

Inheritance Tax Review: Call for evidence

Introduction

The Chancellor has asked the Office of Tax Simplification (OTS) to conduct a review of Inheritance Tax (IHT).¹ The purpose of the review is to explore simplification opportunities across two areas:

- the existing legislative framework, and
- the administrative processes through which taxpayers interact with HMRC in relation to IHT.

The scope of the review is set out in the OTS's scoping document.²

Alongside this call for evidence, the OTS has also published a [survey](#) which seeks to gather data about individuals' experience of IHT.

How to respond

In your written response to this call for evidence it would be helpful if you could outline your experience of the IHT system, and your role or roles in relation to it, for example:

- If you are writing in an individual capacity, how has the IHT legislation or process impacted on you personally? Have you administered an estate?³
- If you are a business owner and considering the implications of IHT, what is your business activity, what is its size, and what form does your business take (unincorporated, corporate, partnership etc.)?
- If you are a professional advisor, do you deal with probate, IHT planning, compliance or all of these? What size of estate do you usually handle? What is the typical net worth of your clients?
- If you are responding on behalf of a representative body, please describe the group and its members.

In answering the questions below, it would be useful if you could consider the potential impact on tax revenues of any suggestions you make.

A list of the professional advisors or representative bodies responding to this call for evidence will be included as an annex in the final report. Individuals who respond will not be named. No comments will be attributed to respondents unless the OTS has received permission to do so.

Please submit your response to this call for evidence by **8 June 2018**. Our email address is ots@ots.gsi.gov.uk.

¹ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/677301/CHX_letter_to_OTS_on_IHT_review.pdf

² https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/681434/OTS-IHT_Review_Scoping_document.pdf

³ This call for evidence will refer to people administering estates as 'executors'.

Consultation Questions

The OTS welcomes responses to all or any of the questions set out below, as well as any general or specific comments on the areas covered by the IHT review. There is no requirement to respond to all the questions; responses focusing on particular areas are just as welcome.

IHT forms, administration and guidance

IHT is paid by fewer than 5% of estates, yet the great majority of those administering estates must engage with IHT to some degree. They will need to fill in forms and deal with HMRC and probate processes. As well as answers to the questions below, the OTS welcomes any further suggestions as to how the IHT processes or guidance could be improved.

Payment and forms

- 1 If you have completed an IHT form, please state which form(s) you completed and whether you completed them in your professional or individual capacity. Please describe any problems you had in navigating the form(s) and provide any suggestions you have on how the forms or related guidance could usefully be simplified, made clearer or made easier to complete.
- 2 In general, the deadline for payment of IHT is 6 months after death, whilst the deadline for submitting the relevant IHT form is 12 months after death. Please describe any problems or issues that arise because of this.

Probate

In general, IHT forms must be processed by HMRC, and IHT must be paid, before probate is granted and the estate can be distributed. The benefit of this mechanism is that it ensures that IHT is generally paid before assets are distributed to beneficiaries, which avoids any need to recover the tax later.

- 3 Does this process create practical difficulties? Bearing in mind the benefit of this mechanism, what could be done to address any such difficulties? To what extent does the instalment payment option where the IHT is attributable to certain assets in instalments help mitigate any issues?

Estates that do not have to pay IHT

The nil rate band (NRB)⁴ is, broadly, the value up to which an estate has no IHT to pay. For most estates, there is no liability to pay IHT because the value of an estate is below the NRB.

In addition, an estate may be above the NRB, but still not have IHT to pay because an exemption applies. For example, where an entire estate has been left to a spouse, the spouse exemption will generally apply with the result that no IHT is payable.

- 4 Are there any disproportionate administrative or compliance burdens in establishing whether the value of the estate is below the NRB, or where the spouse exemption applies? How could these be reduced?

⁴ Currently set at £325,000, transferable between spouses and civil partners, where unused, to give a total possible combined value of £650,000.

- 5 Could the guidance on www.gov.uk be improved to support people handling estates on which no IHT will be paid? If so, how?
- 6 Are there other steps that government could take to raise awareness of the NRB to reduce anxiety around liability to IHT for people who don't have to pay it?

