EQUILIBRIUM

Everything you need to know about inheritance tax

Our approach to IHT

Inheritance tax (IHT) planning is a crucial part of your financial plan. Often people avoid addressing the problem until it's too late – or sometimes, ignore it altogether! The reality of the situation is, you can never be too prepared, and the sooner you start planning, the better.

Intergenerational planning is an equally important part of your financial plan. We see inheritance tax planning as 'preparing your money for your loved ones and intergenerational planning as 'preparing your loved ones' for your money. It is about making sure that the right people get the right amounts at the right time.

By combining inheritance tax with intergenerational planning, we can enable you to look after those you love and leave long lasting powerful legacies.

In this brochure, we'll take a look at some of the allowances and exemptions as well as how best to approach your inheritance tax and intergenerational plan.

At Equilibrium, we believe that no client should pay inheritance tax unless they are comfortable doing so. However, in order to effectively deal with it we need to approach it in stages and as part of an ongoing intergenerational strategy.

Stage 1: Understanding the problem

First things first, we need to find out what your current IHT liability is.

We will start by calculating the value of your total estate, some parts of which could be exempt from IHT, for example, your pension(s), along with certain business assets or agricultural land.

Once we deduct the exempted assets, this will provide us with your net estate value.

Assuming no charitable gifts, the amount of your net estate which is over and above the available nil rate bands (see below) is then taxed at the current IHT rate of 40% (tax year 2024/25).

The final point to consider is whether the IHT problem will resolve itself over time or get worse.

We answer this for you by taking you through a very detailed lifetime cashflow forecast and adding all the information we know about you including your income, expenditure, assets and liabilities.

The aim is to project this forward using reasonable, conservative assumptions between now and the day you pass away. In doing so we can identify where you are now, where you're headed and what impact certain events could have on your future wealth and inheritance tax position.

Stage 2: Getting to know you

How do you go about making decisions?

Solving an inheritance tax liability requires so much more than just a logical or technical solution. We are all the product of our own experiences and these experiences have a huge impact on the values and attitudes we hold towards money. However, our experiences will no doubt differ to those of our children, grandchildren and other beneficiaries and where values and attitudes differ; that's where conflict can arise.

By understanding you, your past and your approach to making decisions with your money, we can help identify where the barriers may be and the steps required to resolve your inheritance tax problem.

At this stage, your planner will ask many probing questions to gather as much information as possible in regards to:

- your past and current circumstances;
- how you approach decision-making;
- your needs and desires now and in the future; and
- ultimately what legacy you would like to leave behind.

Stage 3: Getting to know your family

What are the needs of your individual family members? Have you spoken to them recently? Do they need money now or in the future?

Families can be complicated and tend to look very different from what they were, say, half a century ago. With second marriages and second families on the increase, we understand you may wish for the money to stay within the family rather that losing half of it in a divorce settlement.

We look to establish a family roadmap with details of who your money should go to and how it should be used, giving you the control whilst also meeting your family's aspirations.

Another point to consider is whether you can afford to start passing your wealth earlier than planned, it can help eliminate any nasty surprises further down the line and it may be more enjoyable to see the benefit it has added to your family's life at a time when they need it most.

One thing to bear in mind though is that intergenerational planning should not be at the cost of you - you come first and all your needs must be met before thinking how you can help your loved ones.

Stage 4: Providing a solution and strategy

Equilibrium's service is designed to coach, support and guide you through the process to achieve the outcome you want.

There is no off-the-shelf or one size fits all solution to inheritance tax so your plan has to be as unique as you and your family.

If you would like to involve your children/grandchildren or any other family members, they are more than welcome to come along and join a meeting or alternatively, you can postpone that decision until a later date.

Ultimately, we want to know what you want your money to do for you and your family, before we can even start to find the right tools in order to achieve them.

If you have any questions or would like to know more information about inheritance tax and your intergenerational plan, do not hesitate to get in touch:

askus@equilibrium.co.uk
New enquiries: **0161 383 3335**
Existing clients: **0161 486 2250**

Click here to book a no-obligation, 20-minute chat with one of our friendly experts

Nil rate bands (NRB)

The nil rate band is the threshold above which inheritance tax is payable.

You can pass on assets up to the value of your nil rate band which is currently £325,000 (tax year 2024/25) without creating an inheritance tax bill. So for a married couple, the first £650,000 of your estate is free from inheritance tax.

This nil rate band may be reduced if you make gifts in your lifetime that aren't covered by your tax-free gift allowances and you die within seven years of making the gifts. We will go into this in more detail shortly.

