

Inheritance Tax Review – first report:

Overview of the tax and dealing with
administration

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Foreword

In January 2018 the Chancellor asked the Office of Tax Simplification (OTS) to carry out a review covering a wide range of both administrative and broader technical aspects of Inheritance Tax.

The review has attracted an unprecedented level of engagement, both from advisers and the general public, including nearly 3,000 responses to an online survey, 500 personal emails from members of the public and 100 formal written responses to a call for evidence, supported by the usual extensive range of meetings with interested parties with a wide variety of perspectives.

Given the wide scope of the review, the OTS will produce two reports. The first is on the day to day matters of concern to all who responded; the second will explore key technical and design issues.

This first report summarises the many comments and submissions we've received. It then sets out recommendations on administrative issues, which featured frequently in those responses, and will remain important regardless of any technical or design changes made in the future.

Although less than 5% of people pay Inheritance Tax, executors have to fill in Inheritance Tax forms for half of all deaths. So, the key administrative recommendation is for the government to simplify this by giving renewed consideration to digitising and simplifying the necessary administration.

An overview of how Inheritance Tax works, who pays it and people's concerns, is provided in the next section, followed by the Executive Summary on the administrative issues. We also include in Chapter 3, a discussion of the main comments the OTS has received about the more complex areas of the tax. The OTS will return to these areas in the second report to be published in spring 2019, with the aim of supporting an ongoing debate about the wider simplification of the tax.

The OTS would like to thank Daphna Jowell, who led the review, supported by Charlotte Alderman, Simon Jackson, Zoë Judd, Bethan Kay and Andy Richens, guided by OTS Head of Office David Halsey. We are also very grateful to our HM Treasury and HM Revenue and Customs colleagues, our Consultative Committee members and all those who have willingly given time, ideas, challenge and support.



Angela Knight CBE (Chair)



Paul Morton (Tax Director)

How does Inheritance Tax work?

- Inheritance Tax is paid primarily on the estate (the property, money and other possessions) of someone who has died
- everyone has an amount that they can leave or give to others tax free, this is known as the nil rate band (NRB) and is currently set at £325,000
- for some, the tax free amount can be higher – spouses and civil partners can transfer allowances unused on the first death, to be used on the death of the second spouse, this is known as the transferable nil rate band (transferable NRB). Additionally, there is a residence nil rate band (residence NRB), currently worth up to £125,000 (rising to £150,000 in April 2019 and £175,000 in April 2020). This is available when a person leaves their home to their direct descendants, and is also transferable
- anything above this amount may be liable to Inheritance Tax on death at 40%
- however, there are also a number of additional reliefs and exemptions that can reduce the amount payable. The main ones are:
 - spouse exemption – assets left to spouses and civil partners are exempt
 - charities exemption – assets left to charities are exempt
 - agricultural and business property relief (APR/BPR) – assets may attract relief of up to 100% if certain conditions are met
- gifts made to individuals will not generally be taxable if they were made more than 7 years before the death of the person making the gift. There may be Inheritance Tax due on gifts made in that 7 year period, although the rate may be reduced depending on when it was given
- gifts where the person giving the gift receives some benefit from them in the 7 years prior to their death are treated as if they are still owned on death
- there are also specific gift reliefs, including relief for gifts adding up to less than £3,000 a year, small gifts of less than £250, and gifts of a certain value for weddings
- Inheritance Tax may also be immediately chargeable on some lifetime gifts, in these circumstances the rate is 20%
- trusts have a separate Inheritance Tax regime. For many new trusts there are periodic charges as well as a charge when assets are put in or taken out of the trust, payable by the trustees

Inheritance Tax: some facts

How many people pay Inheritance Tax? ¹

Each year, fewer than 25,000 estates in the UK are liable for Inheritance Tax. This is less than 5% of all deaths.

The number of liable estates has increased every year since the 2009 to 2010 tax year. This is partly because of the freeze of the NRB and partly due to increasing estate values. Much of the increase in estate values is due to increased residential property values.

How many people fill out Inheritance Tax forms?

In the UK, on average, around 570,000 people die each year.² Inheritance Tax forms were completed for 275,000 estates in the UK in the 2015 to 2016 tax year, over ten times the number of estates on which any Inheritance Tax was paid. This means that an Inheritance Tax form was submitted for around half of all the deaths in that year. The forms need to be submitted because the value of the estate must be reported to HMRC, even where there is no tax liability.

How much does it raise?

Inheritance Tax makes up less than 1% of the total tax raised by the Exchequer. Receipts totalled £5.2 billion in the 2017 to 2018 tax year.³ To put this into context, this would cover just over one week's worth of the cost of providing UK pensions and welfare benefits that year.⁴

Inheritance Tax receipts have been steadily increasing. In the 2009 to 2010 tax year receipts were £2.38 billion, and are forecast to continue to do so.⁵ However, the increase in receipts is expected to slow in future as the residence NRB takes full effect.⁶

The tax gap⁷ for Inheritance Tax is estimated at around £600 million per year.⁸ This is relatively high, as a percentage of the total Inheritance Tax due, compared with other taxes.

¹ In July 2018 HMRC published its annual National Statistics on Inheritance Tax up to the year 2015 to 2016.
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/731610/Inheritance_Tax_National_Statistics_Commentary.pdf

² https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/730125/Table_12_3.pdf

³ <https://www.gov.uk/government/statistics/hmrc-tax-and-nics-receipts-for-the-uk>

⁴ Table 5.2, page 76 of
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/726878/PESA_2018_Print.pdf

⁵ <https://obr.uk/efo/economic-fiscal-outlook-october-2018/>

⁶ <https://obr.uk/efo/economic-fiscal-outlook-october-2018/>

⁷ The tax gap is the difference between the tax that should be paid to HMRC and the actual tax that has been paid.

⁸ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/715742/HMRC-measuring-tax-gaps-2018.pdf

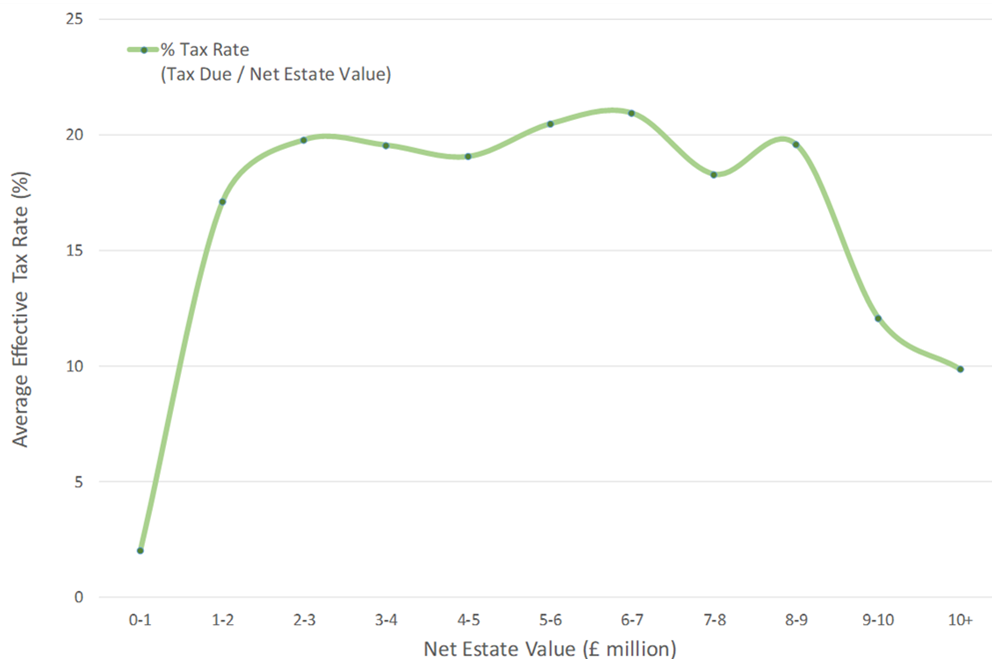
The rate of Inheritance Tax

UK Inheritance Tax is set at 40%. However, as is shown in Chart A, the rate actually paid by the average estate is much lower than the headline rate. It peaks at just over 20%.

When considering the graphs below, it is important to remember that the vast majority of estates have a value of less than £1 million. Fewer than 3% of estates have a value above this.

Chart A shows the average effective tax rate paid by estates and how it changes according to the size of the estate.

Chart A: The average effective tax rate paid by estates



Source: Analysis of HMRC data from Inheritance Tax forms for the 2015 to 2016 tax year which is published here for the first time⁹

Chart A shows that the average effective tax rate (that is, the average rate of tax paid on the estate as a whole) increases from under 5% for estates with a net¹⁰ value under £1 million, up to 20% for estates valued at £2 to £3 million. It then broadly levels off, peaking at just above 20% for estates valued at £6 to £7 million, after which it falls to 10% for estates with a value of £10 million or more.

⁹ The last point on the graph shows the average tax rate paid by estates with a value of £10 million or more. A more detailed breakdown is not provided for estates over £10 million for all the graphs. This is in line with the Statistics Code of Practice rules on trustworthiness <https://www.statisticsauthority.gov.uk/code-of-practice/>.

¹⁰ The net estate value is the total assets in the estate, including lifetime gifts given in the 7 years before death, minus any liabilities of the estate (for example debts).

The increase in average effective rate for estates up to a value of £3 million is due to the effect of the NRB.

Estates with a net value below the NRB of £325,000 do not pay Inheritance Tax and therefore have an average effective tax rate of 0%.

Chart A shows us that the rate steadily increases for estates valued at more than the NRB. This is because the proportion of an estate covered by the NRB (or transferable NRB) decreases. For example, the transferable NRB of £650,000 covers 65% of a £1 million estate but less than 35% of a £2 million estate.

One might expect the average effective tax rate to be closer to the headline rate of 40% for higher value estates but this is not the case.

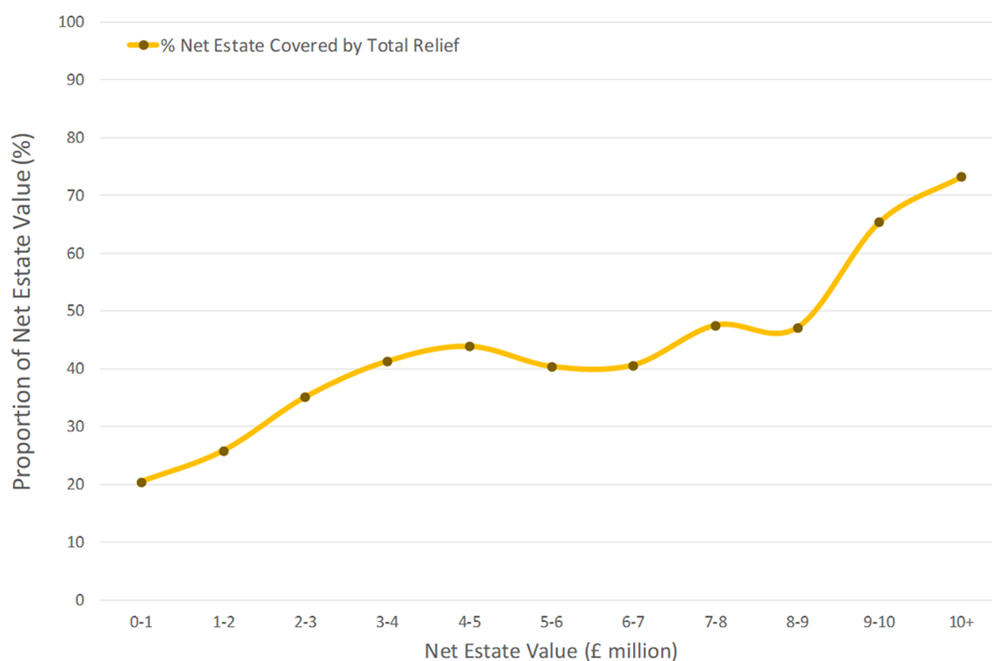
Why doesn't the average effective tax rate for estates reach 40%?

One of the main reasons the average effective tax rate does not reach 40% is the application of the spouse exemption and other reliefs. Many estates are left wholly or mostly to spouses or civil partners. These estates will be subject to little or no Inheritance Tax. Including these estates in the data used for these graphs brings down the average effective tax rate.

Why do higher value estates have a lower average effective tax rate?

The reason higher value estates have a lower average effective tax rate is that a greater proportion of their assets are likely to be covered by a relief. This is clearly shown in Chart B. On average, over 70% of the value of an estate worth more than £10 million is relieved in this way.

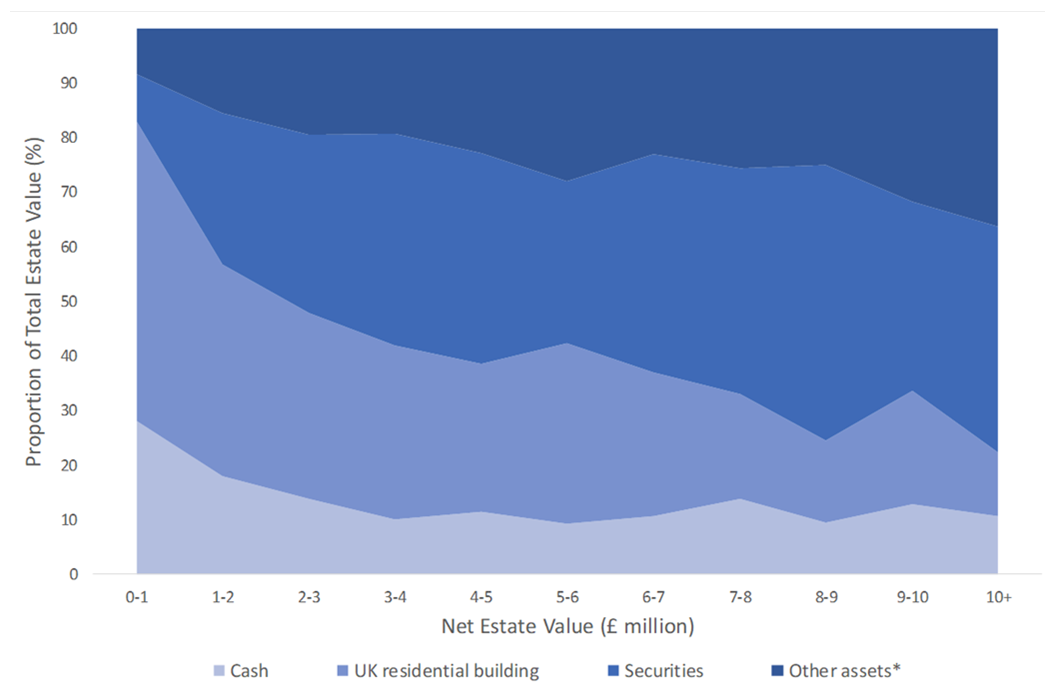
Chart B: Proportion of net estate covered by an Inheritance Tax relief (excluding the NRB)



Source: Analysis of HMRC data from Inheritance Tax forms for the 2015 to 2016 tax year which is published here for the first time

Chart C shows the asset composition of estates of increasing values. This chart helps explain why, on average, the higher the value of the estate, the more relief it enjoys.

