

A Guide to Inheritance Tax and Gifting



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Our Wealth Planners are here to help you take control of your finances and provide you with the confidence you need to go after the things that matter to you.

Succession Wealth Management Limited is a large national UK financial advice firm. Our teams of Wealth Planners deliver high quality independent advice to thousands of clients across the UK, and we're committed to helping people achieve more with their money.

Our clients are at the heart of everything we do and looking after their wealth journey is a privilege to us. The relationships we build last longer than a lifetime, and we are proud to provide advice across generations. When you choose to work with us, we promise to provide an exceptional personal service tailored to your unique financial aspirations.

Inheritance Tax (IHT) and Gifting

There are many things we would like to leave for our loved ones when we pass away, from fond memories to heirlooms, but the one thing we don't want to pass on is a hefty IHT bill.

There are several things you can do to help lessen your IHT burden, including making gifts during your lifetime. This guide provides an overview to help you understand what the tax is, and some of the measures you can take to help to mitigate it.



How much tax will I have to pay?

According to a report published by HMRC, in 2020-2021, only 3.73% of deaths in the UK resulted in an IHT bill. This is because IHT is not paid on the total value of your estate, but on the value of your estate above certain thresholds.^[1]

The main threshold is known as the nil-rate band, and up until the 5th April 2028 is set at £325,000. On top of this, there is also the residence nil-rate band, which grants a £175,000 exemption and is conditional on the main residence being passed down to children or grandchildren. This brings the threshold up to £500,000. If the value of your assets is higher than the nil-rate band, your estate may be liable for a 40% IHT charge.

Here's an example. If a person died with an estate worth £675,000 and left their main home to their child, they would typically pay IHT on the value of their estate above the £500,000 threshold.

A 40% tax bill on this £175,000 would leave their family with a final tax bill of £70,000.

On the flip side, if the value of your estate does not exceed the thresholds when you pass away, your family would not need to pay any tax at all.

What tax benefits do couples get?

One notable exception to the rules regarding IHT is that if you are married or have a civil partnership, your partner could inherit your entire estate without having to pay an IHT bill.

Your partner also inherits any unused IHT allowance when you pass away. This includes both the nil-rate band of £325,000 and the residence nil-rate band of £175,000. This means that if you didn't use any of your allowances, they'd have an allowance of £1 million instead of £500,000. (As long as you leave your home to your children or grandchildren).

Important

Note that there will be a tapered withdrawal of the additional nil-rate band for estates with a net value of more than £2 million. This will be at a withdrawal rate of £1 for every £2 over this threshold.

A brief history of Inheritance Tax

Essentially, IHT is a tax on the estate of a person who has passed away. This includes their money, property, and possessions.

IHT has existed in one form or another since roughly the 17th century. It was first brought about in 1694 to help finance a war against France and, over the years, it has had various incarnations.

- Probate Duty 1694
- Legacy Duty 1780
- Succession Duty 1853
- Estate Duty 1889
- Capital Transfer Tax 1975
- Inheritance Tax 1986

[1] 26th July 2023 | Inheritance Tax statistics: commentary | Gov.uk

Gifting and Inheritance Tax

IHT bills can be quite steep, but thankfully there are ways in which your tax bill can be reduced.

Giving gifts is a simple way to reduce the value of your estate when you die, and to reduce the size of your overall IHT bill.

Before we get into any of the details regarding gifting, it's important to note that you should always keep accurate records whenever you are giving a gift.

These records should include:

- What gift you gave
- Who you gave it to
- When you gave it
- How much the gift is worth

These records can help the executor of your Will to work out the total value of your estate when you've passed away. If you do not, your estate may be liable for more IHT than it should.

When gifting as part of estate and IHT planning, there are two different kinds of gifts. The first are those that are considered outside of your estate immediately. Others are potentially exempt depending on when they're given and when you pass away.

What gifts are free from Inheritance Tax?

1 — Potentially Exempt Transfers (PETs)

Theoretically, you can give gifts of unlimited value, and they won't be considered part of your estate for IHT purposes, as long as you give the gift more than seven years before you die. These gifts are called 'Potentially Exempt Transfers' because they may be exempt from the value of your estate when calculating IHT, providing you survive another seven years.

If you do not survive for the further seven years, then the value of the transfer is added to the value of your estate when calculating your tax bill. This is called the 'seven-year rule'.

However, it's also important to note that PETs must meet certain conditions and are subject to exemptions. For example, you can only gift to another individual or into some trusts (not all gifts to Trusts are considered as PETs), so a gift cannot be made to or from a company.

If you decide to make a sizeable gift but then pass away before those seven years are up, IHT may be due. However, there is a sliding scale of the tax depending on how long you survived after making the gift.

The table below shows the reduction in IHT on the gift depending on how much time has elapsed:

Years between gift and death	Tax to pay on gift
Less than 3 years	40%
3 – 4 years	32%
4 – 5 years	24%
5 – 6 years	16%
6 – 7 years	8%
7+ years	0%

What gifts are free from Inheritance Tax

2 — Gifts to spouse or partner

You don't have to pay IHT on any gifts you give to your spouse or civil partner. This means you can gift your partner as much as you like in your lifetime, as long as they live in the UK permanently.

