Broadcast

Nunn Hayward

FACTSHEET: IHT REGULAR GIFTS OF SURPLUS INCOME

SPECIAL ISSUE

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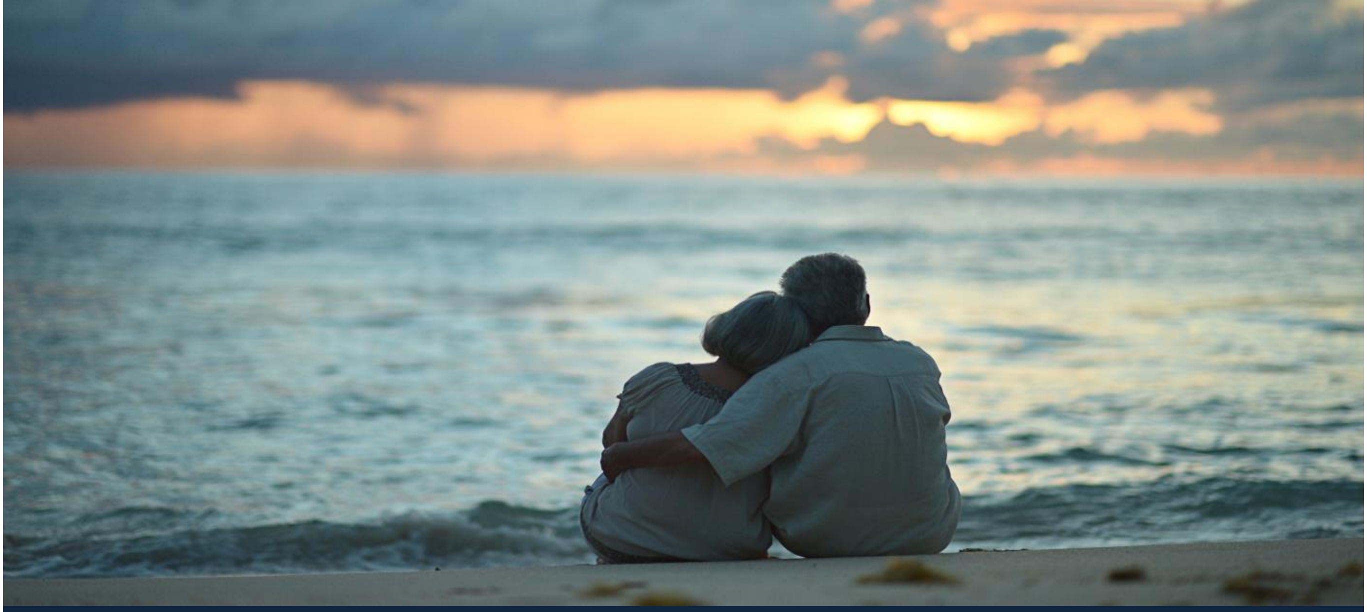

The normal expenditure out of income exemption allows the donor to make a series of IHT effective gifts from surplus income. There is no monetary limit to this exemption so the size of the exempt gift is only limited by the amount of the donor's surplus income. To qualify for the exemption, the gifts must:

- form part of normal expenditure (a regular pattern of gifting)
- be made out of income
- leave the donor with sufficient income to maintain their usual standard of living

Normal expenditure

The gifts must form part of a habitual pattern of gifting. This can be shown from the history of gifts actually made by the donor. Alternatively, where there is no such history, the exemption may still be claimed where it can be shown that the donor had made a commitment to future gifting.

There is no defined period for the length or the pattern of gifting in order to satisfy the condition. For example, a commitment to pay regular premiums to a life assurance contract could be satisfied merely by paying the first premium. Where the commitment is less clear cut, HMRC will typically look at a period of three to four years to establish a regular pattern of gifting.

Gifts do not have to be made to the same recipient every year provided they are paid to recipients within the same class, for example children or grandchildren. The amount of the gifts will typically be of comparable size but where an exceptional gift is made, the exemption may still apply up to the value of the previous gifts, with the excess falling outside of the exemption.

Income

Gifts must be made from current net income and not capital. Income for the purposes of the exemption does not follow what is defined as income for income tax. Instead it follows the normal accountancy rules. This is broadly income received from employment or pension, the natural yield from investments such as interest or dividends (not accumulated income) and income derived from assets such as rental income.

Certain income which isn't subject to income tax, such as income from ISAs, may still be covered by the exemption. Also pension drawdown withdrawals which may include an element of tax free cash are also treated as income. It still must satisfy the other conditions to qualify. For example, stripping out all the tax free cash and gifting it over a couple of tax years is likely to fail to establish a regular pattern of gifting. However, giving away flexi-access drawdown which includes withdrawals which are 25% tax free cash and 75% taxable income over a period of say 10 years would satisfy the exemption.

Some examples of allowable income include:

- salary
- self employed earnings
- dividends
- savings interest
- pension annuities and income from defined benefit schemes
- regular withdrawals from flexible pensions, including any tax free cash element
- ISA income
- rental income
- trust income

HMRC deem that withdrawals from investment bonds are capital in nature even though any gains are subject to income tax through the chargeable events legislation. Consequently bond withdrawals cannot be used to increase the amount of surplus income which can be given away.

Usual standard of living

After making gifts, the donor should be left with enough income to maintain their usual standard of living. If they have to resort to capital to maintain their lifestyle the exemption may be lost or limited.

The usual standard of living will generally be the standard at the time of making the gift. However, where unexpected circumstances cause a change to their standard of living, for example, unemployment or a sudden requirement for residential care, the exemption may not be lost even if they do have to make future gifts from capital. Also, where unexpected circumstances mean that changes in the donor's standard of living provide increased surplus income, this too may be gifted using the exemption.

Record keeping

The exemption is claimed following death of the donor by the personal representatives (PRs) completing HMRC form IHT403. It is helpful to the PRs if the donor can keep records of gifts made, with details of their income and expenditure, using the form during their lifetime. Nunn Hayward have developed our own form to assist in keeping these records that we maintain in conjunction with Self Assessment Tax Return preparation annually.

Gifts into certain types of trust which are chargeable lifetime transfers may need to be reported to HMRC on Form IHT100. For regular gifts from surplus income, it should be assumed that the exemption does not apply when establishing whether the gifts exceed the relevant reporting limits. If this would mean an IHT100 is required, it should be sent to HMRC so that the availability of the exemption can be agreed

We can help

If you would like help or have any questions on any of the topics discussed in this broadcast, please contact us to speak to a member of our dedicated team, call us on **01753 888211** or email **info@nhllp.com**