The second, residential nil rate band (NRB), which the government introduced in 2017, provided an additional amount that could be passed on tax-free against the value of the family home. This can save tens of thousands of pounds worth of tax, but the rules are not that simple.

To use the residence NRB, which is currently £175,000 per person (tax year 2024/25), you must pass your main residence to a direct descendant classed as:
- a child, grandchild or lineal descendant.
- a spouse or civil partner of a lineal descendant.

The residence NRB will gradually reduce, or taper away, for an estate worth more than £2 million, even if a home is left to direct descendants. For every £2 over £2 million, this NRB is reduced by £1 until it disappears completely at £2.35 million (based on a single person's allowance) or £2.7 million (based on a couple's allowance) and only the basic NRB applies.

Both the nil rate band and residence nil rate band can be transferred between married couples and civil partners when one spouse dies (subject to a maximum of two nil rate and residence nil rate bands).

Pensions

In April 2015, major changes were made to the tax charges that apply to benefits paid on the death of a pension scheme member and it all depends on the age at which the member dies.

More recently, the government announced the abolishment of the lifetime allowance and introduced the lump sum allowance of £268,275 and the lump sum and death benefit allowance of £1,073,100.

If you hold a pension and die before 75, your money purchase pensions are paid out to your nominated beneficiary, completely tax-free irrespective of whether they are already crystallised or uncrystallised (subject to the lump sum and death benefit allowance). This can either be as a lump sum with any excess taxed at the beneficiary’s marginal rate or as a regular withdrawal.

However, on death post 75, your nominated beneficiary is subject to their marginal rate of tax on any withdrawals taken.

So in some sense, pensions are therefore now a very flexible form of trust and with a little bit of forward planning, they can play a significant role in your inheritance tax and intergenerational plan.

This is provided you get the death benefit nominations right which is where we can help. Failing to do so or getting nominations wrong can result in money being paid out at the wrong time and valuable tax efficiencies being missed.

Tax-free gift allowances

In addition to the nil rate bands, you can also reduce your IHT liability and benefit your loved ones sooner rather than later. Here are a few simple ways to do this:

- Utilise the annual gifting allowance of £3,000 (£6,000 for a couple).
- Use previous year's unused allowance (this can only be carried forward to the following tax year and no further).
- Make as many small gifts as you wish up to £250 per person (as long as you haven't used another allowance on the same person).
- Gifts on marriage of up to £5,000 to a child, up to £2,500 to a grandchild or great grandchild, and up to £1,000 to any other friend or relative.
- Gifts to charities.
- Regular gifts from income.

Potentially exempt transfers (PETs)

Direct gifts to individuals, and certain trusts, are classed as Potentially Exempt Transfers or PETs. There is no limit on how much you can gift and there are no initial tax charges involved. Direct gifts would then become exempt if you survive seven years from the date of the gift. For this reason, it is always a good idea to keep a record of the amount and date you gave away any asset as the seven-year clock starts ticking for each gift you make.

If you die within seven years of making a PET, it will reduce the value of the nil rate band available on your death, meaning there may be inheritance tax to pay on it.

What about taper relief?

Taper relief applies where the value of a gift is greater than your available nil rate band (i.e. £325,000). Taper relief reduces the amount of inheritance tax on the amount above the nil rate band in the seven years following the gift. For example, if a married couple made a gift of £1m and they had their full nil rate bands, the surplus would be £350,000. The IHT payable would be as follows;

How long ago was the gift made?	How much is the inheritance tax reduced?	Inheritance tax payable (£)?
0-3 Years	No reduction	140,000
3-4 Years	20%	112,000
4-5 Years	40%	84,000
5-6 Years	60%	56,000
6-7 Years	80%	28,000
More than 7 Years	No tax to pay	-

Key points

- Taper relief only applies on gifts.
- It only comes into play when the cumulative value of any gifts within the seven years prior to death exceeds the available nil rate band.
- Taper relief reduces the tax payable on the portion of the gifts over the available nil rate band.
- Gifts always use up the nil rate band first before the value of any other assets or property that you leave behind. Until seven years have passed, IHT would be payable on part of your estate if the value of your estate and gifts exceed the IHT allowance.
- Gifts are removed from the IHT calculation after seven years from the date they were made.

What about gifts into trust?

