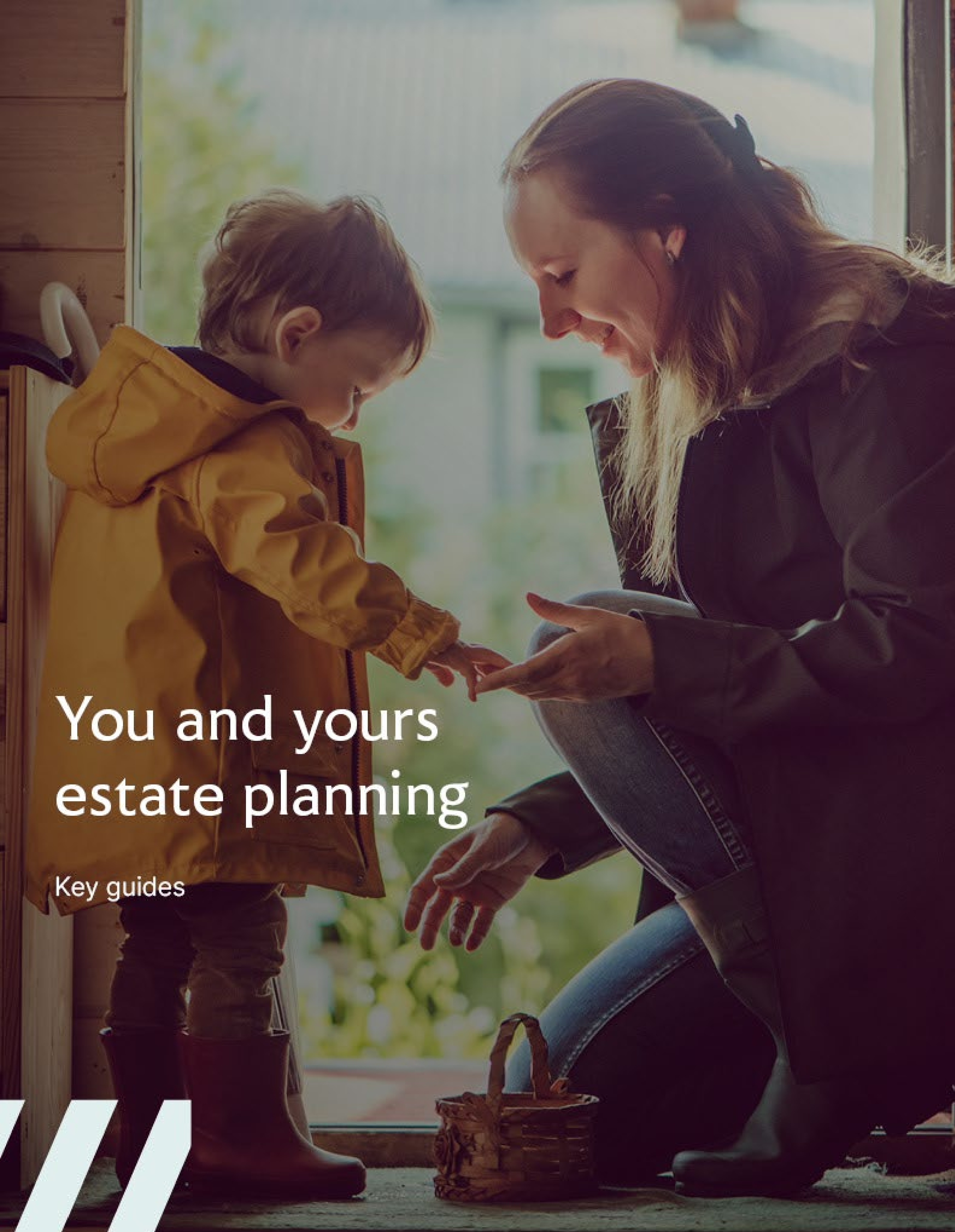

You and yours estate planning

Key guides

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You and yours – estate planning

Introduction

Estate planning – too important to put on hold

All too often, people put off estate planning. This is understandable as, rather than preparing for the here and now, it requires you to consider what will happen when your life is over, hardly something most of us rush to contemplate.

Consequently, estate planning often becomes, and all too often remains, a do-it-tomorrow task. When it could suddenly become all-important it might be too late. After all, accidents and sudden illnesses – such as Covid-19 – can and do happen.

This guide will help you prepare effective plans that will help ensure you control what happens to your estate.

Please note that all examples included in this guide are fictitious.

