GUIDE TO INHERITANCE TAX

Pass more of your wealth on to loved ones

HARGREAVES LANSDOWN

IMPORTANT INFORMATION

We've written this guide to give you useful information about inheritance tax, but it isn't personal advice. Its purpose is to highlight areas you might like to discuss with your adviser or investigate further. Where we mention married couples, this includes registered civil partnerships.

You shouldn't rely on it alone to make decisions. If you need personalised recommendations, or aren't sure if a particular investment is right for you, please ask for advice.

Some of the pages and tools linked to in this guide are offered by our sister company Hargreaves Lansdown Asset Management Ltd.

This guide was correct as at 5 April 2023, and all figures and tax information applies to the 2023/24 tax year and relates to UK residents and domiciles. This applies to UK tax law but we are not tax experts. Tax rules can change and their benefits depend on your circumstances. If you need help with complex tax calculations you may wish to seek advice from an accountant.

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TWO UNFORTUNATE CERTAINTIES

The only two certainties in life.

Death and taxes are often described as the only two certainties in life, as gloomy as it may sound. And inheritance tax (IHT) means they can turn up at the same time.

There are plenty of ways to reduce or remove IHT altogether. And dealing with it earlier means you're likely to be in a better position later on.

To help you pass on more to your loved ones, we've looked at some of the steps a financial adviser would take.

We hope these steps help you put a plan in place. But inheritance tax is a complex area and it's seriously worth considering financial advice if you think you might be impacted.

If you are unsure, or need advice, our advisers can help. Just give us a call on **0117 317 1690**.

HOW MUCH WILL YOU PAY?

The first step is to work out if you'll be affected by IHT.

And if you won't, you don't need the rest of this guide.

The simplest way to check this is by using our online calculator – it does all the work for you. Although it doesn't take into account all personal circumstances.

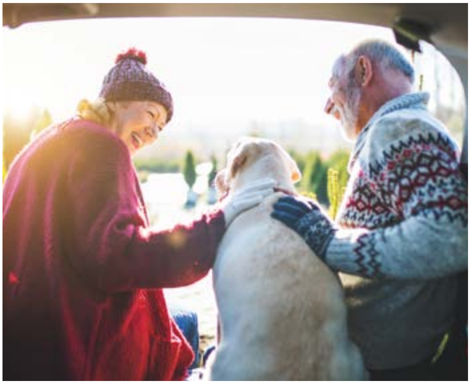
You can find this at **www.hl.co.uk/tools/calculators/inheritance-tax-calculator**

IF YOU'D RATHER CALCULATE IT YOURSELF, HERE'S HOW.

First, work out the value of the assets that you own, but don't include your pensions. You can make certain deductions from the overall value of your assets, such as some investments in small companies (for example, those listed on the alternative investment market, or AIM) and any debts which have not already been deducted in the table opposite.

Once you've worked out the value of your estate (your money, property and possessions), you can subtract the current IHT thresholds.

You won't pay inheritance tax on anything under £325,000*, known as the nil rate band. Under normal circumstances, you'll pay IHT at 40% on the value of your estate over this amount. There is also an additional



allowance if you pass on your family home to direct descendants. It is currently set at £175,000. For any joint assets, just include the value of your share.

These rates are currently frozen until 2028 so be aware that an increase in the value of your estate may push you over the threshold over time.

If you're married, you can combine your thresholds if your spouse will inherit all of your assets on your death. Similarly, if you've been widowed in the past you may be able to claim the IHT thresholds which were unused by your late spouse.

*It may be reduced if you have made gifts within the seven years before your death.

CALCULATE YOUR IHT LIABILITY

YOUR ASSET	VALUE
Your home (after deduction of any mortgage)	£
Any other properties (after deduction of any mortgage)	£
Cash	£
Investments	£
Possessions	£
Life insurance (where not in trust)	£
Trust investments of which you're a life tenant, established following the death of another person	£
Total assets	£
(minus 100% of the property value up to £175,000, or potentially up to £350,000 if you have been widowed*)	£
(minus £325,000 **)	£
Total exposed to IHT	£

