A GUIDE TO ESTATE PLANNING

2017

FINANCIAL ADVICE & WEALTH MANAGEMENT

ESTATE CAPITAL

Help your children inherit more and give them the best future possible.

- *Chartered Financial Advisers*
- *29 years professional experience*
- *Trusted, established and well resourced*

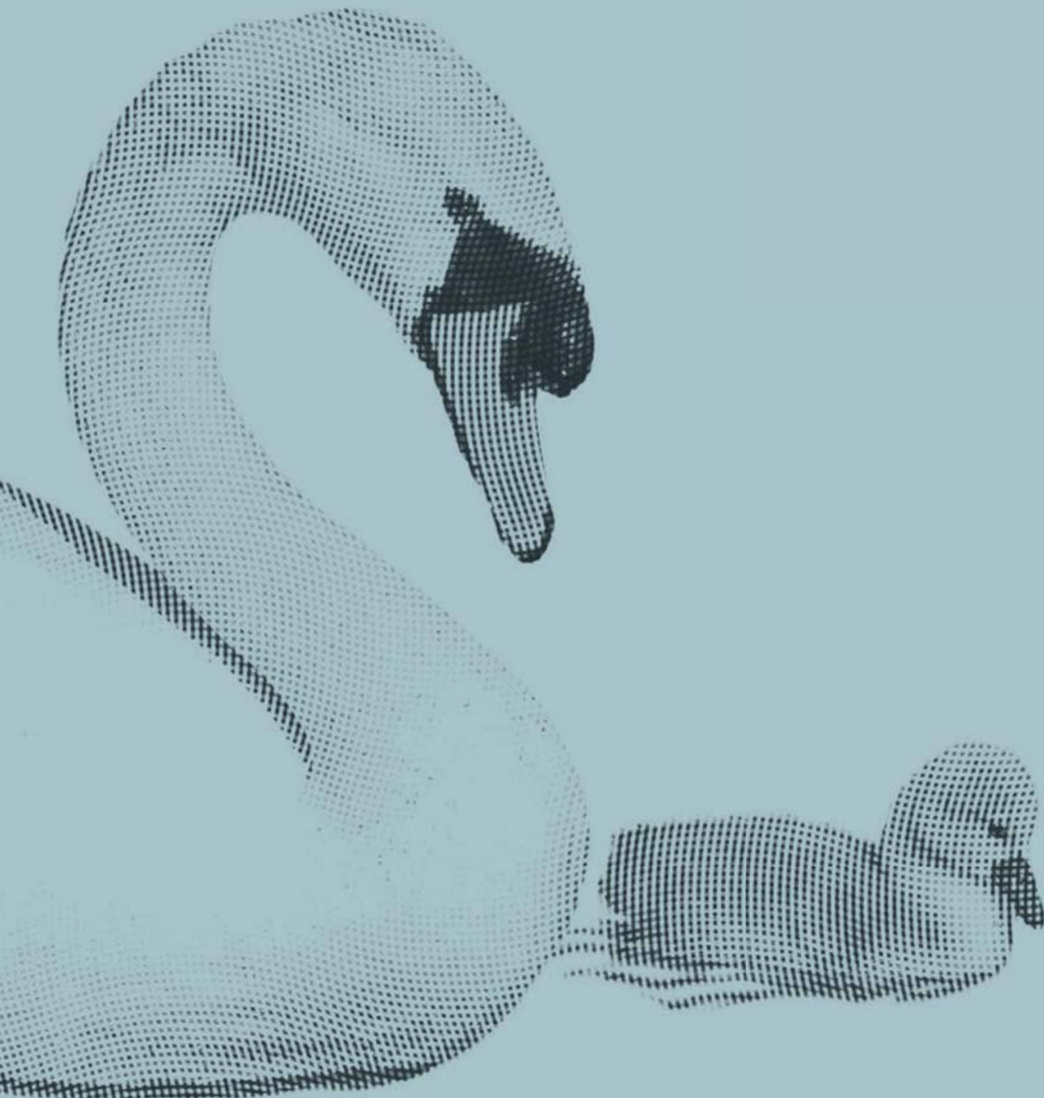
Inheritance Tax is potentially the largest tax demand your children will ever face.

Inheritance Tax is perhaps the most disliked of all taxes. People having worked hard, paid income tax and possibly capital gains tax throughout their lives, are then subject to the heaviest tax of all upon their death. No wonder people wish to reduce or even avoid paying 'death duties'. Inheritance tax is considered a voluntary tax, because with the right planning the liability can be reduced or even avoided.

