

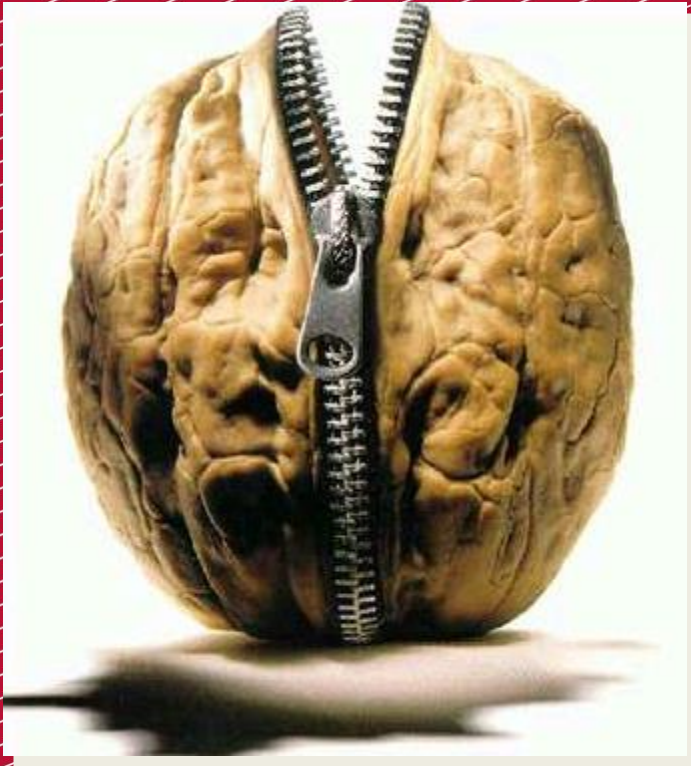
The Residence Nil Rate Band de-mystified

Workshop for Sheffield Life and Pensions

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Residence nil rate band in a nutshell



Content today.....

- Background
- What does the relief apply to?
- Who does the relief apply to?
- Limits on the relief
- How the relief is applied
- Impact of trusts
- Downsizing rules
- Transferability
- ***Planning opportunities***

Background

- Desire to have a £1million nil rate band
- Pressure from the squeezed middle class to take the family home out of the IHT net
- The magic £1million will be reached by 6th April 2020 when
 - NRB = £325,000
 - RNRB = £175,000
 - Total = £500,000 max tax free amount per individual
£1,000,000 for a married couple
- Not quite as good as it seems as it discriminates against:
 - Taxpayers with no children or other descendants
 - Taxpayers who have chosen not to own property but have other assets

What does the relief apply to?

- Deaths from 6th April 2017
- Transfers of property on death bequeathed to children or closely inheriting descendants
- Property means:
 - Residential property occupied at some time by the testator
 - Does not need to be the main residence
- The Executors must elect on which property to claim the relief
- 2 year time limit to make the claim
- Relief can be applied to cash or other assets derived from the sale of property limited to the amount of the sale proceeds

Who benefits?

- Applies to children and other direct descendants
- “closely inherited” widely defined and includes:
 - Step-children
 - Adopted children
 - Foster children
 - Natural children who have been adopted
- Grandchildren and remoter issue
- Spouses and widows of the above as long as they have not remarried

Who doesn't benefit

- Nieces and nephews
- Other 3rd parties
- Children and remoter issue who do not directly inherit, eg property left to discretionary trust
- Property left to grandchildren contingent on them attaining a specified age
 - *Very common in Wills*

Limits on the relief

- Staged introduction:
- Individual limits
 - £100,000 from 6/4/17
 - £125,000 from 6/4/18
 - £150,000 from 6/4/19
 - £175,000 from 6/4/20
- If claiming transferable allowance on second death:
 - £200,000 from 6/4/17
 - £250,000 from 6/4/18
 - £300,000 from 6/4/19
 - £350,000 from 6/4/20

Claw back of relief where estate value exceeds £2million



- Relief clawed back at a rate of £1 for every £2 over £2million
- Cut off levels are:
 - £2.4m for a married couple from 6/4/17
 - £2.5m from 6/4/18
 - £2.6m from 6/4/19
 - £2.7m from 6/4/20

Example 1

- Mr I is divorced
- He dies on 1.7.2018
- His estate worth £2.1million is left to his children
- The estate includes his home worth £450,000
- The max RNRB on death is £125,000
- BUT the estate value exceeds £2million
- RNRB reduced by £2 for every £1 over £2million
- Restriction is £50,000 so RNRB = £75,000