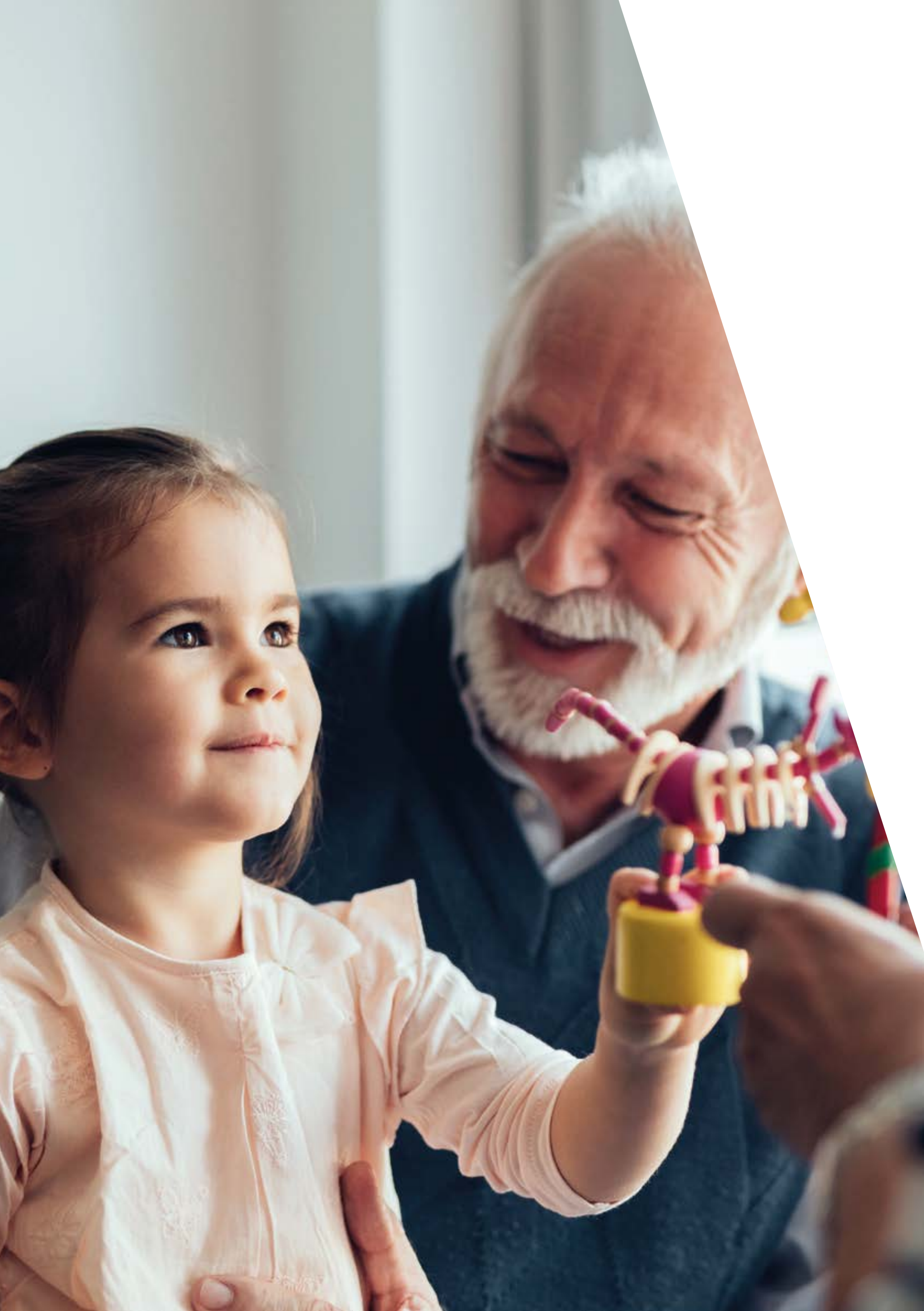
*The value of the main residence nil rate band threshold is only applicable if your main residence is given to a direct descendant and will be reduced, or taken away completely, if your total estate is valued above £2 million on your death.

**Add any additional nil rate band inherited from a late spouse. The figure may be less than £325,000 if you have made any substantial gifts in the seven years before your death.

Please note tax rules are subject to change and benefits depend on personal circumstances. The exact amount of tax payable will depend on your individual circumstances.

40%

The usual rate of inheritance tax



THE BASICS

Before you start reducing your potential IHT bill, you need to have some basics in place.