Inheritance Tax (IHT) can apply to the worldwide assets of UK domiciled citizens. However not all of the estate is taxed, only that above the prevailing Nil Rate Band Allowance and Main Residence Nil Rate Allowance. The nil rate allowance is currently £325,000 per individual so a couple can potentially benefit from £650,000 of joint exemptions. The main residence nil rate allowance starts in April 2017 at £100,000 per individual and rises to £175,000 by 2020.

The cost of Inheritance Tax is 40% on all taxable assets above these thresholds making Inheritance Tax potentially the largest tax demand your children will ever face.

Make better informed estate planning decisions that are right for you.



Estate Planning

You may wish to reduce an inheritance tax liability by considering gifting assets directly to family members, use one of a range of inheritance tax effcient trusts that are available or invest into assets that are exempt from inheritance taxes.

You could also make provisions for your children to have the means to pay any eventual tax bill through a guaranteed Whole of Life Assurance policy.

There are also charities or political causes you could support through lifetime gifts or through your will and take advantage of the exemption such donations have from inheritance tax.

Many options are available to reduce inheritance tax so careful consideration is needed in order to complement not compromise yours and your family's future.

Wills

The first step in estate planning is to write a will. It is important to think about what you want to happen to your estate assets upon your death. You should consult with a solicitor who has will, trust and probate experience to discuss your requirements.

Failure to write a will means that on death your estate assets will be distributed in line with the rules of intestacy. The government sets out these rules and you may not find that your wishes will be followed and your estate distributed to individuals who you didn't intend to benefit.

Have confidence in your future and peace-of-mind to enjoy life now.

We take responsibility for people's life savings. A responsibility we take very seriously.

Allowances

Every individual has a nil rate allowance under which no inheritance tax applies. This threshold is currently £325,000. If a couple had an estate valued in total at £650,000 on death and have not made any gifts in the preceeding 7 years then no inheritance tax would apply.

On top of this nil rate allowance an additional allowance is available to parents who own property and intend to pass the family home to their children. This allowance is lost once the parents' taxable estate exceeds £2 million. The main residence nil rate allowance starts at £100,000 per individual in 2017 and rises by £25,000 per year to £175,000 in 2020. If the value of the family home is less than the allowance only the property value applies.

If a couple with children both died after 2020 where their family home was worth £350,000 within a £1 million estate, there would be no inheritance tax so long as the children inherited the home.

Small Allowances

There are several small gift allowances that are exempt from IHT.

You can gift £3,000 every year as an annual IHT exemption.

£5,000 can be gifted by parents on the marriage of their son or daughter. £2,500 applies to gifts made by each grandparent to a grandchild that is marrying.

You can transfer any number of small gifts but limited to £250 per recipient and you can gift money from surplus income so long as it does not impact or reduce your standards of living.

Charities

Charities often encourage supporters to bequeath assets in their will. Charity donations and gifting is exempt from IHT. There is no limit to the amount of gift. We hear of stately homes being gifted to The National Trust in order to avoid the family paying inheritance tax.

If you were to leave over 10% of your estate to charity you can benefit from a reduced rate of inheritance tax of 36% rather than 40%.

The same exemptions apply to political parties.

Large Gifts

Outright gifts in excess of £3,000 are classed as potential exempt transfers (PET) meaning the gift is subject to a seven year wait until it is fully exempt from IHT. A gift is only liable to inheritance tax if the value of the gift and the estate is over the nil rate allowances. A gift made today is still liable to IHT for the first three years then the level of exemption rises by 20% each year until the end of the 7th year.

A gift has to be permanent in nature and the donor cannot derive any benefits from the gifted asset. For example parents could not gift their home to their children and continue to live in it as if nothing had changed. The parents would have to pay a market rent to their children for living in the property in order for it to be classed as an IHT valid gift.

Trusts

Often people like the idea of gifting money or property to their children in order to avoid IHT but still wish to have some control or even benefit from the asset in some way. This is where trusts have a role.

Trusts allow the person setting up the trust to have ongoing control or influence on the trust assets and what happens to them. A trust allows gifted assets to be managed by appointed trustees on behalf of the trust's beneficiaries.

For example; grandparents can gift money into a trust for the benefit of their grandchildren and appoint the grandchild's parents as the trustees to look after the best interests of the money for the grandchild.

