



HM Revenue
& Customs

Inheritance Tax: Simplification of trust charges – the next stage.

Summary of Responses
December 2013

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Executive Summary

Introduction

- 1.1 This document responds to the consultation: *Inheritance Tax: Simplification of trust charges – the next stage* – published in May 2013.
- 1.2 HMRC is very grateful to all those who responded or participated in meetings (listed in Annex A) for taking the time to consider the issues raised by the consultation document.

Aim of the consultation

- 1.3 The purpose of the consultation was to seek views on:
 - proposals for simplifying the calculation of IHT on relevant property trust charges;
 - a deeming rule for the treatment of accumulated income;
 - proposals to align payment and filing dates to those of the self-assessment framework; and
 - splitting the nil-rate band available to trusts.

Overview of the responses

- 1.4 HMRC received 53 responses from individuals, trustees, practitioners and professional bodies.
- 1.5 Respondents were generally positive about aligning the filing and payment dates despite concerns that the suggested dates of 31 October for filing and 31 January for payment might add to trustees' administration burdens at what was already a very busy time of year.
- 1.6 Comments regarding the proposed standard approach to the treatment of accumulated trust income were mixed but trustees and practitioners were generally concerned about the interaction between trust law and tax law.
- 1.7 The consultation document proposed the splitting of the nil-rate band as an alternative to the requirement on trustees to gather historical information that aggregated settled property in order to determine the rate of tax.
- 1.8 Although respondents welcomed the consultation's key themes of simplification and alignment, most were strongly opposed to the proposals for dividing the nil-rate band. Two main reasons were given: Firstly, it would be an onerous task for trustees to try and gather details of all the trusts the settlor had set up. Secondly, they felt that the proposals were unfair and amounted to retrospective legislation if the proposed changes were applied to existing trusts.
- 1.9 The detailed responses to the consultation are set out in chapter 3.

Key changes

1.10 As a result of the consultation and representations made by key interest groups during the course of meetings, we have made some changes to the original proposals. We now propose to:

- introduce a new rule providing for the treatment of accumulated income to apply to the ten year anniversary charge only;
- align filing and payment dates to six months after the end of the month in which the event occurred;
- consult further on alternative proposals to split the nil-rate band that will meet trustees concerns whilst maintaining tax revenues; and as a result
- put the simplification of the calculations on a slightly slower track so that any new legislation is introduced in Finance Bill 2015; and
- defer the proposal to require trustees to “self assess” IHT due until Finance Bill 2015.

Next steps on the legislation

1.11 Draft legislation for inclusion in Finance Bill 2014 on the treatment of accumulated income and the alignment of payment and filing dates was published on 10 December for technical consultation, and we would welcome comments. If necessary we will review and amend that legislation once the consultation closes on 4 February 2014.

1.12 We will consult further in respect of consideration of the nil-rate band.

1.13 Legislation on the nil-rate band and simplification of calculations will be included in Finance Bill 2015.

2. Introduction

Content of the responses

2.1 The responses commented on the detail of the simplification of the IHT trust charge calculations, the treatment of accumulated income and the alignment of payment and filing dates.

Simplification of trust charges

2.2 The main concerns raised were:

- The proposals would mean an increase in administrative burdens for trustees and practitioners. HMRC would be replacing one set of complexities with another as trustees would need to find out about all other trusts in existence causing difficulties with calculating the charge and signing off the Return. Consequently, trustees would have to start keeping additional records of trusts held elsewhere.
- Some considered that it was unfair to apply the proposed new rules to existing trusts and settlors who had based their legitimate tax planning on the current rules.
- The new regime should only apply to smaller trusts or those set up after a given date.
- Insurance policy trusts would be brought into the new rules when there was very little money in them.

Income that may be accumulated

2.3 Whilst there were mixed views on the proposals, the overall message was that there wasn't much enthusiasm for change.

- The main objection to the proposal to introduce a deeming provision was that there would be a mismatch between the trust law position and the tax law position – that is income which is still income for tax purposes will be capital for IHT (but not other) tax purposes.
- Many respondents asked how payments would be matched – first in first out or last in first out and whether there would be set rules.
- There were also numerous suggestions that two years is not long enough.
- Many respondents said there would be an element of double taxation – the concern here was that income becomes capital so later distribution is taxed as capital and loses the Income Tax credit.

