
The Residence Nil Rate Band:

What is it and how does it apply?

Inheritance tax can be very costly. When you pass away, everything you own – money, property, possessions, debts etc. – forms ‘your estate’. The value of your estate determines how much inheritance tax must be paid. Any inheritance tax will be deducted from the estate itself, so the more you have to pay, the less is passed on to your loved ones.

You can reduce the amount of inheritance tax that is payable by making the most of various tax-saving provisions. One of these is the Residence Nil Rate Band (RNRB).

What is the Residence Nil Rate Band?

The RNRB came into force for deaths on or after 6th April 2017. It can allow a greater portion of your estate to be taxed at a rate of 0% - a ‘nil rate’. As the name suggests, the RNRB can only be applied to your home or another property you use, or have used, as a residence.

A different nil rate band already exists for inheritance tax. Unlike the RNRB, this nil rate band is applied to the whole of your estate. Currently, this means that the value of your estate up to £325,000 is taxed at 0%, with anything above being taxed at 40%.

The RNRB is applied on top of the other nil rate band. If your estate qualifies, this means an even larger proportion of your estate will not be charged to tax.

How much could I save using the Residence Nil Rate Band?

The RNRB is set at a maximum amount, which changes depending on the tax year.

The maximum amounts are:

£100,000 in 2017 to 2018

£125,000 in 2018 to 2019

£150,000 in 2019 to 2020

£175,000 in 2020 to 2021

Beyond 2021, further increases are planned to keep in line with inflation.

For example, in 2017, if your estate's total value is £500,000, you would have:

The £325,000 'normal' nil rate band

+ The £100,000 RNRB

= £425,000 taxed at 0%

The remaining £75,000 would be taxed at 40%

= a tax bill of £30,000

But without the RNRB, £175,000 would be taxed at 40%

= a tax bill of £70,000

In this situation, the RNRB would have saved your estate £40,000

However, there are times when the maximum RNRB will not apply. These are:

- When the value of your home (or the share you own of it) is less than the maximum amount.

If you own a home worth £90,000, the RNRB would be limited to £90,000.

- When only a share of your home is going to your direct descendants.

A £100,000 house being left equally to your brother and your daughter would limit the RNRB to £50,000, because only half is being left to a direct descendant (your daughter).

When a home is being valued it is done based on open market value less any liabilities on it, such as mortgages or other secured loans.

How do I qualify for the Residence Nil Rate Band?

To be able to make use of the RNRB, there are several main requirements (the terms in bold are explained in more detail later in this factsheet):

1. Your **home** must form **part of your estate**
2. Your **home** must be **inherited** by to your **direct descendants**
3. The **total value** of your estate must be **under £2 million**, although a

proportion of the RNRB may still apply. See below under 'What if my estate is worth over £2 million?'

What counts as 'a home'?

To qualify, a home must be a property in which you have lived at some point during your lifetime. You don't need to have lived there for a certain amount of time and the home doesn't even have to be your main residence.

If you have several qualifying properties upon your death, your personal representatives can choose which one of them the RNRB should be applied to. However, the RNRB can only ever be applied to one home.

The home doesn't have to be in the UK either. If you are domiciled in the UK, a home abroad can be chosen, provided it meets the other RNRB requirements.

When will my home be 'part of my estate'?

Generally, all property you own at the time of your death will form part of your estate. There are exceptions however.

Some legal arrangements, such as certain kinds of trust, mean that the property involved is **not** considered to be part of your estate upon your death.

There are situations where the RNRB might still be applied when you have sold or downsized your home. See below 'What if I have sold, given away, or downsized my home?'

Who are my 'direct descendants'?

For the purposes of the RNRB, your direct descendants are:

- Your children, grandchildren, great-grandchildren etc. (your lineal descendants)
- The spouses or civil partners of your lineal descendants
- Your step-children, provided you were married or in a civil partnership with their parent
- Your adopted children
- Your foster children
- Any children to whom you have been appointed as guardian or special guardian

Therefore, direct descendants **do not** include:

- Your nephews and nieces

- Your siblings
- Your parents and grandparents etc.
- Your aunts, uncles and cousins

If you leave your home to a mixture of direct and non-direct descendants, you will still be able to apply some of the RNRB. However, as mentioned above, only a proportion of the RNRB will be available, based on the share which the direct descendants are to receive.

What counts as being 'inherited'?

Inheritance can be through the operation of your Will, through the intestacy rules (when you have no valid Will exists), or through other legal means (such as by a Deed of Variation).

Your direct descendants must become entitled to the home upon your death.

If, for example, the terms of your Will create a trust which requires your grandchildren to reach the age of 21 before they can inherit, the RNRB will not apply if they are still under 21 at the time of your death. This is because they would not become entitled upon your death.

There is no need for the actual home to pass into your descendants' hands, however. The RNRB can still apply even if the home is sold as part of the administration of your estate. Similarly, if you have sold your home prior to your death, the RNRB may still be available in some form. See below 'What if I have sold, given away, or downsized my home?'

Transferring any unused Residence Nil Rate Band between spouses or civil partners

If your spouse or civil partner died without using the maximum amount of their RNRB, the unused percentage can be added to your RNRB.

This also includes spouses or civil partners who died before the RNRB provisions came into force. Because it was impossible to use the RNRB before 6th April 2017, they will be treated as having a 100% unused RNRB.

For example, Arthur died in 2014 and his wife Beatrice died in May 2017.

