HM Revenue & Customs

Inheritance tax: simplifying charges on trusts

Who is likely to be affected?

Individuals settling property into relevant property trusts, trustees and their advisers.

General description of the measure

The measure will align the filing and payments dates for inheritance tax (IHT) relevant property trust charges and treat the income arising in such trusts which remains undistributed for more than five years as part of the trust capital when calculating the ten year anniversary charge.

Policy objective

The measure will simplify the IHT regime for relevant property trusts and reduce compliance costs for trustees and practitioners.

Background to the measure

The measure was announced at Budget 2012. An initial high level consultation document was published in July 2012 and a further more detailed consultation setting out options for simplification followed in May 2013. A response document was published on 10 December 2013.

Detailed proposal

Operative date

The measure will be effective in relation to tax charges arising on or after 6 April 2014.

Current law

Filing and payment dates

IHT payment and filing dates can appear confusing and anomalous. The time limits for reporting IHT periodic and exit charges that trustees are accountable for differ from the time limits for paying any IHT due.

The time limit for delivering an account is currently 12 months from the end of the month in which the transfer is made or if later, three months from the date when the trustee first becomes liable for the tax.

The time limits for paying IHT charges are:

- for chargeable events after 5 April and before 1 October, on 30 April in the following year; and
- for chargeable events after 30 September and before 6 April, six months after the end of the month in which the chargeable event took place.

Trust income

Many trustees have the ability to 'accumulate' or add undistributed trust income to the trust capital. Once such income is accumulated it is treated as an addition to the trust's capital and must be taken into account when calculating the ten year or exit charges.

Where there are discretionary trusts and the trustees have a duty to accumulate income without any power to distribute, income will be treated as accumulated as it arises. However it is more usual for discretionary trustees to have a power to accumulate income as well as a power to distribute it and in such cases the trust deed rarely stipulates a particular point at which accumulation must take place. Neither is there a statutory rule.

Where income is regularly or formally accumulated there is little doubt about the correct treatment of the accumulations within the calculation of relevant property charges. But it can be different where income remains undistributed for long periods and the trustees have not made any formal accumulation. In such cases there can be uncertainty about how the calculations should be undertaken, resulting in questions to, or correspondence with, HM Revenue & Customs (HMRC) to establish an acceptable treatment.

Proposed revisions

Filing and payment dates

Legislation will be introduced in Finance Bill 2014 to align the filing and payment dates for IHT trust charges. Amendments to section 216(6) IHTA1984 (time for delivery of accounts) and section 226 IHTA 1984 (payment of tax) will mean that trustees of relevant property settlements must deliver the IHT account six months after the end of the month in which the chargeable event occurs and pay the tax by the end of the same period. This will ensure that returns and payments continue to be submitted evenly throughout the year.

Trust income

New section 64(1A) IHTA 1984 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. 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.

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2013-14</td><td>2014-15</td><td>2015-16</td><td>2016-17</td><td>2017-18</td><td>2018-19</td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td colspan="6">This measure is expected to have a negligible impact on the Exchequer. The final costing will be subject to scrutiny by the Office for Budget Responsibility and will be set out at Budget 2014.</td></tr>
<tr><td>Economic impact</td><td colspan="6">The measure is not expected to have any significant economic impacts.</td></tr>
<tr><td>Impact on individuals and households</td><td colspan="6">Alignment of filing and payment dates: the measure will not impact on individuals or households. Its affect will be on trustees and their advisers.

Accumulation of income: the deeming rule would provide a standard approach, for the purposes of IHT only, to the treatment of unaccumulated income, bringing certainty and consistency to trustees and practitioners.</td></tr>
<tr><td>Equalities impacts</td><td colspan="6">The Government has no evidence to suggest that the measure will have any adverse equalities impacts.</td></tr>
<tr><td>Impact on business including civil society organisations</td><td colspan="6">Businesses may see a reduction in administration burdens as a result of filing returns and making payments at the same time and having a clearer understanding of when HMRC considers retained income as capital for IHT purposes. The Government estimates that the impacts of these changes on businesses' administrative burdens will be negligible. This measure is expected to have no impact on civil society organisations.</td></tr>
<tr><td>Operational impact (£m) (HMRC or other)</td><td colspan="6">There will be some implementation costs for HMRC but these are expected to be negligible.</td></tr>
<tr><td>Other impacts</td><td colspan="6"><u>Small and micro business assessment:</u> the measure will benefit small businesses (firms with fewer than 20 employees) as a result of the reduction in complexity and administrative burdens.

