TURCAN CONNELL

Briefing Note

Residence Nil Rate Band for Inheritance Tax

Introduction

The summer Budget of 2015 introduced legislation which provides for a new Residence Nil Rate Band (RNRB) for Inheritance Tax purposes. The relevant legislation will come into full effect in respect of deaths on and after 6th April 2017 but also has an important impact in connection with downsizing from 8th July 2015. The RNRB will be in addition to the existing Inheritance Tax Nil Rate Band (the value of an estate which is not subject to Inheritance Tax) which has been frozen at £325,000 for each individual until 5th April 2021.

The RNRB applies when a "qualifying residential interest" is passed to descendants on death on or after 6th April 2017. The maximum amount of the relief has been fixed for tax years 2017/18 to 2020/21 as follows (with increases from 2021/22 being in line with the Consumer Prices Index):-

- £100,000 for 2017/18
- £125,000 for 2018/19
- £150,000 for 2019/20
- £175,000 for 2020/21

The amount of the relief available is the lower of the value of the residence (net of any mortgage) or the above noted RNRB for the relevant year. There will be a tapered withdrawal of the RNRB for estates with in excess of £2 million at the rate of the £1 for every £2 above the £2 million threshold.

What is a "qualifying residential interest"?

The RNRB is only available to set against a qualifying residential interest. This is a dwellinghouse which has been the deceased's residence at some point during the period in which his/her estate included an interest in that property. The value of the property may be owned by the deceased or might also form part of the deceased's estate as a consequence of the deceased being beneficiary of a trust and occupying the property as such. The RNRB is not restricted to a main residence and the deceased's Executors would have a choice as to which property to select if there is more than one, provided the deceased had occupied each property at some point. The property must still be owned as at the date of death even if it was not being used as a residence at that time.

Who should the property be left to in order to benefit from the RNRB?

The property must be "closely inherited" which means that, on death, it must be left to:-

1. Direct or lineal descendants – i.e. children, grandchildren, great-grandchildren, etc. This would include step-children, adopted children and foster children; or

2. Spouses and civil partners of the above lineal descendants and widows/widowers who have not re-married in the case of predeceasing lineal descendants.

The property would be "inherited" if it is left by a Will, passes on intestacy, passes by survivorship (in terms of the title deeds) or passes on death into an Interest in Possession Trust for lineal descendants (or their spouses, etc.). The provisions of the trust in which the property is settled on death are important and any existing trust provisions in a Will should be reviewed to check whether the RNRB would be available or not.

If the above conditions are not met at the deceased's death, it might be possible for the deceased's Executors to vary the terms of their Will after the death in order to get the benefit of the RNRB but ideally Wills should be reviewed during lifetime.

How is the RNRB applied?

The RNRB is only available against tax on the deceased's estate at the date of their death and cannot be set against tax on gifts made within seven years prior to death. The RNRB reduces the overall tax due on death. It is not specifically applied to reduce the tax due on the residence in question.

What if an estate is valued in excess of £2 million?

As mentioned previously, there will be a tapered withdrawal of the RNRB for estates worth in excess of £2 million. The taper applies at a rate of £1 for every £2 above the £2 million threshold. In 2017/18, estates exceeding £2.2 million will not benefit from the RNRB. The £2 million threshold will rise in line with CPI from 2021/22 onwards. The value of the deceased person's estate includes their interest in a qualifying Interest in Possession Trust but does not include the value of any gifts made by the deceased in the seven years prior to their death. The value of the estate is calculated before inheritance tax exemptions and reliefs (such as the spouse exemption or Agricultural and Business Property Relief) are applied.

What happens to the RNRB if it is unused on the death of the first of a married couple to die?

On the death of the second spouse, his or her Executors can make a claim for the first spouse's unused RNRB. There are a number of conditions to be met in order for the RNRB to be transferred in the same way as for the ordinary nil rate band.

Is the RNRB lost if a property is sold and the owner moves into a smaller property or residential care?

Additional legislation is expected shortly to allow the RNRB to apply on death to proceeds of the sale of a residence disposed of on or after 8th July 2015. This legislation should ensure that those who wish to downsize or sell and not purchase a replacement property are not discouraged from doing so. Under the proposed rules, an individual should be able to leave the sale proceeds of a residence (or their replacement residence plus the balance of the sale proceeds of their original residence) to lineal descendants (or their spouses, etc.) and receive the benefit of the RNRB. It will be important to keep good records of disposals of properties after 8th July 2015 in order to benefit from these downsizing provisions.