1: DON'T PRIORITISE SAVING IHT OVER YOUR OWN SECURITY
For now, think of your own needs. You need to strike a balance between making sure you have enough to live on and paying less tax.

Things to consider:
- What you'll need for your lifetime
- What your partner will need if you die before them
- Inflation – rising prices will eat away at the value of your savings
- The possibility and costs of long term care

2: WRITE YOUR WILL
Your will is the foundation of your IHT plan, and legally binding. Writing a will means choosing who will benefit when the time comes, as well as how and when.

If you don't write a valid will, your estate will be subject to intestacy laws, which will determine who benefits. This could differ from your wishes.

3: SELECT YOUR ATTORNEY
You might become unable to manage your own affairs later in life. And making and registering a Lasting Power of Attorney (LPA), to carry out your wishes during your lifetime, can help. This must be in place before you lose the capacity to make your own decisions.

There are two types. One covers financial matters including property, and the other health and welfare decisions. Completing an LPA doesn't mean someone will immediately control your life, they must act with your best interests in mind. They can help you to pay bills or organise care. An LPA can only come into effect when you specify or when capacity is lost.

The benefit is you can choose who can act for you if the time comes. If you don't appoint an Attorney, your relatives will have to apply to the Court of Protection if you lose the ability to make your own decisions. This can be a slow and expensive process. You wouldn't be able to select your own Attorney in this instance, or specify how you'd like your affairs to be managed. The Court would appoint an Attorney for you and this might not be someone you would have chosen yourself.

3

SPENDING, GIFTING AND INVESTING

Three well-known ways to reduce IHT.

1. SPENDING
Spending your money will reduce the value of your estate, and the amount of IHT you need to pay.

It's an opportunity to spend some of your hard-earned cash on things you enjoy, like holidays, the theatre and eating out. But if you buy expensive items like cars and art, these will stay in your estate. Unless you make a real change to your lifestyle, it's unlikely that spending on its own will have much impact on your IHT bill.

2. GIFTING
Money towards house deposits and university fees are great ways to give your loved ones a helping hand for their future.

Gifts like this can reduce the size of your estate and your potential IHT bill, though there are rules.

TYPES OF GIFTS:

- **Exempt gifts** – these are IHT free immediately.
- **Potentially exempt gifts** – these may become IHT free over time.
- **Chargeable gifts** – these might result in an immediate IHT charge.

TAKE CARE WHEN MAKING GIFTS YOU MIGHT:
Lose control. You can't take back a gift or dictate what the recipient will do with it. The gift becomes the property of whoever you're giving it to, so you should consider whether they will be responsible with it.

Lose rights. You'll no longer benefit from any income or capital gain from the gift's value.

You can delay someone receiving the gift and stay in control by using trusts. There's more on this on page 12.

EXEMPT GIFTS

There are several ways you can make gifts free of IHT:

Marriage – married couples can transfer any assets between themselves during their lifetime or on death.

Your annual exemption – each tax year you can gift up to £3,000 to anybody you like. You can also gift any unused allowance from the previous year.

Small gifts – you can gift anyone up to £250 each tax year, provided you haven't already given any other gifts to the same person during the same year.

From extra income – if you have extra income (after tax) that you don't need, you can make regular gifts. You'll need to keep a record of these. You can use form **HMRC IHT403**.

For a wedding – you can give your children up to £5,000 and grandchildren or great-grandchildren up to £2,500 when they get married. You can give anyone else up to £1,000.

To charities or political parties – any donations to these types of organisations, either in your lifetime or in your will, are IHT free. This includes property, shares and land. If you leave at least 10% of your net estate to charity in your will, the rate of IHT reduces to 36%. If you can't find a charity to meet your requirements, it's not complicated to set up your own charitable trust.

The Charity Commission has some simple guidance here:
www.gov.uk/setting-up-charity

POTENTIALLY EXEMPT GIFTS

Outright gifts that don't fall within one of the previous exemptions will usually be IHT free, if you live for seven years or more afterwards. There's usually no limit to the value of these gifts. If you don't live for seven years after making the gift, the portion exceeding the £325,000 threshold will be taxed. The tax due is calculated on a sliding scale based on the time between the gift and death. This is known as taper relief. Please remember that tax rules change and benefits will depend on your individual circumstances.

