UK INHERITANCE TAX PLANNING USING WHOLE OF LIFE ASSURANCE

Anyone who is UK domiciled or is deemed UK domiciled is subject to UK Inheritance Tax (IHT) on their worldwide assets.

If a client was born in the UK, has family there, maintains a home and visits the UK regularly, then it's very likely that they will be caught by the UK statutory residence test and be UK domiciled for UK Inheritance Tax purposes.

Furthermore, even if they leave the UK, shaking off their UK domicile can be a difficult thing to do unless they cut all ties to the UK and essentially take all the necessary steps to establish a permanent presence in another country, acquiring a different domicile of choice.

However, if the client then leaves that country or even a state or territory of a country where a federal tax system is in place, such as the United States of America or Australia, they revert to what is known as their domicile of origin and fall back into the UK IHT net for another 4 years. This isn't something that many people are aware of and, therefore, it's important to have appropriate planning in place.

Just to finish off on domicile, a person is 'deemed UK domiciled' if they are resident in the UK for 15 of the last 20 years of their life. This was reduced from 6 April 2017 from 17 years out of the last 20 years down to 15 years out of the last 20 years, and therefore now affects individuals earlier.

The current rate of Inheritance Tax is 40% and this is levied on all estates where they exceed what is known as the Nil Rate Band (NRB). The NRB is currently £325,000 and it will remain at this level until April 2026.

Now, £325,000 might sound like a lot, however, when a client starts adding up their assets they may find that they could have significantly more than this and, as such, are likely to face a hefty bill.

EXAMPLE

John is 41 years old, UK domiciled and has been working in Oman for the last 20 years. He has a partner and they spend most of his annual leave in the UK each year. He plans to work overseas for another 10-15 years and then move back to the UK on a permanent basis.

John is concerned about IHT as he read an article recently on the subject and wishes to know how this may affect his estate upon his death. John decides to seek professional advice and provides his adviser with details of his assets.

Assets	Current value
Contents	£35,000
Bank accounts/investments	£300,000
Other assets	£30,000
Total	**£365,000**

John's adviser points out that at this point in time John's exposure to UK IHT is £40,000 (total assets of £365,000, minus the IHT NRB of £325,000 = £40,000), which would mean a potential tax bill of £16,000 (£40,000 x 40% = £16,000). John isn't too worried about this and suggests that there will be enough money in his bank accounts to cover it.

But what would the position be in 15 years' time?

If we assume a modest growth level of 5% across all of his assets, then in 15 years' time, his estate would be valued at around **£750,000** leading to an IHT exposure of **£170,000**! If, on his death, there were not sufficient liquid assets to cover this amount, then assets may have to be sold, which is clearly not ideal.

All of this is explained to John by his adviser, resulting in dental surgery being required when his jaw drops to the floor. John asks his adviser whether anything can be done to mitigate his IHT liability and is ecstatic to find that there is.

Planning opportunities

To avoid his estate being placed in this position, John's adviser recommends a Whole of Life Assurance policy such as RL360's LifePlan with the level of life cover being sufficient to pay his intended IHT liability.

On his death, the policy would pay out this amount allowing his IHT bill to be paid without any assets having to be sold. This would preserve the value of his estate for his intended beneficiaries/family.

John decides that he requires Life Cover of £200,000, which is slightly more than his intended IHT liability, however, he thinks it best that there is a 'cushion' built in to cover any unforeseen circumstances. John is surprised to find out that having this level of cover could cost as little as £154 p/m.

John's adviser also points out that for the planning/IHT mitigation strategy to work as intended, the policy must be written into a suitable trust to ensure that the life cover does not fall back into his estate on death, making the position even worse. By placing the policy in trust, the life cover is paid into trust allowing the trustees to ensure that his IHT liability is settled thus enabling his estate to be administered in accordance with his wishes by his appointed personal representatives.

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 understanding of law and Her Majesty's Revenue and Customs' (HMRC) practice as at February 2021.

You should note however, that we cannot take upon the role of an individual taxation adviser and independent confirmation should be obtained before acting or refraining from acting upon the information given. The law and HMRC practice are subject to change.

RL360 Insurance Company Limited. Registered Office: International House, Cooil Road, Douglas, Isle of Man, IM2 2SP, British Isles. Registered in the Isle of Man number 053002C. RL360 Insurance Company Limited is authorised by the Isle of Man Financial Services Authority.