Discretionary Trusts

A discretionary trust is used when the people setting up the trust and who are gifting the capital (the settlors) wish to exercise flexibility over who may benefit from the trust income or capital. The appointed trustees have discretion over who benefits from the trust. The range of possible beneficiaries often includes a spouse, children, siblings, grandchildren or named individuals.

It is a responsibility of the trustees to fulfil their role in line with the settlor's intentions and in the best interests of the beneficiaries.

Any capital placed into a discretionary trust valued over the prevailing nil rate band allowance is subject to a one off charge known as a chargeable lifetime transfer. The charge applies only to the value of the gift over the nil rate allowance and is currently charged at 20%. Every ten years a periodic charge also applies of up to 6% of assets above the prevailing nil rate allowance.

Bare Trusts

A bare trust offers no discretion over the beneficiaries entitlements as they are clearly named as such. The role of a trustee is to look after the best interests of the trust assets and distribute trust income or assets to the named beneficiaries. As the trust is certain there is no lifetime transfer charge applied to gifts made into bare trusts. Bare trusts are commonly used as designation trusts for children's or grandchildren's investment.

Will Trusts

Not all trusts come into force during a person's lifetime. Often a will contains a discretionary trust. These trusts are set up after the person's death and are called Will Trusts.

Different forms of trust have different uses. There are some specific trusts aimed at reducing inheritance tax which also offer the settlor some control, ongoing benefit or access to the trust assets. These trusts are attractive to people wishing to reduce IHT but still benefit from the money gifted if needed.

Discounted Gift Trust

A Discounted Gift Trust (DGT) is a family owned discretionary or bare trust where the settlor can continue to benefit from a regular income paid out from the gifted trust assets. The nature of this income means that the trust assets are discounted by a notional capital value representing the cost to the trust of this lifelong income. This notional capital value creates an immediate reduction in the taxable value of the trust for IHT, so reducing the liability to IHT from day one. The remaining trust assets above this notional discount are considered a gift and still liable to IHT until 7 year have passed. The full value of the discounted gift trust will be exempt from IHT in part straight away and in full after 7 years.

Throughout their lives the settlors will receive an income from the DGT so allowing them to enjoy an income but not the capital of the trust.

Wealth Preservation Accounts

Wealth Preservation Accounts are discretionary trusts that split the money gifted into a series of maturing investments. The number of separate investments is set by the settlor but is commonly 10. The first maturity occurs after 1 year and allows access to the settlor of 1/10th of the trust assets if required. If not the money is offered again in 10 years at year 11. The offer of 1/10th of the trust assets is made every year and can be accepted or declined. The money retained in the trust falls out of the settlor's estate after 7 years. Any return of capital falls back into the settlor's estate.

A Wealth Preservation Account is popular with parents who do not need income but may wish to call upon the gifted capital in the future.

Help your children inherit more and give them the best future possible.

Business Property Relief

Business Property Relief (BPR) is an IHT exemption applied to the assets of a private trading business when they pass from one generation to the next. Most shares in private trading companies, or interests in unincorporated businesses such as a sole proprietor, or partner, will receive 100% business property relief from Inheritance Tax after 2 years of ownership.

A good example would be the shares in a family business when inherited by the children of the business owner.

The company or partnership must be actively trading to qualify for IHT exemption. If a business builds up cash reserves in excess of half its value then the exemption is lost as the business will be classed as an investment business and not a trading business.

Agricultural Property Relief

Agricultural Property Relief (APR) is the farming equivalent of business property relief. Again the farm must be trading and producing farm accounts to be exempt. Agricultural land, together with farm houses, cottages and other farm buildings may receive agricultural property relief either at 100% or at 50% if the farm is rented to a tenant farmer. The full exemption from IHT applies after 2 years of farm ownership. The farm could produce many forms of crop including woodland.

APR is an important exemption that allows family farms to pass down the generations without the liability of IHT.

Business Property Relief Portfolios

Several Investment Management firms use the exemption provided by business property relief on the shares of private trading companies to build bespoke IHT exempt investment portfolios.

Investors can buy into a portfolio of private company shares that fulfil the BPR exemption criteria. These investments will be made into small non listed companies usually trading in asset backed businesses such as bridging finance, solar panel farms, wind farms, property development, car parks, or storage units.

A portfolio of BPR qualifying companies is usually spread over many sectors and different companies. Asset backed company investment can give investors some added comfort in the underlying security of the company. Once owned for two years the shares qualify for BPR and are exempt from IHT.

