



## Deed of variation still has a role in IHT planning

**I**nheritance tax (IHT) planning has taken a bit of a back seat recently, particularly since the introduction of the £650,000 nil rate band for married couples and civil partners. Yet many people already wealthy in their own right, with assets well above the current nil rate band, are now inheriting additional wealth from parents and other relatives. While these people may be taking active steps to mitigate their IHT liability, the effectiveness of a deed of variation is often overlooked.

### What is a deed of variation?

A deed of variation enables beneficiaries of a deceased's estate to re-direct inherited assets in favour of another individual or into a trust. To be valid the deed of variation must be completed within two years of the date of death by the person who has inherited the assets, which must have formed part of the deceased's estate at time of death. For IHT purposes a variation is treated as though it is made by the deceased person, not by their beneficiary who is entering into the deed. The deed varies the disposition of the value of the assets inherited, rather than the actual assets themselves, so even if assets have changed form (for instance a house sold and the proceeds invested) a deed of variation can still be executed, subject to meeting the legal requirements.

Provided a capital gains tax statement is included, the beneficiary creating the deed of variation is not considered to have made a disposal liable to capital gains tax, even if the assets are subject to capital gains tax.

### What are the benefits?

A deed of variation is generally used to make an immediate or possible future IHT saving. One of the most common ways of doing this is to "skip" a generation. For instance, if the person inheriting the assets does not need the inheritance, they may decide to execute a deed of variation making their children the beneficiaries. In that way the assets do not fall within the parents' estate, where they would potentially be subject to inheritance tax on

### When can using a trust be beneficial?

In some cases varying an inheritance so that it passes directly to different individuals may not be desirable or sensible. For instance the beneficiary may wish to retain access to the funds, or they may not want the new beneficiaries to have control of the funds.

In cases such as these, the deed of variation can gift the funds to a trust and, since the gift is treated as having been made by the deceased for IHT purposes, the original beneficiary can continue to benefit from the redirected property at the discretion of the trustees (of which they may be one) without the gift being considered as a gift with reservation.

### How this works in practice

Katie dies leaving an inheritance of £250,000 to her son Bradley. After a few months, Bradley, who is married but does not have children, decides to use a deed of variation to place the whole amount into a discretionary trust for the benefit of his god-children.

Bradley and his wife own a house currently valued at £850,000, have a holiday home abroad and investments worth around £100,000. However, he is self-employed and has made little in way of pension provision.

As he is using a discretionary trust, Bradley is able to include himself as a beneficiary. He hopes that the trust will be able to supplement his and his wife's income in retirement, help fund his god-children during university, and hopefully in due course help them onto the property ladder.

By using a deed of variation, Bradley has removed the inheritance from his estate with immediate effect.

death. In effect this enables a beneficiary to give away assets they have inherited, without having to wait the usual seven years for the gift to fall outside their estate.

A deed of variation can also be used to place inherited assets in a trust, thereby removing them from the beneficiary's estate with immediate effect. This allows the original beneficiary to retain control by acting as trustee

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and also gives them the potential to continue to benefit from the assets under the terms of the trust.

It is important to remember that a deed of variation still has a role to play in IHT planning for married couples and civil partners, despite the introduction of the transferable nil rate band between such couples. With the nil rate band frozen, it may be advisable for assets left to the surviving spouse to be passed on to their ultimate beneficiaries, rather than accumulate in their estate, which may well exceed the £650,000 IHT threshold for married couples and civil partners. Of course, this would only be advisable if they were confident that their remaining assets were sufficient to provide for them for the rest of their life.

### More than one beneficiary?

If the terms of a will are to be varied, all the beneficiaries must be ascertainable and must consent to the variation. This can cause problems if some of them are minors, or where there are a number of different types of beneficiaries, for instance charities, or where people not yet born are included. In this case a court application must be made as the variation has to be approved by the court and professional advice should be sought.

### However, most cases are more straightforward

Martin and Brian's mother dies, leaving £100,000 in cash to each of them. Martin decides to use a deed of variation to pass his inheritance to his niece Sarah, who is 30 years old.

In this case Brian is not party to the deed of variation as the amounts were left to each brother on an outright basis. Martin's money can be passed to Sarah, who can then use it as she wishes.

Inheritance tax planning is complex and an emotive subject, yet one which concerns many people.

LighthouseCarrwood advisers are experienced in working with accountants to advise clients on inheritance tax planning and would be pleased to help your clients ensure that as much of their wealth as possible cascades down the generations.

**LighthouseCarrwood is one of the UK's leading providers of financial planning services to professional practices. We would be delighted to work with you to help your clients reduce their tax liabilities. To discuss how we could work with your firm in a way that suits you and benefits your clients and your business, please contact:**

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