

## **Inheritance Tax nil rate band discretionary will trust provisions: the advantages and disadvantages of keeping them in your Wills.**

This briefing note is for married couples and registered civil partners who made their Wills before the 9<sup>th</sup> October 2007 and included in them nil rate band discretionary will trust provisions to make use of the inheritance tax nil rate band on both the first and second deaths.

Before that date this was the main way that married couples and registered civil partners were able to ensure that their estates had the benefit of two nil rate bands, rather than passing everything to the survivor of them (which is exempt from inheritance tax) and then having the benefit of only one inheritance tax nil rate band on the death of the second of them.

Since 9<sup>th</sup> October 2007, the inheritance tax nil rate band is transferrable between married couples and registered civil partners. Where one spouse/partner dies without making full use of his or her nil rate band, the estate of the survivor will have the benefit of both his or her nil rate band and also the unused proportion of the nil rate band of the first to die. For example, if everything passes to the survivor this is wholly exempt from inheritance tax and none of the nil rate band is used, leaving two nil rate bands available on the survivor's death. If you need any further information on the transferable nil rate band, we have a separate briefing note on this.

Generally, this means that for inheritance tax planning purposes married couples and registered civil partners no longer need to have nil rate band discretionary trust provisions in their Wills. However there are other important reasons why it may be advantageous to keep them in your Wills.

This briefing note sets out the advantages and disadvantages of keeping the nil rate band discretionary trust provisions in your Wills.

### **Advantages of nil rate band discretionary will trust provisions**

- Asset protection, for example:-
  1. The assets held in the trust are not taken into account for financial assessment or means-tested benefits - in particular they would not be taken into account in assessing the liability of the survivor to pay nursing home or care fees.
  2. The assets held in the trust will be protected in the event of the remarriage of the surviving spouse, in respect of any claims which may arise against him or her, for example on subsequent death or divorce.
- The trust arrangements can be wound up entirely in favour of the surviving spouse after three months but within two years of the date of death of the first spouse, without any tax disadvantage. This allows time for an assessment of the financial position of the surviving spouse and also consideration of appropriate tax and estate planning. For example, part of the trust could be passed to children or grandchildren direct, whilst the remainder passes to the surviving spouse/partner. This is treated as a transfer by the deceased spouse/partner for inheritance tax purposes, and not a lifetime gift by the surviving spouse/partner. The inheritance tax transferrable nil rate band rules will still apply to the extent that the nil rate band remains unused after the transfers to the children and spouse/partner.
- The trust provides flexibility to benefit family members or others at the discretion of trustees according to their personal and financial circumstances at a later date, rather than distribution in fixed shares under the terms of a Will. This allows the trustees to provide for a

greater number of family members in differing proportions where appropriate, such as for dependant parents, children or grandchildren, or where spouses have children from their previous marriages.

- The transferrable nil rate band provisions could be abolished, amended or limited in the future. In any event the nil rate band is currently frozen at £325,000 until April 2015 and may not therefore increase in line with the value of your property and other assets over that period.
- Where one or both of a couple own assets which are eligible for IHT business property relief or agricultural property relief, it is often advisable for inheritance tax planning purposes for such assets to pass into a discretionary trust arrangement by will, rather than passing to the surviving spouse, in order to mitigate potential inheritance tax charges arising on the second death if those assets have by then been sold or are not at that time eligible for those reliefs.
- It can also be advantageous for assets which may appreciate substantially in value (for example, land with development potential) to pass into discretionary trust rather than to the surviving spouse, as the increase in value could give rise to a greater inheritance tax liability on the survivor's estate on his or her death.

## **Disadvantages of nil rate band discretionary will trust provisions**

- The complication of having a trust set up on the death of the first spouse, with the additional costs of setting up the trust and its continuing administration.
- The surviving spouse has access to funds from the nil rate band discretionary trust only at the discretion of the trustees, although often the surviving spouse may be one of the trustees and will therefore have a say as to how it is administered.
- If the tax legislation changes in the future it may not be possible to wind up the discretionary trust arrangements without a tax charge.
- Discretionary trusts are taxed at the highest rates of income and capital gains tax, that is, income tax at 50% and capital gains tax at 28%, and there is also a potential charge to inheritance tax every ten years, albeit at a modest rate of tax, the maximum charge being 6% of the value of the trust assets, after taking account of the inheritance tax nil rate band applicable to the trust.
- It may be necessary to use a share in your house as part of the trust assets, which can restrict the freedom of the surviving spouse to do what he or she likes with the property.

## **Summary**

There is no hard and fast rule as to whether or not you should retain the nil rate band discretionary trust provisions in your Wills. It is very much dependant on your family circumstances and it is appropriate to take specific advice on your particular circumstances before reaching a decision on whether or not to change your Wills.

For further advice and guidance on the complex rules that govern these arrangements, please contact one of the specialist advisers in our Wills, Trusts and Probate and Wealth Management teams at Coffin Mew LLP on **023 9236 6005** or email: **wills@coffinmew.co.uk**.