

**THE NEW IHT Landscape for
SPOUSES AND CIVIL PARTNERS**

Howell-Jones Solicitor Clive Barnard is a member of the Society of Trust and Estate Practitioners and Explains the New Inheritance Tax Rules for Spouses and Civil Partners.

Surrey, 15th October 2008. Throughout this article "spouse" and "surviving spouse" should be taken as referring also to "civil partner" and "surviving civil partner".

Background

It is first necessary to appreciate two fundamental principles of Inheritance Tax namely:

1. All assets left by one spouse to the other are free of Inheritance Tax regardless of the amount.
2. Assets passing to other beneficiaries, such as children, are taxable as follows:
 - (a) the first £312,000 is free of Inheritance Tax. Strictly speaking it is taxable at nil per cent, which is why it is referred to as the "nil rate band".
 - (b) the remainder of the assets are taxable at 40%.

Before 9 October 2007 if spouses left the whole of their estates to each other, the Nil Rate Band of the first spouse to die remained unused. This was not a problem if the combined estates of the spouses was less than £300,000.

However, in all other cases the accumulation of assets in the hands of the survivor gave rise to an Inheritance Tax liability on the second death higher than would have been the case if the Nil Rate Band had been given, on the first death, directly - possibly to children or to, more usually, a discretionary trust of which the beneficiaries comprised the surviving spouse and possibly children and grandchildren.

Changes announced on 9 October 2007

The Chancellor announced that from 9 October 2007 it will be possible for spouses to preserve their nil rate band allowances so that any part of the allowance that is unused when the first spouse dies can be utilised on the second death.

When a valid claim to the whole of an unused Nil Rate Band is made, the allowance that is available when the surviving spouse dies *will be twice the Nil Rate Band* in force at the date of death of the survivor. So let's look at an example:

Harold dies on 14 April 2007, when the Nil Rate Band is £300,000, with an estate of £400,000 which he leaves entirely to his wife Wendy. Wendy dies on 17 June 2009 leaving an estate of £600,000 equally between her two children. When Wendy dies the Nil Rate Band is £325,000. As 100% of Harold's Nil Rate Band was unused the Nil Rate Band available on Wendy's death will be double the nil rate band at that time i.e. £650,000. As Wendy's estate is £600,000 there will be no inheritance tax to pay.

The Nil Rate Band that can be carried forward does not depend on the value of the estate of the first spouse to die. In other words, if the first spouse to die left assets worth less than the Nil Rate Band the allowance that can be carried forward will not be reduced. So a case below, might show:

Similar circumstances to the above example, but Harold leaves an estate of £20,000 only. Nevertheless the Nil Rate Band available on Wendy's death will still be £650,000.

If part of the Nil Rate Band of the first spouse to die has been used e.g. by making gifts to children or grandchildren, then a proportion only of the Nil Rate Band can be carried forward. Looking at a third possibility:

Similar circumstances to the first example above but Harold leaves an estate of £250,000 of which he gives £125,000 to his children and the balance to Wendy. As he has used 50% of his Nil Rate Band of £300,000 the amount available on the second death will be 50% of £325,000 i.e. £162,500. Thus the total tax free amount will be £487,500 (£325,000 + £162,500).

Do you need to take any action if you have already made Wills contained Discretionary Trusts of the Nil Rate Band?

There are no longer any major inheritance tax advantages in incorporating discretionary trusts of the Nil Rate Band in Wills.

However there are still benefits e.g. if the surviving spouse needs to enter a Care Home and the matrimonial home has to be sold to meet the fees payable, any assets in the trust should be safeguarded for the benefit of the children and grandchildren. The clients will therefore have the comfort of knowing that at least the amount of the Nil Rate Band will be inherited by their family rather than eroded by 40% Inheritance Tax.

Therefore Wills containing discretionary trusts of the Nil Rate Band have the benefits listed above without having any disadvantages.

This article sets out some of the effects of the new law, which came into effect in July. Specialist advice, preferably from a member of the Society of Trust & Estate Practitioners, should always be taken when preparing a Will.

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