Administering an estate, record keeping and valuations

IHT is unique in that it is not generally administered by the person on whose assets it is paid, but by executors following a death. This can create significant challenges for executors in finding and reviewing the deceased's financial records, especially where the deceased person may have given gifts during their lifetime (see further below). In addition, executors must conduct their review in time to meet the deadlines for paying the tax and submitting returns.

- 7 What, if anything, could be done to help executors administer an estate and fulfil their obligations?
- 8 Have you been required to obtain a valuation of assets for the purposes of completing an IHT form? Was there any difficulty in doing so? Was the cost of the valuation commensurate with any IHT payable? What could be done to simplify this process?

Lifetime gifts to individuals

This section is about gifts to individuals. Different IHT rules apply to gifts to trusts and to other non-individuals but these are not covered here.

Where a gift is either: below certain monetary thresholds,⁵ a regular gift made out of a person's disposable income (the 'normal expenditure out of income' rules) or for the maintenance of a family member, then it may be exempt from IHT regardless of how long before death the gift is given.

In other cases, the IHT rules may interact to give different results depending on the precise situation. Relevant factors include:

- Whether the gift was made in the 7 years before death (gifts made to an individual more than 7 years before their death are exempt from IHT regardless of their size),
- whether all the gifts made in the 7 years before death total more than the NRB,
- whether the person giving the gift retained some sort of benefit from the gift (for example, someone who transfers title to their house to a child but continues to occupy the house without paying a market rent), or
- whether the person giving the gift specifies in their will who should suffer the cost of any IHT on the lifetime gift.

The interaction of the above will affect:

⁵ <https://www.gov.uk/inheritance-tax/gifts>

- whether a gift is fully exempt from IHT,
 - the rate of IHT payable on the gift (the rate of IHT reduces on a sliding scale, known as 'taper relief', depending how long before death certain gifts were made⁶),
 - who is liable to pay any IHT (the usual starting point is that it is the recipient of a lifetime gift who is liable rather than the estate), and
 - the value of the NRB to the estate as a whole (this will depend on whether the NRB is set against the value of assets that would otherwise have been taxed at 40%, or those that would have been taxed at a lower rate due to taper relief).
- 9 Are there any aspects of the interaction between the thresholds and exemptions relating to lifetime gifts that you find especially distortive or complex to understand and apply? Please provide examples.
- 10 How, if at all, should these rules be simplified? What could be done to improve public understanding of the rules? Have you found that the joint liability of the estate and the person receiving the gift can cause problems for executors or HMRC?
- 11 How, if at all, could the monetary thresholds and the various lifetime exemptions be simplified?

Businesses

If a business meets certain criteria, it may qualify for business property relief (BPR) from IHT.⁷ This relief is set at 50% or 100% of the value transferred depending on the type of business property and how it is held.

One such criterion is that the business must be wholly or mainly a trading business⁸ (the '50% trading requirement'). BPR can be restricted where there are non-qualifying 'excepted assets' on the business's balance sheet.

Like the rest of the IHT framework, BPR does not operate in isolation. It is part of a web of tax considerations that business owners need to consider when determining whether, when and how to pass a business on to the next generation. Three such tax considerations are capital gains tax (CGT) gift relief, the 'CGT uplift' on death, and entrepreneurs' relief.

CGT gift relief for business assets applies when a trading business (or a shareholding in a trading company) is given away during lifetime. If available, the effect of CGT gift relief is generally to 'hold-over' any capital gain that might otherwise have arisen, effectively transferring the original allowable cost to the recipient of the gift, and postponing any CGT liability until the recipient disposes of the asset.

⁶ <https://www.gov.uk/inheritance-tax/gifts>

⁷ <https://www.gov.uk/business-relief-inheritance-tax>

⁸ The actual test is negatively framed - the business must not consist wholly or mainly of: (1) generally, dealing in securities, stocks or shares, (2) dealing in land or buildings, and/or (3) making or holding investments.

The CGT uplift on death refers to the fact that when a person dies there is generally no CGT charge on their assets. Instead, the assets are generally treated as though they had been transferred to those inheriting them at their market value on the date of death, and no CGT charge arises.

