

IHT PLANNING

Why life insurance may be the best solution

By Tim Searle – Adviser, HNW Tax



For years, the most effective way to purchase residential property in the UK was by way of a Trust or special purpose vehicle (SPV) since it mitigated capital gains and inheritance taxes. Subsequently, HMRC have launched a raft of anti-avoidance measures over the years, and in 2017 declared that 40% Inheritance Tax (IHT) would be levied on structures owning UK property. In effect, nationalities from all over the world became exposed to this tax regardless of their holding structure, residence, passport and/or domicile.

HMRC, as with all government agencies around the world, openly exchange information with regards to the collection of taxes and legally bind professional firms, like trustees/bankers/lawyers, to disclose the beneficial owners of the same. As HMRC has direct visibility to the owner of the property, there has been a significant increase in the amount of tax collected.

The recent UK Budget stated that only 4% of British households pay IHT and with planning, using some of the 94 exemptions, it can be mitigated. However, the increase in IHT receipts has increased 20%+ year on year since 2017 which suggests overseas buyers are picking up the tab. The need to plan effectively is essential but few overseas property owners have the awareness let alone access to reliable advice to protect their assets.

It is worth noting that when a family member passes, the property automatically passes to the control of HMRC who will not release this asset until payment of the IHT is made within 6 months. The property cannot be sold or passed to family members until this liability has been settled. More importantly, failure to meet this deadline can result in the asset being subject to an unplanned, distressed sale process, or worse, confiscated.

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Insuring against this inevitable tax is an effective way to retain control of the asset and ensure the liquidity is in place to meet the tax bill. However, it is frequently overlooked by property owners and their advisors mainly because their expertise of insurance solutions is limited.

Insurance creates cash at times of need, and it makes financial sense to pass this inevitable risk to a major insurance company. Anyone owning UK real estate should know there is an IHT liability that is only getting larger which can trigger at any time. Passing this risk to an insurance company for a substantial proportion if not all of the IHT liability today makes financial sense and the permutations should be explored promptly. Even for those who think insurance is expensive, this option should be investigated. Furthermore, should the property be sold in future, the policy can be surrendered and your premiums can be returned; the solution may cost you nothing.

It is worth noting that mortgages/debts have to be settled on death so insurance can be a mechanism not only to meet the tax bill but also to settle the outstanding debt(s) so the asset passes clean and clear to the family as was intended. Insurance works in combination with your trustee so liquidity is created and deployed into the trust at a crucial period so tax liabilities can be settled, lenders can be repaid, and cash is created to give the family peace of mind.

Building a legacy property portfolio can be difficult so it is essential to protect these assets for inter-generational wealth succession without the risk of a surprise time sensitive 40% liability to the UK Government. Investors are urged to review how they hold their UK property to determine the level of their exposure. Investors should start with the assumption that this liability will be 40%. Seeking advice at an early stage is important to ensure that, if the insurance route is to be taken, it is in place promptly.

OPTIONS TO PROTECT ASSETS:



Sell

Dispose of the property, survive another 2 years and there is no further exposure to IHT. For sizeable trophy assets, this is not popular since the intention is for the property be passed down the family as an inter-generational asset in accordance with the wishes in the Trust. The sale may also trigger a capital gain which may also be subject to taxation.



Gift

By passing the asset to another person, normally a family member, then surviving for another 7 years will not trigger any IHT when the person gifting dies. That said, the person receiving the gift, typically a younger person, now has the liability. It should be noted that the owner can no longer benefit from the property and the person receiving the gift has full control to sell if they wish. For many patriarchal families, they do not like giving up control of the asset to a younger member of the family for fear of the assets being squandered. By retaining the asset (and control), the property will eventually be liable to 40% tax so the issue has only been deferred.



Insure

Deploy an insurance structure that will pay the IHT liability when, not if, it falls due. This allows full control throughout, creates the liquidity to meet the IHT bill in a timely manner, is far cheaper than paying the full cost in the future and allows the property to pass to the family swiftly.

A warm, golden-hour photograph of a family—a mother, a young girl, and a father—sitting on a grassy lawn and playing chess on a large wooden board. The sun is low in the background, creating a soft, glowing light. A modern house is visible in the background.

For more information

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