

**Tax and  
Private  
Client**

# **The Residence Nil Rate Band**

Where are we?



**RadcliffesLeBasseur**



In order for the **RNRB** to be available, the QRI **must** be 'closely inherited'

## A summary of the RNRB

### Background

The Residence Nil Rate Band (RNRB) was announced in the July 2015 budget as a means of achieving the Conservative Party's manifesto promise to increase the Inheritance Tax (IHT) nil rate amount to £1 million for married couples/civil partners. The £1 million figure is achieved by using a combination of the Nil Rate Band (NRB) tax-free amount (fixed at £325,000 until April 2021), the transferable NRB (spouses/civil partners) and the RNRB.

In summary the RNRB is available when a person, who dies on or after **6 April 2017**, holds a '**qualifying residential interest**' (QRI) at their death, which is '**closely inherited**' by a '**lineal descendant**'.

The RNRB is going to be phased in, so that the maximum RNRB available, or the 'residential enhancement' will be:

- £100,000 in 2017/18
- £125,000 in 2018/19
- £150,000 in 2019/20
- £175,000 in 2020/2021

Following this, the RNRB will rise in line with CPI.

Although the detail (and there is certainly plenty of that) is summarised in this article, it is worth stating at the outset that practitioners, commentators and indeed the general public alike would be well justified in feeling somewhat short changed by this new IHT 'concession'. It is fair to say that the RNRB may change significantly, from its current complexion, over time.

### What is a 'qualifying residential interest'?

A qualifying residential interest is an interest in a dwelling house (including a garden or grounds of any size, but not woodland attracting relief from IHT) that was the deceased's residence at any point during their ownership of the residence. This includes foreign property but not buy to let property.

Where there is a gift to a trust under a will, the RNRB will only be available if the trust in question is a disabled person's trust, 18-25 trust, bare trust, a trust for a bereaved minor or an immediate post death interest; all of course for a lineal descendant(s).

If the deceased owned more than one QRI in different dwellings, their personal representatives must elect one of the properties within two years of their death; the residence does not have to be the deceased's residence for PPR. The residence can include property interests that are no longer owned at death, for example if they have downsized or moved to residential care.

If an individual holds more than one interest in the same dwelling, the interests will be combined for the purposes of the calculation.

### Who are 'lineal descendants'?

In order for the RNRB to be available, the QRI must be 'closely inherited', by one or more lineal descendants. Lineal descendants include children, grandchildren, remoter issue, stepchildren, foster children, adopted children (who are treated as children of both their natural and adoptive parents), a spouse or civil partner of a lineal descendant and a surviving spouse or civil partner of a lineal descendant who have not remarried.

### How is something 'closely inherited'?

The QRI can be closely inherited in a number of ways:

- where there was an actual disposition on the deceased's death (by will, intestacy, survivorship or under a s. 142 or s.144 IHTA 1984 arrangement)
- where the deceased has a qualifying interest in possession and there is an absolute gift on death or a gift to a disabled person's trust, or
- where the property was subject to a gift with reservation of benefit and as a result is treated as part of the deceased's estate.

Where there is a gift to a trust under a will, the RNRB will only be available if the trust in question is a disabled person's trust, 18-25 trust, bare trust, a trust for a bereaved minor or an immediate post death interest; all of course for a lineal descendant(s).

In all other trusts, the RNRB will not be available. This is the case even if the beneficiaries of the trust (i.e. discretionary) are all lineal descendants. Note that gifts to lineal descendants that are subject to an age contingency will not attract the RNRB because it is not an absolute/immediate interest.

The issues surrounding the use of non-qualifying trusts are possibly the most important practical considerations for day-to-day estate planning.

Where the property has been gifted absolutely in the deceased's lifetime, but there was a reservation of benefit, the RNRB can be available only if the gift was made to a lineal descendant.

### The transferable RNRB

Any unused portion of the RNRB can be transferred to a surviving spouse in the same way that any unused NRB can be transferred. This can occur where the first deceased spouse did not have a QRI on their death, or did have a QRI but it was not left to lineal descendants and consequently the RNRB was not available.

The RNRB can only be transferred where the surviving spouse dies on or after 6 April 2017, and, if the pre-deceased spouse died before 6 April 2017, the amount available to transfer to the surviving spouse is £100,000. As with the transferable NRB, the amount of RNRB that can be transferred is capped at an additional 100% of a surviving spouse's available RNRB but more than one pre-deceased spouse's RNRB can be transferred. Taper withdrawal (see below) also applies to a transferable RNRB where the pre-deceased spouse's estate was worth £2 million or more.

Where there is a transferable RNRB available from a pre-deceased spouse or spouses, either the personal representatives of the surviving spouse or the person liable to pay any inheritance tax due must claim this amount within the later of two years from the end of the month in which the surviving spouse died, or three months from the date on which the personal representatives started acting.



### Taper withdrawal provisions

A taper threshold has been set at £2 million until the 2020-2021 tax year, following which it will rise in line with CPI. This means that for every £2 in a net estate above the £2 million threshold, £1 will be withdrawn in relief. So, by 2020/2021 there will be no RNRB available to an estate worth £2.35 million.

'Estate' has the usual meaning under section 5 IHTA 1984 and includes exempt gifts on death, assets qualifying for APR or BPR, assets in which the deceased had a QRI and gifts in which the deceased had reserved a benefit. To this end the taper of the RNRB is not curtailed to the net value of residential property only.

The taper withdrawal is calculated by deducting the taper threshold from the value of the estate. This figure is then deducted from the default allowance (the total of any transferred RNRB and the available residential enhancement) and divided by two.