Chart C: Types of assets held by estates



Source: Analysis of HMRC data from Inheritance Tax forms for the 2015 to 2016 tax year which is published here for the first time

*Other assets include farmland, insurance policies, other land and buildings, loans and other assets

Lower value estates mostly consist of cash and residential property which do not commonly attract relief from Inheritance Tax¹¹ and are relied upon to live and fund peoples' everyday lives.

As estates increase in value, they have proportionately less cash and residential property, and more securities and 'other assets'. These categories of assets include those that commonly attract relief from Inheritance Tax.

For example, certain business assets, including some unlisted shares and shares traded on the Alternative Investment Market (AIM), qualify for business property relief (BPR) at 100% of the value of the asset. Shares are included in the 'securities' section of Chart C.¹² The 'other assets' section of the chart includes farms, which may qualify for agricultural property relief (APR) from Inheritance Tax.

Concerns people have about Inheritance Tax

The OTS gathered evidence from its survey, call for evidence responses and in-depth discussions about a range of concerns and perceptions people have about Inheritance Tax:

- concerns about the administration of the tax
- concerns about areas of complexity within the rules
- wider perceptions about the tax generally

¹¹ To the extent that the estate value exceeds the nil rate bands.

¹² Unfortunately, the OTS has not been able to obtain data showing the asset breakdown of the 'securities' and 'other' section of Chart C according to whether the asset attracts relief from Inheritance Tax.

Inheritance Tax administration

Much of the evidence the OTS gathered related to concerns about administrative issues.

The overarching point that emerged is that Inheritance Tax returns must be made even when there is no tax to pay. Returns are submitted in relation to about half of all UK deaths, even though Inheritance Tax is payable in respect of less than 5% of deaths.

Payment of the tax can also create problems, as the tax may need to be paid before any assets can be sold, potentially creating financial difficulty for the beneficiaries of the estate.

The OTS survey¹³ was undertaken by nearly 3,000 people, and revealed a wide range of views. It is important to highlight that the survey was open to all who wished to take part and, as the respondents were only those who chose to complete the survey, it did not form a representative sample of society. The following is a snapshot of the responses.

- 53% of respondents correctly answered that less than 5% of people are liable to Inheritance Tax. However, 26% of survey respondents thought that 20% or more people paid Inheritance Tax
- 38% of respondents who did not use an adviser recalled spending 50 hours or more on estate administration
- understanding and completing the relevant forms, and obtaining probate, were the most commonly cited processes which took the longest to undertake
- 65% of respondents (who did not use an adviser) answered that despite there being no Inheritance Tax to pay they still had to provide significant amounts of information
- only 11% of respondents who did not use an adviser stated that they found the process simple and user friendly
- only 25% of respondents recalled receiving an acknowledgment from HMRC that their paperwork had been received
- 61% of respondents stated that they did not know how long it would take HMRC to respond once they had submitted their form

The overall picture presented is of an administrative burden. The recommendations set out in this report should, if implemented, go quite some way to reducing this burden at what is often a difficult time for people.

Areas of complexity

Through its wide ranging evidence gathering, the OTS has identified concerns about a number of key areas of complexity within the Inheritance Tax rules. What follows is an overview of the issues raised with the OTS so far. These are set out in more detail in Chapter 3, and will be explored further in the second report.

¹³ See annex D for a more detailed analysis of survey findings.

Nil rate band and residence nil rate band

The OTS has received substantial comment on the various thresholds. While it has been suggested that the NRB is simple and well understood, the residence NRB (which is aimed at helping people to pass on the family home) has attracted a lot of comments. This is due to its complexity and because those who do not have children, or their own home, may not be covered by it. Any changes in this would of course involve an Exchequer cost.

Lifetime Gifts

The main concerns raised with the OTS regarding the taxation of lifetime gifts are that:

- the various gift rules and exemptions can be complex and confusing and are not always well understood, especially those relating to the tapering of the tax rate for gifts given in the seven years before death
- the financial limits for the various exemptions have not kept pace with inflation (it being recognised that increases would have an Exchequer cost)
- for many, it is difficult to either maintain or reconstruct records of lifetime gifts

Businesses and Farms

The OTS has received a wide range of comments about agricultural property relief (APR) and business property relief (BPR), including some which raised some quite broad questions. However, the OTS's focus will be on the practical application and complexity of these reliefs rather than major changes to the reliefs themselves.

The evidence gathered so far suggests the reliefs are broadly working in a straightforward way. However, there are some areas where there is confusion, lack of consistency or where the rules do not account for businesses structured in different ways. This includes issues relating to furnished holiday lettings, joint ventures and limited liability partnerships - where changes could well have an Exchequer cost. The OTS has also heard that the need to claim APR before BPR can lead to increased administration.

Big Picture

The OTS received a wide range of correspondence and reviewed a number of papers about how to reform Inheritance Tax.

Some of this material explored wide ranging issues about how to reform the tax as well as making suggestions about the complexities arising from the reliefs.

Suggestions have also been made about the interaction of the reliefs with the wider tax framework, and the potential distortions that may arise in relation to taxpayers' decisions about and the timing of transactions, especially in situations where BPR or APR apply.

Whether to make any changes in these areas is a matter for government. However, in its second report the OTS will consider these issues in more detail.

Other areas of complexity

The OTS will also consider other aspects of Inheritance Tax including what, if anything, could be done to simplify the rules in the following areas:

- the practical operation of the reduced rate of Inheritance Tax which is available when a certain proportion of an estate is left to charity
- the administration of life insurance products and pensions and the type of products available
- technical aspects relating to trusts
- the rule around giving a gift but enjoying a benefit from the assets given away

Wider perceptions about Inheritance Tax

Inheritance Tax appears to be an almost uniquely unpopular tax. In a 2015 YouGov survey, Inheritance Tax was seen as the most unfair of 11 major taxes, with 59% considering it 'unfair' and only 22% 'fair'.¹⁴

The OTS gathered evidence from its survey, call for evidence responses and in-depth discussions about the perceptions that people of all levels of wealth have about Inheritance Tax. Some of these, inevitably, range outside the OTS's simplification remit, but are included here as part of the background context. The key themes that emerged are set out below.

The rate is seen as high, despite the sizeable threshold

The headline rate of Inheritance Tax is 40%. This is the joint fourth highest headline rate in the OECD.¹⁵ However the average effective tax rate is generally below 20%, as a result of the combination of the standard threshold of £325,000 and the various reliefs which are available.

It's paying tax twice

A common question is why tax should be paid on wealth generated over peoples' life time when this wealth would have already been subject to, for example, Income Tax.

However, this arrangement is not exceptional. Indirect taxation, such as Value Added Tax (VAT), could also be considered 'double' taxation. An individual's earnings are taxed, and then the purchasing of goods and services may also be subject to tax.

It should also be borne in mind that some of the wealth on which Inheritance Tax may be paid is not taxed at any other time, in particular the increase in value of a person's home since it was purchased, as no Capital Gains Tax is paid on this on sales during one's life or on death.

¹⁴ <https://yougov.co.uk/news/2015/03/19/inheritance-tax-most-unfair/>

¹⁵ [https://www.ey.com/Publication/vwLUAssets/ey-worldwide-estate-and-inheritance-tax-guide-2018/\\$FILE/ey-worldwide-estate-and-inheritance-tax-guide-2018.pdf](https://www.ey.com/Publication/vwLUAssets/ey-worldwide-estate-and-inheritance-tax-guide-2018/$FILE/ey-worldwide-estate-and-inheritance-tax-guide-2018.pdf). However, it is impossible to look at taxes in isolation as different jurisdictions design their tax systems accounting for a range of differing factors and provide different reliefs and exemptions. Different jurisdictions will have different average effective tax rates.

People without spouses or direct descendants have fewer options

When someone dies, they can leave their estate to their spouse or civil partner (if they have one) without having to pay Inheritance Tax. That is not the case for someone who lives with their partner but has not married or entered into a civil partnership.

This could be considered to disadvantage those who cohabit or are single. In addition, the current system may be considered to disadvantage those who, for example, leave an estate that does not include a main residence or who do not have children. This is because the newly introduced residence NRB may not be available to someone who has never owned a home or has no qualifying descendants. Any extension of relief in these areas would, of course, have an Exchequer cost.

Concern about the number of people it may apply to

There is some concern that more people are subject to Inheritance Tax than actually pay it. The results of the OTS's public online survey¹⁶ show this is in part true, at least for a large minority of those who took part.

In the OTS's online survey, 53% of respondents correctly answered that less than 5% of people are liable to Inheritance Tax. However, 26% of survey respondents thought that 20% or more people paid Inheritance Tax.

A concern that wealthy people don't pay it

There is a concern that Inheritance Tax is a tax that the richest can avoid through careful tax planning, including the use of various reliefs (as discussed above), by making lifetime gifts and through trusts.

Those that are wealthier do have more flexibility in how they use their assets. They do not need to retain all their wealth to fund their lifestyle through their retirement and their wealth is less likely to be concentrated in a single family home. So the wealthier are, in principle, able to give away more during their lifetime, reducing the amount of Inheritance Tax they could pay.

The charts above do not take into account gifts made more than 7 years before a person's death. Such gifts are not subject to Inheritance Tax and HMRC does not collect data about them.

There is little representative data on lifetime giving,¹⁷ so it is not possible to quantify the extent to which it may affect the size of estates for Inheritance Tax purposes. HMRC have externally commissioned research on lifetime giving, to obtain better data in this area. It is expected that the results of the research will be published in 2019.

There is also a perception that the wealthiest give away their wealth and place it in trusts to avoid paying any Inheritance Tax. However, it is likely this does not take full account of the 2006 changes to the Inheritance Tax regime for trusts (which now

¹⁶ See annex D for further information regarding the OTS's online survey.

¹⁷ Survey data to date does not show the full picture. The English Longitudinal Survey of Aging provides some information for those aged over 50.

includes charges when assets are put into or taken out of trusts, and periodically throughout the trust's existence). Some issues in this area feature in the government consultation on the taxation of trusts published on 7 November 2018.¹⁸

¹⁸ <https://www.gov.uk/government/consultations/the-of-taxation-of-trusts-a-review>

Executive summary

Introduction

The Office of Tax Simplification (OTS) is the independent adviser to government on simplifying the UK tax system. The work of the OTS is rooted in improving the experience of all who interact with the tax system. The OTS aims to improve the administrative process - which is what people actually encounter in practice - as well as simplifying the rules. These are often of equal importance to taxpayers and HMRC.

In January 2018, the Chancellor asked the OTS to carry out a review of Inheritance Tax to make recommendations on simplification and to make the experience of those who interact with it as smooth as possible (see Annex A).¹

Following unprecedented public interest, the OTS published an online survey to enable the general public to contribute their views on Inheritance Tax,² as well as issuing its customary call for evidence. As well as meeting with representative bodies, professional advisers, academics and others as part of its evidence gathering process, the OTS also set up a Consultative Committee to provide advice (see Annex B).

This report sets out recommendations on administrative issues. These were the most frequently raised concerns in the responses and comments received, and will remain important even if significant technical or design changes were to be made to the tax in the future.

A discussion of the main comments the OTS has received about the more complex areas of the tax is in Chapter 3. The OTS will return to those areas in a second report to be published in spring 2019, with the aim of investigating the ongoing debate about how these more complex aspects of the tax could be simplified.

Reducing the administration burden on estates

Why is the administration of Inheritance Tax important?

Administering an estate is a burden on all executors³ whether or not Inheritance Tax is due. The OTS has heard from members of the public about the challenges faced

¹ <https://www.gov.uk/government/publications/ots-inheritance-tax-review-scoping-document>

² <https://www.gov.uk/government/consultations/inheritance-tax-review-call-for-evidence-and-survey>

³ The person or people who are named in the will and have responsibility for administering the estate, including dealing with any Inheritance Tax consequences and applying for probate. If a person does not leave a will, then someone can apply to be an 'administrator' of the estate. In this report we use 'executor' to embrace both roles.

by executors, with many wanting to share their experiences to help make improvements.

This may simply have been reading guidance to establish that no forms need to be submitted to HMRC, or it may have been having to complete a long Inheritance Tax form and pay tax. The process should be easy to follow for either of these scenarios.

There were 588,000 deaths in the UK in tax year 2015 to 2016 and an Inheritance Tax form was completed by just under half of these. This is a high proportion compared to the 24,500 estates on which Inheritance Tax was actually payable.⁴

The OTS's consultation indicates that many people worry about Inheritance Tax

Many of the recommendations in this and the second report should, if implemented, help make Inheritance Tax simpler and easier to understand for those who worry about the tax generally, are not within its scope, or are worried about having to administer an estate.

Observations and recommendations

The OTS has considered all the representations received on estate administration and this section summarises the observations made and recommendations for improvement that are set out in more detail in Chapters 1 and 2.

Forms

Executors must complete either a long form or a short form, depending on their position.⁵ The short form requires much less detail than the long form.

The OTS has observed the following about the forms:

- for many executors, forms cannot be completed and submitted online
- there is no straightforward process to direct taxpayers to the correct form
- although some executors who are dealing with a very simple estate find completing the short form straightforward, many executors find the process challenging
- the amount of information required on the long form is disproportionately high for estates where there is no Inheritance Tax to pay

Key Recommendation

The government should implement a fully integrated digital system for Inheritance Tax, ideally including the ability to complete and submit a probate application.

Short term simplifications

The OTS recognises that a fully digital system will be expensive and will take time to accomplish. Therefore, in the short term, the OTS suggests certain improvements to the existing process to address these criticisms.

⁴ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/731610/Inheritance_Tax_National_Statistics_Commentary.pdf

⁵ The long form is the "Full Inheritance Tax account", or "IHT400" and the short form is the "Return of estate information" or "IHT205". The short form and probate process in Scotland and Northern Ireland are different from those in England and Wales.

Recommendation 2

Pending implementation of a digital system, HMRC should make changes to the current forms to reduce and simplify the administration of estates, including introducing a very short form for the simplest estates and updating the conditions that must be met to be able to complete a short Inheritance Tax form.

Guidance

The OTS has the following main observations about guidance:

- Inheritance Tax guidance on GOV.UK is difficult to navigate and is sometimes inconsistent with other areas of guidance
- there should be worked examples and case studies, especially of situations where no tax is due, along with a step by step guide or 'roadmap' to highlight what an executor needs to do and when
- an online Inheritance Tax calculator would be a helpful tool
- it is challenging to produce simple guidance whilst the underlying rules remain complex

Introducing these changes would help to reduce worry for those who will not have to pay any Inheritance Tax, allowing them to establish this quickly and easily by looking at relevant guidance, case studies and using the online calculator.

The OTS has published a separate paper on guidance⁶ more generally. The observations and recommendations in this report are specific to Inheritance Tax.

Recommendation 3

HMRC should carry out a general review of its Inheritance Tax guidance with the aim of it being:

- targeted to reduce concern for those who worry unnecessarily
- clear, consistent and easy to navigate
- linked or located with other relevant guidance, including probate
- expanded to include worked examples, a road map, timescales and a tax calculator
- sufficient for complex estates to apply the law and practice correctly

In line with some other taxes, HMRC should also consider increasing the use of other educational channels such as webinars.

Communication

The OTS has heard that HMRC communications with executors could be improved and has observed the following:

- HMRC introduced a new 12 week response period in April 2018, during which HMRC should make an initial contact with an executor about any enquiries

⁶ <https://www.gov.uk/government/publications/guidance-for-taxpayers>

into a form – this is a welcome improvement on previous practice, but it is early days for the new process

- receipts are not issued for the payment of Inheritance Tax, and this would provide reassurance to executors

Recommendation 4

HMRC should introduce a system issuing automated payment receipts and, if necessary, further refine the recently introduced 12 week response period, during which any enquiries into the information contained on the form will be made.

