

Inheritance Tax Reliefs

If the gift is of a special type of asset and the necessary conditions are met, relief may apply to reduce the amount of IHT payable, sometimes to nil. The main reliefs are as follows:

- Agricultural property relief: available for farmland and farm buildings anywhere in the European Economic Area (including the UK). Relief is given at either 50% or 100%, depending on the circumstances.
- Business property relief: available for certain business interests and qualifying company shares located anywhere in the world. Relief is given at either 50% or 100%, depending on the circumstances.

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Inheritance Tax

a guide to Inheritance Tax



When is Inheritance Tax Charged?

Inheritance Tax (IHT) is primarily a charge on your assets on death, including your share of assets jointly held with another person. However, lifetime gifts made within seven years prior to your death can also be brought back into charge.

IHT is also charged where an asset appears to have been given away, but where you in fact retain the use of (or a significant benefit in) the asset given. For example, where you give your home (in which you continue to live) to your children and do not pay them full market rent for your occupation.

What are the nil rate bands?

The nil rate band and residence nil rate band are amounts which are chargeable to IHT at 0%. The basic nil rate band is currently £325,000. There is also an extra nil rate band of up to £175,000 (depending on the value of the property and the year of death) if the family home is inherited by lineal descendants e.g., children or grandchildren. This is known as the residence nil rate band.

If you are married, your surviving spouse, or civil partner can “inherit” the unused portion of your nil rate band or residence nil rate band. When a claim is made, this increases the surviving spouse or civil partner’s nil rate band and residence nil rate band on a percentage basis (and not simply by the amount of your unused nil rate band and residence nil rate band).

Example

Mr X died a number of years before Mrs X. On his death, he had an available nil rate band of £325,000.

He left £1,000 to a charity and the remainder of his estate to his wife, Mrs X. The gift to charity was exempt from inheritance tax and the ‘spouse exemption’ applied to the residuary gift to Mrs X, so none of Mr X’s nil rate band was used.

When Mrs X dies, her executors can claim to transfer Mr X’s unused nil rate band, which would otherwise be wasted. Mrs X did not use up any of her basic nil rate band of £325,000 and so the combined nil rate bands mean that Mrs X can leave up to £650,000 tax free.

In addition, as Mrs X leaves the family home to her children (lineal descendants), her executors can claim the residence nil rate band of up to £175,000. As Mr X’s residence nil rate band was not used on his death then Mrs X’s executors can also claim this. This means that Mrs X can potentially leave an additional £350,000 tax free.

It is important to note that the residence nil rate band is capped at the value of the property. So if the property was worth £300,000 then only a total of £300,000 in respect of the residence nil rate bands could be claimed. There are also limits on when the nil rate band is available. It is always important to seek legal advice.



What is the rate of Inheritance Tax on death?

- The nil rate band is charged at 0%.
- The balance is charged at 40%. However, the rate of IHT is reduced from 40% to 36% for individuals who leave 10% or more of their net estate to charity.

There are, however, various exclusions, exemptions and reliefs which can reduce the amount of IHT payable.

Inheritance Tax Exemptions

Certain gifts are exempt from IHT and do not use up your nil rate band. Briefly, the main exemptions are as follows:

- Gifts to your spouse or civil partner.
- Gifts to charities established in the UK, any other EU country, Norway or Iceland.

Additional exemptions are also available for lifetime gifts, if none of the above exemptions apply. They are as follows:

- Normal expenditure out of income.
- Small gifts: you can give as many gifts of up to £250 to as many individuals as you want (but not to anyone who has already received a gift of your annual exemption allowance - see below).
- Wedding or civil partnership gifts: each parent may give the couple £5,000; grandparents and great grandparents may give £2,500; others may give £1,000.
- Annual exemption: £3,000 a year.
- Potentially exempt transfers: outright gifts of any amount become fully exempt if you survive for seven years.

The “normal expenditure out of income” exemption is applied first and the “annual” exemption is applied last, after the application of any other available exemption.