Supposing Beatrice's estate is entitled to the maximum RNRB (£100,000), she will also be able to apply the unused percentage of Arthur's RNRB on top of that. His unused percentage is 100%. 100% of the maximum RNRB at the time of Beatrice's death is £100,000.

Therefore, Beatrice's estate will have an RNRB of £200,000 (her own, plus Arthur's).

It is the unused *percentage* that is transferred not the amount. This is significant when different tax years are involved. If Beatrice had died in May 2018 instead, the maximum RNRB for that tax year is £125,000. Her estate would have her own £125,000 plus 100% of Arthur's unused RNRB.

In 2018/2019 tax year, 100% of Arthur's RNRB equates to £125,000 – rather than the £100,000 in the previous example. Beatrice's estate would therefore have a total RNRB of £250,000.

Only you have to meet the RNRB eligibility requirements when transferring the unused RNRB from a pre-deceased spouse or civil partner. Provided you meet these, you can apply the transferred RNRB on top of your own.

There is no need for your late spouse or civil partner to have any 'connection' to the home in question. There is no requirement for them to have lived in the home, owned it with you, or given it to you.

Transferring unused RNRBs in this way is only possible between spouses and civil partners. Cohabitees and divorcees cannot do so, even if they owned the home in question jointly.

What if I have sold, given away, or downsized my home?

If you have sold or given away your home, some additional rules may allow your estate to still make use of the RNRB. These rules are only concerned with situations where possible RNRB entitlement has been lost; maybe because there is no home left in the estate or it has been replaced by one less valuable.

To illustrate, if Penelope sells her home worth £100,000, and does not buy a new house before her death in May 2017, her estate will have lost the chance to apply the maximum RNRB to her estate.

Alternatively, if she bought a house worth £60,000 before she died, the RNRB would be limited to £60,000. Her estate would have lost £40,000 from the RNRB due to Penelope downsizing to a less valuable home. In both situations, she might still be able to apply the full £100,000 RNRB.

To apply 'lost' RNRB in this way, several conditions must be met:

- You must have sold or given away your home after 7 July 2015.

- The home you sold or gave away met the definitions of 'a home'
- At least some part of your estate is going to be inherited by a direct descendant. However, when downsizing, 'lost' RNRB can only be applied if the remaining, less-valuable home is eligible for the RNRB – for example, that it is being left to direct descendants.

Even if all of these conditions are met, the RNRB cannot exceed the maximum amount which would have applied had the sale or gift not taken place. Also, only one sale or disposal can be accounted for using these provisions.

If no RNRB has actually been lost, these additional rules will not allow any more RNRB to be applied.

If Penelope, in the above example, had downsized from a house worth £200,000 to one worth £150,000 instead, the maximum RNRB would still be £100,000. None of the applicable RNRB would have been lost due to the downsizing.

What effect do trusts have on the Residence Nil Rate Band?

This is a complicated area, which is beyond the scope of this factsheet. A lot will depend on the type of trust involved and your own circumstances.

In general, it is the inheritance requirement which determines if the RNRB will be applicable. This centres on questions of whether the home is considered part of your estate and also, upon your death, whether the home then becomes part of your direct descendant's estate for inheritance tax purposes.

If trusts are involved in your estate plans, please contact us to discuss them in more detail.

What if my estate is worth over £2 million?

Some of the RNRB may still apply. The extent to which it will do so depends on how far over the £2 million threshold your estate's value is.

The RNRB provisions allow for a 'tapering away' after the £2 million threshold. This means for every £2 over the threshold, the RNRB is reduced by £1.

An estate worth £2,020,000, for example, can still apply the RNRB but it will be reduced by £10,000. Supposing the tax year is 2017/2018, the maximum RNRB available would be reduced from £100,000 to £90,000.

This tapering effect is also applied to unused RNRBs transferred from spouses and civil partners. If their estate was worth over £2 million, it will be tapered accordingly and will reduce the 'unused' proportion which can be transferred.

The Government have stated that the £2 million threshold *may* increase in 2020.

Do I have to do anything to make use of the Residence Nil Rate Band?

If you are hoping to make use of the RNRB, you do not need to make any formal claim.

All you really need to do is consider your plans for the future:

- If you are satisfied they will take advantage of the RNRB, make sure you have a Will in place to carry out your intentions.
- If your current plans will not make use of the RNRB, consider whether it is worth making any changes. There could be ways of fulfilling your testamentary wishes whilst saving as much on tax as possible.

Being able to apply the RNRB – and any unused RNRB from a spouse or civil partner – to your estate could make a significant difference to the inheritance tax your estate will have to pay.

Bear in mind that, even though your home does not need to pass by a Will to be eligible for the RNRB, having a Will gives you much more control over what happens to your estate upon your death. If you die without a valid Will, the intestacy rules could mean missing out on the RNRB.

For example, step-children are considered direct descendants for RNRB purposes, but if a step-parent dies without a Will, the intestacy rules mean that they would not inherit.

However, certain uses of the RNRB provisions will require your personal representatives to make formal claims when administering your estate. These include:

- using a late spouse or civil partner's unused RNRB; and
- claiming lost RNRB when 'downsizing'. Keeping details or records to document these events can help your personal representatives when they come to make such claims.

How we can help

If you have any questions about how the RNRB might apply in your circumstances, please get in touch.

Also, if your circumstances involve trusts or the downsizing provisions, it is strongly recommended that you contact us for a full discussion. That way, we can advise you on the RNRB exactly as it relates to your situation.

If you'd like more information call [01904 866139](tel:01904866139)
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