Payment deadlines and probate

The granting of probate gives a person the legal right to deal with someone's property, money and possessions after they have died. Probate is not granted, and assets in the estate cannot be distributed, until both the Inheritance Tax is paid, and the forms have been submitted.

Inheritance Tax must be paid within 6 months of the month of death, whereas Inheritance Tax forms must be submitted within 12 months of the month of death.

The OTS observes the following about the payment and probate process:

- a payment deadline of 12 months following the death would be a simplification for executors but would be costly to implement as it would lead to a deferral of tax receipts
- paying Inheritance Tax before assets can be distributed is difficult for some executors
- to help executors, HMRC and HM Courts and Tribunals Service should explore potential solutions. For example, for low value and other simple estates, the possibility of obtaining probate without submitting Inheritance Tax forms, or on submission of a very simple form, and whether a confirmation of executor status could be provided to help executors obtain information about the estate

Recommendation 5

HMRC should liaise with HM Courts and Tribunals Service on options for streamlining the payment and probate process.

Non-Inheritance Tax matters affecting executors

During the OTS's work on this review several non-Inheritance Tax matters have been highlighted that have a big impact on the administration of Inheritance Tax. The OTS has observed that:

- guidance on related tax areas, such as Income Tax and Capital Gains Tax for estates in administration should be considered alongside the review of Inheritance Tax guidance
- a widely-adopted standardised process for banks and other financial institutions to allow executors to access information or to release funds would reduce the administration burden for executors

- regulating the will writing market would help improve the administration process

Administration of other Inheritance Tax charges

Inheritance Tax is not only a tax on the estate following an individual's death, but is also charged on other events, for example on certain transfers during an individual's lifetime, or in relation to trusts. For these events, a form⁷ must be submitted to HMRC.

The OTS observes the following about the form:

- it is complex and caters for too many different occasions
- there are some circumstances when a form must be submitted by trustees, even though there is no tax due
- it must be signed by all trustees, which can be burdensome, and is inconsistent with other areas of the tax system
- a digital system for Inheritance Tax should include the ability to administer lifetime charges and trust charges

Recommendation 6

HMRC should review the requirement for trustees to submit forms when no Inheritance Tax is due, and no reliefs or exemptions are claimed.

Recommendation 7

Until a digital system can be implemented, HMRC should make changes to the existing form for lifetime charges and trusts. These include: splitting up the current form so there is a simple and tailored form for each occasion; improving the guidance available for completing the form and calculating the tax; and aligning the signature requirements for trustees with other parts of the tax system.

Communication

The OTS observes that:

- HMRC takes a long time to respond to the form and sometimes does not respond at all
- no receipts are issued when HMRC receive the form or an associated Inheritance Tax payment
- HMRC have recently introduced a 12-week review period for forms completed by executors but no comparable review period exists for this form (IHT100)

Recommendation 8

HMRC should introduce a system issuing automated receipts for IHT100 forms and Inheritance Tax payments made alongside the form, and consider introducing a review period during which an enquiry into the information contained on the IHT100 form will be initiated.

⁷ The "IHT100"

Summary of recommendations

- 1 **KEY RECOMMENDATION:** The government should implement a fully integrated digital system for Inheritance Tax, ideally including the ability to complete and submit a probate application.
- 2 Pending implementation of a digital system, HMRC should make changes to the current forms to reduce and simplify the administration of estates, including introducing a very short form for the simplest estates and updating the conditions that must be met to be able to complete a short Inheritance Tax form.
- 3 HMRC should carry out a general review of its Inheritance Tax guidance with the aim of it being:
 - targeted to reduce concern for those who worry unnecessarily
 - clear, consistent and easy to navigate
 - linked or located with other relevant guidance, including probate
 - expanded to include worked examples, a road map, timescales and a tax calculator
 - sufficient for complex estates to apply the law and practice correctly

In line with some other taxes, HMRC should also consider increasing the use of other education channels such as webinars.

- 4 HMRC should introduce a system issuing automated payment receipts and, if necessary, further refine the recently introduced 12 week response period, during which any enquiries into the information contained on the form will be made.
- 5 HMRC should liaise with HM Courts and Tribunals Service on options for streamlining the payment and probate process.
- 6 HMRC should review the requirement for trustees to submit forms when no Inheritance Tax is due, and no reliefs or exemptions are claimed.
- 7 Until a digital system can be implemented, HMRC should make changes to the existing form for lifetime charges and trusts. These include: splitting up the current form so there is a simple and tailored form for each occasion; improving the guidance available for completing the form and calculating the tax; and aligning the signature requirements for trustees with other parts of the tax system.
- 8 HMRC should introduce a system issuing automated receipts for IHT100 forms and Inheritance Tax payments made alongside the form, and consider introducing a review period during which an enquiry into the information contained on the IHT100 form will be initiated.

Chapter 1

Reducing the administration burden on estates

Introduction

- 1.1 This chapter suggests simplifications to the Inheritance Tax administration process for executors and others administering estates. It considers the following areas:
- forms
 - guidance
 - communication with HMRC
 - payment deadlines and probate
 - non-Inheritance Tax matters that affect the administration of Inheritance Tax

Background

- 1.2 The OTS has received many comments from members of the public about the challenges faced by executors, with many wanting to share their experiences to help make improvements.

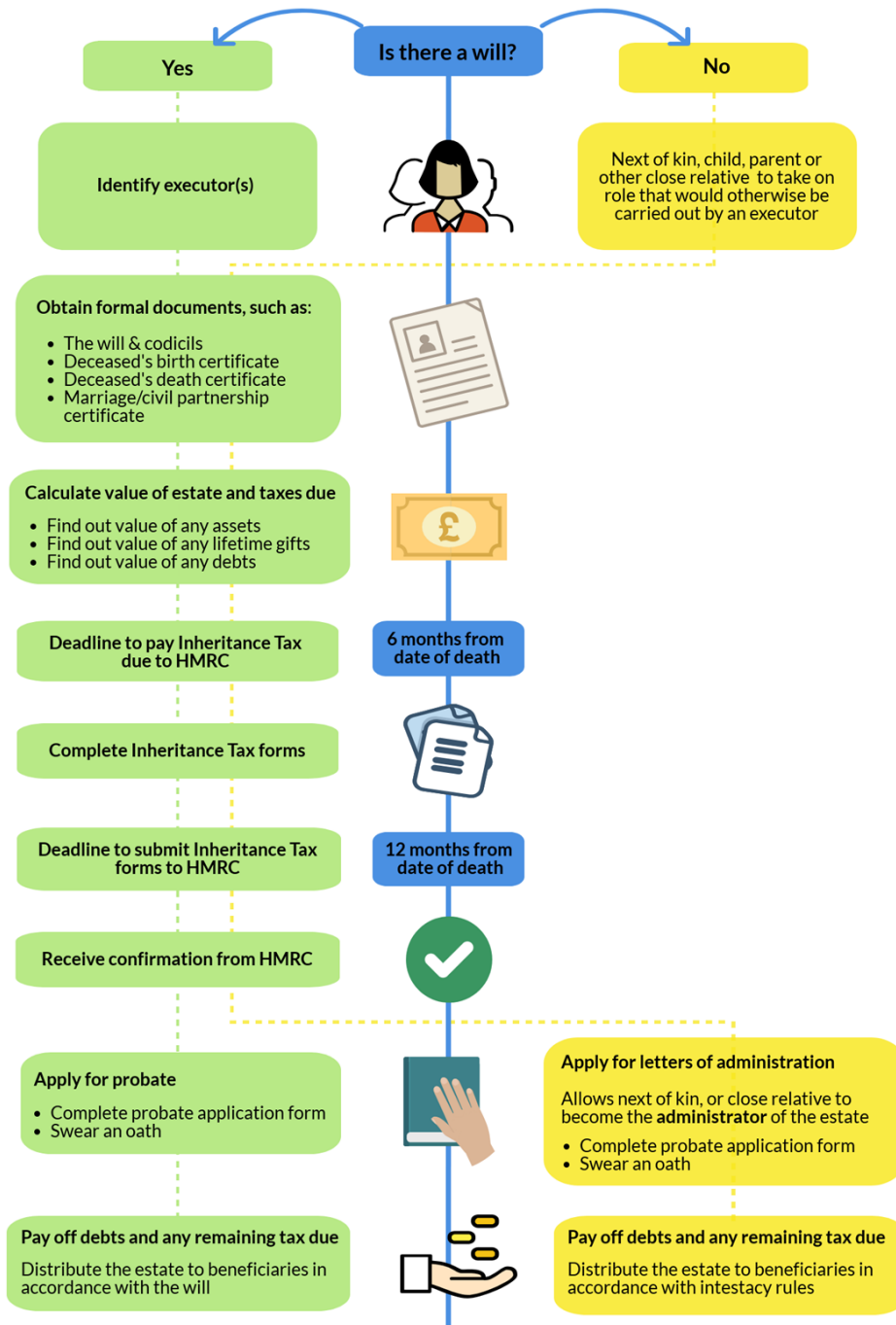
Quote from a member of the public

"I still have nightmares about it and welcome the chance to help secure changes that will ensure that others do not have to go through the same experience."

- 1.3 The responsibility of being an executor is usually placed on an individual at an emotional time, following the death of a relative or friend. It may well involve finding out and handling information about the deceased that they have not been familiar with, and for many it will be the first time they have ever fulfilled this important role. Alternatively, a professional executor may be appointed to take on this responsibility.
- 1.4 Inheritance Tax is only a part of the administration process that executors must navigate through. An executor is also responsible for dealing with other aspects of estate administration, including applying for probate. The granting of probate gives a person the legal right to deal with someone's property, money and possessions after they have died. The Inheritance Tax and probate processes are closely linked, as set out in Chart 1.A.

- 1.5 The OTS has heard that the process can be stressful for executors due to several factors, including the lack of information available about the estate, confusion over what they need to do, and anxiety about how they will pay any tax due.

Chart 1.A: Steps taken by a person administering an estate



Source: OTS

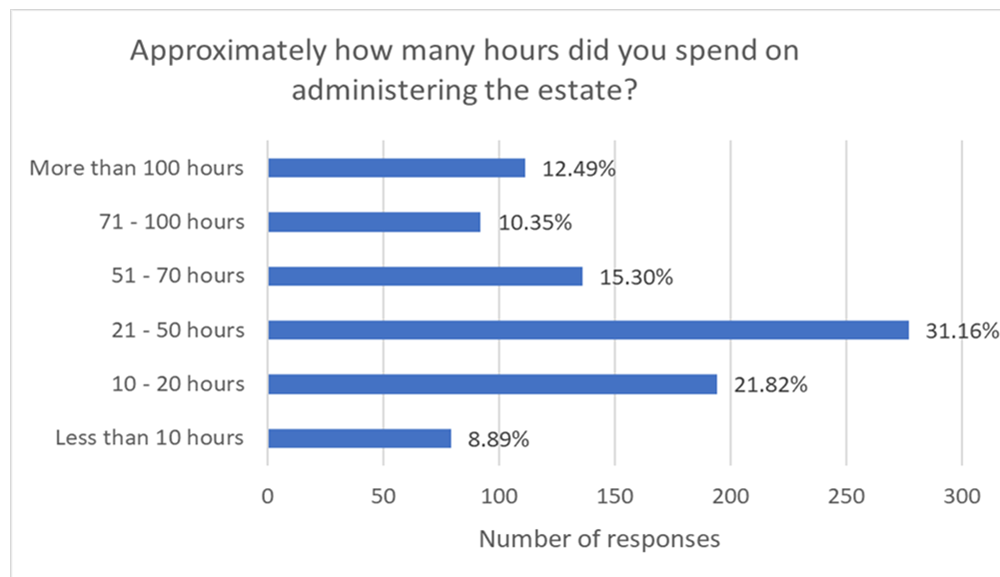
Survey findings

- 1.6 The OTS's survey asked about the experiences of administering an estate, and the time spent doing so.

Time spent

- 1.7 The survey indicated that 38% of respondents (who did not use an adviser) spent more than 50 hours administering an estate, which includes 12% of respondents who spent over 100 hours.

Chart 1.B: Responses* to the question about the amount of time taken to administer an estate without an adviser



Source: OTS survey results

* Total number of respondents: 889

- 1.8 Administering an estate requires an executor to carry out many different tasks and Chart 1.B includes time spent completing the entire process. The survey results suggest that respondents considered that understanding and completing the Inheritance Tax forms was the most time consuming part of this process.

Using an adviser

- 1.9 The survey indicated that many respondents enlisted an adviser to help with the process. Of those who used an adviser, nearly half (48%) said that they had done so because of the complexity of the estate, and over half (58%) said that they used an adviser because they were concerned about making a mistake.¹
- 1.10 The top five reasons given for employing an adviser based on the total number of responses received are as follows:
- 1 I was concerned I would make a mistake
 - 2 The estate was too complicated

¹ Out of a total of 737 people who responded to this multiple choice question

- 3 There was Inheritance Tax to pay
- 4 I did not understand what I needed to do
- 5 The cost was reasonable

- 1.11 A number of alternative reasons were also given under the 'other' category of responses. This was a free text box and included some of the following varied responses as to why people employed an adviser:
- 'You have made it too complicated with too many forms.'
 - 'I cannot be paid for my time so why should I do it free of charge.'
 - 'This tax is unforgiving when you are at your most vulnerable and at your lowest – i.e. death of a relative.'
 - 'I thought I had to.'
 - 'Far too difficult to understand what was needed without a professional. This advice has proved costly and taken an age.'

HMRC customer journey analysis

- 1.12 HMRC recently completed a 'customer journey' analysis of the processes that executors must go through in administering an estate, with a view to improving them. This should have a very positive impact on the experience of executors.
- 1.13 HMRC shared some of the outcomes of this internal project with the OTS. The information gathered through the customer journey analysis was a useful and important addition to the information gathered by the OTS.
- 1.14 The OTS considers that the recommendations made in this report will supplement the changes already being made by HMRC.

