

## **INHERITANCE TAX PLANNING**

### **Opportunities for Non-UK domiciled Individuals**

See our general guide on the cross border aspects of UK Inheritance Tax and how it interacts with Irish inheritance tax. An individual who is domiciled (long term home) in Ireland is only subject to UL inheritance tax on assets situated in the UK. This give the opportunity for non- UK domiciled individuals to avoid UK inheritance tax by putting their assets into non-UK wrappers e.g. a Jersey company so that the asset passing on death (the shares) is not situated in the UK for tax purposes. There are opportunities for certain individuals to create trusts in advance of becoming UK domiciled.

### **Outright Lifetime Transfers**

The making of an outright transfer to children (or indeed anyone else) is exempt from UK Inheritance Tax provided the person giving the gift survives for seven years. However, it may be subject to UK CGT and Stamp Duty or stamp duty land tax in the case of certain assets. UK CGT does will not apply to a non-resident. However, if the donor or recipient is resident in Ireland then Irish CGT or Inheritance Tax or both may arise.

As in Ireland, the gift of income producing assets to children will generally be regarded as the income of the donor from an income tax point of view. If the child is unmarried and under 18 years of age income tax rules provide that the income is taxed as if it is still the income of the parent. These provisions apply for as long as the child is under 18 and unmarried.

The seven years rule under UK Inheritance tax is an important exemption which has no equivalent in Irish Inheritance tax and indeed in the inheritance tax legislation of most countries. Because of the scope for abuse, there is anti-avoidance legislation which applies where transfers are made but some kind of reservation of benefit or conditions

are placed purporting to give control to the transferor. These transfers are not regarded as outright transfers.

If there is any so called "reservation of benefit" in favour of the person making the gift the arrangement will not be regarded as an outright gift and will not be effective for Inheritance Tax purposes. This means it will still be part of the estate of the person making the gift when he dies, as if he had not gifted it at all.

A reservation of benefit arises where there is a disposal of an asset but full possession and enjoyment is not bona fide assumed by the recipient. If, for example, ownership of a painting or valuable asset is given to a child but remains in the parents' house this would be regarded as a reservation. Likewise if a holiday home is passed but the parent uses it as before, there would also be a reservation. If the reservation or limitation is removed then there would be an outright gift which may be exempt from Inheritance Tax after a further seven years.

There are some exceptions which the Revenue allows by concession. An example is where a parent has occasional stays at a house given to the children or uses a gift motor car on a very limited number of occasions.

### **Basic Trusts**

A tax management technique is to leave the "nil rate" allowance for Inheritance Tax in a trust for the benefit of family and to leave the balance to a spouse. This is known as a "nil rate band" discretionary trust. As the trust is of the nil rate amount no Inheritance Tax will be chargeable during the first ten years. There are certain conditions and there must not be a so called "related" trust

Another straightforward trust technique may be appropriate for a person who wishes to provide for his spouse in the event of their death yet incorporate flexibility for his family members. This is often achieved in the UK by way of a discretionary trust of which the

spouse and children are potential beneficiaries with a life interest for the spouse. There may be also overriding powers to give capital to the spouse or other family member.

The spouse qualifies for exemption from Inheritance Tax or her life interest (i.e. her right to the income) If capital is also appointed to the spouse no Inheritance Tax will apply. If the power is exercised in favour of other beneficiaries, the ending of the interest in possession may qualify as a transfer of value which would be deemed to operate as an outright gift so that if the life tenant (e.g. the spouse) does not die within seven years, may pass free from Inheritance Tax in the same way as an outright gift.

### **Marriage and annual Gifts**

Each parent can give £5,000 to a child on the occasion of marriage. Each parent can make annual gifts of £3,000. Each parent can enter insurance policies for the benefit of children out of normal expenditure. In order to claim these exemptions each parent must have sufficient income to make the gift.

### **Insurance policies in trust**

Expenditure out of income is exempt. An important tax planning technique is to use ordinary expenditure to fund life policies written in trust. By being written in trust they will not form part of the deceased person's estate.

Insurance on a tax payer's life is a useful method of dealing with predictable Inheritance Tax liability. It may generally be possible to fund an insurance policy out of the general £3,000 exemption or on the basis that it is part of normal expenditure. The policy should be written in trust so it does not form part of the estate but accrues for the benefit of the persons who will have the tax liability e.g. children.

### **Putting Property in multiple names**

Inheritance Tax arises in relation to inheritances arising when jointly held property passes automatically on the death of the other owner. Having assets in two names as

tenants in common may have Inheritance Tax advantage in that half the value passes to third party beneficiaries on each death. This may be more tax efficient in that the inheritance tax zero rate of two individuals may be available as each half is passed. The need for this course has been reduced since 2008 because spouses can pass their unused zero inheritance tax rate to the other.

Apart from the 2008 legislation there are still substantial tax advantages in placing assets in two or more names. Each owner would be entitled to Income Tax and Capital Gains Tax allowances and lower rates in respect of each half share of the income or sale proceed. Unused tax Income tax and capital gains tax allowances cannot be transferred between spouses nor can they be carried forward. Therefore it is best to split the ownership of assets between spouses for this purpose.

### **Rearranging Affairs within two years of Death**

English Inheritance Tax provides a useful mechanism by which beneficiaries and trustees can re-arrange the terms of a will after death by agreement of them all. This has the advantage of allowing a will to be rearranged so that a more favourable inheritance tax result ensues. It allows beneficiaries to redirect benefits to other members of the family who are less well provided for. It is also possible to disclaim benefits so that they are passed down by a child to a grandchild without a double charge of taxation. If the variation is agreed it is treated as if the new arrangement was in the deceased's will or arose at intestacy law. There is an equivalent Capital Gains Tax relief

Inheritance Tax applies on the basis of the amended variations but the beneficiary who redirects the benefit suffers no tax consequence. The variation must be undertaken in writing within two years of the deceased's death. It must state that a certain section of the Inheritance Tax Act applies before it applies to it. The consent of the Court is required for variations by beneficiaries who are under eighteen or do not have mental capacity.

If assets are distributed from a discretionary trust within two years of death, they may be distributed under certain conditions without exit charge to Inheritance Tax. In effect the will is treated as if the property was left directly. In order for this condition to apply there must be no interest in possession in the property. No event must occur within the two years which would otherwise be chargeable to tax e.g. a distribution of trust property to beneficiaries.

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This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.

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