

INHERITANCE TAX, A VOLUNTARY TAX?



Benjamin Franklin once said: "In this world nothing can be certain except Death and Taxes". While this may be true as we all pay our fair share of tax during our lifetime, we should not have to pay tax on our assets at death.

With careful planning Inheritance Tax ("IHT") can be mitigated by using all available Exemptions and Reliefs.

These exemptions are in addition to an individual's Nil Rate Band (£325,000) and Residence Nil Rate Band (currently £100,000). The Residence Nil Rate Band is not available to everyone as it is restricted in respect of estates over £2,000,000.

Reliefs

Reliefs are available on certain assets providing the necessary conditions are met. If an individual owns any business assets or

agricultural assets, it is important to ensure that necessary conditions are met in order to avail of these generous reliefs.

Business Relief - the rate of Business Relief ranges from 50% to 100% depending on the ownership of the asset. There are a number of restrictions in relation to these assets, therefore it is important to ensure that the assets are held in the correct vehicle to optimise the relief. It is also important to ensure that all the criteria for Business Relief is met so this generous relief is not jeopardised.

Agricultural Relief - may be available in respect of land and farm buildings and is similar to Business Relief. However, there have been a number of court cases in respect of this Relief, therefore it is essential that a review of assets is carried out every few years to ensure an individual will still qualify for this Relief.

Gifts out of Income

Gifts out of income is a very generous Relief but seldom used as most individuals are unaware of it. If an individual's income exceeds their expenditure each year then this excess is added to their capital which serves to increase the size of the estate and so in turn increases their IHT liability. However, an individual can gift this excess to other family members or friends and not increase their capital each year.

For example, Anna is a 73-year-old retired teacher, her annual income after tax is £25,000, however Anna's expenditure totals £15,000 which means £10,000 each year is being added to Anna's capital. Anna's other assets total £1,200,000 which means Anna's estate already has an IHT liability. Due to Anna's excess income, Anna is increasing her Estate's IHT liability by £4,000 each year. However, by making gifts out of income Anna can

ensure that her estate is not added to and the IHT liability is not increasing each year. Gifts out of income is an immediate relief and as soon as the gift is made the asset leaves Anna's Estate.

Exemptions

There are number of exemptions available that everyone should be making use of when possible, such exemptions are:

Potential Exempt Transfers (PET) - A PET is a gift that falls out of an individual's estate if the individual survives more than seven years from the date of gift. Individuals may consider making a PET of cash or an asset that they no longer have a use for. If gifting an asset, the individual may need to consider if Capital Gains Tax may be due.

Annual Exemption - An individual can gift £3,000 per annum which will immediately be outside their estate for IHT purposes. If you do not use this exemption in one year it can carry over into the next year, but the maximum Annual Exemption anyone can use in any one year is £6,000.

For example, Jane has not utilised her Annual Exemption in a number of years but gifts her niece £6,000 in the 2017/18 tax year. As Jane did not use her Annual Exemption in the 2016/17 tax year the £3,000 Annual Exemption is brought forward and Jane can use it and her Annual Exemption from the 2017/18 tax year against the gift to her niece in the 2017/18 tax year. If Jane then makes a gift of £6,000 to her nephew in the 2018/19 tax year she can only offset the Annual Exemption from the 2018/19 tax year as she has already utilised her Annual Exemption from the 2017/18 tax year. Therefore £3,000 of the gift to her nephew may fall into Jane's IHT Estate if Jane does not survive seven years from the date of the gift.

Wedding Gifts - There are a number of exempted gifts that an individual can give on the occasion of marriage or civil partnership. An individual can gift £5,000 to their

Children as a gift when the child is getting married or entering a civil partnership, £2,500 to a Grandchild and £1,000 to anyone else. The gift must be made on or shortly before the ceremony and it is not a valid gift until the ceremony takes place.

Small Gift Exemption - An individual can gift up to £250 per person in any one tax year. The total gifts in a tax year to any one person cannot exceed £250 and cannot be used with any other exemptions.

Spousal Exemption - any gifts made to an individual's spouse are exempt from IHT. Restrictions may apply if the spouse is not a UK Domiciled person and, if this is the case, professional advice should be sought.

Conclusion

Is IHT a voluntary tax? It certainly seems so, as with careful planning it can be mitigated. IHT planning is something that has to happen over time and the earlier the planning begins the better.

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The content of this article is for information purposes only and advice particular to your circumstances should be sought from a professional advisor.

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