if your estate is above the nil rate band, you may be taxed at a rate of 40%.

IHT must be paid in full by your beneficiaries within six months from the date of death. This is only applicable if the assets are not difficult to sell, in this case, they could opt to pay the tax in instalments with interest.

At first glance, this may paint a rather large question mark over the future of your finances.

What is inheritance tax?

Inheritance tax, or IHT, is imposed upon assets transferred to a person from a deceased individual.

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Reducing your liability

There are several ways an individual can reduce their inheritance tax liabilities. One of the most common and accessible ways is through gifting your assets or parts of them. Not all gifts are applicable. Be aware of your options and whether they apply to your circumstances

Gifts

A gift is basically anything that has value. This can be:

- Money
- Personal goods, like jewellery
- A piece of land or property
- Stocks and shares
- The loss in value when transferring assets

Anyone receiving a gift from you within seven years of your death may be liable to inheritance tax if your cumulative gifts exceed £325,000.

John's Inheritance Tax

John wants to gift £8,000 to his daughter, Lucy, for her wedding.

£5,000 of this will be classified as a wedding gift to his child and he will use his £3,000 annual exemption allowance to give a tax-free total of £8,000 to Lucy.



Exemptions: When are gifts tax-free?

You may not have to pay inheritance tax if you give your assets away whilst you are still living.

Spouse or Civil Partner

Gifts are tax-free if they are given to someone who resides permanently in the UK and to whom you are legally married or in a civil partnership.

Annual Exemption

An individual is allowed to give away a total of £3,000 in gifts each year without them being factored into the value of their estate.

Any allowance not used is carried into the next year, but only for one year.

Small Gift Allowance

If you haven't used an alternative allowance already, you are permitted to gift up to £250 each year, free from inheritance tax.

Wedding or Civil Partnership Gifts

If a person is giving a gift at a wedding or civil partnership, this should be done on or before the ceremony takes place.

For the gift to be tax-free, you must only give:

- £5,000 to a child.
- £2,500 to a grandchild/great-grandchild.
- £1,000 to any other individual.

A person is allowed to give a wedding gift as well as another allowance (excluding the small gift allowance).

Reducing your liability

Family Maintenance and Living Costs

Regular payments to family members helping with their living costs count as gifts. To qualify as tax-free, these payments must be made to:

- A child who is under the age of eighteen or is in partaking in full-time education. This can include paying rent for them or paying into their savings account.
- An elderly, ill or disabled relative.
- A former civil partner or ex-spouse.

As long as you pay this from your income and it does not prevent you from meeting your own living costs, then there is no limitation on how much can be tax-free.

These gifts are classified as 'normal expenditures out of income'. This can be combined with other allowances (excluding the small gift allowance).

Taper relief rates over time

Below, we have included a table to show you how the rate of tax can reduce as the years between the gift and the date of death extend.

Length of time between the gift and death	Rate of tax
3 to 4 years	32%
4 to 5 years	24%
5 to 6 years	16%
6 to 7 years	8%
Over 7 years	0%

Gifts of reservation

Gifts of reservation refer to gifts that you still benefit from (e.g. continuing to live in a home you have given to your relative).

These are not tax-free and will be added to the value of your estate.

Benefits of gifts	Drawbacks of gifts
Reduced tax rate if the gift is given within a certain timeframe.	Many rules for various circumstances.

What is Taper Relief?

Taper relief often appears in the form of a percentage. It generally means that the more years that have passed since the gift was given, the less tax is owed.

Taper relief applies if the value of gifts made within the seven years is over the £325,000 threshold.

So, If an individual gives their assets away as gifts before their death, this can help to reduce the tax liabilities that their beneficiaries may have to pay.

As a general rule, if a person lives for seven years after they have given the gift, then no tax will be due. If the individual dies within these seven years, the date that the gift was given will dictate the amount of tax that must be paid.



Enjoy giving to
your family and
see the benefits in
your lifetime with
gifting

Trusts and inheritance tax

How is IHT charged on trusts?