Aligning filing and payment dates

- There was a very positive response in principle to changing existing payment and filing dates though the idea of the taxpayer doing the calculation was less welcome.
- Most respondents did not think that alignment would result in any savings for practitioners, trustees or the customer.
- There were a number of suggestions to the effect that any changes should apply more widely to IHT. However, this is beyond the current remit.

3. Responses

- 3.1 In this chapter we set out the questions asked in the consultation and provide some detail on the responses received. We follow the order in the consultation document and include the original sub-headings to assist. Each section sets out the main themes that emerged during the consultation, before setting out how we are taking forward the issues and ideas raised.

Options for simplification

Question 1: Do these proposals meet the objective of reducing complexity and administrative burdens and in what way(s)?

- 3.2 Many of the respondents said that the proposals detailed in the consultation document would reduce the complexity and administrative burden in calculating a relevant property charge as, under the current regime, the calculation is relatively complex and obtaining the historical information required can prove very problematic in practice. Not having to take into account previous lifetime transfers and non-relevant property would be a welcome simplification. No longer having to establish facts potentially going back 17 years would save a great deal of time and effort trying.
- 3.3 However, there were a number of views expressed stating that the requirements to bring into the calculations non relevant property, related settlements and the settlor's cumulative transfers were relatively insignificant and in most cases trustees will already have the necessary information.
- 3.4 Other respondents were concerned that any benefits of simplification would be outweighed by the additional difficulties in establishing the correct number of settlements created by the same settlor and the record keeping requirements that would need to be put in place to ensure that the information is kept up to date.
- 3.5 There were several views that the current rules should not be changed. Respondents reported that whilst the calculations may be complicated and burdensome the rules are well understood by practitioners and systems are in place to make the calculations. They added that in almost all circumstances the application of the rules and the need for appropriate record keeping can be anticipated at the point of creation of the trust.

Question 2: Does a single rate of 6% present any difficulties, particularly for smaller trusts?

- 3.6 There were mixed views about a single rate of 6% to calculate the IHT due on relevant property trust charges. Although respondents accepted that a flat rate would aid simplification, most were concerned that a rate of 6% would result in higher charges for smaller trusts and if the nil-rate band was split, many non taxable trusts would become taxable.

- 3.7 One respondent suggested that the use of a 6% flat rate should be on an opt in basis and should not commit the trustees to use the same rate for any future IHT events where the tax at stake could be significantly higher. Another suggestion was that a lower rate could be used for smaller trusts such as those with relevant property with a value of less than £1million.
- 3.8 Others commented that the proposed flat rate of 6% could marginally simplify the IHT calculation in specific cases although it was unlikely to save substantial amounts of time overall for practitioners.
- 3.9 There were also a number of respondents that suggested a lower rate of 4%. One professional body said that as the proposals are supposed to be tax neutral, whatever rate is set, must not increase the tax yield.
- 3.10 Some of those who responded made the point that in their view, the introduction of a standard 6% charge in the way proposed would involve a double charge on exits in the previous ten years. They explained that under the current regime the nil-rate band is reduced by the amount of any distributions but this reduction is used only as part of the calculation of the 'estate rate' – there is no double charge because the periodic charge is only on the amount that remains relevant property on the ten year anniversary. In their view the fair way to eliminate this 'double charge' is for previous exit charges not to reduce the nil-rate band available on a ten year anniversary.

Question 3: How much time would the simplified method save trustees and practitioners, on average per trust?

- 3.11 The general view was that for many practitioners the proposals were likely to increase the time required due to the number of additional trusts that would become subject to IHT exit and anniversary charges as a result of the reduction in the nil-rate band available to such trusts.
- 3.12 Respondents were concerned with the additional fact finding that would be necessary if the nil-rate band was divided by the number of settlements created during a settlor's lifetime. They believed that the proposals would simply replace one set of complex rules with another that are potentially even more onerous.
- 3.13 Several others commented that information would also be needed in respect of life policies held in trust – all too often individuals would not be aware that a trust was in existence and as a result it would be difficult if not impossible for trustees and practitioners to establish the number of trusts created by an individual.
- 3.14 Another respondent mentioned that in their experience, the most time-consuming aspect of undertaking a ten year charge calculation is establishing a market value for the assets held by the trustees but this aspect would remain unaffected by the proposed changes. However, they did acknowledge that there would be some time savings due to the fact that it would no longer be necessary to consider the value of related property at the date the trust was settled albeit (in their view) in a small minority of cases.

