Inheritance Tax

Pre-Budget Note

WOMEN'S BUDGET GROUP

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INHERITANCE TAX

Pre-Budget note from the UK Women's Budget Group

Inheritance tax is not a wealth tax, but a tax on the transfer of wealth that happens when someone dies.

Inheritance of wealth hinders intergenerational mobility, limiting opportunities for the majority by concentrating resources among a small rich group and increasing wealth inequality. Those with greater wealth are more likely to receive larger inheritances. [1] And from an equality of opportunity perspective, inheritance hinders social mobility because it gives recipients a head start. Taxing inheritances should therefore work to improve intergenerational mobility by reducing inequality in inheritances, a major source of wealth inequality.

But the current structure of inheritance tax – with its many allowances and reliefs creates opportunities for tax avoidance that allows wealth to remain concentrated in the hands of the few.

This briefing discusses why inheritance tax is important and how the current design of inheritance tax could be improved to make it more effective.

WHAT IS INHERITANCE TAX?

Inheritance Tax is a tax on the value of the property, money and possessions (the estate) left by someone who dies. It is currently levied at 40% of the value of an estate exceeding a £325,000 tax-free allowance. If an estate, worth less than £2m, includes residential property that is passed to a child or grandchild, the tax-free allowance can increase to £500,000. No inheritance tax is paid on estates left to a spouse or civil partner, to whom any unused tax-free allowance can also be passed on. Hence, two parents can between them leave up to £1m to their children without paying inheritance tax.

In 2020/21, 3.73% of deaths led to an Inheritance Tax payment, generating total public revenue of £5.76 bn.[2] Estates valued at £1million or more accounted for 81% (£4.7 billion) of the total inheritance tax paid.[3] Inheritance Tax is expected to raise £7.6bn in 2023/24, around 0.3% of GDP.

THE NEED FOR REFORM

The current structure of inheritance tax, with its many allowances and reliefs, creates opportunities for tax avoidance, more available to those with greater wealth. These allowances help concentrate wealth and hinder intergenerational social mobility. As currently designed, inheritance tax is ineffective and unfair.

Business Relief and Agricultural Property Relief are designed to allow businesses and farms to continue after their owner's death, but in practice are widely used as loopholes to avoid paying inheritance tax, pushing up land prices. Abolishing these reliefs might bring in around £1.4bn per year.[4]

In the longer run, Inheritance Tax (and the associated Capital Transfer Tax) should be replaced by a progressive lifetime receipts tax. Taxing receipts, rather than bequests, at progressive rates[5] (possibly allowed to be spread over many years), should incentivise the distribution of wealth to more recipients.[6] Special provision would be needed for the less well-off widowed and for a joint residence.

[1] ONS (2018) Intergenerational transfers: the distribution of inheritances, gifts and loans, Great Britain: 2014 to 2016
[2] HMRC (2023) Inheritance Tax statistics: commentary
[3] Ibid, Table 12.1
[4] HMRC (2023) Non-structural tax reliefs, December 2023.
[5] A. Corlett (2018) Passing on: options for reforming inheritance taxation. Resolution Foundation.
[6] Adam, S et al. (2011). Tax by design. Oxford: Oxford University Press. Chapter 15: Taxes on Wealth Transfers. Institute for Fiscal Studies.

PUBLIC OPINIONS TOWARDS INHERITANCE TAX

Although inheritance tax is said to be unpopular, most people support it. A survey conducted by Demos[7] showed that 3 in 4 people think that some amounts in inheritance should be taxed. The survey indicated that individuals are less inclined to favour an inheritance tax on wealth that has arisen through earnings from labour than on wealth accumulated in other ways.

FAIRER TAXATION FOR A GREEN AND CARING ECONOMY

There is an urgent need to rebuild our public services, tackle the climate crisis and address rising inequality. But this will require political will and substantial public investment.

It is for these reasons that any decision by a government to cut inheritance tax would be economically unreasonable and socially unjust. But an inheritance tax that fails to prevent wealth being concentrated in the hands of a few and enables wealthier groups to avoid tax is wholly inadequate.

Inheritance tax should be therefore reformed, initially by cutting unfair allowances, and eventually by replacing it with a tax on recipients.

Importantly, any reform of inheritance tax should be underpinned by gender and distributional analysis, examining not only its incidence on men and women (and other groups), but also the total revenue raised, given how vital enabling public spending is to women and those on lower incomes.

UK Women's Budget Group, February 2024

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[7] D. Goss, B. Glover (2023) The Inheritance Tax Puzzle. Challenging assumptions about public attitudes to Inheritance. Demos.