Other impacts have been considered and none have been identified.</td></tr>
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Monitoring and evaluation

The measure will be kept under review through regular communication with the relevant business sector.

Further advice

If you have any questions about this change, please contact Tony Zagara on 03000 585265 (email: antonio.zagara@hmrc.gsi.gov.uk).

1 Inheritance tax: delivery of account and payment of tax

(1) IHTA 1984 is amended as follows.

(2) In section 216(6) (time for delivery of accounts), before paragraph (b) insert—

“(ad) in the case of an account to be delivered by a person within subsection (1)(c) above, before the expiration of the period of six months from the end of the month in which the occasion concerned occurs;”.

(3) In section 226 (payment of tax: general rules), after subsection (3B) insert—

“(3C) Tax chargeable under Chapter 3 of Part 3 of this Act on the value transferred by a chargeable transfer, other than any for which the due date is given by subsection (3B) above, is due six months after the end of the month in which the chargeable transfer is made.”

(4) In section 233 (interest on unpaid tax)—

(a) in subsection (1)(a), after “transfer” insert “not within paragraph (aa) below and”,

(b) after subsection (1)(a) insert—

“(aa) an amount of tax charged under Chapter 3 of Part 3 of this Act on the value transferred by a chargeable transfer remains unpaid after the end of the period of six months beginning with the end of the month in which the chargeable transfer was made, or”, and

(c) in subsection (1)(b), for “any other chargeable transfer” substitute “a chargeable transfer not within paragraph (a) or (aa) above”.

(5) The amendments made by this section have effect in relation to chargeable transfers made on or after 6 April 2014.

2 Inheritance tax: ten-year anniversary charge

(1) IHTA 1984 is amended as follows.

(2) In section 64 (charge at ten-year anniversary), after subsection (1) insert—

“(1A) For the purposes of subsection (1) above, property held by the trustees of a settlement immediately before a ten-year anniversary is to be regarded as relevant property comprised in the settlement at that time if—

(a) it is income of the settlement,

(b) the income arose before the start of the five years ending immediately before the ten-year anniversary,

(c) the income arose (directly or indirectly) from property comprised in the settlement that, when the income arose, was relevant property, and

(d) when the income arose, no person was beneficially entitled to an interest in possession in the property from which the income arose.

(1B) Where the settlor of a settlement was not domiciled in the United Kingdom at the time the settlement was made, income of the settlement is not to be regarded as relevant property comprised in the settlement as a result of subsection (1A) above so far as the income—

(a) is situated outside the United Kingdom, or

(b) is represented by a holding in an authorised unit trust or a share in an open-ended investment company.

(1C) Income of the settlement is not to be regarded as relevant property comprised in the settlement as a result of subsection (1A) above so far as the income—

(a) is represented by securities issued by the Treasury subject to a condition of the kind mentioned in subsection (2) of section 6 above, and

(b) it is shown that all known persons for whose benefit the settled property or income from it has been or might be applied, or who are or might become beneficially entitled to an interest in possession in it, are persons of a description specified in the condition in question."

(3) In section 66 (rate of ten-yearly charge), after subsection (2) insert—

"(2A) Subsection (2) above does not apply to property which is regarded as relevant property as a result of section 64(1A) (and accordingly that property is charged to tax at the rate given by subsection (1) above)."

(4) The amendments made by this section have effect in relation to occasions on which tax falls to be charged under section 64 of IHTA 1984 on or after 6 April 2014.

EXPLANATORY NOTE

INHERITANCE TAX: DELIVERY OF ACCOUNT AND PAYMENT OF TAX

SUMMARY

1. Clause [X] changes the dates by which trustees must deliver an Inheritance Tax (IHT) account and pay tax due for charges arising under Chapter 3 of Part 3 of IHTA.