### Downsizing provisions

It was recognised that this legislation might unfairly prejudice those who had downsized, or even disposed of, their QRI (for example, to release equity to meet care needs or to move to a more manageable property), and as a result downsizing provisions have been outlined. The current proposal (which is in draft form and comments have been invited) is that where the deceased had downsized from a more valuable property, or had sold a residential property on, or after, 8 July 2015, the lost RNRB would still be available. This would take the form of an 'additional RNRB' equal to the RNRB that was lost as a result of the move, up to the value of the unused RNRB.

**“ The amount of the RNRB is limited by the value of the property, so the RNRB cannot exceed the value of the chargeable estate. Any property attracting APR or BPR, and any debts or charges on that property would also be deducted prior to any calculation. ”**

This preserved RNRB, along with any RNRB in the usual way, can be applied against the value of the deceased's estate if a lineal descendant inherits some part of the estate (that is derived from the proceeds of the downsize or sale). The death must occur on or after 6 April 2017 for the RNRB to be available, but there is no time limit as to how long before death the property was sold or downsized, or indeed how many times a downsize can take place, although only one 'downsizing' would be relevant for the purposes of the calculation.

The downsizing provisions are not available where the deceased occupied a property under the terms of a trust and the trustees sell or downsize on their behalf.

### Conditionally exempt property (heritage items)

If any part of the QRI is a conditionally exempt transfer under s.30 IHTA 1984, it is treated as not being closely inherited and as such the RNRB cannot be used. However, the RNRB can be transferred for use upon the death of a surviving spouse as long as no charge is triggered.

The amount of the RNRB is limited by the value of the property, so the RNRB cannot exceed the value of the chargeable estate. Any property attracting APR or BPR, and any debts or charges on that property would also be deducted prior to any calculation.

### How to calculate the RNRB

Firstly, it is necessary to establish whether the deceased has a QRI and if it is closely inherited wholly or in part:

- Has the deceased died on or after 6 April 2017?
- Does the estate include a QRI?
- Has this QRI been closely inherited by a lineal descendant?

If the answer to any of these questions is NO: Consideration should be given to carrying forward the unused RNRB to a surviving spouse (and what evidence may be required on the second death to support this)

If the answer to all of these questions is YES:

- Establish the value of the QRI and include any uplift for downsizing provisions
- Calculate any available RNRB (the relevant residential enhancement at the date of death) and including any transferable RNRB at the date of death from any predeceased spouse
- Establish the value of the deceased's total chargeable estate and consider the application of any taper withdrawal
- Calculate the RNRB combining the above findings and apply this to the deceased chargeable estate

## Practical considerations

It is perhaps ironic to contemplate practical considerations in relation to the RNRB, which in itself is not an entirely practical piece of legislation.

However, there are key planning issues to address both when advising new clients and when considering the application of the RNRB to existing clients (with planning already in place). It is disappointing that rather than simply increasing the NRB tax-free allowance to £1 million as between married couples/civil partners, the government has created an unnecessarily complicated regime that will no doubt cause much irritation and confusion amongst personal representatives and increase the costs and timing involved in the administration of estates.

### Key issues:

- Consideration should be given to what the RNRB means for clients' 'will trust' planning. Only trusts that provide for an absolute or immediate interest will attract the RNRB. This will be relevant for clients whose wills include old style NRB discretionary trusts, full discretionary trusts and wills with flexible life interest trusts. These trusts will not attract the RNRB and indeed in some cases may result in a QRI being locked away following the first death which would be more efficiently transferred to a surviving spouse outright or instead vesting absolutely (closely inherited) to a lineal descendant following second death.
- Consideration should be given to the disadvantages of aggregating a husband and wife's estates where this would push the total estate on the second death over the taper threshold.
- Discussions should be had with clients as to whether the protection or planning benefits of using a contingent trust outweigh the potential loss of the RNRB, and whether they might prefer to use a flexible IPDI with a power to advance capital which includes lineal descendants as beneficiaries, or to leave gifts absolutely with no age contingency.
- Advisors should consider whether to make their clients aware that they may need to review their estate planning.

*The importance of the RNRB should not be ignored. While it may not be currently relevant to all clients, increasing numbers of estates may fall within the legislation as they change in size over time.*

### General observations:

- As with the transferable NRB it will be important to retain relevant documents for later use when claiming the RNRB, for example records of the house valuation on the first death and evidence of downsizing. Personal representatives will need to be aware of the need to elect which property to apply the RNRB against and the criteria and records needed to use transferable RNRB, and the relevant timeframes.
- The RNRB will have no relevance to some estates due to their size (taper withdrawal will wipe out the availability of the RNRB for estates worth over £2.35 million), although the size and complexity of an estate can change greatly over time reinforcing the need for regular estate planning review.
- Elements of the RNRB legislation appear disproportionately unfair, particularly to unmarried people and those with no lineal descendants.
- Where it is possible, consider moving charges away from a property to enable the maximum amount of RNRB to be claimed.

### Get out of jail free card?

- Where a will incorporates a discretionary trust for the benefit of lineal descendants, personal representatives should consider using s.144 to appoint the QRI out to beneficiaries to obtain the benefit of the RNRB.
- Consideration should be given as to whether to use the reservation of benefit 'loophole' so that IHT is not reduced but the RNRB remains available.
- Clients should be made aware that deathbed gifts can be used to reduce the estate to below the taper withdrawal threshold. These gifts may remain within the estate as a failed potential exempt transfer, but they will succeed in reducing the estate value for taper withdrawal purposes.

### And finally...

The importance of the RNRB should not be ignored. While it may not be currently relevant to all clients, increasing numbers of estates may fall within the legislation as they change in size over time.

The key for advisers will be to familiarise themselves with the application of the new regime and where it may have a particular impact upon a client's estate planning.

It will be essential to keep the guidance in this area under review, as changes and refinement to the legislation are inevitable.

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