The advantages of making early plans

Think what can be achieved by arranging your estate planning *now*:

- **You decide on the choice of beneficiaries** If you do not set out in a will whom you wish to benefit from your estate, then the state will do it for you. The results are not always what you would expect and can create unnecessary tax liabilities.
- **You decide what goes to whom** You might want to leave a particular item to a particular person. Without estate planning, those wishes may not become reality.
- **You decide the structure** Leave it to the state to distribute your wealth and normally anyone aged 18 or over will receive their inheritance outright. In some families, that will not be an issue, but in others placing some constraints on how an inheritance is handled could be essential.

With estate planning in place, you will have addressed these important issues rather than leaving them on permanent hold. However, like all other aspects of financial planning, your estate planning will need regular review.

Planning point
Assess your assets and how you would like to dispose of them. Work through the answers to key questions and discuss them with your partner and, if appropriate, your family.

Your will

Failure to prepare a will means your estate will fall under the rules of intestacy. This default can produce some surprising – and unwelcome – results, as explained below.

Your will needs to be kept up to date. Something that was prepared a decade ago may still be satisfactory, but across such a long period of time your situation and your family's circumstances will probably have changed. Tax legislation has certainly done so. Remember too that marriage will normally result in the automatic revocation of an existing will. Divorce does not have the same effect, but it does mean the former spouse or partner is treated as having died before the will becomes operative.

A typical will can be divided into three main elements:

1. **Appointments and funeral wishes** The duty of executing the terms of your will falls to the people you appoint as executors in the will. It is best to appoint at least two executors: your husband/wife or civil partner alone – if they survive you – may struggle to cope with bereavement and estate administration. The choice of executors (and guardians for minor children) is not one to be taken lightly, as both roles involve considerable responsibility.

   The first section of the will often also deals with funeral arrangements, such as whether you want to be cremated, and perhaps where your ashes should be scattered.

2. **Distribution** This central part of the will sets out the 'who, what, when and how' of your bequests. This will include specific legacies of cash and/or particular assets to named individuals or charities.

   Repayment of debts, the costs of your funeral, outstanding taxes and any other liabilities will usually be met from the part of your estate that is not covered by the legacy provisions. What is left (the 'residue') will ordinarily form the bulk of your estate. This can be divided up however you wish or simply passed outright to a single beneficiary.

   Dealing with the residue will usually be where the questions of 'how' and 'when' are addressed:
   - If some of your beneficiaries are minor children, a trust will be necessary, and it is best to seek advice about this. For example, few parents are happy to see an 18-year old receive a substantial windfall with no strings or restrictions attached.
   - You may want a surviving husband/wife or civil partner to receive the income from your estate, but on their death, you may prefer any capital to pass to your children from a previous marriage. Again, a trust can achieve this.
   - In some instances, it may be best to leave the decision on the distribution of the residue to trusted members of the family or friends, acting as trustees. You can give them guidance and, in your will, include a list of potential beneficiaries. However, as your trustees have the final decision, they will be able to take account of the circumstances upon your death.

3. **Executor/trustee powers** This final section of your will is the part that sets out in legal terms the powers of your executors and, if any trusts are created by your will, the powers given to the trustees. Usually the will is drafted to maximise their flexibility of operation.

A will can be as simple as a few lines or it can be complex and cover many pages. DIY wills are possible and many people use a simple will form or online will-writing services. Whoever prepares your will, it remains a legal document, a point which has regularly created problems in the interpretation of DIY wills.

For your own and your family's peace of mind, in nearly all cases it is best to have your will prepared by a solicitor or professional will writer. The error in a poorly drafted will may only emerge after it is too late for you to make any changes.

Planning point

Take some time to review your existing will, with your husband/wife or civil partner, and review theirs. Do they reflect your current circumstances and wishes?

A word about probate

Before your executors can carry out the terms of your will, they need to obtain probate. This may involve a considerable amount of administrative work, most notably IHT returns and payment of any inheritance tax and probate fees due. If your estate does not have enough cash to cover these levies, your executors may need to borrow to meet the bill. In England and Wales, the current probate fee for estates of £5,000 and over is £300.

In Scotland you need to apply for letters of confirmation in the Sheriff's court and submit an inventory to release money and property. There is a scale of charges based on the value of the estate.

In Northern Ireland you need to apply for a grant of probate or where there is no will, letters of administration from the Probate Registry. The cost for estates worth over £10,000 is £284 with an additional £71 fee for a personal application.