DETAILS OF THE CLAUSE

2. Subsection 2 adds a new subsection (ad) to section 216(6) of IHTA. The effect of subsection (ad) is that trustees of settlements on which tax is chargeable under Chapter 3 of Part 3 of IHTA, must deliver the IHT account six months after the end of the month in which the chargeable event occurs.

3. Subsection 3 adds a new subsection (3C) to section 226 of IHTA. The effect of subsection (3C) is that the due date for payment of tax chargeable under Chapter 3 of Part 3 of IHTA 1984, is six months after the end of the month in which the chargeable transfer is made. Subsection (3C) does not affect the provision at section 226(3B) which sets out the payment date where a settlor dies within seven years of a transfer and additional liability arises under Chapter 3 of Part 3 IHTA.

4. Subsection 4 amends section 233 IHTA (interest on unpaid tax) to bring it into line with the new payment date.

5. Subsection 5 provides for the changes to apply to tax charges arising on or after 6 April 2014.

BACKGROUND NOTE

6. The time limits for reporting IHT periodic and exit charges arising under chapter 3 part 3 of IHTA that trustees are accountable for differ from the time limits for paying any IHT due under chapter 3 part 3 IHTA.

7. The time limit for delivering an account is currently 12 months from the end of the month in which the transfer is made or if later, three months from the date when the trustee first becomes liable for the tax.

8. The time limits for paying IHT charges are:

- for chargeable events after 5 April and before 1 October, on 30 April in the following year; and
- for chargeable events after 30 September and before 6 April, six months after the end of the month in which the chargeable event took place.

9. This change aligns and simplifies the filing and payment dates for these charges.

10. If you have any questions about this change, or comments on the legislation, please contact Tony Zagara on 03000 585265 (email: antonio.zagara@hmrc.gsi.gov.uk).

EXPLANATORY NOTE

INHERITANCE TAX: TEN YEAR ANNIVERSARY CHARGE

SUMMARY

1. Clause [X] introduces a new provision to treat income arising in "Relevant Property" trusts which remains undistributed for more than five years as part of the trust capital when calculating the ten year anniversary charge.

DETAILS OF THE CLAUSE

2. Subsection 2 adds new subsections (1A), (1B) and (1C) to section 64 of IHTA. New subsection (1A) sets out the conditions for treating property held by the trustees of a settlement as part of the trust capital when calculating the ten year charge (the deeming rule). Those conditions are that the property is income of the settlement, it arose before the start of the five years ending immediately before the ten year anniversary, it arose from relevant property comprised in the settlement and when the income arose no person was beneficially entitled to an Interest in Possession in the underlying property.

3. New subsection (1B) excludes from the deeming rule (in the case of settlements made by persons not domiciled in the UK) income which arose from relevant property but is at the ten year charge represented by property situated outside the UK or is represented by a holding in an Authorised Unit Trust or Open-Ended Investment Company.

4. New subsection (1C) excludes from the deeming rule income which arose from relevant property but which is reinvested in exempt gilts which would (if properly treated as accumulated income) be excluded property.

5. New subsection (1C)(b) ensures that that exempt gilts within a settlement will only be excluded property where all the beneficiaries who could ever become entitled to capital or income from the settled property meet the necessary condition.

6. Subsection 3 amends section 66 of IHTA and adds new subsection 2A. The effect of the amendment is that income brought within the charge as a result of s 64(1A) is charged to tax at the full rate in section 66(1).

7. Subsection 4 provides for the changes to apply to tax charges arising under section 64 IHTA on or after 6 April 2014.

BACKGROUND NOTE

8. Where income is regularly or formally accumulated there is little doubt about the correct treatment of the accumulations within the calculation of relevant property charges. But it can be different where income remains undistributed for long periods and the trustees have not made any formal accumulation. In such cases there can be uncertainty about how the calculations should be undertaken, resulting in questions to, or correspondence with, HMRC to establish an acceptable treatment.

9. New s64(1A) 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. 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.

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