3.15 Others simply stated that it would be difficult to quantify the time saved as no two trusts would be the same. There was also a general view that greater savings in time are likely to be achieved instead through improvements to forms on which trust charges are required to be reported.

Question 4: Will there be significant costs to trustees and practitioners familiarising themselves with the new system and if so can you quantify these?

3.16 A number of respondents stated that this was a difficult question to answer without knowing what the final changes would be. They acknowledged however, that if simplification was achieved, the costs of familiarisation would be minimal. But some had reservations on whether this could be achieved alongside HMRC's other aims of retaining the current levels of inheritance tax revenue and maintaining an acceptable degree of fairness.

3.17 One respondent made the point that the proposals were not likely to impact the vast majority of trust cases that have no significant involvement with professional tax advisers and which do not pay any appreciable amount of tax under the current rules. In their view, the proposed new rules were most likely to impact on those trusts which do hold appreciable wealth, and involve professional tax advisers and IHT is paid. They believed that the proposals would result in increased research and interaction with settlors and trustees of any other settlements established by them in order to establish what the position might be. They added that this was likely to be time consuming and could result in irrecoverable time costs.

3.18 Another respondent did not perceive that the new rules would take a long time to understand so in their view training costs for professionals were not likely to be high – perhaps a couple of hours, with costs of around £300 per professional. However, they believed that it was likely that costs would be incurred in explaining the new system to existing trustees and considering the tax affect the new rules would have. They estimated that costs for this, depending on the size of the trust, could amount to around £300-£500 per trust.

3.19 Others mentioned that if there was a two tier approach with an opt in for existing trusts, this could result in increased costs as trustees considering advances may need to pay professionals to perform two lots of calculations to see which regime they were better off making the advance under.

3.20 One respondent stated that although practitioners would need to familiarise themselves with the new rules, they expected the time required to implement the new rules for each new trust to be much more considerable. They envisaged that the new rules would be much more onerous because of the increase in the number of smaller trusts incurring charges and consequently trustees were likely to incur additional professional fees in order to comply with their filing and payment obligations.

3.21 Various respondents recognised that the rules on trust charge calculations would remain a specialist area and those involved in administering trusts would cope with the changes as they have coped with other changes in recent years. In

terms of costs, they did not think that these would be significant provided any changes adhered to the criteria of simplification.

- 3.22 Two respondents mentioned that as a result of the proposed changes bringing smaller trusts into the tax net, certain trusts may encounter liquidity problems due to the investment strategy adopted at the time the trust was set up or the fact that they contain illiquid assets such as life policies. They argued that the proposed changes would increase the compliance burden on trustees of existing small trusts.

Nil-Rate Band

Question 5: Do HMRC's proposals in paragraphs 54 – 58 on the way in which the nil-rate band should be split for ten year and exit charges provide the right balance between fairness and the risk of manipulation?

- 3.23 Most respondents felt that the proposals did not strike the right balance between fairness and the risk of manipulation. They argued that if HMRC's intention was to deal with IHT avoidance then this could have been addressed by targeted legislation which would have been fairer.
- 3.24 Many respondents claimed that if the intention behind the amended rules was to simplify the calculations, trustees of existing trusts should be given a choice to adopt the new rules. Those that do not wish to 'opt-in' to the new regime should be able to continue to prepare calculations under the current rules.
- 3.25 There were also a number of views that the proposed division of the nil-rate band unfairly penalises sensible and moderate estate planning which up until now has been acceptable to HMRC. Respondents said that it would be unfair to retrospectively impose charges on arrangements put in place with due regard to HMRC rules and settled legal principles.
- 3.26 Many of the respondents felt that a change to the nil-rate band is not simplification but a fundamental change to the IHT regime. There were many views expressed that it is fundamental to the structure of IHT that with other gifts during lifetime an individual can recycle their nil-rate band after a seven year period. Respondents claimed that HMRC had not given a reason as to why the same should not apply in connection to a transfer into a trust. They did not see any particular difficulty with the current system of reviewing chargeable transfers made in the previous seven years.
- 3.27 Others were concerned that well settled law which had been approved in case law and also recently in HMRC's guidance relating to the General Anti Abuse Rule should be overturned retrospectively bringing many formerly non reportable and non chargeable settlements into charge.
- 3.28 One firm of accountants pointed out that many death in service benefits are written in trust so that beneficiaries do not suffer IHT on what is essentially a compensation payment. They were concerned that such trusts might be

incorporated in any division of the nil-rate band, and suggested that consideration is given to any legislation that is introduced to exclude such trusts.