Alternative Investment Market

The Alternative Investment Market (AIM) is a stock exchange listing for smaller companies often obtaining their first stock market listing. Shares that are listed and traded on the Alternative Investment Market have the added attraction of being exempt from Inheritance Tax after 2 years of ownership under BPR rules.

Not all shares listed on AIM qualify for IHT exemption through BPR. If a stock is dual registered on another exchange or invested in land, property or financial assets such as an Investment Trust or Real Estate Investment Trust (REIT) the exemption does not apply.

Enterprise Investment Schemes

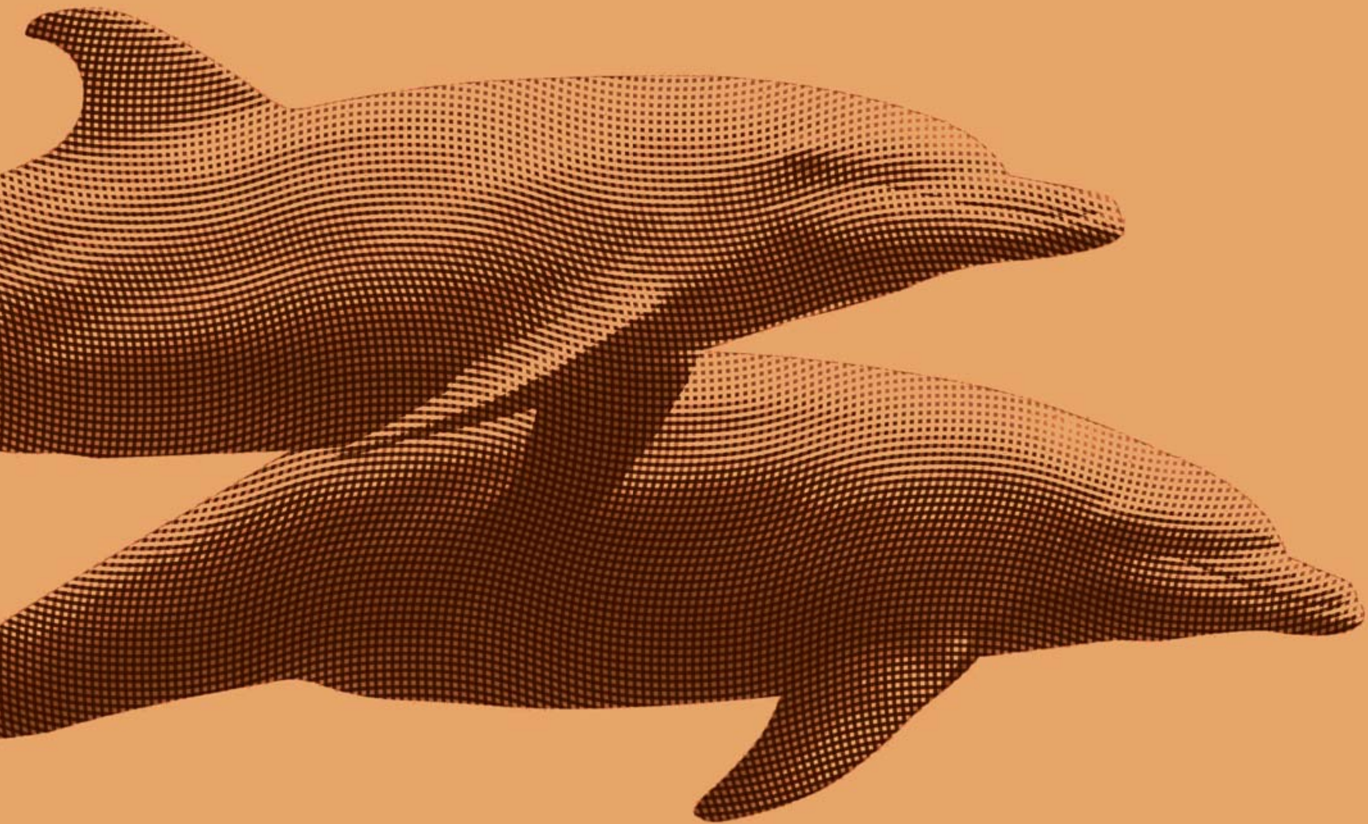
There are incentives to private investors who are considering supporting a business with start-up capital. New businesses that qualify as Enterprise Investment Schemes (EIS) benefit from several tax reliefs. The nature of the investment is speculative due to the stage in life of the company.