Forms

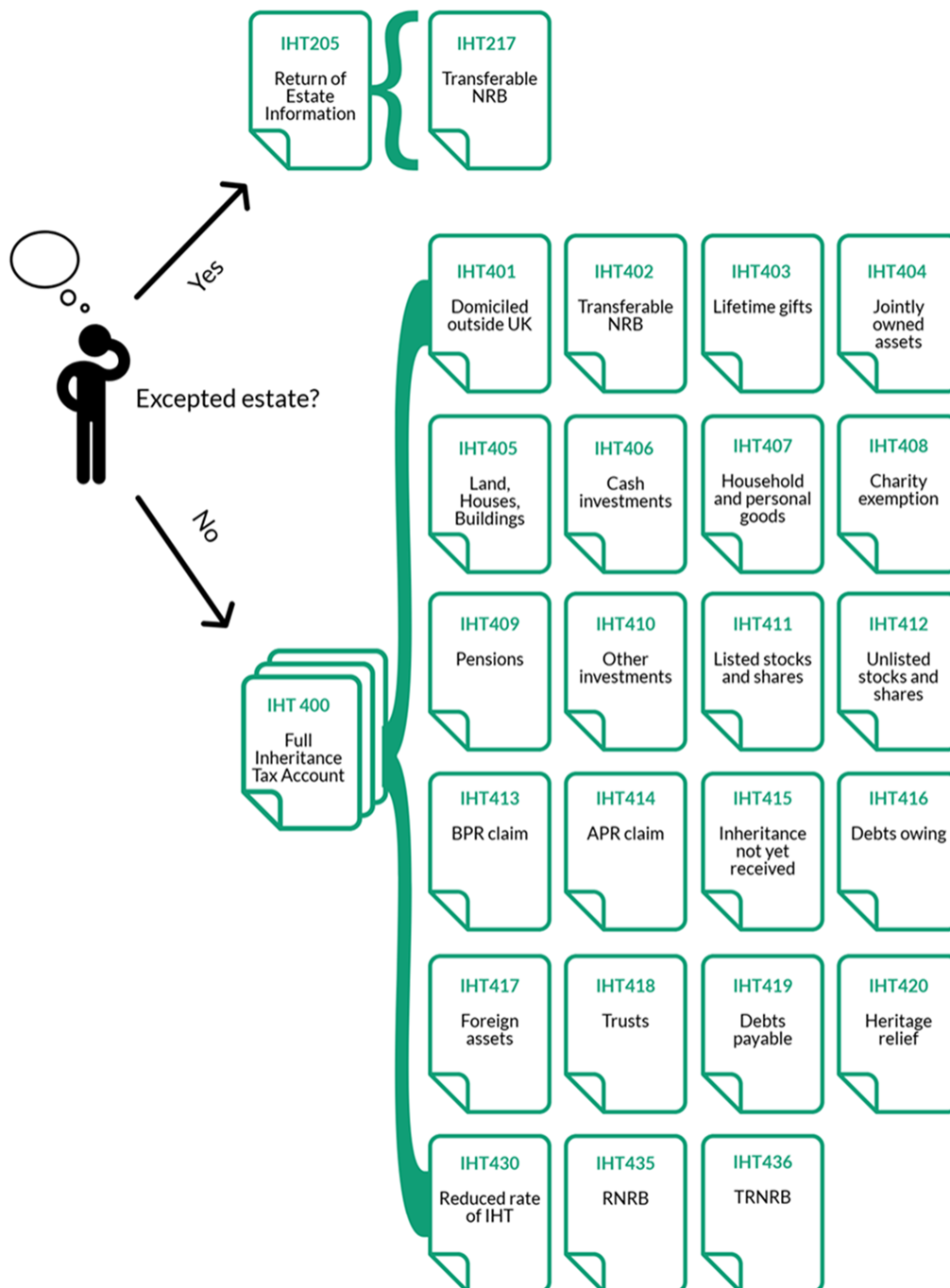
- 1.15 The need to complete Inheritance Tax forms does not depend on Inheritance Tax being due. There are many instances where forms must be completed even when there is no Inheritance Tax to pay.
- 1.16 There were 588,000 deaths in the UK in tax year 2015 to 2016 and an Inheritance Tax form was completed in relation to just under half of these.²
- 1.17 If probate is required, then Inheritance Tax forms need to be completed. Without submitting the correct forms and paying any Inheritance Tax due, probate will not be granted, and therefore assets cannot be distributed.
- 1.18 Executors must complete either a long form (Full Inheritance Tax account/IHT400) or a short form (Return of estate information/IHT205). The short form requires much less detail than the long form.
- 1.19 One of the main tasks for an executor is to decide whether Inheritance Tax forms need to be completed and if so, which forms to complete.

² <https://www.gov.uk/government/statistics/inheritance-tax-statistics-table-123-estates-notified-to-hmrc-numbers-and-tax-due>

- 1.20 Estates which fall under the definition of an 'excepted estate' can complete the shorter form. In most cases, if there is no Inheritance Tax payable on the estate then it will be an excepted estate, but this is not always the case. A definition of excepted estates is included in Annex C.
- 1.21 If the estate is not an excepted estate, then a long form is usually required. However, under certain circumstances where a set of conditions are met, such as when the estate passes entirely to an exempt beneficiary³ (for example a spouse or charity), then a reduced long form can be completed. This is the same form, but some sections are not required.
- 1.22 Either way, the long form requires a large amount of information. Usually several supplementary pages will need to be completed to expand on the information given in the main form.
- 1.23 Once an executor has established if the estate is an excepted estate, they will know which form to complete. Approximately 80% of estates that report to HMRC complete the short form, while the remaining 20% complete the long form.
- 1.24 Executors can either complete the forms themselves or employ an adviser to complete them on their behalf. The deadline for submitting the forms to HMRC is 12 months after the death. The short form must be submitted within the same deadline.

³ See annex C for definition of a beneficiary

Chart 1.C: Summary of Inheritance Tax forms and supplementary forms



Source: OTS

Observations

Confusion over which form to complete

- 1.25 There is no straightforward process to direct taxpayers to the correct form and this inevitably leads to confusion. There are a range of experiences, and although some executors who are dealing with a very simple estate find

completing the short form straightforward, the OTS has heard that many executors find the process challenging.

- 1.26 The OTS has heard that some executors began to complete the short form and realised part way through completing the form that they should have completed the long form. There are several reasons for this:
- the definition of an excepted estate is complex and is not well understood. If an executor is uncertain whether the estate qualifies as an excepted estate, then they are unable to establish which form to complete
 - executors may not read the guidance fully or find the guidance to be unclear
 - there are questions within the body of the short form which, if answered in a certain way, result in the need to complete the long form instead. The phrase 'stop filling in this form you will need to fill in form IHT400 instead.' is repeated 5 times
 - at the end of the short form, a figure must be given for the value of the estate. If this value is above the excepted estate limit, then a long form must be completed. It is therefore possible to complete the entire short form before being re-directed to the long form
- 1.27 At the end of the short form, executors are told that if the estate fails to qualify as an excepted estate then they may face financial penalties or face prosecution.⁴ For the inexperienced executor who may not be a beneficiary of the estate, this is a worrying prospect.

Quote from a member of the public

"There are so many IHT forms that after a few months we realised that we needed help, or we were going to miss the six month deadline. The advisers we used seemed reasonable to me, but even when they sent us the completed forms, I was not sure I understood everything. Both my brother and I have degrees, are around 60 and have worked in technical jobs, so we are by no means ignorant or innumerate, but the complication of the process is just too much."

- 1.28 Although the existence of two forms is confusing to inexperienced executors, it is clear from the responses the OTS has received that professional advisers understand the boundaries between the two forms and do not often spend time completing the wrong form.
- 1.29 There are prompts at various stages to check that the person completing the form knows that there are two separate forms and reiterates the criteria for an excepted estate. When a copy of the short form is downloaded from

⁴ IHT205 form:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/459092/IHT205_2011_.pdf

HMRC's website, there is an automatic pop up which explains situations where the short form is not appropriate.

A long form must be completed for some estates even when there is no Inheritance Tax payable

- 1.30 The OTS has received correspondence from many taxpayers who felt that the amount of information required on the long form is disproportionately high for estates where there is no or very little Inheritance Tax to pay.
- 1.31 The survey responses indicated that 65% of respondents who did not engage an adviser, and 50% of those who had, felt that they still had to provide lots of information despite no Inheritance Tax being due.

Quote from a member of the public

"The burden of form filling is a tax in itself."

- 1.32 There are many different scenarios when a long form is required even though there is no Inheritance Tax to pay. For complex estates, it is reasonable that HMRC may require detailed information but for simple estates, for example those in the following four scenarios, it is difficult to understand why such detailed information is required.
- where the estate is worth more than £1 million but is left entirely to a surviving spouse or civil partner
 - where the estate is worth more than £1 million but there is no Inheritance Tax due because some or all the estate has been left to charity
 - when a part of the transferable NRB was used up on the first death, but the estate was left entirely to a surviving spouse or civil partner
 - whenever the residence NRB, introduced in April 2017, is claimed, and the estate is below the relevant tax free amount

Manual process for completing the forms

- 1.33 The process for completing Inheritance Tax forms has not been digitalised and most forms can only be submitted on paper. Only 12% of survey respondents who did not use an adviser said that they had submitted forms electronically to HMRC.
- 1.34 The short form can be completed and submitted online, however advisers are not able to use this online service and must submit all forms manually.
- 1.35 Forms can be downloaded from HMRC's website, but they are not fully compatible with freely available software and are very difficult to complete on a computer. Forms are often completed by hand, which is time consuming and does not allow for changes to be made easily without completing the entire form again.
- 1.36 There is some software which allows a PDF version of Inheritance Tax forms to be edited on a computer, but it is costly to purchase, and even with the costly software, it is not an easy process to complete.

Quote from a member of the public

"They are PDF forms with text and number entry fields that can be filled in on screen. Many of the number entry fields did not work correctly."

"In the end I gave up and started pasting text on top of the fields. Sometimes the whole PDF could not be added to or changed when it was reopened, and in these cases I had to import new PDF pages from an unfilled version of the form."

"When I informed the IHT helpline about these problems they said that this must explain why many of the forms they received were full of apparently inconsistent data."

HMRC started work on a project to put the Inheritance Tax forms online

- 1.37 As part of a wider drive to improve compliance, HMRC started a project to put the Inheritance Tax forms online. The project began in 2014 and aimed to create digital versions of the current Inheritance Tax forms.
- 1.38 In April 2018, HMRC announced that the digital transformation of Inheritance Tax would be delayed, along with several other transformation projects.
- 1.39 There were many challenges to creating digital forms, particularly in trying to cater for all possible circumstances, including the most complex estates. The OTS has heard that the forms are too complex and do not lend themselves to being made digital because of the complexities within the Inheritance Tax rules.
- 1.40 A simplification of the technical aspects of Inheritance Tax rules could allow the long forms to be simplified which would make a comprehensive digital version of the forms more realistic. In its second report, the OTS will make recommendations that will address this.
- 1.41 The ambition of the HMRC project was initially to put all Inheritance Tax forms online. However, at a later stage, it was decided to focus HMRC resources on digitising the short form (IHT205). The short form is now available to complete online for taxpayers in England and Wales.

No forms can be completed online in Scotland or Northern Ireland

- 1.42 The confirmation process in Scotland is a paper based probate process. To receive confirmation, hard copy documents need to be presented to the court in person. Executors receive a bond document of confirmation once the process is complete. No forms are available to complete online in Scotland and Northern Ireland.

Conclusions

Inheritance Tax online – a fully integrated digital system for Inheritance Tax

- 1.43 The OTS concludes that a fully digital system is required to allow executors or their advisers to provide information directly to HMRC. This would be an

entirely different experience to the current form filling exercise carried out by executors.

- 1.44 The OTS envisages an online portal, like the Self Assessment Income Tax system shown in Chart 1.D. The current supplementary forms to the long form would be replaced and the online system would expand to meet the circumstances of the estate as necessary.

Chart 1.D: Tailoring the Income Tax return

The screenshot shows the 'Tailor your return' section of the HMRC online tax return system. On the left is a sidebar titled 'File a return' with a list of steps: 1. Welcome, 2. Tell us about you, 3. Tailor your return (highlighted), 4. Fill in your return, 5. Check your return, 6. View your calculation, 7. Save your return, and 8. Submit your return. The main content area is titled 'Tailor your return' and 'Page 2 of 3'. It contains a series of questions for the tax year 6 April 2017 to 5 April 2018, each with 'Yes' and 'No' radio button options. The questions are: 'Did you receive any interest etc., for example, from UK banks, UK building societies, UK unit trusts?', 'Did you receive any dividends, for example, UK companies, authorised unit trusts, open-ended investment companies, foreign companies (up to £300)?', 'Did you receive any UK pensions, annuities or state benefits, for example, state pension, occupational pension, retirement annuity, Incapacity Benefit?', 'Were you or your partner (if you have one) entitled to receive Child Benefit during the year 2017-18 (this applies if someone else claims Child Benefit for a child who lives with you and pays you for your child's upkeep)?', 'Did you receive any other UK income, for example, employment lump sums, share schemes, life insurance gains?', 'Have you made any income tax losses in the year 2017-18?', and 'Are you liable to pension savings tax charges or have you received payments from overseas pension schemes?'. At the bottom of the form is a green 'Save and continue' button.

Source: HMRC online services

- 1.45 Executors would complete a list of questions, in a similar way to the Self Assessment Income Tax system, which would create a tailored return. There would no longer be two separate forms, which would simplify the process by eliminating the need to choose between forms at the outset. Ideally, the online portal would also include the ability to complete and submit a probate application, where necessary. This should significantly reduce duplication.
- 1.46 The OTS recognises that it would be difficult to implement a completely digital system in Scotland because the court process requires hard copy documents to be presented to court in person. However, the new digital system would enable Scottish taxpayers to enter information into the system and print a completed document to present to court.
- 1.47 A fully integrated digital system could allow taxpayers to make online payments and include additional features such as automated confirmations

and reminders. It would also allow HMRC to improve data collection and analysis.

1.48 The key attributes of the proposed digital system:

- a system which expands and contracts. Only information relevant to the circumstances of the deceased are requested
- functionality to partially complete the information, save and return to it later without data being automatically deleted after a fixed period. The user should be able to see a full list of all the required information at the outset
- automatic calculation of the amount of Inheritance Tax payable
- ability to make tax payments through an online payment system with an automatic receipt

Key Recommendation

The government should implement a fully integrated digital system for Inheritance Tax, ideally including the ability to complete and submit a probate application.

Short term simplifications: improve taxpayer experience by simplifying the existing forms

1.49 A fully digital system will be expensive and will take time to introduce.

1.50 In the short term the OTS suggests the following changes which would both simplify the process and improve taxpayers' experience:

- use straightforward online gateways, which clearly direct executors to the appropriate form
- introduce a very short form for estates with a low value based on total assets. The form should require a rough estimate of the value of the assets. For these very simple estates, it should ideally be possible to provide the necessary information as part of a combined tax and probate form
- update the current Inheritance Tax forms to allow them to be more easily edited on a computer
- update the forms and expand the definition of an excepted estate to take account of the residence NRB and the transferable residence NRB

Recommendation 2

Pending the implementation of a digital system, HMRC should make changes to the current forms to reduce and simplify the administration of estates, including introducing a very short form for the simplest estates and updating the conditions that must be met to be able to complete a short Inheritance Tax form.

Guidance

1.51 Guidance on Inheritance Tax is extensive. An initial search will lead many people to the GOV.UK website. Published metrics indicate that the

Inheritance Tax guidance on GOV.UK may be getting as many as 1 to 1.5 million hits a year.⁵

- 1.52 Unlike Income Tax and Capital Gains Tax, the Inheritance Tax burden can fall on those who may take no personal benefit from the estate at all (the executors or trustees) and they therefore need to be particularly clear about their potential liabilities before making any distributions. Clear guidance is therefore of great importance to both executors and trustees.

Sources of Inheritance Tax guidance

- 1 Inheritance Tax guidance on GOV.UK
 - 2 Notes to the Inheritance Tax forms – there are separate notes for each of the Inheritance Tax forms. For the IHT400, the notes are over 90 pages long.
 - 3 HMRC’s Inheritance Tax Manual – this is HMRC’s internal guidance notes. It is published online for anyone to view.
 - 4 Trusts and Estates Newsletter – this is published regularly and provides Inheritance Tax guidance to professional advisers. It can also be found on the GOV.UK website.
- 1.53 The OTS has published a separate paper on guidance⁶ more generally; the observations and recommendations that follow are specific to Inheritance Tax.