Inheritance tax is charged on a person's estate (their money and possessions) upon their death. If the value of the estate exceeds the threshold set by the government, which is currently £325,000, then inheritance tax at a rate of 40% is charged on anything above that threshold.

Charity donation deduction

A reduced rate of 36% applies if the person's will leaves more than 10% of their estate to charity. It's important to note that inheritance tax can also apply while you're still alive if you transfer some of your estate into a trust.

When Inheritance Tax is due

Inheritance Tax is due on trusts in the following scenarios:

- When assets are transferred into a trust
- When a trust reaches its 10-year anniversary (there are 10-yearly Inheritance Tax charges)
- When assets are transferred out of a trust (known as "exit charges") or the trust ends
- When someone dies and a trust is involved in sorting out your estate

What are trusts for?

There are multiple reasons why a person may set up a trust:

- To pass on assets after death.
- To pass on assets during their lifetime.
- They are too young to handle their affairs.
- To control family assets.
- These are not tax-free and will be added to the value of your estate.

Getting advice

Depending on the type of trust and how it has been setup, there are many nuances to how inheritance tax might affect it.

To understand how a trust would affect your inheritance tax liability, we recommend getting in touch for an IHT review. A financial adviser will be able to give a more comprehensive answer than this guide would be able to achieve.



Using life insurance

Life insurance

You can use life insurance to pay your inheritance tax bill.

This policy will be taken out on your life to provide a payment to your beneficiaries in the event of your death, with the level of cover dictating the amount of money that will be paid out.

We understand that inheritance tax can be burdensome for beneficiaries, especially if they need to sell assets or take out loans to pay this tax.

Life insurance allows individuals to pay off inheritance tax, whether the insurance is paid out in regular instalments or one lump sum.

There are two main types of life insurance: term life insurance and whole life insurance.

Term life insurance policies

This kind of policy will run for a period of time which you have agreed upon. The payment will only go forward if you die during this set timeframe.

Currently, there are three types of term life policies:

1. Increasing: To stay in alignment with inflation, the level of cover will rise as the policy continues.
2. Decreasing: The level of cover is designed to reduce each year, generally for the purpose of mortgage repayments.
3. Level: This is considered to be the most affordable option, with the level of cover remaining the same throughout. The payment will be a lump sum if the individual dies within the term specified.

This option is affordable and has a relatively straightforward structure. However, the cover is temporary and the policy doesn't build cash value

Whole life insurance policies

If an individual makes consistent payments, the policy will pay out whenever they die.

This can be beneficial when planning around inheritance tax, as the lump sum can be used to pay this off.

Despite this, the policy does have its drawbacks. There is the possibility that someone could ultimately end up paying more than their beneficiaries will get out if they live longer than expected.

Will inheritance tax affect my life insurance?

Your life insurance may be subject to inheritance tax.

The amount it pays out will be part of your estate when you are no longer living. If your estate's value exceeds the £325,000 threshold, it will be subject to inheritance tax.