3.29 One of the professional bodies remarked that it was essential that whatever system was introduced, it should be simple to operate and be demonstrably revenue-neutral given that the driver for change was the fact that the information requirements have become unworkable. They also stated, along with another professional body, that the lack of statistical evidence concerning the numbers of trusts affected by the proposed changes, and the lack of financial modelling in the Tax Impact Assessment, suggested that policy was being proposed without the practical implications being properly addressed.

Question 6: Are there any other ways that the nil-rate band could be split that would not risk a loss to the Exchequer?

3.30 One of the key points made by respondents was that simple division of the nil-rate band would be unacceptable. They suggested that the settlor should be able to make an election to pro-rata the nil-rate band to account for the level of funds held in each trust or pro-rating the nil-rate band in accordance with the market value of the relevant trusts at the time of the relevant event. Whatever method was used, each settlor must be given the flexibility in the method of allocation to prevent wasting any unused nil-rate band.

3.31 Other suggestions included:

- The introduction of a de-minimus so that trusts with an asset value of less than £1000 could be ignored when dividing the nil-rate band.
- Trustees should be given the opportunity to rearrange relevant property settlements or wind them up prior to implementation or the new rules should not apply to existing settlements unless the trustees so elect.
- There should be an opt-in provision so that trustees that do not have the information available to calculate the charges under the current regime can opt-in to the proposed new regime. This will ensure that those trustees that have kept appropriate records will not be disadvantaged.
- The introduction of similar measures that have been in place in relation to CGT and more recently introduced for IT where the CGT annual allowance and IT lower rate band of £1,000 is shared between related settlements subject to a maximum of five. Trustees should be aware if a settlor has created at least five settlements and this information is readily available to HMRC under the self-assessment system.
- To consider trusts established within a seven year period independently. Any trusts established more than seven years apart would be discounted.
- Allowing a settlor to elect to exclude a particular trust from the calculation used to divide the nil-rate band; and allowing the settlor to elect to split the nil-rate band based on the market value of assets held in the trust.

- Existing trusts should benefit from grandfathering of the existing rules for a reasonable period of time (perhaps until the next periodic charge or ten years to allow for a complete charging cycle) to enable trustees to consider the impact of any changes with beneficiaries and take action as necessary.
- New trusts could be subject to progressive rates of IHT – e.g. trust fund value up to first £50,000 exempt, between £50,001 and £200,000 3%, between 200,001 and £350,000 4% etc.
- There should be a system that operates on full years rather than quarters.
- Consideration in favour of applying the rules to trusts created after a determined future date only. This would avoid the retroactive tax charges on pre-existing trusts. However this would create an additional tax regime that would be against the principle of simplification.
- Rather than a complete change of regime a twin track approach could be adopted so that a simplified regime applied to smaller trusts at a reduced rate of tax, and that the current rules could continue to apply (either by opting in or opting out) to the larger and complex trust arrangements.

Further proposals

- To reform and simplify the elements of the IHTA section 71F charge (on age 18 to 25 trusts) which mirror the rules for relevant property trusts. Section 71F (7) (8) and (9) refer to a settlement rate calculated by reference to a postulated chargeable transfer, involving the settlor's previous chargeable transfers, related settlements, historic values etc. These provisions should be reformed and simplified at the same time and in line with the ten year charging regime.
- Another possibility is to have a de-minimus nil-rate band available regardless of the number of trusts set up by the settlor. Any trust can then simply work with the de-minimus amount, which may be particularly useful for smaller trusts. This proposed treatment is the same as was introduced for the basic rate band so such a precedent has already been set.

Commencement provisions

Question 7: Would applying the new rules from a set date cause trustees and practitioners any difficulties?

Question 8: In what other way could the new rules be implemented?

3.32 One respondent said that bringing the new rules in from a set date would add an additional layer of complexity when dealing with trusts. It is already necessary to consider if a trust was created before 1974, 1982, and 2006 to decide on the correct treatment for IHT and income/capital gains tax provisions.