Observations

GOV.UK

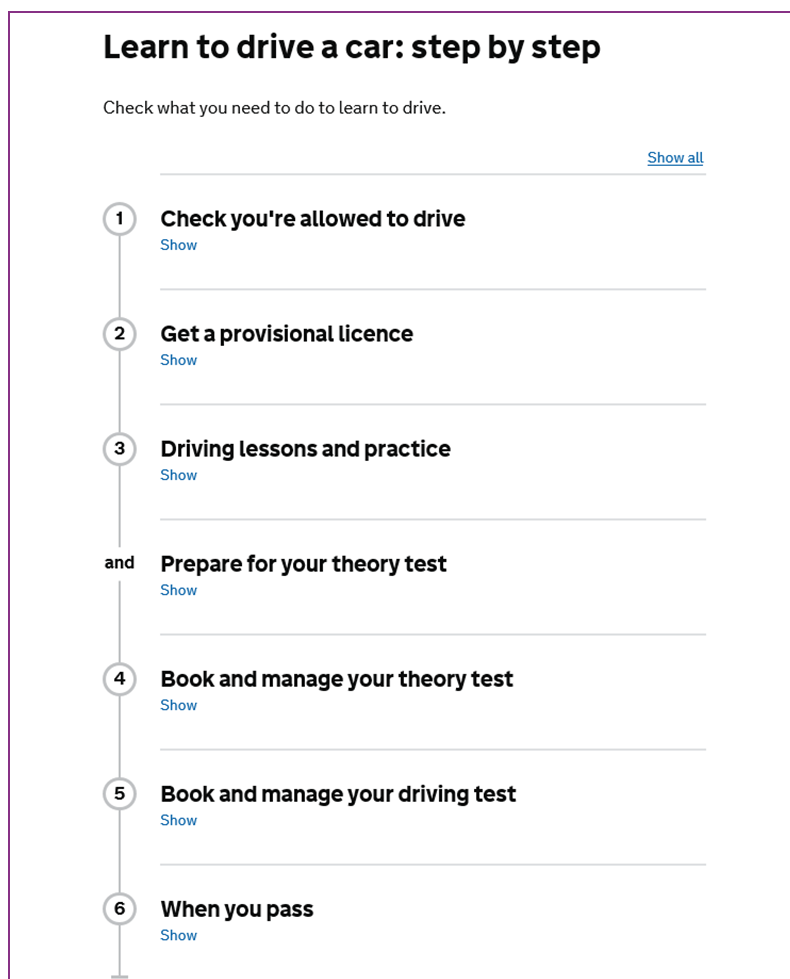
- 1.54 Respondents to the call for evidence shared a wide range of concerns about Inheritance Tax guidance, with the Inheritance Tax guidance on GOV.UK a key area of concern.
- 1.55 Respondents noted that the Inheritance Tax guidance on GOV.UK is difficult to navigate. The guidance is a complex web of linked pages with no clear ‘route map’ to guide the user. It is not easy to find the answer to your question even if the answer is on the website.
- 1.56 Guidance can be clear and easy to use. Examples of this can be found elsewhere on GOV.UK. For example, the OTS has been referred to the government’s ‘learn to drive’ guidance, where a step by step approach has been used very successfully.⁷

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

⁶ <https://www.gov.uk/government/publications/guidance-for-taxpayers>

⁷ <https://www.gov.uk/learn-to-drive-a-car>

Chart 1.E: An example of step by step guidance



Source: www.gov.uk/learn-to-drive-a-car

- 1.57 Although the learning to drive example is a more self-contained topic than Inheritance Tax, it should be straightforward to set out the steps for the Inheritance Tax process using a similar format. The OTS understands this is something that HMRC are already considering.
- 1.58 The OTS has heard that some guidance on GOV.UK is so over-simplified it is difficult to understand. Much of the content on the GOV.UK website is also, of course, covered in the HMRC manuals. Whilst the HMRC manuals are more detailed, they can be difficult for individuals to use because they have been written for experienced HMRC staff and are largely used by professional advisers.
- 1.59 There are also inconsistencies in Inheritance Tax guidance. In some cases (for example in relation to valuations) there are discrepancies between the guidance found on GOV.UK and the notes to the Inheritance Tax forms. In other cases, inconsistencies relate to the use of terminology. For example, the residence NRB is confusingly referred to as an 'additional threshold' on GOV.UK.
- 1.60 Some important guidance, such as when to expect HMRC's response to a submitted form, is available from other sources (for example, the Trusts and

Estates newsletters) but not on the main GOV.UK Inheritance Tax guidance pages.

Gaps in guidance

- 1.61 Many of the responses focused on what is missing from government guidance.
- 1.62 Some indicated that an explanation is needed of the situations in which no Inheritance Tax will be due, to provide clarity and alleviate anxiety. Although many respondents to the OTS's survey were aware of both the NRB and the spouse exemption, it was nevertheless a theme of the responses to the consultation that there should be such a section of the guidance.
- 1.63 It was suggested that case studies or worked examples in the guidance would be helpful in clarifying the key thresholds and exemptions and helping people understand their own position. For example, a case study could include an estate with assets below the NRB, a taxpaying estate and an estate which includes gifts given in the 7 years before death (known as failed potentially exempt transfers).⁸

Quote from a member of the public

"IHT is unlike any other official process. Normally, there are worked examples of the most common scenarios on GOV.UK. This is frustrating if you have complex affairs, but perfect for most people.

IHT is completely the opposite – there are few worked examples and lots of explanations of complex exemptions that affect only a few people. IHT "explanations" dive straight in to all the complexity."

- 1.64 Several responses to the call for evidence suggested that what is needed is a chronological road map or flow chart, showing step by step what executors need to do, and when, showing clear timescales for taxpayer obligations and HMRC responses, and including the probate process. This would be similar to the learn to drive guidance described in Chart 1.E above.
- 1.65 Others suggested that a checklist of executors' responsibilities would be helpful, as would a statement about how long an executor should retain records relating to the estate they have administered.
- 1.66 It was also suggested that an Inheritance Tax calculator should be produced, along the lines of the Stamp Duty Land Tax, and other tax calculators. The OTS notes that several organisations outside government have produced online Inheritance Tax calculators which are useful to individuals.
- 1.67 It was observed that the guidance on the rules relating to lifetime gifts, particularly on the appropriate and proportionate level of record keeping that should be undertaken by those giving gifts in their lifetime, was insufficient.

⁸ See Annex C for a definition of a failed potentially exempt transfer

- 1.68 Several charities noted in their responses that the allocation of Inheritance Tax between the charitable and non-charitable beneficiaries of an estate was poorly understood by taxpayers and executors, and that additional guidance was needed.
- 1.69 Finally, respondents in Scotland suggested that separate guidance should exist to deal with Scottish matters, given the differences between Scottish and English probate and property law.

Liquid assets

- 1.70 Another theme of the consultation responses was that there is a lack of clarity around what to do when there are not enough liquid assets in the estate to meet Inheritance Tax liabilities. To some extent, this is an issue with the interaction between tax and probate, and this is discussed further elsewhere in this report. However, the guidance in this area is spread out and can be difficult to locate, especially if you do not know in advance what you are looking for.
- 1.71 The following appear to be common areas of confusion:
- what assets can you liquidate before obtaining probate to pay Inheritance Tax?
 - what documentation might a bank or investment house typically require, to liquidate assets and pay the proceeds direct to HMRC?
 - when do the instalment payment provisions apply?
 - when can you apply for a grant on credit?
 - what are time to pay arrangements?
- 1.72 Clearly not all these areas are under control of HMRC. However, they are all connected to the issue of liquidity and would benefit from the guidance being in one place or signposted.

Conclusions

A general review of Inheritance Tax guidance is needed

- 1.73 HMRC should conduct a review of all its Inheritance Tax guidance, considering all the points set out above. Whilst some aspects of Inheritance Tax guidance are separate from probate, the guidance on executor obligations, timescales and process should be integrated with probate guidance as far as possible.
- 1.74 Guidance needs to be clearer, more consistent and easier to find. Guidance should include examples and case studies explaining the position for individuals with estates below the nil rate bands. Different forms of customer support could be used to provide additional support and guidance. These could include guidance videos and wider use of webinars.
- 1.75 Terminology should be consistent and explained throughout the guidance. All existing inconsistencies should be removed and any gaps in the guidance should be filled.

- 1.76 This includes guidance on paying Inheritance Tax where there are illiquid assets, and where necessary, links to sources outside HMRC.
- 1.77 HMRC's customer journey work has highlighted similar issues to those made by respondents to the OTS's consultation and, in some cases, HMRC has begun taking steps to remedy the problem. This is extremely welcome. However, there is more that could be done and if necessary, HMRC should allocate short term resource to this.
- 1.78 Improved guidance would benefit HMRC as well as the public, by freeing up HMRC resource through reductions in customer correspondence and the use of the telephone helpline.
- 1.79 However, it is important to add that although the Inheritance Tax guidance could be substantially improved, it will be challenging to produce simple guidance whilst the underlying rules remain complex. An example of this is the residence NRB. It will be difficult to produce a case study simply explaining who is able to benefit from this relief. The rules are so complex that a 'simple example' would need to be narrow and caveated.
- 1.80 It is also important to remember that guidance needs to cater for the full range of estates from the very simple to the highly complex and that detailed guidance is still required for practitioners.

Recommendation 3

HMRC should carry out a general review of its Inheritance Tax guidance with the aim of it being:

- targeted to reduce concern for those who worry unnecessarily
- clear, consistent and easy to navigate
- linked or located with other relevant guidance, including probate
- expanded to include worked examples, a road map, timescales and a tax calculator
- sufficient for complex estates to apply the law and practice correctly

In line with some other taxes, HMRC should also consider increasing the use of other education channels such as webinars.

Communication with HMRC

- 1.81 Completing the administration process can be a challenging period for individual executors due to the complexity of the process, only made worse by the recent death of a relative or friend. Good communication from HMRC at this time is key to reducing uncertainty and apprehension for executors.

Chart 1.F: Points of communication between HMRC and executors



Source: OTS

Observations

Communication by HMRC could be improved

- 1.82 The OTS has heard feedback that weeks or months might pass following submission of forms or correspondence without any response from HMRC. This can be distressing, particularly for individual executors who may not have been involved in such a process before and who will wish to distribute the estate to the beneficiaries as soon as possible.

Quote from a member of the public

"As a family, we had to postpone taking some decisions about assets due to the delay in a determination from HMRC. "

- 1.83 The HMRC Inheritance Tax helpline is a useful tool for executors completing the administration process. However, historically almost 30% of calls have been chasing progress. In 2017, HMRC received around 140,000 calls to its Inheritance Tax helpline, and of these nearly 40,000 (or 29%) were progress chasing.⁹
- 1.84 This picture is supported by responses to the OTS survey, where 61% of respondents who had not used an adviser said that they did not know how long it would take HMRC to respond once they had submitted their form.
- 1.85 Once a response has been received from HMRC, the OTS has heard that written communications can be of varying quality.

⁹ Source: HMRC management information that is published here for the first time.

- 1.86 Improved communication would reduce the number of calls to the helpline, freeing up HMRC resources, and the time spent on the Inheritance Tax process by executors overall.

HMRC have introduced a 12 week response period during which they will make any initial enquiries

- 1.87 There is currently no statutory enquiry window for Inheritance Tax. This means that there is no fixed deadline in the tax legislation for HMRC to make enquiries into an Inheritance Tax form.
- 1.88 However, as part of the ongoing drive to improve the experience of the taxpayer, HMRC introduced a new response period in April 2018.¹⁰ This involves HMRC writing to executors within 12 weeks following the submission of an IHT400 to confirm whether they wish to make any enquiries into the information contained on the form. If no correspondence has been received from HMRC in the 12 week period, the executors can assume no enquiries will be made, unless new information comes to light. Executors are then able to apply for a statutory clearance from HMRC which confirms that HMRC are satisfied that any tax due has or will be paid. Many choose to do this in order to obtain certainty, particularly because executors are personally liable for any unpaid Inheritance Tax.
- 1.89 Although the new review period is not a fixed statutory window, the OTS has heard that it could be more appropriate than a fixed enquiry window because it allows executors to amend their Inheritance Tax forms without falling into the interest and penalty regime. This is particularly appropriate for Inheritance Tax because amendments can be made to forms many months after they have been submitted due to new information about the deceased's affairs coming to light.
- 1.90 Professional advisers have welcomed the change, but some have cautioned that the review window could be removed at any time because it does not have a statutory basis.

Quote from The Society of Trust and Estate Practitioners

"Until a few weeks ago, we would have been asking for more commitments from HMRC on turnaround times. We are, however, most encouraged by the contents of the special Trusts and Estates Newsletter published in April this year and look forward to this being carried forward into practice."

Receipts are not issued for the payment of Inheritance Tax

- 1.91 The OTS has heard that receiving a receipt for the payment of Inheritance Tax would provide reassurance to executors who are often anxious that they are carrying out their duties correctly.
- 1.92 The OTS understands that HMRC previously issued receipts and that they continue to do so if a receipt is requested. The process for issuing receipts is

¹⁰ <https://www.gov.uk/government/publications/hm-revenue-and-customs-trusts-and-estates-newsletters/hmrc-trusts-and-estates-newsletter-special-edition-april-2018>

manual and it would be prohibitively time consuming to issue a manual receipt to all taxpayers.

Conclusions

The 12 week review period is a welcome improvement

- 1.93 Following HMRC's customer journey analysis, major improvements have recently been made to the communications sent by HMRC, and more are being planned.
- 1.94 The improvements were introduced by HMRC in April 2018 and it would be sensible to wait some time before determining how well the 12 week review window has been received by individuals and professional advisers. If necessary, refinement should be undertaken in response to feedback, after which consideration could usefully be given to putting it on a statutory basis (while making allowance for amendments to forms).

Improved communication

- 1.95 The OTS believes that reinstating training in written communication would help to make sure that all written communication from HMRC is of a high standard.

Automated receipts

- 1.96 It remains the case that receipts are not automatically given for the payment of Inheritance Tax. The OTS understands that work is in progress on further automation.

Recommendation 4

HMRC should introduce a system issuing automated payment receipts and, if necessary, further refine the recently introduced 12 week response period, during which any enquiries into the information contained on the form will be made.

Payment deadlines and probate

Background

- 1.97 Following a death, if the deceased person owned assets which need to be distributed, there must be an administration process. Executors are appointed through the deceased's will to carry out a number of duties which result in the deceased's assets being passed on to their chosen beneficiaries. Where there is no will, there are other processes for appointing someone, usually the next of kin, to administer the estate. As seen in Chart 1.A (in the introduction to this chapter), the processes are very similar.
- 1.98 Executors are responsible for obtaining probate, which involves submitting the correct Inheritance Tax form and paying any Inheritance tax due. Once HMRC have received the forms and payment, the executors can apply for probate. After probate is granted the assets can be distributed to the beneficiaries of the estate.
- 1.99 The deadline for payment of Inheritance Tax is 6 months following the end of the month of death and interest is charged if it is not paid within 6

months. Executors must submit the correct Inheritance Tax forms within 12 months of the end of the month of death.