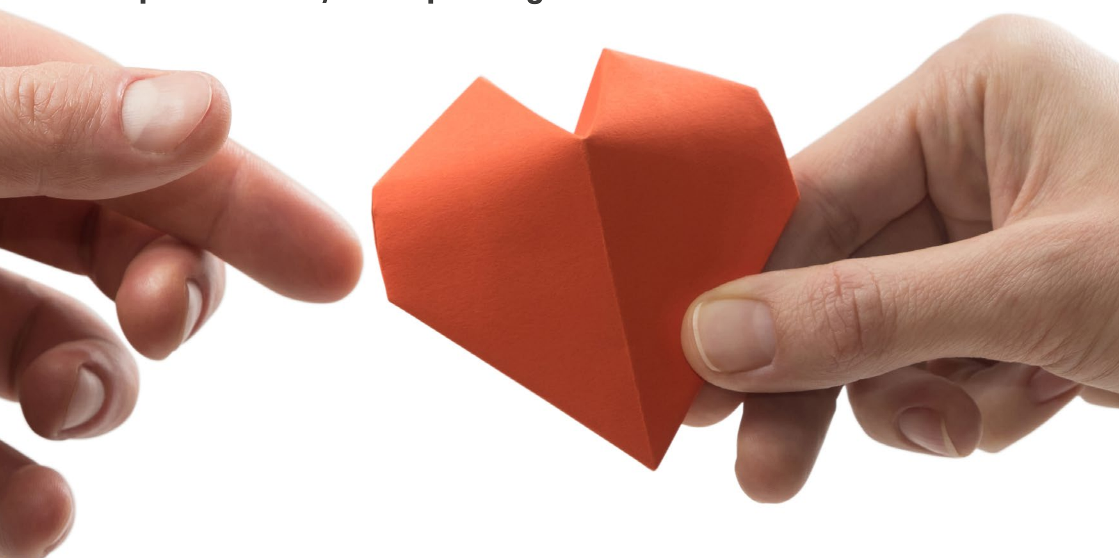
Trusts provide the ability to make gifts whilst keeping an element of control over the money. Depending on the type of trust used, you can choose who receives the gift, when they receive it and what they can use it for.

You can also use certain trusts to make a gift and still benefit from the money. For example, you can choose to give away the growth and retain access to the capital or receive an income from the trust during your lifetime.

Similar to direct gifts to individuals, you need to survive a minimum of seven years before gifts into trust leave your estate completely and are not considered for the purposes of IHT. However, the most you can gift into a trust (free from tax) in a given seven year period is the equivalent of your available nil rate band. Above this, you will pay inheritance tax during your lifetime at 20% on the surplus amount.

Trust planning is a complex area so it is important that you seek professional advice to ensure that you are utilising the correct trust for your needs and circumstances.

See our related **article on trusts**.
equilibrium.link/estate-planning-trusts



Charitable giving

As mentioned, gifts to UK registered charities are immediately outside of your estate and exempt from inheritance tax. However, you can go one further by leaving a legacy in your will.

If you leave 10% of your taxable estate (the value of your estate minus the nil rate bands) to charity, the rate of IHT drops from 40% to 36%.

Not only can this leave a powerful legacy for your chosen causes, but by donating more to charity in your will, your beneficiaries can actually receive more in certain cases as shown in the example below.

Potential IHT liability	No donation £	5% donation £	10% donation £
Total assets	1,500,000	1,500,000	1,500,000
Taxable estate post reliefs	500,000	500,000	500,000
Charitable gift %		5.0%	10.0%
Charitable donation amount		25,000	50,000*
Revised taxable estate	500,00	475,000	450,000
IHT rate applying	40%	40%	36%
Revised estimated IHT liability	200,000	190,000	162,000
Total assets less IHT & gift	1,300,000	1,285,000	1,288,000

*An additional **£25,000** to charity means your beneficiaries get an extra **£3,000**.

Business Relief

Under Business Relief rules, you may be able to reduce the value of your inheritance tax bill by owning or investing in a business. You can claim Business Relief at either 50% or 100% relief depending on the asset such as:

- A business or interest in a business (including a sole trade and partnership).
- Land, buildings or machinery owned by a partner or controlling shareholder of a business.
- Unquoted shares including certain shares listed on the Alternative Investment Market (AIM).

In order to qualify for Business Relief, you will need to own the assets for a least two years and on death. As such, it can provide opportunities to move significant assets outside your estate faster, whilst also allowing the investor to retain access to the assets during their lifetime if needed.

However, it's always important to understand what the underlying assets you are investing into as the level of investment risk can vary significantly.

At Equilibrium, we are able to access not only our own Equilibrium AIM portfolio but also alternative investment opportunities that qualify for this relief. In doing so, we aim to establish a blended portfolio bespoke to your circumstances and risk profile.

Get in touch

There is no doubt about it, inheritance tax is complicated. However, help is at hand as our financial planners can work with you to develop an inheritance tax and intergenerational plan so the right people get the right money at the right time.

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Click here to book a no-obligation, 20-minute chat with one of our friendly experts

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