3.33 It was suggested that HMRC could apply the new rules to all affected trusts from a given date but to allow an election to use the old rules for a transitional period

of perhaps two years, to allow financial planning that has already been made on the basis of the old rules to proceed.

3.34 Other respondents believed that it would be inherently unfair to apply the proposed new rules to those trustees who have maintained good records and complied with the current regulations. They felt that it would be appropriate to provide trustees with an opt in to use the simplified methods if they do not have the necessary historic records to comply with the current rules and there is very little tax at stake.

3.35 One of the professional bodies commented that although it would seem superficially fair that existing trusts should be able to be taxed under the present relevant property regime, the impracticality of running two regimes in parallel militates against this. They added that a substantial lead in time, in excess of one year, would be their preferred option.

HMRC's response

3.36 We have considered all of the responses and recognise that there are genuine concerns around the IHT calculation of trust periodic and exit charges and in particular with the division of the nil-rate band. The two key objections to the proposals were that that they would replace one set of complex rules with another that was potentially more onerous for trustees and their advisers and that it was unfair to apply what was perceived to be retrospective legislation to existing trusts.

3.37 In view of the comments made during the meetings held with the professional bodies and other interest groups and the representations made in the responses received, we will consider alternative ways in which the calculations can be simplified fairly, without loss to the Exchequer and without the risk of fragmentation of settlements and will consult further on this. The Government is committed to ensuring fairness in the tax system and reducing undue burdens on trustees and their advisers. Consequently, this part of the measure will now be deferred until Finance Bill 2015.

3.38 However, simplifying the calculations by removing the need for historical data without some means of dividing the allocation of the IHT nil-rate band between trusts created by the same settlor could result in significant loss to the Exchequer as it would allow individuals to set up multiple trusts each benefitting from its own nil-rate band and therefore not liable to any IHT charges.

3.39 Many respondents asked why trusts should not be able to renew the nil-rate band after seven years in the same way that individuals can. We believe that the tax system should be neutral in its treatment of trusts, neither penalising nor encouraging their use i.e. wherever possible to provide equality of treatment between direct transfers to individuals and indirect transfers to individuals via trusts.

3.40 Relevant property trusts incur

- a 20% “entry” charge on lifetime transfers into trust exceeding the IHT nil-rate band (currently £325,000, being a cumulative amount over the past 7 years), which is paid by the settlor or the trustees;
- a 6% “periodic” charge every 10 years payable by the trustees on the value of the trust over the nil-rate band; and
- a pro-rata “exit” charge when assets are taken out of trust between 10-yearly anniversaries, again payable by the trustees.

3.41 The aim of the charges is to ensure that relevant property trusts are exposed to charges broadly equivalent to what would be incurred if a death charge had been levied once a generation. In our view recycling the nil-rate band every seven years goes against this aim.

Accumulation of Income

Question 9: Are there any issues with using this method as a practical way of dealing with accumulations?

Question 10: Do you anticipate any additional administrative burden resulting from the proposed changes to the calculation of IHT on accumulated income? If so, what would you estimate to be the average cost per trust?

3.42 Approximately one third of respondents welcomed the proposed standard approach in dealing with accumulated income. Many of them agreed that this area causes continued uncertainty amongst trustees and practitioners. Though along with most respondents they did have two main concerns – the interaction between trust law and tax law and the period after which income is deemed to be capital.

3.43 Those that welcomed the proposals said that the introduction of this new provision could bring greater certainty. It may also encourage the trustees to have a regular review of the trust’s income and to make an active decision over whether to distribute it or accumulate it.

3.44 Others were against any change in this area stating that accumulation should remain at the discretion of the trustees, or be imposed by existing trust law or the trust instrument. Whilst some respondents neither supported nor disagreed with changes in this area they instead expressed their concerns with the proposals and made practical suggestions on how a deeming provision might best work.

3.45 Virtually all respondents felt that a period of two years was insufficient for trustees to be able to consider the beneficiaries’ needs. Many pointed out that there were various reasons why income would be retained. Trustees often retain income for the future needs of their income beneficiaries knowing that it will be required for use within a set period of time, for example to pay school or university fees. One professional body commented that treating income as being

capitalised after only two years for IHT would seem to be at variance with the way that the trustees might undertake their duties. The period suggested by respondents after which retained income should be deemed as accumulated ranged from three to six years.