HOW TAPER RELIEF WORKS

TIME BETWEEN GIFT AND DEATH	IHT RATE
Less than 3 years	40%
3 – 4 years	32%
4 – 5 years	24%
5 – 6 years	16%
6 – 7 years	8%
More than 7 years	0%

The total amount of potentially exempt gifts in the seven years before death which falls within the value of the tax-free threshold will reduce it accordingly, so more of your assets will become taxable.

CHARGEABLE GIFTS

A chargeable gift is one that doesn't fall into the above categories, so it may be charged to IHT immediately. Gifts to a discretionary trust are the most common example.

A charge is usually made if the total value of gifts made in a seven year period exceeds the £325,000 threshold.

Chargeable gift rules are complicated and we recommend you ask for advice. You can speak to our advisory helpdesk on **0117 317 1690**.

3.INVESTING

Some investments offer IHT savings, but they are also higher risk.

BUSINESS RELIEF (BR)

Certain companies qualify for 100% relief from IHT, meaning there is no IHT to pay. You must have held the shares for at least two years prior to your death to qualify.

Provided that it qualifies, you could pass on a family company, business, unquoted shares or AIM-listed shares on your death, without being subject to an IHT charge. There's no limit on the amount you can transfer.

All investments can go down as well as up in value, though you have a greater chance of getting back less than you put in with BR companies. They are more volatile and risky than investing in larger companies.

One of the ways you can benefit from BR is by investing in enterprise investment schemes (EIS). You can start to defer capital gains tax too, if you've held them for more than three years. They can also provide income tax relief, of up to 30% on the first £1million invested each tax year.

EIS companies are usually small companies looking to grow quickly, making them a high risk investment. They're usually illiquid, which means you might not be able to cash in when you want to.

INVESTING FOR CHILDREN

Giving your children and grandchildren a great start in life is usually high on the priority list. And can be part of your IHT plan too.

Junior ISAs – you can add up to £9,000 each year to this tax-efficient account for children under 18. There are two types; a Cash Junior ISA and a Stocks and Shares Junior ISA. Junior ISA's are free from UK income and capital gains tax. The child can access the money in the JISA from their 18th birthday.

Bare trusts – these are the simplest type of trust. You can make a gift into an investment account to create a trust. Usually, it's the child who is liable for any tax. So in practice, there is rarely tax to pay. Although if this type of gift is made from parents to a child and the gross income exceeds £100 per year, all the income will be taxed as if it were the parents. But if you're unsure, it's always a good idea to speak to an accountant.

Junior pensions – these are a great starting point for a child's future retirement. You can add up to £2,880 to their pension each year and receive 20% tax relief from the government, bringing the total amount to £3,600. This can grow free of UK tax. The child will only be able to access the money from age 55 (57 from 2028) or later as pension rules do change.

By adding money into these accounts you'll benefit from an IHT saving if the gift is immediately exempt or if you survive seven years from the date of a potentially exempt gift.

TRUSTS AND PENSIONS

Two lesser-known IHT opportunities

TRUSTS
Trusts are usually used to save tax and keep control of assets. You pick the trustees (which can include yourself) who will make decisions like when, and to who, the trust is distributed.

You can make gifts into a trust, which are held there until the trustee decides it's time for someone to receive them.

The benefit of doing this is so you can stay in control.

Discretionary and bare trusts are the most popular choices. Bare trusts are the simplest type. They're usually set up for a child, with one or two adults acting as trustees. Bare trusts are also known as absolute trusts; the beneficiaries are nominated at outset and cannot be changed. Once they reach age 18 (16 in Scotland), they are entitled to the trust's assets.

For these reasons, they're usually used to save for children where the amounts are smaller and the investor is happy for the proceeds to be paid at age 18.

By using a discretionary trust:

1. You, or other people you've appointed as trustees, are in control of the money until the time is right to hand it over
2. As your family grows, you can choose who benefits, when and by how much
3. Money is usually protected from divorce or bankruptcy

With all trusts:

4. The trustees choose where to invest the money
5. Any growth, income or interest usually sits outside of your estate, and usually you can't benefit from it
6. The seven year clock starts ticking on any money paid into the trust
7. Gifts can be made as a one-off, ad-hoc or regular payments

There are other types of trusts that do allow you to receive income or capital. The most popular are discounted gift trusts and loan trusts.

