LLEWELYN DAVIES

CHARTERED ACCOUNTANTS

INHERITANCE TAX TIME BOMB AS HOUSE PRICES ARE HIGH

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Fiscal time bomb

Rising house prices have planted "an unexpected time bomb" under thousands of families / civil partnerships.

When you die, your estate pays Inheritance Tax (IHT) at 40 per cent on assets above a £325,000 threshold, and house price rises are pushing more and more people above that level.

Client dies leaving assets:

House	300,000
Cash	100,000
Investments	100,000

	£500,000
	=====

IHT Liability:

(£500,000 – 325,000) x 40% = £70,000

There are reliefs of up to 100% available in respect of Agricultural and Business Property if certain conditions are met. However IHT is harder to escape where the home is the main asset. Certain gifts are tax free, including gifts to your spouse, to political parties and to UK charities.

From 6 Aril 2012 a lower rate inheritance tax of 36% will apply where 10% or more of the deceased persons net estate is left to charity.

Marriage/civil partnership helps. In this case the property is owned jointly, the survivor automatically gets the whole house when one of them dies and no tax is due on assets, which transfer from one partner to another. The unused percentage of the inheritance tax nil rate band allowance can be transferred on a person's death (whatever the date of death) to the surviving spouse/civil partner who dies on or after 9 October 2007.

A common strategy for married couples is to leave assets on death to their children and other loved ones up to the IHT threshold, and the rest to their spouse. Nothing is taxed on the first death, but £325,000 worth of assets have been removed tax-free from the surviving spouse's estate. This works well if the couple give away investments, cash, a holiday home and other assets on the first death. It is far harder to escape tax by giving away part of your home while you still live there. You may be able to construct a scheme involving a trust or two, which take ownership of the house. This "is an incredible minefield" and a suitably experienced Legal Adviser should be used.

If you and your child live in the house together, you should be able to own the property 50-50, cutting the tax liability. Even then there could be problems if the arrangement could be seen as a vehicle for reducing tax. Alternatively taking out life insurance (again in trust) can be used to pay the tax bill on your death. A simple way to protect yourself is to buy a smaller property when your children leave home. You can use the surplus cash to take advantage of various IHT allowances.

Some assets are not liable for IHT at all, such as lump sums paid on your death by a pension scheme where its trustees have discretion as to who receives it. Other assets transferred during your lifetime can be potentially exempt transfers depending on how long you survive. If you survive seven years after these, there is no IHT to pay.

Other exempt transfers are:

- Regular annual gifts from your income.
- Presents of under £250 in a year to any number of people.
- A gift of £5,000 to a child getting married.
- Gifts of up to £3,000 a year.

You may also wish to take a copy of our leaflet "Care Fees & Inheritance Tax Planning".

This material provides only an overview of the subject and no action should be taken without seeking professional advice. No responsibility can be accepted for any loss occasioned by any person acting or refraining from action as a result of this material. Please therefore contact our Offices to determine the appropriate tax strategy for your particular circumstances. Initial consultation is at no charge or obligation.

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