- 3.46 A number of respondents felt uneasy with provisions that separated the trust law treatment of the settlement from the tax law treatment. Some felt that the proposal to deem income to be capital once a certain period has expired after receipt was unnecessary. They felt tax treatment should follow trust law and where there is a power to accumulate but a trust to distribute, a deemed accumulation in a tax statute cannot change the character of the income. They argued that income received by trustees where it has not been accumulated has not lost its character of income and pointed out that frequently it would still be distributed as income to beneficiaries in a later year.
- 3.47 Other respondents pointed out that ability to accumulate or distribute income is subject to statutory provisions as well as those in particular deeds of settlement, therefore HMRC must exercise care in introducing a deeming rule. There was concern from a substantial number of respondents that the proposals would be inequitable if they meant that undistributed income would be treated as capital after two years and subsequent distributions would be subject to an exit charge without regard to the tax credit and related tax pool. One professional body added that there must be arrangements to ensure that there is no double taxation under the income tax and IHT regimes, a view reflected by a number of other respondents.
- 3.48 One respondent stated that the proposals should only be treated as guidance and not written into statute. They added that if the trustees can show why income has not been accumulated then they should not have to treat it as such.
- 3.49 A number of respondents believed that it was likely that there would be an added burden on trustees and practitioners resulting from the proposed changes. In their view there would be an added complexity to the trust accounting, with the requirement to keep track of income generated each year and to transfer undistributed income to capital at the appropriate date. It would also be necessary to keep the trustees advised as to the level of available income in a settlement and to advise them on whether they should pay out additional income before the end of each tax year. One respondent estimated that the time taken to deal with the trust could be increased by approximately one hour per trust per annum for practitioners or possibly longer for unrepresented trustees. For their firm, this would equate to a further £200 plus VAT per year per trust.
- 3.50 Some respondents mentioned the fact that matching rules would be needed to decide which income is deemed to be distributed either on a first in first out or last in first out basis. One respondent stated that one of their clients has a policy to accumulate any income that has not been distributed within five complete tax years after the income has arisen. This shows that the trustees carefully consider the income received by the trust on an annual basis but the five year accumulation policy allows them flexibility to deal with the beneficiaries' needs, depending on their personal circumstances and income requirements.

HMRC response

- 3.51 Although trustees for relevant property trusts may have, in practical terms, the option of either distributing or accumulating income, in trust law terms these powers are framed in different ways – most commonly there will either be a trust to distribute and a power to accumulate or a trust to accumulate with a power to distribute. In both cases the power will lapse if not exercised within a reasonable time, but what is a reasonable period will differ according to the context.
- 3.52 Often the income is retained for many years and reinvested within the income account but when the 10 year anniversary arrives the trustees will maintain (where there is a mere power to accumulate) that the power still exists but they have not yet decided whether to accumulate. HMRC sometimes challenges this sort of analysis and in effect argues that if the power has expired but the income has been retained there has been a de facto accumulation – but without recourse to litigation it is not clear what the true legal position is. Similarly where there is a trust to accumulate and a power to distribute, trustees will argue that even where income has been retained for long periods and reinvested, they still have the power to distribute it. HMRC therefore considered a deeming rule would provide certainty about the IHT position in these situations and avoid long running disputes between the taxpayer and HMRC.
- 3.53 However, we have listened to respondents' views and we recognise that this might be confusing and unsatisfactory for trustees and practitioners and could lead to accounting difficulties and additional administration work where income is retained. This is particularly so in relation to proportionate charges before and between the anniversary charges. Consequently we have given this issue some further thought and we believe that it would be clearer if we framed the requirement in the legislation so that it applies to the ten year anniversary charge only.
- 3.54 The revised rule will treat income that has remained undistributed for more than five years at the date of the ten year anniversary as if it was part of the trust capital for the purposes of the ten year anniversary charge. Framed in this way we do not think issues of double taxation will arise. This is because the income retains its nature as income and is only treated as capital for the purposes of the ten year anniversary charge. If this income is later paid out of the trust, it would not be subject to an exit charge because it will be income in the hands of the beneficiary and subject to income tax.
- 3.55 To avoid the need for trustees to keep very detailed records, tax would be charged on the ten year anniversary at the full rate on any such undistributed income without any proportionate reduction to reflect the period during which the income has been retained.
- 3.56 We realise that trust accounts may not necessarily show how the income in hand figure at the ten year anniversary is made up but the revised rule ought to encourage trustees to ensure that they had distributed the earliest net (after trustee expenses) income first. In such cases, HMRC would accept a first in first out approach giving the taxpayer the greatest benefit at the ten year anniversary.