Investors that subscribe to shares in an EIS qualifying business can recover income tax on up to 30% of the cost of the shares. The income tax relief is offset against the investor's income tax in the year of subscription. There is no capital gains tax charged on any gains made on the disposal of shares. Both the income tax relief and capital gains tax relief are conditional on the shares being retained for a minimum of three years.

Shares in EIS companies also qualify for inheritance tax exemption after 2 years of ownership.

Make better informed estate planning decisions that are right for you.

Have confidence in your future and peace-of-mind to enjoy life now.



Pensions

The new pension freedoms introduced in April 2015 have made pension funds even more attractive. Private pension funds can now be passed in full on the plan holder's death via a nomination of beneficiaries to a spouse, child or grandchild. Any transfer of a pension fund from one generation to the next is not liable to inheritance tax.

Private pensions can now be seen as a family asset that can pass down the generations. Wealthy individuals are now considering not taking a retirement income from their pension fund but instead from their estate assets as these assets are liable to inheritance tax.

The initial attraction of a pension is a secure income in retirement supported through tax relief on contributions and tax free growth. The additional benefit of passing the full fund to one's spouse and then children exempt of inheritance tax adds greatly to their appeal.

Life Insurance

All the previous means to reduce or avoid inheritance tax involve individuals making investments into IHT exempt assets, trust funds or absolute gifts. Some people want to keep their money and hold on to their estate as it is. They may be wary of significant gifting or using trusts that give up some control.

As an alternative you could plan to provide your children with the means to pay the eventual inheritance tax liability. A simple and relatively low cost option is to use a whole of life assurance plan written in trust to your children with the sum assured set to the expected IHT liability. The monthly premiums would be paid out of income and the death benefits would be held in trust outside the estate and passed directly to the beneficiaries upon death who then have the means to pay the 'death duties' and obtain probate.

As there is no IHT liability between married couples, a whole of life assurance is usually set up on a joint life basis. The sum assured is paid out on the death of the second spouse which is when the inheritance tax is due.

With all life insurance, premiums are age and health sensitive so planning early is beneficial.

What is Inheritance Tax?

Inheritance Tax is a tax on death. The tax is applied to your estate if its taxable value exceeds the individual exemption allowance of £325,000. Not all assets held within an estate are taxable as some assets are exempt from inheritance tax.

What assets are liable to Inheritance Tax?

Assets that are subject to inheritance tax typically include your home, other property, land, deposit accounts, shares, investment funds, insurance bonds, jewellery, art and antiques. Any assets of a similar nature held abroad are also included in your taxable estate.

What are the main exemptions from Inheritance Tax?

There is no inheritance tax charged upon transfers on death between married couples or civil partners. Each individual benefits from a current nil rate allowance of £325,000 and therefore couples have a joint allowance of £650,000. Any unused allowance can be transferred to the surviving spouse.

On top of the nil rate allowance, homeowners with children can benefit from the main residence nil rate allowance. This allowance starts at £100,000 per individual in 2017 and rises by £25,000 each year to £175,000 in 2020. This allowance only applies to the value of the family home when inherited by the home owner's children.

Other exemptions are given to privately owned businesses and farms that if trading are exempt from inheritance tax.

What is the cost of Inheritance Tax?

The value of the taxable estate above the nil rate and main residence nil rate allowances is subject to a 40% tax charge. If a net taxable estate was worth £2 million after all allowances were deducted then the inheritance tax demand would be £800,000.

Who pays the Inheritance Tax?

The inherited estate is liable to pay the inheritance tax. The liability must be settled or agreed to be settled with HMRC prior to the granting of probate and the estate distribution.

If there are insuffcient disposable assets in the estate then other assets will need to be sold to raise the capital.

When is Inheritance Tax paid?

The estate is required to pay inheritance taxes prior to the grant of probate and the distribution of estate assets to the beneficiaries of the will. Depending upon the nature of the assets, payment can be spread over a period of time. HMRC generally expect IHT to be paid within six months of death.

Should I write a will?

It is important that to ensure that your assets pass to the people you want them to then you should write a will. A will avoids your estate from being distributed in line with the intestacy rules and gives clarity to your family over your wishes.

Wills can always be changed, re-written or updated.

We take responsibility for people's life savings. A responsibility we take very seriously.

Financial Advice & Wealth Management

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