Trusts can be complicated, so if you're considering them we recommend you ask for advice. You can speak to our advisory helpdesk by calling us on **0117 317 1690**.

Discounted gift trusts provide immediate IHT savings and a regular income.

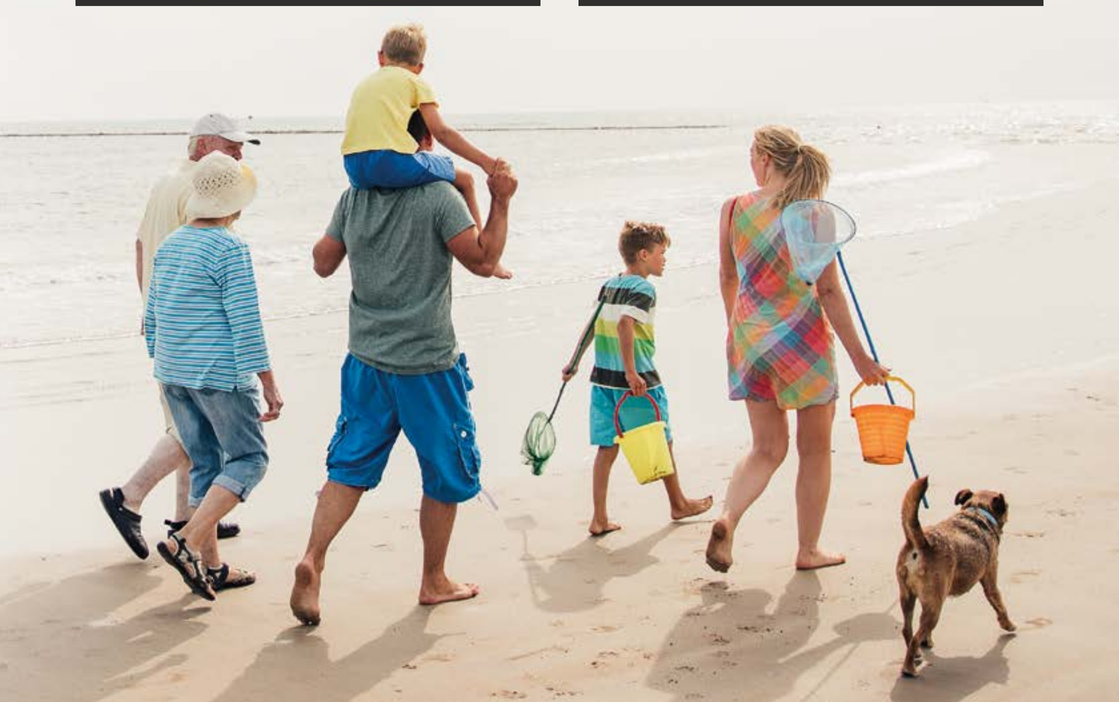
HERE'S HOW:

- A gift is made into the trust, usually of £100,000 or more.
- The gift is split into two parts.
- The first part is treated as a gift and will fall out of the estate after 7 years.
- The second part (the discount) is used to provide income to the investor for life, and is immediately IHT free.
- The amount of the discount is based on the age and health of the investor.
- The longer you're expected to live, the greater the discount, and the larger the immediate IHT savings.

Loan trusts slow down the growth of the value of an estate and the amount of IHT.

HERE'S HOW:

- You loan money to a trust, which is invested.
- As it's a loan you can get full or partial repayment at any time.
- The outstanding loan amount is always in your estate.
- But any growth sits outside and is IHT free.
- The loan is set up interest free and regular repayments can be made to provide an income stream.



PENSIONS

Normally, pensions fall outside of the estate. You can name as many beneficiaries as you like and there's no IHT for them to pay.

If you die before you're 75, and your pensions are below the lifetime allowance currently set at £1,073,100 million, your beneficiaries can usually withdraw what they like from your pension without paying tax.

If you chose to receive an annuity which is paid to a beneficiary after your death, those payments could also be tax-free.

Visit www.hl.co.uk/annuities for more information on annuity options.