Example 2

- Mr J dies on 7.8.2018 leaving an estate of £2.1million
 - Includes property worth £450,000 left to spouse
 - Residue to children
- No RNRB can be claimed on his death as house is left to wife
- Still have to calculate the unused RNRB which is transferable
- Maximum relief is £125,000 for 2018/19
- Estate exceeds £2million so tapered
- Restricted by £50,000
- $\text{£75,000} / \text{£125,000} = 60\%$

Example 2 continued

- Widow dies on 16.4.2020
- Her estate is worth £1.8m which includes house now worth £500,000
- Entire estate left to children
- Max. RNRB on her death = £175,000
- Her estate is below £2m so available in full
- Transferable RNRB :
 - Maximum amount of £175,000 x 60% = £105,000
- Total RNRB claimable = £280,000

*Consequence of the taper
is 60% IHT in the margin*

Definition of the estate for RNRB purposes



Estate comprises:

- All assets in the estate
- No allowance for exemptions or reliefs so before deductions
- Assets held in IIPs and IPDIs
- Gifts with reservation of benefit brought back into charge

Excluded from the estate value:

- Gifts not subject to a reservation of benefit
- Assets held in relevant property trusts

Limits on relief - observations

- Claim will usually be made following second death for a married couple
- Doesn't matter when the first spouse died
- It does matter what the value of the estate was on first death
 - Could be a problem finding information on the value of the estate on first death if several years ago
- Value in the estate could be double counted if estate passes from one spouse to another on second death
- No doubling up of the estate value limit for married couples

Example 3 - the double restriction

- Husband and wife jointly own property worth £500,000 held as tenants in common
- Both have a child from a previous marriage
- Non-property assets are:
 - Husband £1.8m
 - Wife £200,000
- Both leave Wills leaving their shares of the property to their respective child and remainder of estate on IPDI trust for surviving spouse

Example 3 continued

- Husband dies first on 30 May 2017:
- Total estate value = £2,050,000
- Full RNRB for 2017/18 = £100,000
- RNRB on gift of property to son restricted to £75,000
- Balance of value of property covered by NRB
- Allowances used:
 - Max available RNRB – nothing transferable as max relief claimed
 - £175,000 of NRB
- No tax paid as balance of estate passes to IPDI for spouse

Example 3 continued.....

- Wife dies on 30 August 2019:

| RNRB computation | |
|--|-----------|
| Half share of property | 250,000 |
| Other assets | 200,000 |
| IPDI | 1,800,000 |
| Total | 2,250,000 |
| RNRB restricted from £150,000 by £125,000, ie half of the excess value of £250,000 over £2million even though own estate is only £450,0000 | 25,000 |

- Further problem is the benefit of the relief is apportioned across the estate and the IPDI trust

Example 3 continued

Total allowances in this case will be:

| Relief | Value £ |
|--------|------------|
| NRB | 325,000 |
| TNRB | 150,000 |
| RNRB | 25,000 |
| Total | 500,000 |
| | |

Apportioned across the estate and the trust

£100,000 : £400,000

so the IPDI benefits from £250,000 of the wife's allowances!!

How the relief is applied

- Although based on the property in the estate the relief does not attach to the property
- The effect of the relief is that it is spread across the whole estate
 - Not like APR/BPR which attaches to specific gifts
- Value is net of any mortgages

2 or more properties

- Nomination by PRs
- They choose which is the qualifying residence
- That applies even if one of the properties is held in trust
- Trustees have no say in the decision
- No joint election
- PRs should choose the most valuable property if that will increase the relief
- The relief reduces the tax on the estate and the trust proportionately

Can the relief be claimed on a transfer of property into trust?



- Depends!
- Bare trusts
- IPDI
- Old style qualifying IIP
- Disabled person's trust
- 18-25 trusts
 - All OK
- Discretionary Trust
- Trusts for orphaned children, ie grandchildren
 - Do not qualify



How to preserve relief for grandchildren

Scenario where a Will leaves property to children and a gift over to grandchildren if the child predeceases

- Bare trusts
- Outright gift
- IPDI
- DPI

Any age contingency makes a trust a relevant property trust and relief denied

- Many Wills have the wrong provisions for this scenario

Trust traps

- **Trusts following life interest to spouse?**
 - Must be an absolute interest for lineal descendants
 - Unless a Disabled persons interest
 - Life interest followed by an outright gift to a descendant
- **Can outright gift be subject to an overriding power of appointment?**
 - **No** – would be treated as a settlement and no RNRB
 - Would need to exercise power of appointment in life tenant's lifetime
 - No overriding power arising on death

What can be done?