Observations

It would be simpler if the Inheritance Tax payment deadline and deadline for submitting the Inheritance Tax forms were the same

- 1.100 The OTS has received a great deal of correspondence on this aspect of the administration process and there is a general agreement that it is confusing to have two separate deadlines. In practice, much of the work required to complete the Inheritance Tax forms must be carried out within the first 6 months as it is also required to accurately calculate the amount of tax to be paid.

Quote from a member of the public

"In practical terms the deadline is simply viewed as 6 months. Having a tax payment deadline shorter than a reporting one is nonsensical."

- 1.101 HMRC have provided the OTS with data from a sample of around 800 estates where there was tax to pay from a 6 month period in 2017. This shows that on average an Inheritance Tax form was filed, and a payment of tax made, within 4 months of the death. However, it also showed that approximately 10% of payments made were after the 6 month deadline. The data provided does not show whether any of these estates went on to make amendments to their forms or make any further payments.

6 months is not long enough to calculate how much Inheritance Tax should be paid for all estates

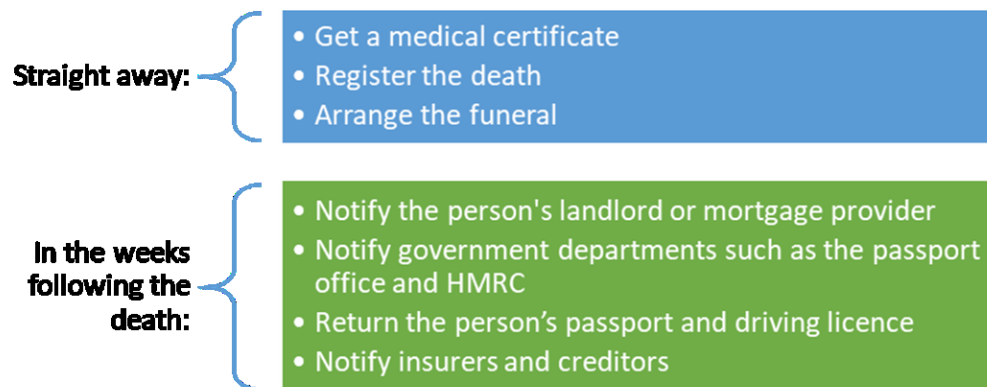
- 1.102 The requirement for Inheritance Tax to be paid 6 months after the month of death means a calculation has to be completed in this time. The data provided by HMRC shows that many estates are able to complete the forms and make payment within this time but approximately 10% do not meet the 6 month deadline.

- 1.103 The OTS has heard that 6 months is not long enough for some executors for two main reasons:

Reason 1: Carrying out administration tasks is not a top priority when a relative or close friend has died.

- 1.104 Executors are often a relation or close friend of the deceased person and will be grieving. There are other priorities when a relative or friend dies such as arranging the funeral, and the Inheritance Tax administration process does not begin straight away, which shortens the amount of time available before the payment deadline.

Chart 1.G: The Money Advice Service's list of things to do after a person has died



Source: Advice published on the Money Advice Service website¹¹

Quote from a member of the public

"The six-month time limit before interest is imposed takes no account of the multitude of tasks for a bereaved person, nor the potential psychological impact of being bereaved. In my opinion, twelve months would be more realistic and reasonable, allowing for more considered decisions at what can be an emotionally challenging time."

Reason 2: Gathering information is time consuming and difficult

- 1.105 Gathering information takes a long time and even if the process did start straight away, 6 months may not be long enough to find all the information required to calculate the amount of Inheritance Tax due. To complete the calculation, there are several steps to undertake: finding details of all the deceased's assets and liabilities; finding details of any gifts made by the deceased in the 7 years prior to death; and obtaining valuations.
- 1.106 For complex estates with a wide range of asset classes, the information gathering process can take much longer than 6 months. Therefore, executors must estimate the amount of tax due and will be subject to interest if they have underestimated the amount of tax due. Even for simple estates, if record keeping was inadequate, the process could take longer than 6 months.
- 1.107 It can be difficult for executors to obtain information from banks, building societies and investment houses as they each have different requirements for releasing information. The OTS has heard that dealing with these organisations can take a long time and can greatly increase the overall amount of time spent applying for probate. This topic is analysed further in the section entitled 'Non-Inheritance Tax matters' at paragraph 1.120.

¹¹ Source: <https://www.moneyadvice.service.org.uk/en/articles/what-to-do-when-someone-dies#notify-the-persons-landlord-and-other-organisations>

- 1.108 In some cases, banks or other institutions will not release information about the assets to executors until probate is obtained. For example, they may not release bank statements (which may be needed to determine whether lifetime gifts were made) until probate is obtained. For certain non-UK investment accounts and other assets the executors cannot obtain any information at all about the asset prior to obtaining probate. This means that executors provide estimates or make guesses about the assets in order to obtain probate, at which point they can receive detailed information. In some cases, this information will lead to an amendment to a form or a change in the amount of tax due.

Quote from Saffery Champness

"6 months is not long enough to deal with the issues arising in more complex estates"

"either tax is paid late, or an incorrect amount is paid, with the need to make later adjustments"

- 1.109 The top two aspects of the process identified as taking the longest were 'obtaining probate' and 'understanding and completing the forms' by respondents to the OTS's survey.

The need to pay Inheritance Tax before probate can be obtained can create a funding gap for executors

- 1.110 Executors need to pay Inheritance Tax before they can obtain a grant of probate. As they are generally unable to access or distribute assets without the grant of probate, they must find available funds elsewhere to pay any tax due.
- 1.111 Some, but not all, banks will release funds from the deceased's bank account to pay Inheritance Tax without a grant of probate. This is only helpful for cases where the deceased had sufficient cash in the bank and where the deceased happened to choose a bank which allows the release of funds in this way.
- 1.112 Similarly, some investment accounts, but not all allow executors to sell stocks and shares to pay Inheritance Tax without the grant of probate. Furthermore, if this is the only way executors can fund the payment of Inheritance Tax, they are forced to sell the investments without allowing them or the beneficiaries to choose the best time to sell given stock market movements and trends.
- 1.113 The OTS has heard that loans are available to executors to fund Inheritance Tax but that these are difficult to obtain and often have very high interest rates.

Quote from Gillespie Macandrew

“it can be difficult to find a bank willing to lend and, even where this is possible, it can be difficult to arrange the borrowing and agree terms within the 6-month payment deadline. Also, in our experience, the arrangement fees for such borrowings are usually high and the interest rates are usually higher than on conventional loans.”

- 1.114 HMRC have a facility for executors to apply for a grant on credit in circumstances where they are unable to pay Inheritance Tax before the grant of probate, but this is only available in a narrow set of circumstances.

Quote from The Society of Trust and Estate Practitioners

“The facility for obtaining a grant of credit is helpful, but is not widely known about, even within the professions that deal with probate and estate administration.”

- 1.115 This problem is well understood and there are multiple potential solutions. However, there is no one solution for all executors as it depends on the individual circumstances of the deceased and the requirements of the banks or intermediaries involved.

Conclusions

A 12 month payment deadline would be a simplification, but this would not address many of the difficulties faced by executors

- 1.116 A payment deadline of 12 months following the death would allow executors more time to gather information and would align payment options with the deadline for submitting the Inheritance Tax forms.
- 1.117 A payment deadline which is aligned with the deadline for submitting Inheritance Tax forms would be a simplification for executors and might lead to fewer amendments to Inheritance Tax forms. However, it would not necessarily address some of the underlying problems faced by those administering an estate, for example the difficulties that may be faced by executors in obtaining information about the estate or funding the Inheritance Tax prior to obtaining probate.
- 1.118 In addition, extending the payment deadline to 12 months following the death would be a costly measure for the government as there would be a delay in the receipt of Inheritance Tax when the measure is first introduced, which would lead to a gap in tax revenues for that period.

Streamlining the payment and probate process

- 1.119 As an alternative, the OTS proposes the following options to help improve the experience of executors:

- allow executors to obtain probate without submitting Inheritance Tax forms, or on submission of a very simple form, for estates of a low value or estates where no Inheritance Tax is due
- consider whether executors could be given a formal certificate confirming their status in situations where it is not possible for executors or their agents to obtain information about the deceased's assets without a formal document. This is not an Inheritance Tax matter and should be considered further by HM Courts & Tribunals Service (HMCTS)

Recommendation 5

HMRC should liaise with HM Courts and Tribunals Service on options for streamlining the payment and probate process.

Non-Inheritance Tax matters

Background

- 1.120 The OTS Inheritance Tax review has highlighted a few non-Inheritance Tax matters that have a big impact on the administration of Inheritance Tax. They can make the process more complex and increase people's anxiety about Inheritance Tax.
- 1.121 Although not directly linked to Inheritance Tax, the impact of these matters on the process is significant and therefore the OTS has included relevant observations and conclusions below.

Observations

An Executor may need to engage with other areas of the tax system

- 1.122 This report focuses on the Inheritance Tax aspects of administering an estate. However, an executor may also have to engage with other areas of the tax system, for example Income Tax or Capital Gains Tax. An example may be where the deceased was self-employed and submits Self Assessment returns. In this case it is the responsibility of the executor to ensure that the correct amount of Income Tax has been paid for the tax year up to the date of death. HMRC will tell the executor if they need to complete a tax return for this period.
- 1.123 Additionally, the executor may need to complete an Income Tax or Capital Gains Tax return for the period the estate is in administration, where there is any tax due.
- 1.124 It is helpful that unless the following conditions apply, the executor can informally contact HMRC to let them know there is tax due, rather than completing a full Self Assessment return:
- the total Income Tax and Capital Gains Tax due for the administration period was more than £10,000
 - the estate was worth more than £2.5 million at the date of death
 - the date of death was before 6 April 2016 and more than £250,000 a year came from the sale of the estate's assets by administrators or executors

- the date of death was on or after 6 April 2016 and more than £500,000 a year came from the sale of the estate's assets by administrators or executors

1.125 However, if any of these conditions are met then a full Self Assessment return will need to be submitted to HMRC.

1.126 The OTS has heard that it is difficult for executors to find information on paying other taxes that are due, especially for the period the estate is in administration. This is a separate process to the one for Inheritance Tax. There is little information available on GOV.UK about whether any reliefs or allowances are available for this period, and only limited guidance on how to notify HMRC and pay what is due. The guidance for this area of estate administration is brief, and is separate from the Inheritance Tax guidance on GOV.UK, sitting instead with the guidance on Self Assessment returns without being cross-referenced.

Not all banks and investment houses have the same requirements

1.127 Executors will need to engage with any bank, building society or investment house which held assets for the deceased. Executors will need to make contact for the following reasons:

- 1 to inform them of the death
- 2 to find out what cash/assets are held
- 3 to arrange for the cash/assets to be transferred or sold to either to pay Inheritance Tax or to distribute the estate to the beneficiaries

1.128 Each bank, building society or investment house will have their own requirements to allow access to information about the accounts held with them. They will also have their own requirements to allow assets or cash to be transferred out of their accounts.

Quote from Gillespie Macandrew

"the approach of brokers varies, and some will allow the stocks/shares to be sold before confirmation has been obtained but others will not."

1.129 There is no consistency across banks in these requirements. Some banks have a clear maximum amount they will distribute without probate and some do not. Where there is a maximum amount, there is no consistency in the level of the cap. This inconsistency causes uncertainty for executors including over whether probate is required. It can lead to lengthy communications between executors and banks, which adds to the feeling that the Inheritance Tax process is long winded and draining.

1.130 The OTS has heard that some banks have been known to release large balances to the next of kin even when they are not executors. This can be challenging for executors who are responsible for ensuring the estate is distributed to the correct beneficiaries.

1.131 Limits for distributing assets without probate:

Barclays - £50,000¹²

Santander - £50,000¹³

Nationwide - £30,000¹⁴

HSBC – all cases assessed individually¹⁵

NS&I - £5,000¹⁶

1.132 The OTS has also received submissions from executors who have struggled to get investment houses to liquidate a portfolio, and use the sale proceeds to pay Inheritance Tax direct to HMRC, prior to probate being obtained. The ability to sell shares and other liquid assets and use the proceeds to pay Inheritance Tax can be particularly important to prevent executors having to take out loans to pay Inheritance Tax. There is no single clear process here that is followed by all banks and investment houses.

Will drafting is inconsistent, and fees are not published

1.133 Individuals can draft a will themselves or use a will writing service. There are many different types of will writing service available.

1.134 At the cheaper end of the market there are off-the-shelf will packs, which can be purchased from the high street. The individual completes the pack themselves and does not use a solicitor. At the other end of the market a qualified and experienced legal adviser drafts the will.

1.135 Not all will writers are regulated or legally qualified and the OTS has heard that the standard of service provided is inconsistent. If an unregulated adviser or a will pack is used, it is unclear how to make a complaint or to challenge unsuitable will drafting.

¹² <https://www.barclays.co.uk/content/dam/documents/personal/miscellaneous/Bereavement-guide.pdf>

¹³ <https://www.santander.co.uk/csdlv1r/BlobServer?blobtable=MungoBlobs&blobkey=id&blobcol=urldata&blobheader=application%2Fpdf&blobheadervalue1=inline%3Bfilename%3DBereavement+guide+do-ec-108.pdf&blobwhere=1314025300573&blobheadername1=Content-Disposition>

¹⁴ https://www.nationwide.co.uk/-/media/MainSite/documents/guides/dealing-with-the-unexpected/P3162_bereavement_support.PDF

¹⁵ https://financialplanning.hsbc.co.uk/pdf/45346_Bereavement_Support_Guide_BOOKLETPAGES.pdf

¹⁶ https://www.nsandi.com/files/published_files/asset/pdf/death-claims-brochure.pdf

Complaint published on the Legal Ombudsman's website

"Mr G, an elderly gentleman, approached a firm of will writers to draw up a will and paid them nearly £2,000 to do the work.

After a period of time Mr G had not received any indication that the will had been drafted so he contacted the firm to complain. However, the firm failed to answer his calls. It soon became clear that they had no intention of doing the work or returning his money.

Mr G discovered that the firm had closed down and contacted the Society of Will Writers for help. They suggested he bring his complaint to the Legal Ombudsman.

When we investigated we found that the firm fell outside our jurisdiction.

Will writing is not a reserved activity and so is not covered by the Legal Services Act 2007. A solicitor, who would be an authorised person under the Act, was a partner in the firm but because there was no evidence to show that he had been involved in Mr G's work (chiefly because no work had been done) we were unable to investigate the complaint."

Source: <http://www.legalombudsman.org.uk/publications/will-writing/case-studies.html#missE>

- 1.136 A well drafted will ensures that the deceased's estate passes to their intended beneficiaries. A poorly drafted will can lead to unintended consequences, including unexpected Inheritance Tax outcomes. The OTS has heard of cases where poor drafting has led to costly legal proceedings, assets passing to unintended beneficiaries or unintended Inheritance Tax consequences, for example Inheritance Tax being disproportionately borne by one of the beneficiaries of the will.
- 1.137 The fees charged by advisers to draft a will or administer an estate are variable and not always advertised. The OTS has heard that it can be very difficult for executors to compare prices or predict the cost of using an adviser, but notes that from December 2018 all regulated law firms will be required to publish information in this area.¹⁷

Conclusions

The guidance on other taxes should be considered alongside any review on Inheritance Tax guidance

- 1.138 The current guidance on paying any Income Tax or Capital Gains Tax that may be due for estates in administration should be clearer and easier to find for executors. This should be considered alongside the Inheritance Tax guidance when HMRC conducts an overall review of its guidance, as it can be an important part of an executor's role when administering an estate.

