Estate Planning

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Your estate is comprised of everything you own but one thing is for certain – you cannot take it with you when you die. When that happens you may want to make sure that as much as possible of your estate reaches your heirs, rather than being depleted by tax beforehand. Rising house prices and a recovering economy means tens of thousands more families will be hit with Inheritance Tax bills which is why it is important for everyone to plan ahead.

"If you do not have a plan, the law and the taxman have one for you. But you may not like it."

Mark Chandler, Head of Estate Planning

Your Will

Making a will is your first essential step in estate planning.

If you have no will, you will die **intestate**, and the law will decide who inherits your assets. This could produce undesirable results, for example, your surviving spouse or civil partner may not inherit all your assets. Intestacy rules mean that your estate will be distributed based on what family members there are and their relationship to you.

You may also be deemed to have died intestate if your will is invalid. This could happen if it is not signed; it is not witnessed correctly; it cannot be found on your death and there is no copy; or you have remarried. So, it is important to keep your will up-to-date and formally drafted to ensure that all assets in your estate are covered and passed to the right people.

Lasting Powers of Attorney

You may also want to plan what happens if you are alive but unable to make decisions for yourself because of mental or physical incapacity. A Lasting Power of Attorney (LPA) appoints an individual, or individuals, of your choice to manage your affairs in the short or long term.

If you do not have an LPA and become incapacitated, your family will need to apply to the Court of Protection to become a deputy, which is costly and time-consuming with no certain outcome.

There are two types of LPAs. A **property and financial affairs** attorney can help make decisions on things such as money, tax, bills, bank and building society accounts, property and investments, pensions and benefits.

A **health and welfare** attorney can make decisions on elements such as where you should live, whether a care home may be appropriate, and medical treatment. If given the power, they can also make decisions about life-sustaining treatments.

Inheritance Tax

Inheritance tax (IHT) is paid at 40% on the value of the assets that you leave when you die, above certain limits. Most people's estates are assessed for IHT on death, but the tax can also be chargeable and payable during your lifetime on the transfer of assets - particularly transfers into some types of trust.

If you are married or have a civil partner, you can leave your entire estate to your partner free of IHT, but anything left to family and friends may be taxed.

Currently, the first £325,000, or £650,000 for married couples, is exempt. This is known as the personal exemption or nil rate band. Only amounts above those levels will be liable to IHT. However, other chargeable or potentially exempt transfers can impact the estate.

Examples of Inheritance Tax

Value of estate on death	Single Person	Married Couple (due on 2nd death)
Up to £325,000	£0	£0
£500,000	£70,000	£0
£750,000	£170,000	£40,000
£1,000,000	£270,000	£140,000
£3,000,000	£1,070,000	£940,000

These figures assume that the full nil rate band is available on death

In addition to the standard nil rate band, there is a residence nil rate band (RNRB), available when you leave residential property to direct descendants. This was introduced at £125,000 in 2018 to 2019; £150,000 in 2019 to 2020; and £175,000 in 2020 to 2021. Just like the standard nil rate band, any exemption unused on the first death of a married couple or civil partners could be transferable. The rules which apply to qualification of the RNRB are complex and it is important to take professional advice based upon your own circumstances.

Gifting

You can reduce inheritance tax by gifting during your lifetime. Some gifts are always IHT free, including those between spouses or civil partners. HMRC also allows certain **small gift exemptions**. These are £3,000 a year (plus previous year if not already used); marriage gifts (£5,000 for parents and £2,500 for grandparents); and small gifts of up to £250 to any number of people. It is possible to make gifts from net income, providing you can show that you can maintain your lifestyle.

Although regular gifting can reduce an inheritance tax problem, in many cases, it has little impact given the size of the estate and the rate at which it is growing.

Larger gifts which did not meet the exemption criteria are referred to as **potentially exempt transfers**. These are unlimited and free of inheritance tax of death, providing you survive for seven years after making the gift.

Gifts into some trusts are classed as **chargeable lifetime transfers** and may lead to an immediate tax charge at the date you make the gift. Gifts during your lifetime into a discretionary trust are probably the best example. Cumulative gifts over a 7-year period of up to £325,000 per person into discretionary trusts do not result in an immediate tax charge, however gifts above this level may attract initial, decennial and exit tax charges.

If you decide to leave at least 10% of your net estate to charity, the taxable element of your estate will pay tax at 36% rather than the usual 40%. The charitable element itself is tax-exempt.

Protecting Bloodline Inheritance

Owning your home as **tenants in common** rather than joint tenants provides additional planning opportunities for potentially protecting inheritance in terms of residential care fee assessment and marriage following bereavement, also known as second marriage syndrome.

On first death, the survivor owns half of the house and a right to reside in the other half via a **life interest trust**. This potentially serves to mitigate the loss of at least half of the home should the survivor require residential care and have exhausted all other funds.

