

Transitional Interests

Trustees and beneficiaries of "interest in possession" settlements have been offered an extra six months to adjust to new inheritance tax trust rule changes.

The Government changed the IHT rules for existing IIP trusts in the Finance Act 2006 and introduced a transitional period so that trustees could reorganise trusts set up on or before 21 March 2006 without being immediately affected by the new rules.

Under the legislation trustees had until 5 April 2008 to complete the transition. The transitional period will not now end until 5 October 2008.

The Treasury says the upcoming Finance Bill 2008 will clarify inheritance tax rules where trusts in place on or before 21 March 2006 on IIP terms come to an end on or after 22 March 2006 and are replaced with new IIP trusts for the same beneficiary.

Inheritance tax and capital gains tax valuations

The general rule is that if the value of an asset on death is agreed for inheritance tax purposes that value must also apply for capital gains tax purposes. This rule works well as ordinarily the inheritance tax event precedes the capital gains event, namely the subsequent disposal of that asset.

This year's Finance Bill will introduce the legislation announced in the Pre-Budget Report to allow the unused amount of the nil rate band to pass to the surviving spouse.

By the time of the death of the surviving spouse, the value of an asset inherited by the surviving spouse may already have been determined for capital gains tax purposes. This might be, for example, because that spouse has sold the asset.

The new legislation will ensure that a previously determined valuation for capital gains tax purposes is not displaced by a different one established for inheritance tax purposes. Otherwise the capital gain tax calculation would need to be re-opened.

Inheritance tax - use of unused nil rate band

Since 9 October 2007 individuals have been able to set any unused nil rate band on their spouse's death against their own estate in addition to their personal nil rate band. The nil rate band is the amount of the estate on which there is no Inheritance Tax to pay.

An estate is not subject to inheritance tax if it is within the nil rate band (currently £300,000). Transfers between spouses are generally free of inheritance tax. If an individual leaves all their estate to their surviving spouse then the nil rate band is effectively wasted. Many married couples have in the past drawn up relatively complex wills to ensure that the nil rate is used on the first death.

The new rules allow a surviving spouse or civil partner to use any nil rate band that their spouse, or civil partner, did not use against their inheritance tax estate, in addition to their own nil rate band. The new rules apply to deaths after 9 October 2007. They are also retrospective, meaning that the unused nil rate bands arising on

deaths before 9 October 2007 can be added to the nil rate bands of surviving spouses, or civil partners that die after that date.

[New IHT reporting rules](#)

These were published prior to the Budget and greatly simplify the IHT reporting process. They will come into force on 6 April this year with an effective start date of 6 April 2007.

The changes mean the reporting threshold has increased from £10,000 to a transfer that does not exceed the IHT threshold for gifts of cash or quoted shares and 80% of the IHT threshold for other asset classes.