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underlining the need for quality IHT advice



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Colin Jelley assesses the proposed changes to inheritance tax (IHT) in the 2007 pre Budget report and their impact on the advice process.

You would be forgiven for thinking that when the media widely reported a doubling of the nil rate band (NRB), that the current NRB of £300,000 would grow to £600,000. Alas, what the Chancellor actually announced was that the NRB would now be transferable to spouses and civil partners* where it was not used on first death.

As our 'Soapbox' poll shows on the opposite page, many of you who have reviewed the proposed changes to IHT in the pre Budget report have concluded that in many cases the proposals will not make any difference. Clients who have recognised that they have a significant IHT liability, and have sought advice, will already have accounted for both their own and their spouse's or civil partner's* NRB under existing wills.

However, it is still important to understand the proposals fully and how this will affect your advice process.

the proposals

Under the current rules transfers between spouses and civil partners are generally exempt from IHT, with any unused NRB potentially 'wasted' on first death. The pre Budget report proposals are intended to enable the unused NRB on first death to reduce the IHT liability on the surviving spouse's or civil partner's estate. On the death of the survivor any unused NRB from the first death would be available for the personal representatives of the estate to claim. The maximum NRB available to the estate of the survivor would be twice the standard NRB, hence the reported 'doubling' of the NRB to £600,000.

Where part of the NRB had been used on the first death, the amount of the NRB available to be transferred will be based on the proportion of the NRB that was unused, as illustrated in the following example.

Example

On first death the chargeable estate is £150,000. The NRB is £300,000 and therefore 50% of the original NRB is unused. When the surviving spouse or civil partner* dies the NRB is £350,000, which would be increased by 50% to £525,000.

**£350,000 NRB + 50% of £350,000
(£175,000) = £525,000 NRB**

maximum benefit

The amount of additional NRB that can be accumulated by any one surviving spouse or civil partner* will be limited to the NRB in force at the time of their death. Where a person dies having survived more than one spouse or civil partner*, they will be able to benefit from the unused NRBs from each earlier death, but still subject to the same maximum limit of just one additional NRB.



how to make a claim

Any claims for transfer of unused nil rate band amounts will be made by the personal representatives of the estate of the surviving spouse or civil partner* when they make an IHT return.

While the legislation will be not be introduced until the Finance Act 2008 and despite the claim not being made until the death of the surviving spouse or civil partner,* it is clear that there will be a requirement to keep sufficient records including copy documents from the first death to enable a claim to be successfully processed. For recent deaths these may be obtained very easily, but may prove more difficult for deaths that happened many years ago.

should you use the NRB on first death?

Some commentators have suggested that it might be better not to use the NRB on first death under a will trust –

instead choosing to take a view that future increases in the NRB will exceed asset growth, as well as avoiding potential future ten-yearly periodic and exit charges where the will creates a discretionary trust.

Clearly, the more cautious among us may well consider the security of using the relief as and when it is available as a better option, but this point alone is a clear advice issue. The risk of controlling the distribution of assets versus the potential future savings in tax has added a new dimension to using an individual's nil rate band.

going forward

No matter which approach is taken, it is clear that a well documented audit trail will be imperative. There is no doubt that the pre Budget report has further underlined the need for quality IHT planning advice. ■

*As defined by the Civil Partnership Act 2004.

This article is based on Skandia's interpretation of the law and HM Revenue & Customs practice as at 30 November 2007. We believe this interpretation to be correct but cannot guarantee it. Tax relief and the tax treatment of investment funds may change.

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An insert will be available for Skandia's client guide to inheritance tax and trusts in early 2008 to explain these proposals, including a technical note on 'how to make a claim'.

informer Live! Soapbox poll

over half of advisers say proposed IHT changes will make little difference to clients.

Our latest informer Live! Soapbox poll asked if you felt the Chancellor's proposed changes to inheritance tax in the pre Budget report would be good for your clients. Over half of you (53%) believe it will make no difference to your clients, with 26% believing it will be good for your clients and 21% saying it will not be good.

Phil Carroll, Skandia UK Tax and Estate Planning Manager, comments:

'Clearly the majority of advisers recognise that with planning it was possible to make use of the inheritance tax nil rate bands of both individuals. The Chancellor's announcements will simply create another method to achieve this.

People who have never been married and those who are divorced will see no change to their situation. The real beneficiaries of the changes are those widows and widowers whose spouses did not fully use their NRB. The need for careful planning and tax administration has not gone away'.

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