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New rules of Inheritance Tax on businesses and land

What families need to know and how to plan for the future

The October 2024 Budget proposed sweeping changes to Inheritance Tax (IHT), significantly tightening the laws that were previously more forgiving for families with trading businesses and farmland. Effective from April 2026, these types of assets will have reliefs capped at 100% for the first £1 million of qualifying assets. For valuations exceeding £1 million, the relief will reduce the IHT payable by 50%. While this is lower than the standard 40% rate, the inclusion of businesses and farms within the IHT net has sparked fierce debate, leaving many families scrambling to reassess their estate planning strategies.

This article looks at the implications of these changes, outlines steps to minimise their impact and explains why early planning is essential for securing financial peace of mind for future generations.

LIFETIME GIFTING IS A STRAIGHTFORWARD SOLUTION

For families affected by the new rules, lifetime gifting offers one of the simplest and most tax-efficient ways to minimise IHT liabilities. Assets gifted during your lifetime fall outside your estate for IHT purposes if you survive for seven years after making the gift. For business owners, additional planning strategies like holdover relief could address potential Capital Gains Tax (CGT) consequences when transferring shares or other assets. With holdover relief, the recipient inherits the assets at the donor's original base cost, thus avoiding CGT at the time of gifting.

However, gifting does present its challenges. Most importantly, these strategies are only practical if you can afford to give away assets without jeopardising your financial security. Detailed cash flow planning will help you understand how to ensure your income and future lifestyle needs remain intact. Encouragingly, the £1 million IHT relief for businesses and farms is now set to renew every seven years, similar to the nil rate band, allowing for multiple gifts over time while maintaining flexibility.

SELLING ASSETS AND PREPARING FOR TAX LIABILITIES

If gifting isn't a viable option, you might consider selling your business or land. However, this approach requires careful preparation, as the proceeds from a sale after April 2026 will attract the full 40% IHT rate on death instead of the reduced 20%. To mitigate this, families may think about placing assets in trust before a sale to shield the proceeds from the higher rate. Keep in mind, though, that the cost and administrative burden of trust arrangements are expected to increase after April 2026.

Additionally, selling assets triggers immediate CGT liabilities, so it's vital to plan for how to meet these costs. With the current economic climate of higher interest rates, there's growing popularity in utilising tax-efficient products like gilts or qualifying corporate bonds to generate post-sale income. These products can help preserve wealth and provide stability, especially in times of economic uncertainty. The effectiveness of this approach depends on individual circumstances and financial goals.

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LIFE INSURANCE AS A SAFETY NET

For families concerned about funding an IHT bill, life insurance can provide an effective solution. When a significant liability is anticipated, a policy written in an appropriate trust can be specifically established to cover the IHT charge. Policies are often designed to complement other strategies, such as gifting. For example, term life insurance may be utilised to cover the seven-year period during which a gifted asset remains part of the estate.

These policies are typically affordable and, when set up through a trust, can ensure that the insurance payout is exempt from IHT. However, premiums rely on factors such as age and health. We can guide you to assess whether this is a suitable option for your needs.

COMBINE STRATEGIES AND BEGIN EARLY

Given the complexity of the new rules, many families may benefit from adopting a blended approach. Combining lifetime gifting, trust arrangements and targeted use of life insurance provides more flexibility to meet the challenge. The earlier you start planning, the broader the range of options available to you. Acting now allows you to align your tax strategy with your personal goals and protect the business or land you've worked so hard to build. ■

IS IT TIME TO TAKE ACTION AND SAFEGUARD YOUR FAMILY'S FINANCIAL FUTURE?

If these changes to Inheritance Tax will affect your family, it's crucial to begin planning as soon as possible. We can ensure your estate is structured efficiently and your legacy is preserved for future generations. To discuss your circumstances and explore the available options, contact us. Together, we can develop a tailored plan to safeguard your family's financial future.