

RESIDENCE NIL RATE BAND

When an individual passes away, their Estate (i.e. the value of all sole and jointly owned assets at the date of their death) is subject to inheritance tax ('IHT'). For IHT purposes, each individual has a nil rate band ('NRB') allowance. Currently, the first £325,000 of an Estate is taxed at 0% and there will be no IHT. However, the remaining Estate over the NRB is liable to IHT at 40%.

NRB is frozen at £325,000 per person until 6 April 2021

Normally on the first death of a married couple there is no IHT payable in relation to what the surviving spouse inherits due to the 'spouse exemption'. However, when the surviving spouse dies and the next generation inherits the Estate, it is likely to be liable for IHT at 40%.

Background

Property values have risen in recent years. Average property prices in Cobham, Surrey are at just over £1,000,000. The forecast from Savills estate agents is that property prices in the area will increase in the next 5 years by 25.7%, which means... more IHT!

Her Majesty's Revenue and Customs ('HMRC') demand prompt payment from Personal Representatives ('PRs') administering the Estate. A proportion of IHT attributable to a property is due roughly 6 months after death. The PRs may still not have access to the Estate assets or there may be limited cash available. Banks can choose to pay from the deceased's bank account directly to HMRC in this situation.

If the Bank does not pay directly to the HMRC, PRs must find another way to raise the IHT, normally by taking out a bridging loan. This escalates the pressure to collect in the assets as quickly as possible to repay the loan and limit the amount of interest arising. Such stress is, of course, unwelcome in a period of mourning.

Married Couples & NRBs

In 2007, the Transferable Nil Rate Band was introduced which allows married couples to make use of both NRBs on the second death. If the first spouse to die has unused NRB after their Estate has been administered, then the unused percentage of this NRB can be claimed by the surviving spouse's PRs. However, with rising property prices and a freeze on the current NRB figure of £325,000 until April 2020, the IHT net is still cast widely.

The Government announced in the July 2015 Budget a new 'residence nil-rate band' ('RNRB') which was welcomed by many. This will come into effect from **6 April 2017**. It is a means of achieving the Conservative Party's manifesto promise to increase the IHT NRB to £1 million for married couples/civil partners.

The new relief will be available when the deceased's main residence is passed on to direct descendants (e.g. spouse, children or grandchildren) and the allowance will **increase from £100,000 in 2017/18 up to £175,000 in 2020/21** before rising in line with the Consumer Price Index from 2021/22. Any unused RNRB percentage can be transferred to a surviving spouse's Estate.

Downsizing

In later life, many people downsize their family home or find that they need to sell their property in order to pay for care home fees. To help people in this situation avoid missing out on the RNRB, the Government has introduced an 'additional RNRB'.

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The proportion of the RNRB that may have been lost as a result of downsizing or selling the property will be taken into account when calculating the relief available. The new property or assets of an equivalent value to the lost RNRB must still be left to a direct descendant and the sale of the main residence or the downsizing must have occurred **after 8 July 2015**.

The Finer Details

The RNRB is designed to assist those who find themselves hit by IHT because of rising property prices. However, there are limits on when it can apply.

The allowance is tapered if the value of the gross Estate is above £2 million and is not applicable if the gross value exceeds approximately £2.34 million. There will be a divide between people who will find that the RNRB will help reduce or eliminate their IHT bill and those whose Estates are valued above £2 million (not just the value of the property). The latter will find that there may be little or no relief.

Another important limitation is that the RNRB can only be used on death and cannot be used against a gift of the property made during lifetime. It is still unclear how the RNRB will interact with transferable RNRBs from previous marriages, with post-death variations to the Will or if the property has been left in trust.

We await the finer details on the application of the new RNRB allowance and will observe HMRC's response to claims to see how the allowance works in practice. As with all tax allowances, it appears that the new RNRB is not the straightforward windfall the headlines suggest.

Action

Ensure any existing Wills are reviewed and amendments made if, for example, there are provisions which would deny the new relief (e.g. nil rate band trusts, contingent interests for grandchildren vesting later than at 18 etc.)

If you would like to make an appointment to discuss tax-planning and your Wills or for assistance administering an Estate, contact our Head of Private Wealth Julie Man on 01932 590643 or email julie.man@mundays.co.uk.