Gifts and exemptions from Inheritance Tax

Overview

Making a gift to your family and friends while you're alive can be a good way to reduce the value of your estate for Inheritance Tax (IHT) purposes and benefit your loved ones immediately. But estate and tax planning is a complex area. So getting professional advice can help you avoid several big pitfalls when making a gift.

How much can I give to my spouse or civil partner tax-free?

Married couples and civil partners can pass their estate to their spouse tax-free when they die. In other words, the surviving spouse can inherit the entire estate without having to pay Inheritance Tax. They can also pass on their unused tax-free allowance to their spouse. For example, if a husband dies and his estate was under £325,000, his wife can take his allowance and add it to her own tax-free allowance.

How much can I give to my children and family tax-free?

How much you wish to give your children or other members of your family is completely up to you. But to ensure that it's tax-free, it's **important to plan** Simply put, so long as you live more than 7 years from when you make this gift, your children or family won't have to pay IHT on your gift when you die.

But if you don't live more than 7 years after you've made the gift, they may have to pay IHT. In this situation, your gift becomes known as a 'potentially exempt transfer (PET).

You should also bear in mind that your gift could incur other types of tax, such as Income Tax or Capital Gains Tax. A gift of shares for example, may incur Income Tax.

If you're thinking about giving away money or assets to your family and friends to reduce Inheritance Tax, it's very important you make a record of the following -

- Who you gave it to
- When you gave it
- What you gave
- How much it's worth.

This will make it easier for the executor of your estate to work out during probate what parts of your estate are liable for tax.

How much can I give to charity tax-free?

There is no limit to how much and how often you can give to a charity without incurring Inheritance Tax. You could also get some relief on other types of tax such as Income Tax, when you do this.

If you leave at least 10% or more of the 'net value' of your estate, it's possible to reduce the rate of Inheritance Tax on some assets from 40% to 36%. This could save thousands of pounds.

How much is the annual 'gift allowance'?

While you're alive, you have a £3,000 'gift allowance' a year. This annual exemption means you can give away up to a total of £3,000pa without incurring IHT.

Gifts that are worth more than the £3000 allowance are subject to Inheritance Tax. The amount of tax to pay on these gifts depends on whether it was given within 7 years before the person died.

You can carry over any leftover allowance from one tax year to the next, up to a maximum of £6,000. If you do this, you have to use up all your allowance in that tax year. In other words, you can't accumulate several years' worth of allowance and use it up in a single large gift.

What else can I give tax-free?

- **Gifts worth less than £250 -** You can give as many gifts of up to £250 to as many people as you want. Although not to anyone who has already received a gift of your whole £3,000 annual exemption. None of these gifts are subject to IHT.

Gifts & Exemptions from Inheritance Tax

- **Wedding gifts -** if it's given to a child and is worth £5,000 or less, or given to a grandchild or great-grandchild and is worth £2,500 or less, or given to another relative or friend and is worth £1,000 or less.

- **Gifts to help with living costs -** to help pay the living costs of an ex-spouse, an elderly dependent or a child under 18 or in full-time education are exempt.

- **Gifts from your surplus income** - if you have enough income to maintain your usual standard of living, you can make gifts from your surplus income. For example, regularly paying into your child's savings account, or paying for a life insurance for your spouse or civil partner. To make use of this exemption, it's very important that you keep very good records of these gifts. Otherwise, Inheritance Tax is very likely to due on these gifts when you die. The rules for this exemption are complex - for example, these gifts must be regular, so you need to be committed to keeping up with making these gifts. It's best to speak to a legal adviser first if you want to use this exemption. If you get it right, this is a good way of making gifts on birthdays or at Christmas, or even to pay life insurance premiums. .

- **Charitable gifts -** if you give a gift to a charity, museum, university or community amateur sports club, this is exempt from tax.

- **Political party gifts -** you can give an Inheritance Tax-free gift to a political party under certain conditions.

What is a 'potentially exempt transfer'? (PET)

You don't immediately incur IHT when you make certain gifts while you're alive. And if you live more than 7 yrs after you've made the gift, it becomes fully exempt from IHT. During that 7 yr period, your gift is a 'potentially exempt transfer' or PET, but if you do not survive the gift by 7 yrs, the exemption fails. The PET is now part of your estate, and subject to IHT. How much tax is due depends on when it was given.

Gifts where you still have an interest in it - no matter when you've given it - don't qualify as a PET. For example, if you continue to live for free in the house you gave your child more than 10 years ago. The house is still part of the estate and subject to IHT. This is known as "reserving a benefit" in the property.

What else is exempt from Inheritance Tax?

Certain other assets are exempt from IHT , or at least eligible for a reduced rate, and these include –

- Business
- Agricultural property
- Woodland property
- Heritage assets

Clearly the above areas are "specialist" and require appropriate input from an expert adviser

In conclusion

When you make your will, it's always a good idea to plan your estate and what should happen to it when you die. Making gifts and transfers in your lifetime is one way of planning your estate and It's a good way of reducing IHT. But the law in this area is quite complex so please seek advice from a solicitor/IFA.
Speak to us in the first instance and we will work together with your solicitor, or introduce you to one, in order to make the most appropriate plans for your estate.

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