If you die age 75 or older, withdrawals will be taxed as the beneficiary's income at their marginal rate (0%, 20%, 40% or 45%, depending on their withdrawals and other income).

If they're a Scottish tax payer the Scottish rates will apply (0%, 19%, 20%, 21%, 42% and 47%, depending on their withdrawals and other income).

WHO WILL BENEFIT?

It's important to let your pension provider know who you'd like to benefit from your pension. You can do this using an expression of wish form. Your nomination is not legally binding, but it does make your intentions clear.

KEEP IT IN THE FAMILY

You could save your loved ones thousands.

Tax rules and benefits are constantly changing, our financial advisers can check you're up-to-date and are making the most of your personal allowances.

We won't waste your time or money.

We'll only recommend you meet a specialist financial adviser if it's right for you.

SPEAK TO OUR ADVISORY HELPDESK
The first step to finding our whether advice could help reduce your inheritance tax liability is to speak to our advisory helpdesk. They are not advisers, but can help you work out if advice could help you and will discuss the charges involved.

If it looks like we could help, we'll book your free initial consultation with an adviser.

You can reach the advisory helpdesk on **0117 317 1690**. Lines are open from 8.30am until 5pm from Monday until Friday.

Or you could book a call back at a time that works for you. Book your call back at **www.hl.co.uk/financial-advice/speak-to-an-adviser**

Questions our advisors get asked

Can I give my home to my children and still live in it, inheritance tax free, if I pay a rent to them?

In principle yes, providing the leasing of the property is arranged on commercial terms. A formal lease/tenancy agreement is wise in these circumstances. It is important to bear in mind:

- The property will no longer be yours: your children could sell at any time or the property could become part of a future divorce agreement or bankruptcy
- The property will become an investment belonging to your children and subject to capital gains tax on the growth in value and income tax on the rent you pay them
- Giving your home to your children will normally be a potentially exempt transfer and will not be inheritance tax free for 7 years

HMRC dislike inheritance tax saving schemes that involve the family home and these are likely to be subject to the greatest scrutiny. If you try any inheritance tax planning that involves the family home, you should work on the basis there is no guarantee of success.

Why do I have to record gifts?

The principle of self-assessment is you should always declare your tax affairs fairly and honestly. When HMRC challenge a tax return or probate, they work on the basis of 'guilty until proven innocent' – the onus is on the executors to prove what has been done. Therefore if your executors do not have clear documentation of your gifts or other inheritance tax plans, inheritance tax is likely to be paid.

How would a professional review my inheritance tax situation?

The first step is to calculate the potential liability and when this might fall due. Therefore they would require full details of your financial circumstances and a summary of your will (if you have made one). Next would be to ensure that you had sufficient income and capital to meet your own needs and requirements. Then the adviser would consider the options available to you to reduce the taxable value of your estate: gifting, use of trusts, life assurance, etc. before making specific recommendations. Reducing IHT often uses more than one strategy.

When is the best time to start inheritance tax planning?

This depends upon a number of factors including the size of the estate, the amount of the liability and when it is likely to fall due.

The majority of investors accumulate assets during their working lives. At retirement, assets are converted from producing growth to income to supplement pensions. Therefore it makes sense for investors to take stock and review their inheritance tax position at or shortly after retirement or upon receipt of a windfall.

How often should I review my inheritance tax plans?

Generally speaking you should review your gifting strategy once a year, since there are various annual exemptions which can be used. Therefore it makes sense to review your inheritance tax plans at the same time. For investment based plans you should review how they are doing at least annually.

What are the tax implications of passing my inheritance on to my children?

If you gift all or part of an inheritance you receive on to your children it is treated as a gift made by you and is subject to normal gift rules. There could therefore be an inheritance tax liability. However, it is possible to alter a will after death in order to avoid inheritance tax. By creating a 'deed of variation', the beneficiaries of a will can agree to change a deceased's instructions in order to distribute assets in an inheritance tax-efficient manner. For example, having the legacy paid directly to your children rather than you. This has to be arranged within 2 years of death. Please note tax rules are subject to change.

ABOUT US

We're Hargreaves Lansdown – a secure, FTSE-listed company helping UK savers and investors for more than 40 years.

GET IN TOUCH

Call us: **0117 317 1690**
(Monday – Friday, 8.30am – 5pm).

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