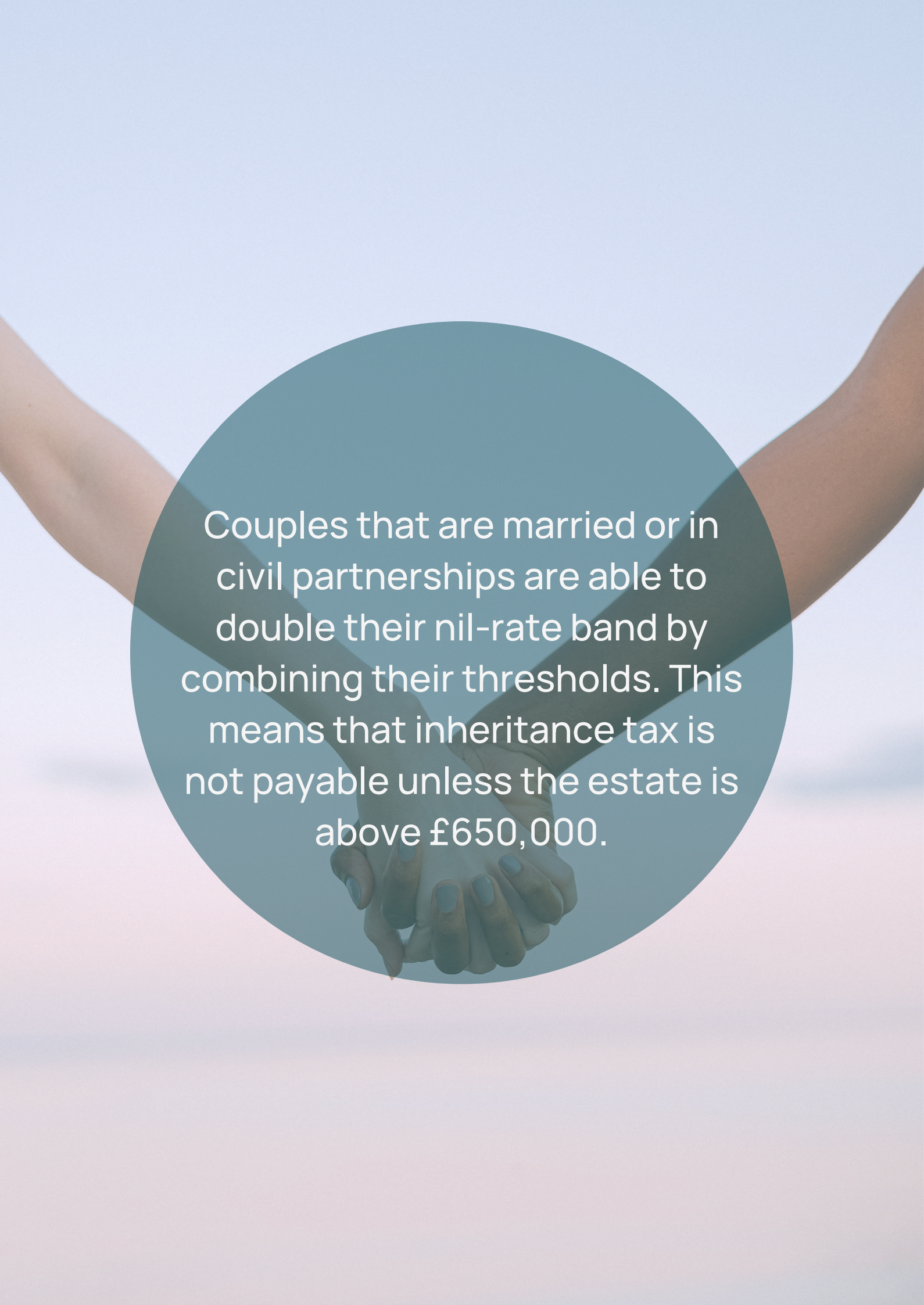
Can it be avoided?

Fortunately, there is a way for you to avoid inheritance tax on your life insurance policy.

One strategy you can use is to set up your life insurance policy in a trust.

The payment would be separate from your estate, so it would not increase its value.

This will place your beneficiaries' interests at the forefront of your financial plans, ensuring that they receive the maximum benefit from your insurance policy.

A background image showing a couple's arms and hands holding each other over a beach. The hands are clasped together, with one hand having blue nail polish. The background is a soft-focus view of a beach with sand and water under a clear sky. A large, semi-transparent teal circle is centered over the hands, containing the text.

Couples that are married or in civil partnerships are able to double their nil-rate band by combining their thresholds. This means that inheritance tax is not payable unless the estate is above £650,000.

Equity release

What is equity release?

Equity release allows homeowners access to the value of their property without having to put it up for sale, providing them with tax-free cash to gift or spend as they wish.

You can use equity release as an estate strategy to reduce your inheritance tax liabilities.

This is because the calculation of IHT is based on your assets. Equity release will need repaying so this cash is not considered to be a part of your estate, reducing your inheritance tax.

A lifetime mortgage and a home reversion are the main two options for an equity release.

How it works

With equity release, debts are repaid before anyone receives the assets as inheritance. A solicitor would pay the debts as a part of the probate and the remaining assets would be given as an inheritance.

Lifetime mortgage

This allows an individual to take out a mortgage if the property is their main residence.