¹⁷ www.sra.org.uk/sra/news/press/better-information-june-2018.page

A standardised banking process would reduce the administration burden for executors

- 1.139 The OTS concludes that a standardised process and consistent guidelines for all banks, building societies and investment houses would improve the experience of those dealing with an estate. The OTS observes that this is an area where improvements can be made to a non-tax matter, which would simplify the administration process for Inheritance Tax. It would encourage the relevant trade bodies to collaborate and develop such a standardised process.

Making a will should be as straightforward as possible

- 1.140 The variety of service providers and varying standards of service make the process of making a will more complex than it should be. The OTS observes that regulating the will writing market and requiring all advisers to advertise their fees should improve the experience of those completing the administration process and help prevent unintended Inheritance Tax consequences.

Chapter 2

Administration of other Inheritance Tax charges

Introduction

2.1 Inheritance Tax is not only a tax on the estate following an individual's death, but is also charged on other occasions, some of which happen during an individual's lifetime. The occasions where an Inheritance Tax charge may occur, other than on an estate, are listed below:

- chargeable lifetime transfers, including failed potentially exempt transfers (failed PETs)
- ending of a qualifying interest in possession
- trust exit charges
- trust 10 year anniversary charges
- assets ceasing to be held on special trusts
- cessation of conditional exemption and disposal of trees or underwood
- chargeable event in respect of an alternatively secured pension fund on death of a relevant person

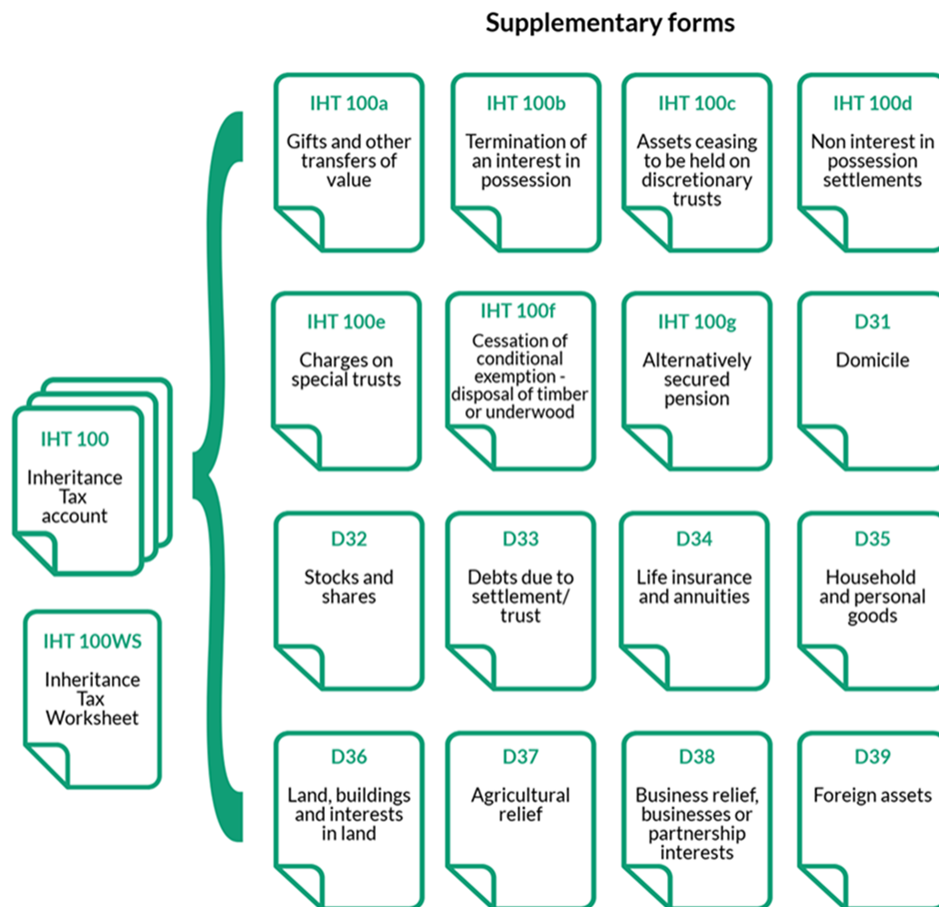
2.2 Annex C includes material providing a short explanation of the Inheritance Tax treatment of trusts and other chargeable events.

2.3 The OTS has heard from multiple respondents who have highlighted complexity in the administration of other charges, such as those for trusts. The OTS has found that some areas of administration could be simplified to improve the process for those engaging with it.

Forms

Background

Chart 2.A: Summary of IHT100 and supplementary forms



Source: OTS

- 2.4 The main form used to tell HMRC when Inheritance Tax is payable on a trust or other chargeable event¹ is the IHT100. This is an 8 page form, but there are also many supplementary forms which may need completing depending on the circumstance. These forms are shown in Chart 2.A. Additionally, there is a worksheet available, the IHT100WS, to help calculate the Inheritance Tax due.
- 2.5 The person who is responsible for completing the IHT100 varies depending on the reason for the form being submitted. This means that the form must cater for both the different circumstances and the differing roles of those completing it.
- 2.6 The IHT100 may also need to be submitted in some cases where there is no Inheritance Tax due.

¹ See annex C for a definition of a chargeable event

Observations

Complex form

- 2.7 The OTS has heard from many respondents to the call for evidence that the IHT100 is complex to complete, and tries to do too many things within one form. A common criticism is that the form is 'not fit for purpose'. The IHT100 caters for a multitude of circumstances, including when Inheritance Tax may be chargeable on trusts, and taxable lifetime events such as chargeable gifts from an individual to a company.

Quote from a member of the public

"The IHT100 tries to cover too many different scenarios, and as such it lacks clarity. Even with the guidance notes it's not at all friendly, particularly to a non-professional."

- 2.8 This means that, as well as the IHT100, there are a range of supplementary pages to cater for each occasion. These forms often cross-reference each other, meaning information must be manually inputted more than once on different forms.
- 2.9 The calculations that are necessary to compute the Inheritance Tax due for trust 10 yearly or exit charges are extremely complex. Respondents have noted that the worksheet provided by HMRC to help to calculate the Inheritance Tax charge is overly long and hard to follow. This is likely to be due in part to the complexity of the calculations. However, advisers often instead attach their own calculations to the forms when they send them to HMRC and have told the OTS that there are other resources available that are simpler and easier to follow.
- 2.10 The OTS has heard that the IHT100 is not up to date and has not been amended in some time, and so it has not incorporated legislative changes that have been made. This adds to the complexity of completing the form.

Quote from The Society of Trust and Estates Practitioners

"In general terms we would advise that, as we believe HMRC agree, Form IHT100 is not fit for purpose. It has not been updated to take into account the changes that were brought in, 12 years ago, by Finance Act 2006. It is overly complicated and adds to the problems in calculating what is already an overly complex tax..."

- 2.11 The IHT100 is not an online form, and whilst you can complete the form on your computer, it must then be printed out and posted to HMRC. Respondents have stated that it would be easier if they could complete and submit the forms online.

It is unclear how lifetime gifts which become chargeable to Inheritance Tax should be reported

- 2.12 When a gift becomes chargeable to Inheritance Tax because the person who gave the gift dies within 7 years of making the gift (a failed PET), it is unclear who is responsible for reporting the gift to HMRC.
- 2.13 Strictly the recipient of the gift should complete an IHT100 to provide details of the gift to HMRC within 12 months of the death. However, in most cases the gift is reported on the Inheritance Tax forms completed by executors of the deceased's estate and HMRC does not also require in practice that this is reported by the recipient of the gift.
- 2.14 It is confusing for taxpayers for there to be a formal obligation to submit an IHT100 form which is not enforced in practice.

Trustee signatures

- 2.15 When an IHT100 is completed and submitted to HMRC by trustees, the form must be signed by all the trustees. The OTS has heard that this can be difficult because a trust may have any number of trustees, and they may be situated in different countries. It is not necessarily the case that the trustees will be able to meet to complete and sign the form together. This can lead to delays where the forms must be sent to each of the trustees to gain their signature. This time must be factored in when completing the forms to ensure that they are submitted by the deadline.
- 2.16 There is an inconsistency here with other areas of the tax system. Where trustees must submit an Income Tax return, HMRC do not require the signature of all the trustees on the form.
- 2.17 Instead where there are 2 or more trustees, one of them is nominated as the 'principal acting trustee' and they complete the form on behalf of the other trustees. The other trustees are still accountable and liable for the tax if it is not paid.

Completing a form when no tax is payable

- 2.18 The IHT100 needs to be submitted to HMRC whenever there is an occasion where Inheritance Tax is due with respect to a trust or when there is another chargeable event. However, there are some circumstances when the form must be submitted by trustees, even though there is no tax due.
- 2.19 Trusts that do not necessarily need to complete a form on the 10 year anniversary and exit charges are known as excepted settlements.² Trusts cannot qualify as excepted settlements if the settlor was not UK domiciled, or any one of the trustees are not resident in the UK, or there were any other settlements made by the settlor on the same day.³ However, even if a trust is an excepted settlement, the trustee may need to submit a form if, broadly, the value within the trust is at least 80% of the NRB. For the trusts where this is the case, they will have to submit an IHT100, even though there is no Inheritance Tax payable. This is the case even if no reliefs or exemptions have

² See annex C for a definition of excepted settlements.

³ Known as related settlements

been claimed. Additionally, where the trust has professional trustees, or uses a professional to complete the forms, the trust will incur a charge for them to do so.

Conclusions

Reduce the administrative burden where no tax is due

- 2.20 HMRC should review the requirement for trustees to submit a form to HMRC where there is no Inheritance Tax due. The excepted settlement regulations⁴ should be reviewed to ensure that the IHT100 is only submitted where necessary. This would benefit both trustees and HMRC, as it will reduce the number of IHT100s that need to be processed by HMRC that result in no tax being collected.

Recommendation 6

HMRC should review the requirement for trustees to submit forms when no Inheritance Tax is due, and no reliefs or exemptions are claimed.

Inheritance Tax online – a fully integrated digital system

- 2.21 Although the IHT100 is used in different circumstances to the other Inheritance Tax forms, the problems are similar to those outlined for the short and the long form for estates that were discussed in Chapter 1. The recommendation made for these forms, that the government should implement a fully integrated digital system for Inheritance Tax, would also solve the problems that arise with the IHT100. An online system that caters for whoever is using it, and asks only those questions relevant to their circumstances should apply for all areas of Inheritance Tax, including trusts, failed PETs and chargeable lifetime transfers.
- 2.22 The digital system would calculate the Inheritance Tax after inputting the information needed. This would remove the need for the taxpayer to do complex calculations, and reduce errors.

Key Recommendation

The government should implement a fully integrated digital system for Inheritance Tax, ideally including the ability to complete and submit a probate application.

An alternative approach: improve the taxpayers experience by simplifying the existing forms

- 2.23 If an online system including these areas cannot be delivered, then HMRC should consider improving the experience for taxpayers by:
- splitting the IHT100 up so there is a simple, tailored and up to date form for each of the different chargeable occasions
 - improving the guidance available for completing the forms and calculating the tax due, including considering an online calculator
 - mirroring the rules for Income Tax returns that allow the forms to be signed by only the 'principal acting trustee'

⁴ <http://www.legislation.gov.uk/ukxi/2008/606/contents/made>

Recommendation 7

Until a digital system can be implemented, HMRC should make changes to the existing form for lifetime charges and trusts. These include: splitting up the current form so there is a simple and tailored form for each occasion; improving the guidance available for completing the form and calculating the tax; and aligning the signature requirements for trustees with other parts of the tax system.

Communication

Background

- 2.24 The deadline for submitting an IHT100 is different depending on what the form is being used to report, which can cause confusion for taxpayers. For trustees using an IHT100 to report Inheritance Tax charges resulting from a trust 'event', the deadline is 6 months from the end of the month in which the 'event' happened. If an IHT100 is used to report a non-trust related event, the deadline for submitting the form is 12 months from the end of the month in which the 'event' happened. The deadline for payment of Inheritance Tax is 6 months from the end of the month in which the event occurred for all types of events.
- 2.25 Once an IHT100 has been submitted, there is no published timescale for a response from HMRC.

Observations

Receipts and communication

- 2.26 Respondents have told the OTS that it is confusing to have multiple deadlines for submission of the IHT100.
- 2.27 The OTS has heard feedback that HMRC take a long time to respond to an IHT100 form and sometimes they do not respond at all. HMRC do not acknowledge receipt of the form or receipt of any payment of Inheritance Tax made with the form. Taxpayers need to contact HMRC to check that the form and payment have been received.
- 2.28 If HMRC acknowledged receipt of the form and payment, this should reduce the number of calls received by the helpline to check the progress of an IHT100 form.

Review period

- 2.29 HMRC have recently implemented some changes to how the long form for estates (IHT400) is dealt with, which is outlined further in Chapter 1. The main change was the introduction of a 12 week review period. A letter is sent to executors to acknowledge receipt of the long form (IHT400) and to explain that if HMRC want to make further enquires, they will make their initial contact within 12 weeks. If no further communication is received in this period, the executors can assume no further enquires will be made.
- 2.30 No comparable review period exists for the IHT100, which causes uncertainty for taxpayers.

Conclusions

Automated receipts and acknowledgements

- 2.31 The OTS recommends that HMRC introduces automated receipts for IHT100 forms and for payment of Inheritance Tax alongside the form. This mirrors the OTS recommendation in Chapter 1 to introduce receipts for payment of Inheritance Tax paid on estates.

Review period

- 2.32 HMRC should consider introducing a review period for IHT100 forms. Although comparable to the one they have introduced for the long form (IHT400), it may not be appropriate for the length of the period to be the same.
- 2.33 A review period will give taxpayers certainty, and help to reduce the amount of contact received by HMRC to chase progress.

Recommendation 8

HMRC should introduce a system issuing automated receipts for IHT100 forms and Inheritance Tax payments made alongside the form, and consider introducing a review period during which an enquiry into the information contained on the IHT100 form will be initiated.