Regulations that took effect on 1 January 2022 have substantially reduced estate reporting requirements where no IHT is payable on an estate, for example when everything passes to a surviving spouse on first death. The exempt excepted estates category limit was increased from £1 million to £3 million.

And if you don't make a will…

Whether or not you have a will, anything you own jointly with someone else will pass to the other joint owner(s) on your death. The exception to this arises where your ownership takes the form of a tenancy in common (which would be unusual for married couples and civil partners).

If you die without having a valid will, the laws of intestacy apply. These differ depending on the part of the UK in which you are domiciled – which may not necessarily be the same as the country where you are living when you die.

Intestacy rules often do not produce the distribution of your estate that you might expect. For example, the surviving husband/wife or civil partner will not necessarily receive everything, as the example below shows.

Example – The unwelcome intestacy surprise

Henry and Ann had been married for over 30 years when Henry died in a fishing accident in Scotland in early August 2023. He had made no will, but both he and Ann assumed everything would be left to her, as a childless widow. The family home does indeed pass to Ann because it was owned jointly (as joint tenants), but Henry's £900,000 personal estate (plus personal chattels) are being dealt with under intestacy.

Although he died in Scotland, the English intestacy laws applied as his home and roots were in Kent rather than Kirkcudbrightshire. As such:

Ann will receive £322,000 outright and Henry's personal chattels.

Ann is also entitled to half of the remaining estate (i.e. £289,000).

The other £289,000 will pass to Patrick, the 37-year-old 'permanent student' son from Henry's first brief marriage in the mid-1980s.

Had Henry died four weeks earlier, before an overdue uprating in the fixed net sum was made, Patrick would have received £315,000 and Ann a total of £585,000. In either case, a large part of Henry's nil rate band would have been used up and not transferable to Ann's estate.

Unscrambling the unfortunate effects of intestacy may be possible using a legal document called a deed of variation, but it requires the agreement of some parties to give up all or part of their benefits. They may be legally unable to do so because they are minors, or they may be adults who are unwilling to do so – like Patrick in the example above. There could be similar difficulties with attempts to rectify wills after a death; family ties may not count for much when money is involved.

Powers of attorney

Whenever you make (or amend) your will, you should also consider putting in place a power of attorney. Again, these differ in their names and types across the different countries of the UK.

In England and Wales, there are two types of lasting power of attorney (LPA), both of which let you appoint one or more people (your attorneys) to make decisions on your behalf if infirmity prevents you from doing so.

- **Health and welfare LPA.** This covers decisions about areas such as:
  - your daily routine (e.g. eating, washing, dressing);
  - the provision of medical care;
  - if you should move into residential or nursing care;
  - whether life-sustaining treatment should be refused.
- **Property and financial affairs LPA.** This covers your finances, handling areas such as:
  - paying your bills;
  - collecting your benefits;
  - sorting out your tax affairs;
  - selling your home.

Property and finance LPAs replaced the old enduring power of attorney (EPA) in October 2007. EPAs established before the changeover are still valid, regardless of whether they have been registered.

In Scotland there are three types of power of attorney (PoA) which must be registered with the Scottish Office of the Public Guardian:

- A continuing PoA covers your financial and or property affairs.
- A welfare PoA for decisions around your health and welfare which can only be used once you have lost capacity to make those decisions.
- A combined PoA which includes provisions of both other types and is the most common.

In Northern Ireland, you can set up two types of PoA:

- An ordinary or general PoA to look after your financial affairs if you are temporarily ill, in an accident or going abroad for a long period of time. This ceases to be valid, however, if you become mentally incapacitated.
- An enduring power of attorney (EPA) allows your appointed representative to act on your behalf should you become incapable, when your attorney(s) must apply to register the EPA with the High Court (Office of Care and Protection) for it to become effective. This can cover both financial and welfare issues or come into effect in specific instances, for example if you become physically disabled but remain mentally capable.

Although not strictly part of estate planning, arranging powers of attorney can be of great value to your beneficiaries, as they allow your affairs to be handled efficiently later in life. As with intestacy, there is a state fall-back (through the Public Guardian), but the whole process can be slow, expensive and impersonal.

Planning point
Establishing PoAs can be very beneficial for your family in managing your affairs should the need arise.

How inheritance tax works

Do not ignore the impact of inheritance tax (IHT). Very broadly speaking, IHT is levied on your estate at death and on certain gifts made during your lifetime.

