Case study / Tax Consultancy

Inheritance tax / £100,000 savings (expected)

Managing exposure to IHT and CGT on an estate of approximately £1.25m with 6-figure savings.

The problem

Mr X, who was in his mid 60s and recently widowed, approached us for advice on Inheritance Tax (IHT). His total estate was around £1.25 million and as a result IHT was a potentially significant issue.

His estate included his home valued at around £600,000, a second property worth around £400,000 and investments of around £250,000. He also had a significant pension which met his day-to-day needs for income. He has three grown up children, one of whom lives in the second property. He was concerned that on his death he could have a significant IHT liability.

The solution

We analysed Mr X's position then prepared a report for Mr X setting out the basic IHT position (a potential IHT liability of over £100,000) and then explained the various ways in which IHT can be reduced through gifts and exemptions. We then applied the basic principles to the specific situation of Mr X. Whilst giving away his house might solve the IHT problem, it would be impractical as he needed it to live in. Since the second property generated no income and he didn't need the income generated by the investments, he could potentially give away all of these which would mean that after 7 years there would be no IHT on the gifts. However, closer analysis of the reliefs available, including in particular the new residence nil rate band, showed that if he gifted either the second property or the investments, the balance of his estate would be covered by nil rate bands. Given his son's occupation of the second property, a solution was to transfer part of the property to trust now such that that part suffered no IHT and to transfer the balance in seven years when the original gift will have fallen out of account. There would be a small amount of Capital Gains Tax to pay on the transfer as the property had only increased in value by a small amount since purchase. Once in the trust, the property was then out of Client X's estate and also not in the estate of his children and therefore protected from divorce etc. Due to his son's occupation, main residence relief should be available to the trust on any future sale of the property. Expected savings for client - £100,000.

We said

"The solution to our client's problem required a consideration of IHT, CGT and SDLT together. Assuming Mr X survives for 7 years, the use of a trust will save over £100,000 of IHT and allow future gains on the second property to be free of CGT because his son's occupation of the home under the terms of the trust will qualify for main residence relief. It also puts assets into a secure and flexible environment to provide for his children and grandchildren."
Alan Ross, Tax Director,
Wilson Partners