Planned Succession
Personal Estate & Business Succession Planning

The Society of Will Writers

Inheritance Tax (IHT) planning and your family home

For the majority of people the family home is their most valuable asset and, through house price inflation alone, more people than ever will be subject to IHT. Whilst there are ways to mitigate it, taking the value of one's home out of this trap is far from easy and, for most of us, all but impossible.

If you are married or in a civil partnership things are a bit easier, in that at present there is no IHT between spouses or civil partners. If, however, you're not married etc., then the situation is very different, in that regardless of whether you have a Will or not if the value of the property exceeds what is called the Nil Rate Band (NRB) being the amount that one can give away free of IHT (it currently stands at £325,000), the balance will be taxed at 40%. That means on a property valued at, say, £650,000, the estate would have to pay out £130,000 in tax. If the only asset is the house, then where will the money come from?

Whilst it's possible to give your property away during your lifetime, there are six things to watch out for: -

1. If the value of the gift is more than the NRB, then it'll be treated as something known as a Chargeable Lifetime Transfer (CLT) and will attract entry, periodic and exit charges, albeit that could still work out less than the 40% charge upon death.
2. Regardless of the value, the gift may well be classed as a Potentially Exempt Transfer (PET) which, in broad terms, means that for IHT purposes it stays in your estate for the first four whole years but tapers off to zero over the next three.
3. If you continue to live in the property and don't pay a market rent, then it's what's called a Gift with Reservation of Benefit (GROB) and, for IHT purposes, the gift is treated as still being in your estate.
4. The person to whom you've given the property may themselves end up an IHT problem as well as a Capital Gains Tax (CGT) one and, if you are paying a market rent, an income tax liability.
5. By giving away the property you lose your security, in that you'll be exposed to whatever happens to the new owners, such as the property having to be sold if they get into debt, suffer a bankruptcy or get divorced etc..
6. If the gift is not what is known as being at 'arm's length', i.e. the recipient is wholly unconnected such as an equity release provider, it may be subject to Pre-Owned Assets Tax (POAT).

It's not all doom and gloom though, in that it is possible to give a share in the property to someone else (an adult child say) and who shares the running costs of the home. This must be a permanent arrangement, and you will need to provide HMRC with evidence proving that the other person is also responsible for their share of the maintenance costs. If that is not the case, or if the other person moves out at a later date, then the value of the property will be added to your estate once again.

Trying to remove one's home from the IHT trap is difficult, fraught with dangers and not something one should lightly do. That said, for some people it does represent a legitimate IHT mitigation strategy but be very careful before acting.

There is the much vaunted increase in the NRB to include up to £350,000 from the value of one's main residence, which will not fully apply until 2020 and only then if the money's going to 'direct' heirs, i.e. children, stepchildren, adopted and foster children, and grandchildren and the estate includes a family home worth at least £350,000. That said, once the property value reaches £1m the relief starts to taper off and disappears altogether if it's worth £2.7m or more. Likewise, neither the Treasury nor HMRC seem to know how the additional tax free amounts will come in to play if the deceased's main residence was sold some time before death and the proceeds either spent or invested elsewhere. Meanwhile, based on current industry understanding, the trust clauses used to create and protect a tenancy in common give sufficient scope to at least allow the direct descendant criterion to be fulfilled.

This fact sheet is based on our understanding of current taxation, legislation and HM Revenue & Customs practice as at September 2015, all of which are liable to change without notice. The impact of taxation (and any tax reliefs) will depend upon your individual circumstances.

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