ACCA Think Ahead

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INHERITANCE TAX PLANNING SUGGESTIONS BY MY TAX MATE LTD

There are several ways one can plan for inheritance tax.

1)Gifts:

a) Gifts of £250 to as many different people as you wish in each year. The recipients can include children and grandchildren, relatives, friends, etc.

b) Gifts out of disposable income which do not affect your lifestyle are also inheritance tax free.

c) Everyone has an annual exemption of £3000 each which can be in addition to other exemptions - this may be used for just gifting or to pay into an ISA or other investment in the names of grandchildren or other loved ones.

d) Make use of the children's ISA which has a limit of £9000 every year. Such gifts are regarded as potentially exempt transfers [the portion above exempt amount]. You could use your £3000 exempt allowance each year. One can also use the previous years £3000 allowance if not already used.

e) Each person is allowed to make a marriage gift of £5000 to children on their marriage or £2,500 to grandchildren.

f) Spending your excess money is also a way of saving inheritance tax.

g) Funding a child's, grandchild's or loved ones living expenses, as long as it is regular income and doesn't affect your lifestyle, it is allowed - one can fund a child's living costs or tuition fees - this can be combined with the £3000 annual allowance.

2) **Donations:**

Leaving a legacy in ones will to a qualifying registered in the UK can save tax by lowering the inheritance tax rate from 40%. However, the minimum amount you must donate is 10% of your net free estate after liabilities/ deductions.

3) **Residential home:**

Residential homes have a personal IHT allowance of £500,000 instead of the normal £325,000 if passed onto children; so it's always useful to have decent amount of assets in your home rather than cash, other investments or properties.

4) **Agricultural land:**

Passing on Investments in agricultural land can be inheritance tax free.

5) **AIM Companies:**

Shares in alternative investment companies are also eligible for inheritance tax relief if held on for two years as a minimum. One can also find or choose portfolio managers that specialise in investments in companies that qualify for business relief/ alternate investment companies. The risks are higher for such investments though. Having ISA's that hold business relief companies like alternate investment companies also qualify for inheritance tax relief.

6) **Property Companies:**

a) If you have a property portfolio, having it classified as an investment company does not allow some tax reliefs that would be allowed for trading companies. A property Company which has at least about 4 properties and is actively managed and run like a business can make itself classified as a Trading Company. If you have enough properties and your business is classified as a trading rather than an investment property business, then transfers of properties into a limited company structure can be exempt from capital gains tax and stamp duty because of incorporation relief.

b) Holding properties in the limited companies can have advantages if you give shares to children or grandchildren. One may not want to relinquish control or give up the income - it is possible to give the potential beneficiaries class B shares where they receive dividends and have pro-rata share of equity/ assets but have no voting rights. Other permutations where you still receive most of the dividends are also possible. But though the initial investment is a potentially exempt transfer, the amount of the growth/ appreciation in value is inheritance tax free as the assets are already vested in the names of the potential beneficiary shareholders.

7) **Trusts:**

a) Trusts can be used to mitigate inheritance tax but are complicated and need specialist advice. Some trusts are liable to tax charges. Bare trusts or irrevocable trusts for grandchildren where funds invested produce income the grandchildren can receive and the income received is covered by the annual income personal allowance of £12,570 are very tax efficient vehicles for saving tax. There is also capital gains allowance of £3000 for each recipient of any capital gains. The funds or gifts that are transferred into trust are potentially exempt transfer. However, the inheritance tax reduces after three years by 10% each year until after year seven it's nil.

b) Certain investment management companies specialise in investment bonds in Bare trusts. One such company, Brown Shipley requires a minimum of £1 million in investment assets; it is possible to explore other companies for Trust bonds.

c) Interest in possession trusts are trusts where the donors/ trustees can continue to receive the income, the assets passing to the beneficiaries on death. However, some of these types of trusts are levied a tax charge every 10th anniversary. The 10-Year Charge (also known as the Periodical Charge) is a tax that applies to certain types of trusts, specifically discretionary trusts, accumulation trusts, some interest in possession trusts and certain types of relevant property trusts. The tax is assessed every ten years and is based on the value of the assets held within the trust at the time of the charge [Trust asset value up to £325,000 is not taxable]. It essentially acts as a way for HMRC to collect tax on the assets that are being held within the trust for long periods, rather than waiting until the assets are distributed or the trust is dissolved.

The initial transfer to the trust, like all transfers to a trust, is a potentially exempt transfer with the £325,000 allowance every seven years. The inheritance tax rate reducing from the 40% by 10% every year after the third year so it is nil after 7 years of the transfer (of up to the allowance of £325,000).

8) **Emigrate:** Finally, a drastic measures would be to move your assets & yourself to a country with lower inheritance. Just moving to a low inheritance tax country would not be adequate because your assets left in the UK would be taxed IHT.