Should the survivor remarry, not make a new will and then die, intestacy rules would see the new spouse taking a disproportionate amount of the estate. By severing the tenancy and creating a life interest trust in your wills (for the surviving spouse), this ensures that your share of the property passes to the children on second death. Flexibility regarding downsizing can be achieved within the will.

To preserve the new residential nil rate band, property needs to pass to direct decedents.

Trusts

Trusts

You can establish a trust during your lifetime or, through your will, on your death. You can appoint trustees of your choice - this can include you and
your spouse during your lifetimes - who will manage the trust on your behalf. Following your death, the trustees will act with consideration to your wishes.

Trusts offer several benefits.

- On your death, the trust asset can pass to your chosen beneficiaries with no need for probate.
- In certain circumstances, trusts can protect your assets from creditors.
- You can control who benefits from your assets during your lifetime and on your death.
- Depending on how the trust is structured, it is possible to invest your assets into a trust to mitigate inheritance tax, income tax, and capital gains tax (principle private residence relief).

You may also wish to reserve some influence over your assets for the trustees to observe after your death. For example:

- you may want to delay the age at which beneficiaries inherit
- you may want your heirs to receive their inheritance in stages
- you may be concerned about your heirs getting divorced and want to protect the assets inherited from you being included in a divorce settlement.

Trusts can also be useful in preventing assets reaching a beneficiary facing insolvency proceedings and those making poor lifestyle choices, such as involvement in alcohol and drugs.

Whole of life cover – written in trust

Insurance policies can help with IHT by paying out a lump sum that your beneficiaries can use to pay the liability. With whole of life insurance, the level of cover can be set to match all or part of the inheritance tax you anticipate your heirs will suffer on your death, thus protecting them from the liability.The cost of cover is dependent on your age and health. Although it can be an effective solution, it is not for everyone and you will need to be able to afford the premium.

Planning Opportunities

Business Property Relief Scheme

Business Property Relief (BPR) was first introduced in the 1976 Finance Act. Then, its main aim was to ensure that after the death of the owner, a family-owned business could survive as a trading entity, without having to be sold or broken up to pay an inheritance tax liability. Over time, successive governments recognised the value of encouraging people to invest in trading businesses regardless of whether they run the business themselves.

When an investment qualifies for Business Property Relief, the asset can fall outside the Estate for the purposes of IHT after just two years. This kind of arrangement could be particularly beneficial for those with an IHT liability and whose age or health may preclude planning using gifting strategies such as potentially exempt transfers and trust arrangements which require a survival period of 7 years from date of investment.

Investment into a qualifying Business Property Relief plans provide the following benefits:

- 100% inheritance tax free for BPR qualifying investments held 2 years and until date of death
- Full access to Capital if circumstances change
- A two-year survival period to secure IHT relief
- If death occurs within 2 years a surviving spouse or civil partner can hold for the remaining unexpired period and until death

Enterprise Investment Scheme (EIS)

The Enterprise Investment Scheme (EIS) was introduced by the government in 1994 to encourage the funding of small-medium enterprises (SMEs) by offering attractive tax advantages for investors. EIS investment vehicles can be a great way to support the growth of these companies and, in turn, the UK economy.

You have the potential to claim **30% income tax relief** on investments up to £1 million in the current or previous tax year (subject to income tax liability, personal circumstances and a three-year holding period).

If you have a capital gains tax bill coming up you can **defer paying the tax on any gain** realised for up to three years before, or one year after the date your EIS shares are allotted.

100% of your investment can qualify for IHT relief if you hold the shares for at least two years and at death.

Discounted Gift Trust

A Discounted Gift Trust (DGT) is a trust-based inheritance tax (IHT) planning arrangement for those individuals who wish to undertake IHT planning but who are unable to lose full access to their investment. In a DGT, access is typically provided by means of a series of pre-set capital payments to the investor who will be the settlor of the trust.

The term 'discounted' is used because the value transferred on establishing the trust is less than the amount invested. This is the logical consequence of the fact that the settlor is entitled to a stream of capital payments. The settlor is typically entitled to payments on specified dates subject only to be alive on those dates. The settlor's transfer or gift is the bond/policy premium less the value of the payments receivable during his/her lifetime.

Assuming the settlor survives 7 years from the date of investment, the trust fund is considered to be outside of the estate

Wealth Preservation Trust

The Wealth Preservation Accounts are arrangements designed to save inheritance tax. They allow a client to gift money into trust to reduce their potential inheritance tax liability but also allows them predetermined access to annual payments (if required) to supplement their income. On inception, the Account is immediately assigned into a bare trust and then into a discretionary settlement.

The benefits of a Wealth Preservation Account are similar to the gift trust, however the initial discount (percentage immediately moved out of the estate) is not available. Income flexibility, however, is much greater with the WPA.

To be effective for IHT purposes a 7-year survival period is needed.

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