

Transferring an unused Inheritance Tax threshold

Since October 2007, you can transfer any unused Inheritance Tax threshold from a late spouse or civil partner to the second spouse or civil partner when they die. This can increase the Inheritance Tax threshold of the second partner from £325,000 to as much as £650,000 in 2009-10, depending on the circumstances.

How does the transfer work?

Everyone's estate is exempt from Inheritance Tax up to a certain threshold: £325,000 in 2009-10. This threshold is also known as the 'nil rate band'.

Married couples and registered civil partners are also allowed to pass assets from one spouse or civil partner to the other during their lifetime or when they die without having to pay Inheritance Tax - no matter how much they pass on - as long as the person receiving the assets has their permanent home in the UK. This is known as 'spouse or civil partner exemption'.

If someone leaves everything they own to their surviving spouse or civil partner in this way, it's not only exempt from Inheritance Tax but it also means they haven't used any of their own Inheritance Tax threshold or nil rate band. It is therefore available to increase the Inheritance Tax nil rate band of the second spouse or civil partner when they die - even if the second spouse has re-married. Their estate can be worth up to £650,000 in 2009-10 before they owe Inheritance Tax.

To transfer the unused threshold, the executors or personal representatives of the second spouse or civil partner to die, need to send certain forms and supporting documents to HM Revenue & Customs (HMRC). HMRC calls this 'transferring the nil rate band' from one partner to another.

When can the threshold be transferred?

The threshold can only be transferred on the second death, which must have occurred on or after 9 October 2007 when the rules changed. It doesn't matter when the first spouse or civil partner died, although if it was before 1975 the full nil rate band may not be available to transfer, as the amount of spouse exemption was limited then. There are some situations when the threshold can't be transferred but these are quite rare. See the section below for more information.

How to make the claim

When the second spouse or civil partner dies, the executors or personal representatives of the estate should take the following steps.

Step 1: Work out what percentage of the threshold you can transfer

The size of the first estate doesn't matter. If it was all left to the surviving spouse or civil partner, 100 per cent of the threshold was unused and you can transfer the full percentage when the second spouse or civil partner dies, even if they die at the same time.

Note that it isn't the unused amount of the first spouse or civil partner's nil rate band that determines what you can transfer to the second spouse or civil partner, it's the unused percentage of the nil rate band that you transfer.

If the deceased made gifts to people in their lifetime that were not exempt, the value of these gifts must first be deducted from the threshold before you can calculate the percentage available to transfer. You may also need to establish whether any of the assets that the first spouse left could have qualified for Business or Property Relief.

Step 2: Assemble documents from the first death to support a claim

You will need all of the following documents from the first death:

- a copy of the first will, if there was one
- a copy of the grant of probate (or confirmation in Scotland), or the death certificate if no grant was taken out
- a copy of any 'deed of variation' if one was used to vary (or change) the will

If you need help finding these documents from the first death, get in touch with the relevant court service or general register office for the country you live in (see links below under 'More useful links'). The court service may be able to provide copies of wills or grants; the general register offices may be able to provide copies of death certificates.

Step 3: Complete and send in the relevant forms

You'll need to complete form IHT402 to claim the unused threshold and return this together with form IHT400 and the forms you need for probate (or confirmation in Scotland).

You must make the claim within 24 months from the end of the month in which the second spouse or civil partner dies.

Exceptions - when the rules are different

In the following two cases, the rules for transferring a threshold are different:

- if the estate of the first spouse or civil partner had qualified for relief on woodlands or heritage property
- if the surviving spouse or civil partner had an unsecured pension as the 'relevant dependant' of a person who died with an Alternatively Secured Pension

The rules are complicated and you might want to contact the Probate and Inheritance Tax Helpline for advice.