August 2023

TIPS FOR MINIMISING INHERITANCE TAX – LIFETIME GIFTS

In last year's Autumn Statement, the Chancellor confirmed that the Inheritance Tax (IHT) thresholds would be frozen until at least 5 April 2028. The current Nil Rate Band (NRB) therefore remains at £325,000 for the foreseeable future, with the Residence Nil Rate Band (RNRB) offering up to an additional £175,000 relief from IHT. The NRB has effectively been frozen since 2009 and would be worth around £475,000 today if it had been increased in line with inflation. In the face of increased property values over the past decades, more estates are being pulled into the scope of IHT and with the current main rate of IHT being 40%, IHT bills can be significant.

So, what can you easily do to minimise your IHT bill? Giving away money by way of gift can be relatively straightforward and I have highlighted below some helpful tips, but these are by no means an exhaustive list and, as always, each individual's circumstances will be different and specific advice tailored to your needs is essential.

Exemptions for Lifetime Gifts

A large part of IHT planning is making use of the exemptions which are available to us all. Most straightforward gifts of any value can be made completely free of IHT provided the donor lives for 7 years after making the gift and does not reserve any benefit whatsoever in respect of the gifted property (e.g. one cannot just give a property away and continue to enjoy living in it rent free). Such gifts should however only be made after consultation with your tax adviser and your solicitor in order to ensure that all relevant factors (including possible Capital Gains Tax consequences) are taken into account.

In addition, the following gifts may be made each tax year without using up any part of an individual's NRB:

- Small gifts of up to £250 to each of as many individuals as the donor wishes to benefit. This cannot be used to cover part of a gift or gifts totalling more than £250 to the same person during any given tax year;
- Annual gift allowance of up to £3,000. This exemption is applied to larger gifts not covered by the £250 exemption above. It can also be carried forward for one tax year only if it is not used in the year in question;
- Gifts that are a wedding or civil partnership gift worth up to £5,000 to a child, £2,500 to a grandchild or great grandchild and £1,000 to anyone else;
- Gifts to charities in the UK or EEA, museums, universities, political parties, housing associations, national heritage bodies or community amateur sports clubs.

Gifts From Surplus Net Income

Perhaps one of the most overlooked IHT exemptions is one entitled "normal expenditure out of income". For gifts to qualify for this exemption (which means that even if the donor dies within seven years, they are still not subject to IHT) there are three main criteria which have to be met:

- The gifts must have been made as part of the normal expenditure of the donor and generally speaking there has to be some regularity to the gifts being made;
- Taking one year with another, the gifts must be made out of income (not capital); and
- After allowing for all gifts etc. forming part of the normal expenditure, the donor must be left with sufficient income net of income tax to maintain his or her normal standard of living.

You must also maintain careful records of your gifts and expenditure in order for your Executors to be in a position to prove that you were able to maintain the same standard of living after making the gifts. If your Income Tax Returns and tax calculations are retained they should go a long way to providing details of your taxable income and if you also summarise your annual expenditure and your non-taxable income from time to time this would no doubt be appreciated by those dealing with your affairs after your death.

By way of example, let's assume that Rob has an income net of income tax of £50,000 per annum and having reviewed his regular expenditure on holidays, utilities etc. and his other general expenditure (let's assume he is fortunate enough to have paid off his mortgage) there is a surplus of net income of £12,000 in most years. He has two children and he decides to set up a standing order to each of them of £300 per month. He would also like to set up a standing order to accounts in the names of his two grandchildren of £200 per month. Provided that his circumstances remain roughly the same, after 5 years of making those payments he will have contributed £60,000 to his children and grandchildren, considerably helping their financial circumstances and potentially reducing his IHT liability by £24,000.

Although lifetime gifts are a useful means of reducing future IHT bills, it is important to ensure that you do keep enough for your own needs in the future, whatever those may be. As life expectancy increases, providing for future care becomes an important factor and none of us can be certain what lies ahead.

The above is for general guidance only and no action should be taken without obtaining specific advice.

Bath
37 Great Pulteney Street
Bath
BA2 4DA
+44 (0)1225 460491

Chippenham
67 & 68 St Mary Street
Chippenham, Wiltshire
SN15 3JF
+44 (0)1249 444666

Trowbridge
5 Wicker Hill
Trowbridge, Wiltshire
BA14 8JS
+44 (0)1225 764441