Currently the tax rate at death is normally 40%. However, everyone has a nil rate band (frozen at £325,000 until at least April 2028) and, to the extent that this has not been set against the total value of lifetime gifts in the preceding seven years, it is available on death. The table below shows the effective rate of tax on an estate of a single person, assuming no reliefs and exemptions are available, but they qualify for a full nil rate band at death (but no residence nil rate band):

- If you make an outright lifetime gift, regardless of its size, you pay no IHT initially, but the value of the gift is brought back into your estate if you die within the following seven years.
- Other lifetime gifts that you do not make outright – notably gifts into most types of trust – may attract lifetime IHT. This is at a lifetime rate of 20% to the extent that they exceed your available nil rate band and any exemptions. There may also be further tax, up to another 20%, if you die within the following five years.

The IHT burden

Total estate £	Inheritance tax payable £	Effective rate on estate %
400,000	30,000	7.5
500,000	70,000	14.0
600,000	110,000	18.3
750,000	170,000	22.7
1,000,000	270,000	27.0
1,500,000	470,000	31.3
2,500,000	870,000	34.8

Planning point
Inheritance tax is generally charged at 40% on death and 20% on certain lifetime gifts.

The Inheritance tax regime

This brief description is an extreme simplification of the current IHT regime. The rules include:

Transfers

Transfers between spouses and civil partners These are exempt from IHT, provided the recipient is domiciled in the UK. Non-domiciled aspects are beyond the scope of this guide.

The transferable nil rate band To the extent that one spouse or civil partner does not use their full nil rate band at death, it is transferable to the survivor's estate. The precise rules are complex, but the effective result is that a couple currently has a combined nil rate band of up to £650,000 (£325,000 x 2). The transferability means that there is no need to ensure that the first of a couple to die uses their nil rate band, as was once the case. However, the transfer must be claimed in the estate IHT return – it is not given automatically.

Residence nil rate band An additional nil rate band can be set against the value of your home where it is left to a direct descendant. The band is £175,000 for 2023/24 and will remain at that level until at least the end of 2027/28. Like the nil rate band, any unused portion is transferable between spouses and civil partners (on claim), but unlike the nil rate band it is subject to a 50% taper if your estate is worth more than £2 million (also frozen until the end of 2027/28). As a consequence there is no RNRB available if the deceased holds assets of more than £2.35 million at the date of death (£2.70 million where a full RNRB is transferred from a deceased spouse). Special rules deal with downsizing or selling up completely (e.g. on moving into a care home).

Example – The residence nil rate band in practice

Jack and Jill each had an estate of £1.2 million when Jack died in November 2023. His will left everything to Jill, who died four months later. Thus, Jill inherited 100% of Jack's nil rate band and, as his estate was under £2 million, 100% of his residence nil rate band (of £175,000).

However, on Jill's death her estate was worth £2.4 million, which brought the tapering rule into play. Instead of having a total residence nil rate band of £350,000 (2 x £175,000), the amount available to her estate was reduced by £200,000 (£400,000/2) to just £150,000.

If Jack had used his £325,000 nil rate band on first death to make gifts to beneficiaries other than Jill, there would still have been no IHT on his death, but Jill's estate would have been correspondingly smaller after her death. As a result, the available residence nil rate band would have been £312,500 (£350,000 – £75,000/2).

Planning point
Consider what gifts you could make over the next few years to use your exemptions and reliefs.

Gifts

The three exemptions work on a tax-year basis:

- The most widely known is the £3,000 annual exemption, which can cover any type of lifetime gift, in whole or in part.
- The small gifts exemption covers any number of outright gifts of up to £250 per person – useful if you have plenty of grandchildren.
- The least well-known is the normal expenditure gift. Regular gifts are exempt from IHT if you make them out of your income and they do not reduce your standard of living.

Charities, etc. Gifts and bequests to UK charities, political parties and for the public benefit are exempt from tax. Charitable bequests can also result in the IHT tax rate on your estate being cut to 36%, provided these total at least 10% of your net estate.

Wedding gifts Wedding gifts are exempt, but subject to very modest limits (no more than £5,000) based on the relationship between the donor and the bride/groom.

Example – Using the normal expenditure rules

Joan inherited her late husband Harry's investment portfolio, but not his fondness for fast cars and fine wine. She was saving, on average, £2,500 a month from her income. In addition, £6,000 a year of dividends was rolling up in the ISAs that she had inherited from Harry.