- Section 142 and 144 can help in some cases
- RNRB cannot apply to a discretionary trust in a Will
- Appoint out
 - Absolutely
 - Or on appropriate trusts
 - Strict time limit – within 2 years of DOD
- **Beware** – can't use S142/144 on a discretionary trust which follows a life interest trust in a Will
- **Avoid** IPDI in a Will with remainder on discretionary trust

Downsizing

- Includes changes in property from 8.7.15
- Three scenarios in which relief available:
 - Deceased sold property and bought a cheaper property
 - Sold only residence and went into care or rented property
 - Gifted property
- RNRB claim based on the value of the original property provided that the equivalent value is left to descendants

Further detail on downsizing

- Relief capped at the full RNRB available on death
- Key value is the net value after deducting mortgage
 - Watch equity release loans &
 - Charge on property to secure a debt to a trust
- Key concepts
 - Downsizing addition
 - Lost relievable amount
 - Qualifying former residential interest
- Only one disposal of a former home can be taken into account
- If more than one disposal PRs can choose which is most favourable

The downsizing calculation

There will be a different amount of lost RNRB depending on whether the deceased has either:

- Downsized to a less valuable home
- Disposed of a home

Downsizing to a less valuable home

- Could be a loss of RNRB if the deceased downsized to a less valuable home but still has a home on death
- Only applies where the value of the home at death is below the maximum RNRB available to the estate
- Downsizing rules won't apply if either:
 - There's no loss of the RNRB because the value of the home at death is equal to or more than the maximum RNRB
 - The RNRB isn't available because although there is a home in the estate on death, the home isn't left to a direct descendant

Disposing of a home

- Where there is no home in the estate the RNRB will be equal to the downsizing addition
- The amount of the RNRB which has been lost will depend only on:
 - The value of the former property
 - The maximum RNRB at that time
- If the home was disposed of between 8 July 2015 and 5 April 2017 the maximum RNRB is deemed to be £100,000
- If the value of the home on disposal was more than the maximum RNRB at that time HMRC will treat the lost RNRB as 100% of the maximum RNRB available on death
- Relief is the lower of
 - The amount of RNRB that's been lost by the disposal
 - The value of the other assets left to the direct descendants

Record keeping

- Very important to retain documents to substantiate a future RNRB claim on downsizing
- Recommend the following documents are kept:
 - Completion statement
 - Copy of registered title before transfer
 - Any declaration of trust pre transfer
 - TR1
 - Signed statement from the client that it was a residence

Other planning tips

- Are nil rate band discretionary trusts back in vogue?
- Claim NRB on first death by gift to discretionary trust
- Value not aggregated on second death
- Leave sufficient in estate to claim 2 x RNRB on second death
- Don't fund discretionary trust with a charge on property
- Advantage if 2nd death estate could be brought back under £2million
- If high enough property value could fund with part share of property
- Discount on value
- BPR/APR assets
- Unmarried couples
 - Consider using DT on first death
 - Better to pay 6% every 10 years rather than 40% on 1st and 2nd deaths
 - Look at the big picture and do the maths

Remarried widows/widowers



- Up to 4 NRBs and RNRBs
- Always ask the question
- Careful drafting of Wills
- Review how the assets are held

Lifetime gifts

- Gift share of property to co-occupying adult child
- Exemption from GWRB
- Watch downsizing rules
- Death within 7 years – failed PET and no RNRB relief
- Retain sufficient property interest to cover RNRB
- *Do the maths*

Example 4 - Lifetime gifts of property – avoid the taper

- Widow terminally ill
- Husband died leaving whole estate to her
- Widow's Will leaves estate to children
- Estate worth
 - Property £700k
 - Portfolio £2m
- No RNRB available as estate over threshold
- Give home to children and pay open market rent
- Failed PET still taxable but estate worth less than £2m on death
- Full RNRB claimed
- Tax saving £140,000

The big picture

- Potential tax saving £140,000
- Review estates over £2m to see if the estate value can be reduced to avoid the taper provisions
- Review estate as a whole
 - Pensions in trust not part of estate for £2m limit
 - Spend other capital before pensions
- Planning between spouses to see what each will leave
- Try and avoid double counting on second death

The Legal Bit.....

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Thank you for listening

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