Furthermore, married couples and civil partners are allowed to pass on their entire estates to their spouse tax-free when they pass away.

As we mentioned earlier, partners can also inherit their deceased spouse's unused IHT allowances.

For example, if a husband dies and leaves his entire estate to his wife, she can take his unused tax allowance and add it to her own.

3 — Annual exemption

Each tax year (6th April to 5th April) you can give away £3,000 worth of gifts without their value being added to your estate. This is called your 'annual exemption'.

This exemption can be carried over from the previous year, but only up to a value of £6,000, so if you're looking to use gifts to reduce the value of your estate, you need to carefully manage it.

4 — Small gifts

You can give as many gifts of up to £250 to as many individuals as you like in any tax year. However, you cannot give one of these gifts to someone who has already received your whole £3,000 annual exemption.

5 — Weddings

Marriages and civil ceremonies are another opportunity to give gifts tax-free and the amount that you can gift varies depending on who is getting married.

Typically, you can give a gift of up to £1,000 per person without the amount being included in the value of your estate.

However, this amount may be greater if you're gifting to family. If one of your children is getting married, then you can give up to £5,000 without it being added to the value of your assets, while you can gift up to £2,500 to a grandchild or great-grandchild.

6 — Gifts from income

If you have enough income to maintain your usual standard of living, you can gift surplus income - for example, by paying it into a child's savings account.

This can be a very valuable IHT exemption, but it is also complicated, and this is why it's particularly important that you keep good records of your gift-giving if you're planning to gift in this manner.

For this exemption to apply you must meet three conditions:

- The gift must be made out of income 'taking one year with another'.
- The gift formed part of your normal expenditure – this generally means that the gift should be regular in terms of value and frequency.
- You should be left with enough income to maintain your standard of living.

One of the tests that HMRC use to determine whether gifting in this way is allowed due to excess income is to see whether the gifts you give are regular. Typically, there needs to have been an established pattern of gift-giving to satisfy them that it is a normal expenditure. Because of this, if you do intend to gift in this way, make sure that you can maintain the regular payments, and keep good records.

For example, Mr Smith is 80 years old and retired. He has a steady income of £60,000 per year, consisting of pensions and investment income. He can save £2,500 per month or £30,000 per year.

For the last five years, Mr Smith has been making regular monthly gifts out of his surplus income of £1,000 per month to his son and daughter. As he has been giving the gift regularly for such a long time, HMRC will likely accept that this is a normal expenditure.

If HMRC does accept these gifts are part of his normal expenditure, Mr Smith will still be able to make use of his annual £3,000 IHT allowance.

Leaving gifts in your Will

If you want your money to go to a good cause after you die as well as reducing your IHT bill, you may want to consider leaving some of your money to charity in your Will.

To encourage more people to give money to charity, any cash, or asset that you leave to a charity, either during your lifetime or in your Will, will be exempt from IHT.

Furthermore, leaving money to a charity in your Will can reduce the overall amount of IHT that is due on your estate. This can potentially also bring the value of the estate below the threshold of the nil-rate band, in some cases.

If you leave at least 10% of your estate to charity in your Will, the Government will reduce the amount of IHT you have to pay, meaning that you will pay a 36% tax instead of a normal 40%.

This can mean that not only would you be helping a charitable cause, but you could reduce your tax bill.

Reliefs when gifting certain assets

Certain assets also receive relief from IHT when they are gifted, although to successfully get relief they must meet certain criteria:

— **Business Property:**

If you own a business, you may be eligible for Business Property Relief, which can reduce the value of a business property by up to 100% when it's being transferred. This transfer can be made in life or as part of a Will, as long as the business has been owned for at least two years.

— **Agricultural Property:**

If you own a farm, you can pass it on free from IHT, although it must meet certain conditions. Certain farm assets, such as agricultural machinery, are also not exempt.

— **Woodland Property:**

Woodlands used for commercial purposes can potentially get IHT relief of up to 100%. If the land is used for timber, the tax can also be postponed until the trees are felled, provided that you have owned the woodland for five years before your death.

These are only a few of the variety of reliefs that you can potentially apply for but working out which properties are eligible for relief can be confusing. There are also many other steps that may be appropriate for you if you're worried about IHT.



Contact us

If you would like to discuss this, or any aspect of financial advice with one of our Wealth Planners, feel free to email us at hello@successionwealth.co.uk or call us on 0800 051 4659 and we will arrange for someone to contact you.



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The information in this guide is based on our current understanding of taxation legislation and regulations. Any levels and bases of, and reliefs from, taxation are subject to change and tax implications will be based on your individual circumstances.

The value of your investment(s) and the income derived from it, can go down as well as up and you may not get back the full amount you invested.

You should seek legal advice to ensure that your Will reflects your wishes and is legally binding.