

Using IPME+ to reduce IHT liability

FOR FINANCIAL ADVISERS ONLY

This guide looks at how an IPME+ product could be used to help a UK domiciled or deemed UK domicile individual cover a potential UK inheritance tax (IHT) liability when making gifts.

What is IHT?

IHT is a one-off tax payable on the value of an estate of an individual who has died.

Anyone who is UK domiciled or deemed UK domicile is subject to UK IHT on the value of his or her worldwide estate.

Key IHT Figures

£325,000	The nil-rate-band (NRB), up to which no IHT is chargeable.
40%	The amount that IHT is payable above the NRB.
6 Months	The period in which the IHT bill must be paid.

Statistics published by HM Revenue & Customs (HMRC) revealed that £6.1bn was collected from UK IHT receipts between April 2021 and March 2022.

Gifting

A gift (unless exempt) from one individual to another is a 'potentially exempt transfer' (PET). There is no tax to pay when the gift is made nor is there a limit on how much can be gifted.

- If the donor survives the PET by seven years, the gift is exempt and will be outside of the donor's estate for IHT.
- If the donor dies within seven years the PET will fail and will become a chargeable transfer (failed PET).

A gift could be anything for example: cash, a property or a policy of life assurance/capital redemption.

IHT on failed PET

IHT is charged at 40% above the available NRB. Where a failed PET was made more than three years before the death of the donor, the amount of IHT payable on the gift could be reduced by 'taper relief'*.

! It is the recipient of a gift that is liable for paying any IHT on a failed PET.

* Taper relief would not be available if the failed PET were to fail within the NRB.

Case study

Mr Smith is aged 55, UK domiciled and resident in the UAE. He would like to make a gift of £150,000 to both his son and daughter to help purchase a house. Mr Smith has recently undertaken trust planning and has no NRB remaining.

The gifts would be a PET with the value (£300,000) remaining inside of the his estate for seven years from the date the gift is made.

Should Mr Smith die immediately after making the gift, the IHT liability would be as follows:

£120,000 ((£300,000 – 0) x 40%), with each of his children liable for **£60,000** (£120,000 / 2).

IHT liability

Year	IHT rate	Taper relief	IHT liability
1	40%	0%	£120,000
2	40%	0%	£120,000
3	40%	0%	£120,000
4	32%	20%	£96,000
5	24%	40%	£72,000
6	16%	60%	£48,000
7	8%	80%	£24,000

The responsibility for paying the tax on the failed PET would fall on the son and daughter who were the recipients of the gifts. This could mean the recipients having to either:

- selling the house that they purchased to raise funds for the IHT bill,
- delaying the purchasing of the house by up to seven years until the gift is exempt
- borrowing money to cover the IHT liability

Mr Smith is looking for a product that could protect his children from any IHT liability linked to the gifts.

Potential solution

The highest amount of IHT due on the PET whilst it remains inside of the estate (seven years) would be **£120,000** $((£300,000 - 0) \times 40\%)$.

Mr Smith could take out an IPME+ with a term of seven years. For a fixed monthly premium throughout the term of the policy, the policy could provide a fixed lump sum that would cover the maximum IHT liability on the failed PET.

Year	IPME+ Cover	IHT Liability*	Total Premium Paid	IHT Saving
1	£120,000	£120,000	£1,049	£118,951
2	£120,000	£120,000	£2,098	£117,902
3	£120,000	£120,000	£3,146	£116,854
4	£120,000	£96,000	£4,195	£91,805**
5	£120,000	£72,000	£5,244	£66,756
6	£120,000	£48,000	£6,293	£41,707
7	£120,000	£24,000	£7,342	£16,658

The above is based on a male, non-smoker, aged 56, UK national and resident in the UAE.

* The total IHT liability is reduced each year after year 3 due to taper relief being applied.

Impact

If Mr Smith were to die in year four, the gift of £300,000 would be a failed PET. With taper relief applied, the son and daughter would each be responsible for paying an IHT of **£48,000** $(£96,000 / 2)$ that must be paid within six months.

With the IPME+ policy in place an amount of £120,000 would be paid out, which has only cost the donor £4,195.

A payment of £120,000 could be made to the client's son and daughter to use against the IHT liability without them having to find funds or sell their properties.

In this example, having the IPME+ in place has provided a saving of £91,805 on the two gifts. **

Consideration

- It's strongly recommended that the IPME+ be placed into a suitable trust. This would ensure that the lump sum is not added back into the deceased's estate.

In the above example, an extra £120,000 added back to the estate could result in £48,000 $(£120,000 \times 40\%)$ less being available to cover the IHT liability meaning that only £72,000 $(£120,000 - £48,000)$ would be available.

- A trust would also void requirements for Isle of Man probate and allow any funds to be distributed more quickly.
- The individual that deals with your estate will need to work out total gifts made in the 7 years before death. Detailed records of the following should be kept:
 - What gift was given and to whom,
 - the value of the gift
 - when it was given.

This option may not be suitable for everyone. Careful consideration needs to be given as to when gifts have been made. This planning opportunity may not be required where the PET falls within the NRB.



Important notes

For financial advisers only. Not to be distributed to, nor relied on by retail clients.

Please note that every care has been taken to ensure that the information provided is correct and in accordance with our current understanding of the relevant law, as at May 2022

You should note however, that we cannot take on the role of an individual taxation adviser and independent confirmation should be obtained.

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