Aligning filing and payment dates

Question 11: Are there any issues with bringing IHT within the concept of Self Assessment?

- 3.57 Respondents were generally positive on the proposal to bring IHT within the scope of the self-assessment regime. They agreed that the current time limits for payment, which vary according to the part of the year in which the transfer falls, are anomalous and should be reformed. They also recognised that aligning the filing and payment dates would be of benefit to trustees and practitioners as it would mean that both these matters could be dealt with at the same time, thus improving efficiencies.
- 3.58 Most did not consider there to be any issues with the proposals other than the fact that there would be an increase in the already heavy workload around 31 October and 31 January for both practitioners and HMRC. One respondent made the point that practitioners are busy enough as it is preparing ordinary tax returns by 31st January and if they had to do all inheritance tax returns as well by a fixed date, as opposed to being able to stagger them over the year, it would simply impose a greater burden – greater burdens on practitioners usually resulted in greater costs on trustees.
- 3.59 Several respondents said that the alignment should allow for returns to be filed by 31 January. They believed that an October filing date would be too tight a deadline for many trusts. One professional body made the point that part of the rationale of simplicity of alignment is lost if ordinary trust returns and accounting are carried out to 31 January deadline and the IHT returns have a 31 October deadline. Some expressed concern that the proposals would give a period for making a return that varied arbitrarily between seven and 19 months from the making of a transfer.
- 3.60 One practitioner suggested that it would be far better to align the rules for all IHT returns, including those relating to death, to the current position on death, i.e. that the tax is due 6 months from the end of the month in which the event occurred, and the return is due within a year (and by implication, remove the different payment date for some chargeable events occurring between 6th April and 30th September inc).
- 3.61 Regarding the proposal to require trustees to self-assess their IHT liabilities, it was felt that such a self-assessment approach could be justified where the system had been simplified or efficient online calculators were provided.
- 3.62 There was a suggestion that there should be an option, as for self-assessment for individuals, trustees and partnerships, to ask HMRC to calculate the tax liability provided the trustees submit the return by a given earlier date. This option could be restricted to trustees who were not professionally advised. Other respondents stated that they would prefer that trustees could always ask HMRC to calculate the tax for them as this would remain a complex area, despite any of the proposed simplifications.

3.63 Another suggestion was for HMRC to issue returns on an annual basis, with a simple “nil” return feature. A notice could be sent to complete a return, with a single tick box and signature box which could be filled in and returned, to indicate that no reportable transactions have taken place. Various respondents recommended the introduction of e filing for IHT and that a revision of the existing forms was needed to make them more accessible.

Question 12: How much time will trustees and practitioners save as a result of the payment and filing dates being aligned with the SA framework?

3.64 Virtually all respondents said that aligning filing and payment dates with the SA framework would not save them time. However some respondents recognised that alignment would allow administrators to work on an annual basis which would encourage better compliance. But others were equally concerned that alignment of the filing dates with the normal self-assessment process could lead to IHT work being overlooked in the effort to complete the existing self-assessment filing requirements.

3.65 Some respondents remarked that trustees would not save any time unless the forms are made simpler as the actual work will be the same, just at a different time of the year. They considered an improvement to the forms would improve efficiencies and reduce costs in this area.

3.66 Several respondents said that in their view it was not possible to estimate how much time could be saved but they believed that the savings could be significant especially if the rules were not simply aligned but integrated within the SA system.

Question 13: What would the impact be on trustees and practitioners’ clients?

3.67 Most respondents were positive about the impact of alignment on trustees and practitioners as the rules would be easier for everyone to understand. They believed that alignment would enable practitioners to timetable work more efficiently and the completion of the return would become part of the compliance cycle rather than being a discrete process. It would therefore take place at a time when the practitioner was in possession of all relevant information, including accounts. As a result the quality and accuracy of returns submitted could be improved.

3.68 However, one respondent commented that it should not be assumed that the same professional advisers complete the IHT work, as the existing self-assessment work.