They will still retain ownership over the property and may have an opportunity to allocate funds for particular purposes, such as inheritance.

There are two choices when it comes to the repayment of the loan. Either, repayments are made or the interest is left to build.

The loan repayments will commence upon the sale of the property, typically when an individual dies or is placed in long-term care.

Home Reversion

An individual can sell a portion of their home in exchange for a lump sum. They can keep on living in the property but the provider of the equity release will own a share of it, meaning they will receive a payment if the property is sold.

Benefits of An Equity Release

- It can be a useful estate strategy if a person has valuable properties and limited liquid assets.
- Gives access to the wealth retained in property which can supplement retirement income or be left as an inheritance.
- Equity release plans provide tax-free cash to spend outside of a person's estate, reducing their IHT liabilities.
- Provides an option for someone who doesn't want to or cannot downsize.

Drawbacks of An Equity Release

- A home reversion scheme may not pay the property's full market value.
- It can reduce inheritance funds if the debts need to be repaid.

Using pensions to pass on wealth

Pensions

Feel like you don't know enough about your pensions? Don't worry; you're not the only one.

In 2022 The National Centre For Social Research concluded from their 2020/21 planning and preparing for later life survey that nearly one in four adults aged 40-75 years old didn't have a private pension and 16% had not begun to save for their retirement.

A lack of financial planning could leave you with numerous obstacles to face as you approach retirement. Pensions are one of the best ways to invest your savings for the future.

The type of scheme, annuities you set up, and age you die usually dictates how your pension savings are passed on.

Annuities

You can purchase annuities, and they will provide you with guaranteed income in retirement, whether for life or an agreed number of years.

Using a pension to minimise IHT

Currently, your pension pot is generally exempt from inheritance tax. This is because it is not considered part of your taxable estate, meaning it passes outside of your will.

To choose who inherits your pension, you must make arrangements with your pension provider to nominate your beneficiaries.

Currently, if a person dies before age 75, their beneficiaries do not pay income tax or inheritance tax on pension payments or lump sums received, provided payments are made within two years of death.

Many people are unaware that pensions can play a crucial role in inheritance tax planning. This is because, currently, your pension pot typically sits outside your estate, meaning it isn't usually subject to inheritance tax.

Current pension rules (until April 2027):

- If you pass away before age 75, your beneficiaries typically pay no income tax or inheritance tax on pension payments or lump sums received, provided these payments are made within two years of your death.
- If you pass away aged 75 or older, beneficiaries pay income tax at their marginal rate, but still no inheritance tax.

Important Pension Rule Changes (from 6 April 2027)

From 6 April 2027, significant changes apply:

- Pension lump sums will be included in your taxable estate for inheritance tax purposes if you die aged 75 or older.
- Lump sums will also be subject to inheritance tax if you die before age 75 but payments aren't made within two years of your death.
-

This forthcoming change makes proactive pension planning critical to manage your family's inheritance tax liabilities.

Pension rules can be complex and are subject to significant changes. We strongly recommend speaking to one of our advisers to ensure your pension and estate plans remain optimally structured for your loved ones.

Call us today on 0151 220 2619 to arrange a comprehensive pension and inheritance tax review.

Planning for inheritance tax

Inheritance tax can be a difficult thing to discuss but knowing how much tax is due on your assets will begin the conversation about maximising the wealth you want to leave your loved ones.

Calculating your IHT

Calculating your inheritance tax is a big part of this process, providing you with an awareness of how much tax is due. Ultimately, this allows you to make any necessary preparations to reduce the financial impacts of inheritance tax.

How to calculate your IHT

To calculate the amount, you will need to:
Add up the value of all of your assets (possessions, money, property, investments).
Deduct any liabilities (debts, mortgages etc.)
Subtract the nil-rate band and the RNRB (if you are leaving your main residence to direct descendants).
The amount that remains will be taxed up to 40%.

Example: The value of all of your assets is £600,000.

£600,000 - £500,000 (nil-rate tax band plus residence nil-rate band) = £100,000.

This amount could then be taxed up to 40%, so, £40,000 will be deducted.

