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IHT planning tips: Business Relief and Discretionary Will Trusts

Synopsis: How using business relief qualifying investments can offer inheritance tax benefits.

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Using Business Relief (BR) qualifying investments can be a very effective means of inheritance tax planning,

A Business Relief qualifying investment will be exempt from inheritance tax (IHT) once it has been held for two years, making it especially attractive for those clients who are concerned they may not live seven years due to ill health or advanced age.

How can this effective planning be made even more beneficial?

Is it possible to benefit the next generations?

How can we crystallise the Business Relief at the earliest opportunity?

Can the assets be protected?

The answer to these questions involves combining the BR IHT exemption with a discretionary trust, held within the client's will. Updating the client's will to direct any BR qualifying assets, which are exempt from IHT, into a discretionary trust has several key advantages.

Firstly, it allows the BR to be crystallised on first death. This is especially useful for married couples/civil partners as it removes the need for the surviving spouse/surviving civil partner to maintain the investment until second death, which may be many years.

The trustees of the trust can then hold the funds in a lower risk investment strategy as the BR exemption has been achieved.

Despite being exempt from IHT, BR qualifying assets are included in the estate of the owner for the purposes of the £2m Residence Nil Rate Band taper rules. Directing the BR assets to a trust on first death will ensure the surviving spouse/surviving civil partner can have access to the funds but not personally own them for taper purposes.

In addition to benefitting the surviving spouse/surviving civil partner, future generation(s) can also benefit by using will trusts.

Firstly, the assets are owned by the trustees of the discretionary trust which means they will not be included in the IHT estate of the next generation, even if the investments are moved away from BR qualifying investments. Potentially, this could provide multiple generation IHT planning.

A discretionary trust will also provide protection for both the next generation and the surviving spouse/surviving civil partner from events that can diminish family wealth. Generally, assets held on discretionary trust are protected from future divorce, bankruptcy and long-term care. In addition, assets are protected from future beneficiaries who may be reckless or extravagant.

It is also important to note that a discretionary trust will still be subject to the relevant property regime which means that ordinarily entry, exit and periodic IHT charges will apply. However, at the time the assets are passed into the trust there would be no entry charge as the assets qualify for BR. What follows, is that there would therefore be no exit charge in the first ten years. And, for the purposes of the periodic charge, assets which qualify for BR can be deducted to arrive at the chargeable value.

Any specific advice regarding the creation of the will needs to be provided by a legal professional.

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