3.69 Several respondents mentioned that any changes to the filing and payment dates would mean that there would be a need for all to become aware of the new rules and for practitioners to be able to explain the benefits of any new arrangement. They also made the point that whilst the alignment of the IHT returns within self-assessment might be seen in a positive light, if it coincides with the imposition of potentially significant charges upon trusts that have

previously benefitted from a full nil-rate band, it was anticipated that this would have a negative impact upon clients.

Question 14: Will alignment bring benefits to customers in terms of reduced fees?

- 3.70 The responses to this question were mixed. The majority of respondents did not think that alignment would result in a reduction in fees as they did not envisage any significant time savings.
- 3.71 Others said that although it was very difficult to judge, they did expect to see a marginal benefit as a result of alignment in terms of fees and it would make dealing with IHT compliance much easier.
- 3.72 A number of respondents re-iterated that if HMRC was looking to benefit customers, a first step would be to revise the form IHT100. Another suggested that fee reductions could be achieved if multiple events could be combined in a single return.

HMRC response

- 3.73 We have given the alignment of filing and payment dates further consideration and have concluded that aligning the dates to the 31 October and 31 January will only provide any real benefits if the IHT charges were brought wholly within the self-assessment system. However, the changes needed to the IT infrastructure and the funding requirements to make this happen mean that this is unlikely to be achieved in the short to medium term.
- 3.74 Furthermore, we have taken respondents' comments on board and acknowledge that the proposals are likely to increase practitioners' and trustees' workloads at an already extremely busy time of the year. We therefore propose that the best way to remove the filing and payment mismatch would be to align the two at 6 months after the end of the month in which the event occurred. This would ensure that returns and payments are submitted more evenly throughout the year and reduce burdens on trustees' and practitioners' time.
- 3.75 The revised proposal would in our view still provide trustees ample time to calculate periodic and exit charges and submit the necessary returns on time.
- 3.76 The consultation also proposed that trustees should be required to "self assess" their IHT liability and declare the amount due on the basis that HMRC would be simplifying the IHT trust charge calculations at the same time. Since we are now recommending that the simplification of the trust charges is deferred until Finance Bill 2015, we do not think that at this stage it would be appropriate to impose an express requirement on trustees to include an "assessment" when delivering an account for IHT.
- 3.77 We have also noted the many comments and recommendations about improvements to IHT forms. As mentioned in the Summary of Responses to the

July 2012 consultation published in March 2013, HMRC will consider making changes to IHT forms whenever costs permit and improvements are considered worthwhile.

4. Next steps

Further consultation

- 4.1 Draft primary legislation for inclusion in Finance Bill 2014 on the alignment of filing and payment dates for IHT ten year anniversary and exit charges and the treatment of accumulated income was published on 10 December for technical consultation; we would welcome comments. If necessary we will review and amend that legislation once the consultation closes on 4 February 2014.
- 4.2 We will consult further in respect of consideration of the nil-rate band.
- 4.3 Legislation on the nil-rate band and simplification of calculations will be included in Finance Bill 2015.

Annexe A: List of stakeholders consulted

Written responses – representative bodies and firms

Association of Accounting Technicians
Association of British Insurers
Association of Taxation Technicians
Baker Tilly
Boodle Hatfield LLP
Canada Life
Chartered Institute of Taxation
Churchgate Accountants Ltd
Citroen Wells Chartered Accountants
Country Land and Business Association
Crowe Clark Whitehill LLP
Deloitte LLP
Ernst & Young LLP
Francis Clark LLP
Frank Hirth PLC
George Hay Chartered Accountants
Gorings Chartered Accountants
Grant Thornton UK LLP
Historic Houses Association
Institute of Chartered Accountants England and Wales
Institute of Chartered Accountants Scotland
Jackson Stephen LLP
Johnston Carmichael LLP
Law Society Scotland
London Society of Chartered Accountants
Meridian Private Client LLP
Moore Stephens LLP
PricewaterhouseCoopers LLP
Saffery Champness Chartered Accountants
Sagars LLP
Scottish Land and Estates
Skandia
Smith & Williamson LLP
Society of Trust and Estate Practitioners
Standard Life PLC
Technical Connection Ltd
The Association of Corporate Trustees
Thomas Eggar LLP
Toby Harris Tax Consultancy
UHY WKH Partnership
Way Investment Services Ltd
Wilds Business Advisers and Chartered Accountants
Wrigleys Solicitors LLP

Written respondents – individuals

There were also 10 responses from individuals

Meetings

HMRC also met with 8 representative bodies during the consultation period.