Gifting

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- Small gifts to individuals not exceeding £250 in total per tax year per recipient ar exempt. The exemption cannot be used to cover part of a larger gift.
- Gifts between spouses are generally exempt unless one spouse is domiciled abroad in which case it is limited to £325,000 forever and anything above this is a potential exempt transfer.
- £3,000 per annu may be given by an individual without an Inheritance Tax charge. An unused annual exemption may be carried forward to the next year but no thereafter.
- Gifts for wedding or civil ceremony of up to £1,000 per person (£5,000 if the gift is to your child, £2,500 if they are a grandchild or great-grandchild).
- Gifts of a value higher than £3,000 will be potentially exempt transfers (PETs) *potentially exempt from Inheritance Tax provided you live for seven years after making the gift and do not retain a benefit.*

For the gift qualify it must be made after 18 March 1986, by an individual, to another individual or into a disabled persons Trust.

After three years taper relief reduces the rate of tax charged on that transfer.

To work out the taper relief, you first work out what the value of the tax payable on that gift would normally be (currently 40% of the gift). Then you work out what taper relief on the gift would be and deduct this from the previous valued you worked out. Please turn over for an example.

The current rates of taper relief associated with these gifts are:

Time between date of gift and death:	**Taper relief applied to tax due:**
3 to 4 years	20%
4 to 5 years	40%
5 to 6 years	60%
6 to 7 years	80%

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Example:

At your death you go over the Inheritance Tax threshold and therefore tax is payable on a gift of £10,000 which you gave your son three years before you died.

First work out what the tax would normally be (40% of £10,000 = £4,000)

Then work out what the tax would be based on the taper relief (20% of £10,000 = £2,000)

Then you deduct the taper relief from what would normally be payable (£4,000 minus £2,000) which means there would be £2,000 tax to pay on the gift.

After seven years lifetime gifts become fully exempt and fall outside of your estate for Inheritance Tax purposes.

If, at your death, your estate goes over the Inheritance Tax threshold, your executors will need to declare any lifetime gifts you made within the previous seven years to your death when they apply for the grant of probate (a grant is required before the assets will be released to your executors to distribute in accordance with your Will).

If they are not declared and HMRC subsequently find evidence of any such transfers then the tax is due from the recipient of the gift.

Gifts with reservation of benefit

For gifts to fall out of your estate you must live for seven years and must not retain a benefit in the gift.

If you gift a property but continue to occupy it or enjoy the rental income it produces, it is a gift with reservation of benefit and will remain within your estate for Inheritance Tax purposes regardless of the seven year rule.

If you would like to gift the family home but remain living there, you can look at paying monthly rent and provided certain rules are adhered to, this will then fall outside of your estate for Inheritance Tax purposes. Please ask to see our factsheet 'The Family Home'.

Excess income over expenditure

Gifts made out of surplus income may be exempt from Inheritance Tax. Income means salary; the returns from self-employment; rent received; commissions; dividend income from shares; interest paid on a bank /building society account.

If income was originally from an income source which has become a capital source then HMRC may refuse it. We consider income becomes capital after two years unless there is evidence to suggest otherwise.

Gifts made from capital contents of a purchased life annuity or any surplus income arising from a discounted gift trust where you draw down 5% per annum from the trust would not qualify as excess income over expenditure. The rules regarding this have to be satisfied for the revenue to accept it.

The gift must be made as part of ‘normal expenditure’, derived from income and the transferor must be left with sufficient income to maintain their usual standard of living.

‘Normal expenditure’ means you must show expenditure which, at the time it took place, was consistent with the usual spending pattern.

You can show this by examining the expenditure over a period of time which may show a pattern (for instance a regular payment of 15% of your income every year) or you can show it was ‘normal expenditure’ by establishing the assumption of a commitment or intention regarding future expenditure and thereafter complying with it (which will then in due course show a pattern).

There is no fixed minimum term however page 6 of the revenue’s IHT403 form sets out the required evidence and should be completed properly from the start and a new one made each year, you must ensure each one is kept and submitted as supporting evidence when the time comes.

The gifts should clearly be documented; therefore you should write a letter to the intended beneficiaries with your intentions and copies should be kept.   Annual exemption; maintenance of dependents and surplus income can all be claimed.

Maintenance of Dependents

Income can be applied between spouses or civil partners for their maintenance; to a child or spouse’s child for their education, maintenance or training up to 18 or until their full-time education or training comes to an end; and to a dependent relative. As long as it constitutes reasonable care and maintenance then as such will not be seen as gifting and therefore falls outside of your estate for Inheritance Tax purposes.

Maintenance of Dependents – when gifts of capital can apply

The case of McKelvey v HMRC SpC 694 was concerned with the Inheritance Tax exemption under s 11 of Inheritance Tax Act 1984 (IHTA 1984) for dispositions for maintenance of the family and dependants.

A daughter lived with and cared for her widowed mother. She was diagnosed with a terminal illness and realised that she would need to make provision for her mother to pay for nursing care after her own death. Accordingly, the daughter transferred properties to her mother which could be sold to pay for nursing costs and claimed that they were exempt transfers within s 11(3). This reads: “A disposition is not a transfer of value if it was made in favour of a dependent relative of the person making the disposition and is reasonable provision for his care or maintenance.”

HMRC accepted that gifts of this kind could be exempt, but not in this case because her mother refused to move into residential accommodation and the properties did not need to be sold. No part of the value of the properties had been used for the mother's care and therefore the transfers could not have amounted to reasonable provision for that care; no provision was in fact required.

The special commissioner decided that the stance of HMRC was too harsh. The meaning of reasonable provision in this context was an objective standard and it was clear that at the time the gifts were made the mother would need paid care. The deceased's decision to make the gifts for the purpose of providing funds for her mother's future care was reasonable.

HMRC then argued that even if that were the case, the value of the properties exceeded a reasonable amount and therefore an apportionment was necessary to disallow the excess. Accordingly, some calculations were made suggesting that the mother's care would have been needed for 5.5 years at a cost of £21,000 per annum plus a further £25,000 to cover the contingency of her admission to a home. The value of the properties exceeded this total by £28,500—and that amount was therefore ineligible for the exemption and was a chargeable transfer.

It is disappointing that the special commissioners chose to be so precise when the grounds for such precision seemed absent. What if the nursing care had been required for 5.75 years and the costs had gone up during that period? The figures would be completely different. However, having regard to the case of Phizackerley, [2007] STC (SCD) 328, the executors may have been happy with anything.

In that case, the special commissioner acknowledged that s 11 was wide enough to cover the transfer of a house but only if it relieved the recipient from income expenditure, for example on rent; a transfer for the purpose of giving the other party security was not reasonable provision within the meaning of S11.

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