Most of the time, calculating the amount of inheritance tax that your family will be due to pay can be straightforward, but this is not always the case.

The many considerations that come with inheritance tax can make planning challenging.

This includes the size of your estate, the funds that you will need for your future expenses and how much you can afford to leave to your loved ones.

Nonetheless, having knowledge of your tax liabilities is always useful and speaking to a financial adviser will help you combat the challenges you may face.

Speak with a member of our team today to discuss how you can get on track to reaching your financial goals.



Creating a will

The creation of a will helps to reduce any future problems with estates after an individual's death.

By doing this, you can control the distribution of your assets and ensure they are allocated in the way that you envisioned.

Can Creating A Will Impact My Inheritance Tax Liabilities?

As well as providing control, a will is a strategy that can reduce inheritance tax liabilities.

It can do so in the following ways:

- Identifying beneficiaries who are exempt from IHT: Leaving assets to a spouse or civil partner will reduce tax liabilities because of the general exemption.
- Specifying your assets to be a part of a trust: This is generally the case with interest in possession trusts as there will be no inheritance tax to pay if the asset remains in the beneficiary's trust and interest.
- Gifting to individuals or charities: An individual could use their annual exemption allowance to gift a sum of £3,000 without being taxed and assets left to charities can not be taxed.

Having a will can help maximise your allowances and ensure that your assets are given to specific individuals according to your noted conditions.

A will not only reduces inheritance tax liabilities but can also prevent disputes among loved ones.

Because family conflict is a common problem with estate planning, we want to make sure you are exercising strategies that can prevent this and allow you to provide tax-free income to your relatives when you are no longer living.



Additional taxes

Inheritance tax may not be the only tax that an individual's estate owes. You need to be aware of the ways that taxes interact with one another.

Understanding how IHT interacts with other taxes will help you to minimise your tax liabilities, ensuring that you maximise your assets.

Beneficiaries might also face other taxes, such as capital gains tax or income tax, on inherited assets.

Capital Gains Tax

Capital gains tax applies to any profit made on investments that are sold for a higher price than they were purchased for.

So, for example, if an individual was selling their business, they would be obligated to pay capital gains on the difference between the selling and purchase prices.

If the deceased's property or assets are sold before their death, then capital gains tax would not be applicable.

If the property or assets are sold during the probate and the value has increased since the date of death, the beneficiary will need to pay capital gains tax.

Income Tax

Any income generated on a deceased individual's assets may be subject to income tax. This can include any interest built up on savings, rental income, or dividends.

If the person's property or business produces income after their death, this will belong to their estate.

The executor of the will must report this to HMRC so the correct tax calculations and deductions are made from the estate.

So, a beneficiary will be required to pay income tax on the deceased's assets if they produce a regular income.

Relief from inheritance tax

What are the tax rules on business and agricultural property?

Inheritance tax can apply to an individual's business or agricultural property. If an estate is above the nil-rate band, the beneficiaries must pay up to 40% on these assets.

However, there are reliefs available to help with these types of assets.

There are criteria you must meet to receive these reliefs before you can apply for them.

Criteria & eligibility

If you own a business or agricultural property, you could be entitled to relief from IHT. These are in place to reduce the amount of IHT payable on the transfer of these assets.

Business Relief

This reduces the value of a business during the calculation of IHT. Shares and ownership of the business are included in the estate.

Relief can be given on 50% or 100% of the business assets. This can be passed on while you are still living or as a part of your will.

100% relief can be given on a business or an interest in a business as well as any shares in a company that is unlisted.

50% relief can be given on shares that control more than half of the voting rights in a company that is listed. It can also give relief on land, buildings, and machinery that was owned by the deceased or held in a trust that the business has a right to benefit from.

Agricultural Relief

Agricultural property refers to land or pasture owned for the purpose of growing crops or rearing animals. Depending on your eligibility, you may be able to pass this asset down to your beneficiaries without any IHT liabilities.