She did not need this surplus income but was reluctant to give away the underlying capital in case it was needed to cover nursing home fees. She therefore chose to give her three children £12,000 a year each as birthday presents. The total annual gift of £36,000 matched her excess income and was therefore covered by the normal expenditure rules.

To help her executors, Joan made sure she kept note of her income and expenditure, providing proof that she did not need the cash she was gifting.

Reliefs

Business and agricultural reliefs: Businesses and agricultural property can benefit from generous IHT reliefs, provided certain conditions are met:

- 100% relief is given for shares in unlisted trading companies (including some of those listed on the Alternative Investment Market (AIM)), sole trader or partnership business interests, owner-occupied farms and tenanted farms where the lease started after 31 August 1995.
- 50% relief applies to property and other assets owned by an individual and used by a trading company that they control, or by a partnership in which they are a partner. The 50% relief also applies to tenanted farmland where the lease started before 1 September 1995.

Taper relief: The amount of tax payable at death on a gift that was made within the previous seven years is subject to a sliding scale. For example, the tax payable on an outright gift made five and a half years before death is reduced by 60%.

To clarify, the taper applies to the *amount of tax*, not the value of the gift. Therefore, a gift that attracts no tax cannot benefit from taper relief but is treated as part of your estate at death.

Tax avoidance legislation has steadily increased over the years. For example, the 'gift with reservation' rules would prevent you making any IHT savings by putting your home in your children's names and then continuing to live there rent-free.

The future of IHT: The Labour Party's manifesto made no comment on IHT, prompting speculation that it could be one area where additional revenue may be raised. Shortly before the election was called, three of the most likely targets – business relief, agricultural relief and pension IHT freedom – were highlighted as ripe for reform by the Institute for Fiscal Studies.

Making your plan

Estate planning and IHT planning are often lumped together, but if you have a spouse or civil partner, their long-term financial security will probably have a higher priority than tax planning.

Achieving your estate-planning goals and minimising the impact of IHT will involve a range of actions, starting with making the all-important will and potentially including:

- **The use of trusts** Trusts are often set up purely for estate-planning purposes, e.g. setting aside funds to meet the costs of educating grandchildren.

- **Lifetime gifts** Currently gifts made in lifetime that exceed the available annual and other exemptions escape IHT if they are made outright more than seven years before death. Some people ignore this generous treatment of gifts because they are worried about their future income and security. Fortunately, the tools of financial planning can help alleviate these concerns.
- **Maximising allowances, reliefs and exemptions** As far as practicable you should take advantage of the annual IHT exemptions, particularly the normal expenditure gift rule if you have (or can generate) surplus income. If you own a business or a farm, you need to ensure that you use the appropriate reliefs to the full. You can also take advantage of IHT business relief by holding certain types of investment for at least two years; these include some (but not all) AIM shares, which can be held within ISAs.
- **Pension planning** Pension tax rules mean pensions must be considered in IHT planning. A pension can provide you with the certainty of income that allows you to make lifetime gifts and represents an IHT-free fund. Some pension plans can be passed down from generation to generation, free of IHT and possibly also free of income tax on any payments. The effective abolition of the lifetime allowance has created new opportunities in this area of planning.
- **Life assurance** For larger estates, there will almost certainly be tax due on the estate at death. For married couples and civil partners, that tax bill usually arises on second death, because there is normally no point in incurring a tax charge any earlier. Life assurance can provide for this in a way that does not increase the size of your estate and will take advantage of your annual exemptions.

It can also be possible to adjust your estate after your death, if the affected beneficiaries agree to any changes. This is done with a deed of variation, and could be helpful with, for instance, minimising IHT.

How we can help

We can help with your estate planning and IHT planning in several ways:

- Working with your other professional advisers to optimise the estate and tax-planning aspects of your will.
- Advising on the various tax implications involved in lifetime gifts.
- Reviewing your pension provision and suggesting ways to improve its role in your estate planning.
- Arranging investments and life assurance to help reduce or fund IHT.
- Keeping you updated on any Budget changes.
- Helping you understand how trusts work.
- Keeping you advised on how any new legislation could affect your estate planning.

The value of the investment and the income from it can fall as well as rise and investors may not get back what they originally invested, even taking into account the tax benefits.
The Alternative Investment Market (AIM) invests in assets that are high risk and can be difficult to sell.
Tax treatment varies according to individual circumstances and is subject to change.
The Financial Conduct Authority (FCA) does not regulate will writing, tax and trust advice, lasting powers of attorney, inheritance tax planning and estate planning.
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