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The new residence nil rate band explained

The residence nil rate band (RNRB) arose from the Conservative Party's 2007 statement of their wish to increase the inheritance tax nil rate band to £1m. However, as with all taxes, it is not quite as simple as that!

Inheritance tax nil rate band

Inheritance tax is charged at 40% on the amount by which a person's estate exceeds their nil rate band (NRB) – currently £325,000 – after exemptions and reliefs. Unused NRB of the first spouse or civil partner to die – transferable nil rate band (TNRB) – can be claimed on the death of the survivor, making a combined NRB of up to £650,000.

Residence nil rate band (RNRB): The basics

The RNRB is available for deaths on or after 6 April 2017, where the deceased owned a home, or share of a **home**, which is **inherited** by their **direct descendants**.

It will be phased in, starting at £100,000 for tax year 2017-18 and rising by £25,000 per year until it reaches £175,000 on 6 April 2020.

The RNRB tapers away by £1 for every £2 where the estate exceeds £2m.

Unused RNRB can be claimed on the death of a surviving spouse or civil partner, even where the first spouse or civil partner died before 6 April 2017.

Where the deceased moved to a less valuable home, or ceased to own a home after 8 July 2015, a downsizing addition can be claimed if the former home would have qualified for the RNRB if it had been kept.

Home

The RNRB applies to a property which is included in the deceased's estate and has been lived in by the deceased – It does not have to be their main residence. If the deceased had more than one property, their personal representatives can nominate which property will qualify, provided the deceased lived in it at some point.

Direct descendants

"Direct descendants" include children, grandchildren or other lineal descendants; spouses, civil partners, widow(er)s or surviving civil partners of lineal descendants; step-children, adopted children and fostered children; and children for whom the deceased has been appointed guardian when they are under 18. Children of a co-habitee are not direct descendants.

Inheritance

The direct descendants must inherit the home on the deceased's death under their Will or the rules of intestacy, or by some other legal means as a result of the death (for example, by survivorship under a joint tenancy). It makes no difference whether the home is specifically referred to in the Will, or if it forms part of the residuary estate.

If the home is inherited by direct descendants and others, its value will be apportioned between them. The home does not have to be transferred into the descendants' names – it will still qualify if it is sold by the personal representatives.

The direct descendants must become entitled to the home on the death of the deceased. If the home has been left to direct descendants on condition that they must reach a certain age, the home will be held on trust and (save as set out below) the RNRB would not apply to the shares of those who are under the specified age at the date of death.

The problem with trusts

Where the home is held in trust following the death, the RNRB will apply only if the direct descendants inherit property on an immediate post death interest (IPDI) trust, a disabled person's trust (under s.89 Inheritance Tax Act 1984), or a bereaved minor/18-25 trust. Bereaved minor and 18-25 trusts can only be created by parents, so a share in a home inherited from a grandparent will not qualify if the grandchild is under the age of inheritance at the date of death.

A share of the home may be held on an IPDI trust before death, for example to protect the share of the first spouse or civil partner to die against being used to pay the survivor's care fees or against the survivor's remarriage. In this case, the home will be included in the survivor's estate for inheritance tax purposes and it will qualify for RNRB if direct descendants inherit it.

If the home is held in a discretionary trust during the deceased's lifetime, as is the case with some asset protection trusts, or passes into a discretionary trust under the deceased's Will, it will not qualify. However, in the case of a discretionary Will trust, if the trustees make a deed of appointment, passing the home to direct descendants within two years of death, the descendants will be treated as inheriting the home on death for the purposes of inheritance tax and the RNRB.

Do I need to change my Will?

You should review your Will if the value of your estate exceeds your NRB (including any TNRB from your spouse or civil partner) and you wish direct descendants to benefit from the RNRB.

If you have left your home to your children, with a substitute gift to the children of a deceased child at a specified age, you might wish to remove the specified age from your Will. However, first consider that your children may all survive you; and if they do not your grandchildren may reach the specified age before you die; and if they do not, whether the advantage of the full RNRB outweighs the possible disadvantages of a grandchild inheriting at a young age.

If your Will leaves your home on discretionary trust, you should take legal advice as to whether to change your Will, or to rely on your personal representatives appointing your home out of the trust within two years as explained above.

The RNRB is complex, particularly in relation to downsizing and to trusts and this article can only give the basic facts. We recommend that you should discuss your Will and inheritance tax liability with a specialist lawyer, preferably with the "STEP" (Society of Trust and Estate Practitioners) qualification, who will be able to guide you through any changes you may need to make.

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