The following list illustrates the assets that can qualify for Agricultural Relief:

- Farm cottages, farm buildings, and farmhouses
- Stud farms for rearing horses, grazing, and breeding
- Trees that are planted and harvested every ten years
- Land that is not being farmed under the Habitat or crop rotation scheme
- The value of milk quota affiliated with the land
- Agricultural shares and securities
- Properties owned for two years by the owner or seven years if occupied by someone else.

To claim Agricultural Relief, the property must be part of a working farm residing within the UK, Channel Islands, Isle of Man, or the European Economic Area.

What doesn't qualify?

What does not qualify for Agricultural Relief:

- Livestock
- Derelict buildings
- Harvested crops
- Farm equipment and machinery
- Property that is subject to a binding contract for sale

What does not qualify for Business Relief:

- Only an option if the deceased owned the business for two years prior to their death
- You can't claim business relief on an asset that also qualifies for Agricultural Relief.

Getting advice on inheritance tax

How we can help you

- ✓ We figure out a starting point and begin talking about the current status of your finances.
- ✓ We'll ask you what you want from your finances and the destination you want to head towards. This can help us to identify the areas that require improvement.
- ✓ With your wishes in mind, we'll be able to work with you to paint a clear map of your financial future, tailoring the plans to meet your goals.

Our services

- Retirement planning and pensions
- Investment advice
- Estate planning: will writing, powers of attorney & tax planning

We take the time to understand your current circumstances to help guide you through the next steps.

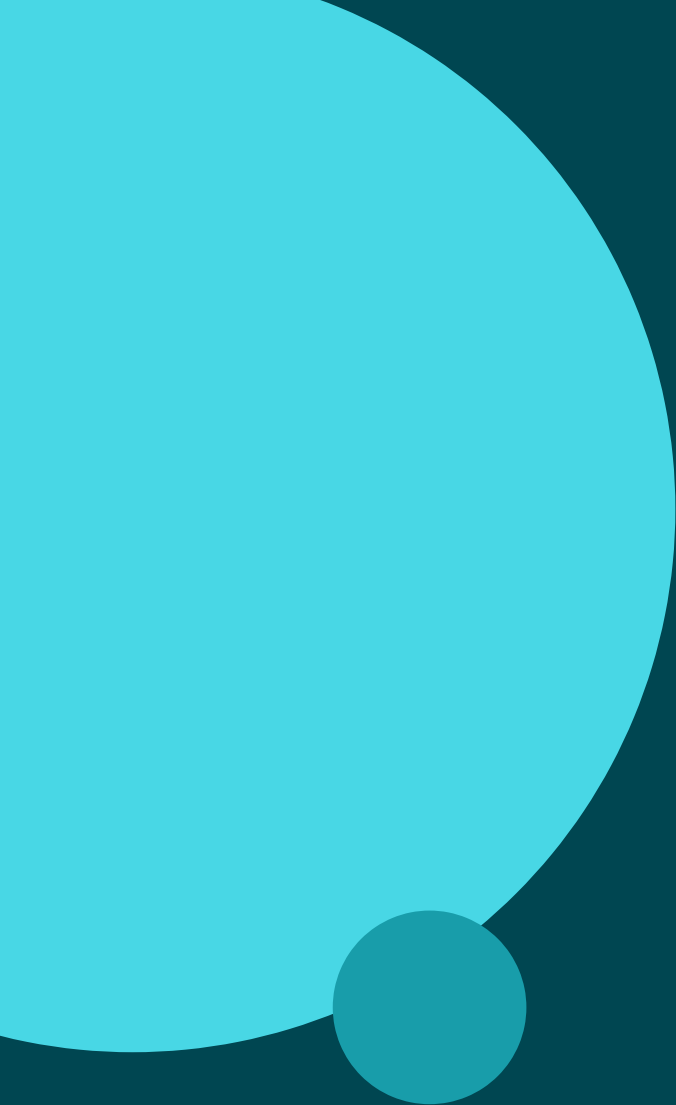
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At TheWealthPoint, we are committed to placing our clients at the heart of our business, ensuring that their needs are understood and accommodated for.

Our team has years of expertise, allowing them to address any concerns you may have about the future of your finances so that they can work hard to tailor financial plans that suit you best.



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