Entrepreneurs' relief is a CGT relief that reduces the CGT rate to 10% in certain situations where an individual disposes of an interest in a trading business.⁹

The trading requirements for CGT gift relief and entrepreneurs' relief are more restrictive than those for BPR (no 'substantial' non-trading activities can be undertaken (the '80% trading requirement')), making it more difficult to make lifetime gifts without an upfront CGT charge than to secure relief from IHT on death.

For further information about how the different tax considerations interact across the business lifecycle, please see the OTS's Business Lifecycle paper.¹⁰

- 12 How, if at all, does the IHT framework, including the related tax considerations set out above, make business decisions challenging? For example, does it affect or distort decisions regarding:
 - a) whether to sell or transfer a family business to another vehicle or directly to the next generation during lifetime or wait until death,
 - b) the structure of the business (for example, how to hold non-trading assets),
 - c) the choice of business vehicle (for example a corporate entity, partnership, unincorporated business), or
 - d) investment in unlisted trading companies (including those traded on the alternative investment market (AIM))?
- 13 Do the different requirements for trading across BPR, CGT gift relief and entrepreneurs' relief cause complexity and, if so, how could this be addressed? Are there any other inconsistent definitions or approaches either within IHT, or across IHT and CGT and if so, does this cause complexity? Do you have any other suggestions as to how to remove complexity around the interaction between CGT and IHT?
- 14 The availability of BPR is not generally dependent on the size of a person's interest in a business or holding it for any period after death. Does this feature of BPR add to or reduce complexity?

Farming businesses

If a farming business and farmhouse meet certain criteria,¹¹ they qualify for agricultural property relief (APR), usually at 100%. In addition, other related tax considerations such as BPR, entrepreneurs' relief, CGT gift relief and the CGT uplift rules mentioned above may also apply to farming businesses.

⁹ <https://www.gov.uk/entrepreneurs-relief>

¹⁰ <https://www.gov.uk/government/publications/simplifying-the-taxation-of-key-events-in-the-life-of-a-business>

¹¹ <https://www.gov.uk/guidance/agricultural-relief-on-inheritance-tax>

- 15 How, if at all, does the IHT framework, including related tax considerations set out above, make business decisions challenging? Does it affect or distort decisions regarding:
- a) whether and when to sell or transfer the farm to another vehicle or to the next generation, or downsize during one's lifetime, or wait until death,
 - b) the choice for farm owners of letting out farmland versus farming themselves or via a contract farming arrangement,
 - c) the inhabitants and use of the farmhouse,
 - d) the choice of business vehicle for the farm (for example a corporate entity, partnership, unincorporated business), or
 - e) the structure of the business (for example, how to diversify or hold non-trading assets)?
- 16 Could the criteria for being a farmhouse or the process of determining the agricultural value of the farmhouse be simplified? If so, how?
- 17 What, if any, complexities arise from the fact that BPR and APR overlap, at least in part? Are there discrepancies in the way that they operate? Would it help if APR was replaced by BPR or if the two were merged?

Charitable giving

If a person gives to charity in their will or during their lifetime, this is exempt from IHT. If 10% or more of a person's net estate is given to charity in their will, IHT may be payable on the whole estate at a lower rate of 36%. There are also complex rules about the incidence of IHT between exempt and non-exempt parts of the residue on death.

- 18 How well do you think the charitable exemption and the lower rate of tax on death is understood by advisers or the public? Please tell us about any areas of complexity in the application of this rate, or the charitable exemption, along with any suggested improvements.

Other areas of complexity

- 19 Please tell us about any other areas of complexity in applying any IHT rules, reliefs or thresholds not already mentioned in your response, along with any suggested improvements. You may, for example, wish to comment on the residence nil rate band, the IHT treatment of trusts, the IHT treatment of personal pensions and life insurance products, or the conditional exemption for certain works of art or heritage assets.

Wider IHT system

- 20 Do you think that the IHT system should be reformed more widely to simplify it? If so, how? Should some IHT exemptions be removed to fund a lower or graduated rate or a higher NRB? If so, which ones? Are there any useful lessons that could be learned from other countries? If so what, and from which countries?