Chapter 3

Areas of complexity

Introduction

- 3.1 This chapter sets out some of the key areas of complexity within the Inheritance Tax rules, with a brief explanation about how they work. It also expands on the views that have been heard by the OTS during its consultation, as set out in the Foreword.
- 3.2 However, the chapter does not go into detail, and no recommendations are made on these areas in this report. The views and comments the OTS has received will be considered further and any recommendations will be made in the second report.
- 3.3 The areas covered in this chapter are:
- the nil rate band (NRB) and residence nil rate band
 - lifetime gifts
 - businesses and farms
 - big picture reform
 - other areas of complexity

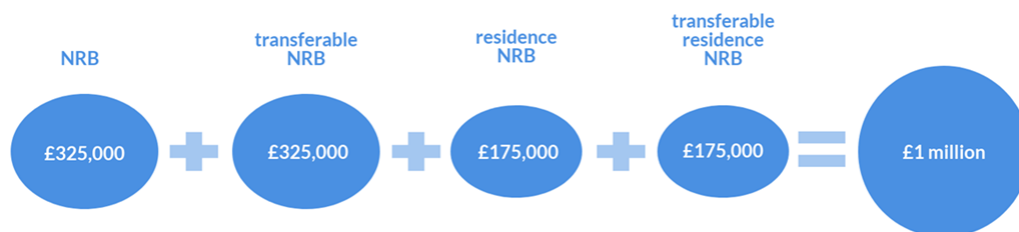
Nil rate band and residence nil rate band

- 3.4 Inheritance Tax is generally charged at 40% on the value of an estate on death that exceeds an individual's nil rate bands. The nil rate bands can be made up of several different aspects, as outlined below.
- 3.5 The nil rate band (NRB) is available to all estates and is currently set at £325,000. Any estate below this value will not have to pay Inheritance Tax. The value of an estate includes gifts given in the 7 years before death.
- 3.6 If an individual was married or in a civil partnership, they may also be entitled to a transferable NRB. This arises if the NRB is not fully used when the first spouse or civil partner dies, so that the unused percentage can be transferred and used on the death of the second.
- 3.7 Where none of the NRB is used on the first death, perhaps because the whole estate passed to the spouse, this increases the threshold available on the second death up to £650,000, which is the combined total of the two individuals' NRBs.
- 3.8 From April 2017, there is a further amount available in some circumstances called the residence nil rate band (residence NRB). Broadly, this is available

where an estate includes the individual's home, which is being passed on to their children or grandchildren. The residence NRB is tapered, so that the amount available is reduced by £1 for every £2 an estate is over £2 million.

- 3.9 The residence NRB is being phased in until April 2020 when it will be worth up to £175,000, and is also transferable between spouses and civil partners (known as a transferable residence NRB).
- 3.10 This means that in tax year 2020 to 2021 the amount available before Inheritance Tax may be payable on an estate could be as high as £1 million (if the whole of a previous spouse or civil partner's threshold is transferred). This is shown in Chart 3.A and is made up of the NRB of £325,000, transferable NRB of £325,000, residence NRB of £175,000 and the transferable residence NRB of £175,000.

Chart 3.A: The nil rate bands



Source: OTS

Comments made

- 3.11 The OTS has received substantial comment on the various nil rate bands, and while it seems that the NRB is simple and generally well understood, the residence NRB has, in particular, attracted a lot of comment.
- 3.12 In correspondence received by the OTS, Inheritance Tax has also been criticised for disadvantaging those who are not married or in a civil partnership, as they cannot benefit from the transferable NRB or the transferable residence NRB. Any change to this would of course have an Exchequer cost.

Transferable NRB

- 3.13 The amount of the NRB that is available to be transferred depends on the proportion that is unused at the time of the first spouse or civil partner's death.

Example

Alex is working out the amount of transferable NRB that will be available for his mother's estate. His parents were married and his father (Robert) died in June 2002, leaving most of his estate to his wife (Joan) and £50,000 to Alex himself.

At the time of Robert's death, the NRB was £250,000. Transfers between spouses are exempt, so Robert used only £50,000 of his £250,000 NRB, or one-fifth.

The proportion of the transferable NRB available for Joan's estate is four-fifths, and this applies to the value of the NRB at the time of Joan's death. This is £325,000, meaning that the transferable NRB available is £260,000.

- 3.14 The transferable NRB was introduced in 2007. Previously, trusts were often used to preserve the first spouse's NRB, but the transferable NRB removed the need for such tax planning.
- 3.15 While some responses have suggested it is difficult to administer an estate in situations like the above example, where only part of the NRB is available to be transferred from the first spouse or civil partner, it is widely seen as a simplification.

Residence NRB

- 3.16 The residence NRB (which is aimed at helping people to pass on the family home) has been widely criticised as being very complex and disadvantaging those who do not have children, as well as those who have not owned their own home. This means that estates of the same size can have differences in their Inheritance Tax liability depending on their family relationships and the assets held.
- 3.17 The downsizing rules protect the residence NRB available where an individual has downsized their home, and have been highlighted to the OTS as an area of particular complexity, including when making a will.
- 3.18 Many respondents have suggested that the residence NRB should be removed, and instead the NRB should be increased, perhaps by the same amount. However, this would be very costly unless other changes were made because, unlike the residence NRB, the NRB is available to everyone. Others have suggested that the residence NRB is so complex it would be better simply to remove it.

Lifetime gifts

- 3.19 When an individual gives a gift to someone, there is no Inheritance Tax payable at the time by either the individual giving the gift or the recipient of the gift. Often, there will never be any Inheritance Tax due on the value of the gift. Lifetime gifts can be a simple way for individuals to reduce the amount of Inheritance Tax payable on their assets.
- 3.20 A gift from one individual to another is called a potentially exempt transfer (PET).¹ If the person giving the gift lives for more than 7 years, the gift is exempt and no tax will be payable, subject to certain anti-avoidance rules.

¹ PETs do not include gifts which are not fully given away. Where a person giving the gift enjoys some benefit from the gifted property in the 7 years to death, the gift is treated as if it is still owned on death. For example, if an individual gives away their house but continues to live in the house at less than a market rent, the house is treated as if it is still in their estate on death.

- 3.21 However, if the individual giving the gift dies within 7 years, then it becomes a failed PET, as it is no longer exempt. If the value of failed PETs exceeds the NRB, then Inheritance Tax will be payable.
- 3.22 The rate of tax on failed PETs is reduced on a sliding scale for gifts made between 3 and 7 years before the death of the individual giving the gift. This is known as taper relief.
- 3.23 Additionally, there are several exemptions available for lifetime gifts. These are summarised in Chart 3.B.

Chart 3.B: Summary of exemptions available for lifetime gifts



Source: OTS

Comments made

- 3.24 A common criticism of Inheritance Tax is that wealthy individuals (who are likely to be well advised) can give away many of their assets before they die and pay less Inheritance Tax than others, who need a greater proportion of their assets to support their living costs.

Reliefs and Exemptions

- 3.25 There are many exemptions and reliefs relating to lifetime gifts and the OTS has heard that they are not always well known or understood. The OTS has also received many comments criticising the fact that the limits for the annual exemption, the small gift exemption and the exemption for gifts on marriage have not increased since Inheritance Tax was introduced. Increases to these, would of course have an Exchequer cost.

Records

- 3.26 The administrative challenge of either maintaining records or reconstructing records after death is problematic. A key area of concern is that executors find it difficult to find or reconstruct records of lifetime gifts given for a 7 year period, and are uncertain of the level of evidence they need to supply to HMRC, especially when claiming exemptions. This is particularly difficult where executors are people who do not necessarily benefit at all from the estate but who are personally liable for IHT if they distribute the estate in good faith, but a failed PET later comes to light.

Taper relief and failed PETs

- 3.27 The OTS has heard from advisers that the tapered rate of Inheritance Tax on failed PETs is difficult to explain to clients and is poorly understood, with many individuals expecting all failed PETs to be subject to taper relief. A common area of confusion is that it is not the value of the gift that is tapered, but the rate of tax. In addition, many individuals do not know how the NRB is allocated or understand the inequalities this can cause for recipients. This complexity is illustrated in the example below.

Example

Sarah gives £325,000 to her son James in 2013. In the following year she gives the same amount to her daughter Claire. Sarah dies in 2018. Sarah has made no other gifts.

Both gifts are within 7 years of Sarah's death and are therefore failed PETs and may be subject to Inheritance Tax.

The NRB of £325,000 is offset against the gift to James as this is the first gift Sarah made. There is no Inheritance Tax for James to pay on the gift he received.

The NRB has been used up on the gift to James and so Claire is liable for Inheritance Tax on the full value of the gift to her.

The gift was made in 2014, 4 years prior to Sarah's death so the taper relief applies, and the applicable rate of Inheritance Tax is reduced to 32%. Claire must pay £104,000 of Inheritance Tax and is left with an after tax gift of £221,000.

- 3.28 Another issue concerning the taxation of gifts in the 7 year period before death is who pays any tax due. In the example above, Claire is liable to pay the Inheritance Tax due on the gift from her mother. However, if she did not pay, HMRC could then reclaim the tax due from the executors. The OTS has heard that this can cause problems, as this reduces the value of the estate available to be distributed to other beneficiaries and in addition means executors are nervous about distributing the estate until they have absolute finality on the lifetime gifts.

Chargeable lifetime transfers

- 3.29 The OTS has heard that there is confusion about the interaction of failed PETs and chargeable lifetime transfers. Chargeable lifetime transfers are gifts made in an individual's lifetime that have an immediate charge to Inheritance Tax. They include gifts to trusts or companies that add up to more than the value of the NRB (currently £325,000) in any 7 year period.² Many people, having heard of the '7 year rule', assume that only gifts in the 7 years before death will be relevant when considering an estate with lifetime gifts. However, this is not necessarily the case, as where there have been chargeable lifetime transfers within 7 years of a failed PET these must be taken into account, which can increase the period to be considered to 14 years.

Businesses and farms

- 3.30 Businesses and farms benefit from relief from Inheritance Tax if certain conditions are met. The reliefs are known as business property relief (BPR) and agricultural property relief (APR).

Business Property Relief (BPR)

- 3.31 Where an estate includes a business that qualifies for relief, then BPR reduces the amount of the value of the business chargeable to Inheritance Tax, either by 50% or 100%.
- 3.32 The property qualifying for relief is:
- property consisting of a business, or an interest in a business (100% relief)
 - unquoted shares in a company (including AIM shares) (100% relief)
 - quoted shares or securities where the owner had a controlling holding (50% relief)
 - land or machinery owned personally and used in the trade of a company controlled by the owner, or a partnership in which that person was a partner (50% relief)
- 3.33 The property must have been held by the deceased for two years up to the date of death.
- 3.34 An important condition for relief is that the business must not consist wholly or mainly of holding investments. While wholly or mainly is not defined in the legislation, it is thought of as a greater than 50% test. Where mixed activities are carried on, it is possible for the whole business to qualify for BPR where the investment activity is not the main part.

Agricultural Property Relief (APR)

- 3.35 APR is available for the following types of property:
- agricultural land or pasture

² Chapter 5 of the government consultation on the taxation of trusts published on 7 November 2018
<https://www.gov.uk/government/consultations/the-of-taxation-of-trusts-a-review>

- woodland or buildings for the intensive rearing of livestock or fish, where occupied with and ancillary to the agricultural land or pasture
 - cottages, farm buildings and farmhouses which together with the land, are of a 'character appropriate' to the property
- 3.36 The agricultural property must be in the UK, Channel Islands, Isle of Man or an EEA state. This contrasts with BPR, which has no such restriction. To qualify, property must generally have been held and used for agricultural purposes for 2 years up to the date of death where the property is occupied by the owner, or 7 years where it is occupied by someone else.
- 3.37 The relief is 100% of the agricultural value if the owner farmed it themselves, or it was let on a tenancy that began on or after 1 September 1995. The relief is 50% in other cases. The agricultural value is the value if the property could only be used for agricultural purposes, and has relevance when valuing the farmhouse or development land, which may have a market value above this.
- 3.38 Where a property qualifies for both APR and BPR, APR must be claimed in priority. However, you may claim BPR on any agricultural property that does not qualify for APR, if it meets the conditions.

Comments made

- 3.39 There has been a variety of comments on these two reliefs. The OTS has heard from some who have raised quite broad questions about the reliefs, recognising that they treat certain types of business assets more favourably than other assets and may influence when and how businesses are passed down generations.
- 3.40 However, as regards simplicity, the OTS has heard that these reliefs work in a broadly straightforward way. The areas that respondents raised where there could be simplification, or where clarification of treatment is needed, are summarised below. Some of these areas have been highlighted previously by the OTS in the business lifecycle report published in April 2018 on simplifying the taxation of key events in the life of a business.³

Furnished Holiday Lettings

- 3.41 The OTS has heard that the Inheritance Tax treatment of furnished holiday lettings causes confusion and is inconsistent with other taxes. In general, furnished holiday lettings are an investment business for BPR purposes, and so are not eligible for relief. For Income Tax and Capital Gains Tax they are treated as a trade. Any changes in these areas could of course involve an Exchequer cost.

Joint Ventures and Limited Liability Partnerships

- 3.42 Another area that has been criticised in the responses to the call for evidence is the lack of clarity about the treatment of certain business structures, particularly those that include joint ventures and limited liability partnerships (LLPs). Respondents were concerned that Inheritance Tax does not reflect

³ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/699972/OTS_Business_Lifecycle_report_final.pdf

common business practices in these areas. Changes here could of course involve an Exchequer cost.

Wholly or mainly test

- 3.43 The OTS has heard that the wholly or mainly test can be challenging to apply. It is difficult to determine what percentage of a business will be treated as 'holding an investment'. For estates, the test is applied on death at a single point in time and this creates uncertainty for business owners as they cannot predict the timing of the test or the relative value of the investment part of the business in the future.

Other comments made

- 3.44 Some respondents have suggested that there should be better alignment between the criteria for BPR and for Capital Gains Tax reliefs. However, others have suggested that there is a clear understanding of the different reliefs, and that they have different criteria because they apply in different circumstances.
- 3.45 Respondents have also suggested that:
- the need to claim APR before BPR results in an extra administrative burden
 - there is a lack of clarity in the APR treatment when farmers partially retire, or are unwell
 - the different rates of relief add to the complexity
 - the practical burden of obtaining valuations is too great in situations where it is clear that BPR applies
 - the length of time it may take to obtain confirmation from HMRC that BPR is applicable on death is too long

Big picture

- 3.46 The Inheritance Tax system is widely recognised as being complex and difficult to navigate. The current rules have evolved over time, and are a combination of Capital Transfer Tax and Estate Duty, with additional anti-avoidance provisions added on more recently. It is unclear what the original policy objectives were for some of the reliefs, or for the system as a whole. This view is set out clearly in the Mirrlees review⁴ and has been echoed by the stakeholders engaging with this Inheritance Tax review.

Comments made

- 3.47 There have been a range of comments and suggestions about how to reform Inheritance Tax. Some of this material explored issues and ideas reaching wider than the simplification remit of the OTS.
- 3.48 There have been a number of suggestions from a range of stakeholders in response to the OTS's call for evidence, that the Inheritance Tax system should be overhauled in favour of a simpler and more user-friendly system.

⁴ <https://www.ifs.org.uk/uploads/mirrleesreview/design/ch15.pdf>

- 3.49 Some have suggested that Inheritance Tax should be replaced by another system, the most common being a gift tax. This is echoed in reports by other bodies such as the Resolution Foundation⁵ and the Institute of Public Policy Research,⁶ and to some extent in the Mirrlees review.
- 3.50 The OTS asked in its call for evidence whether some exemptions should be removed to reduce the rate or increase the NRB. There were a variety of responses, including some respondents suggesting a lower or graduated rate of tax, others suggesting that an increase in the NRB would be preferable and others stating that the reliefs play an important role and should not be removed.
- 3.51 Suggestions have also been made about the interaction of the reliefs with the wider tax framework, and the potential distortions that may arise in relation to taxpayers' decisions about and the timing of transactions. One example is in relation to the effect of the Capital Gains Tax uplift on death, especially in situations where BPR or APR apply.
- 3.52 Whether to make any changes in these areas is a matter for government. However, in its second report the OTS will consider these issues in more detail.

Other areas of complexity

- 3.53 There are other areas of the Inheritance Tax system that are complex, and the OTS will consider these further. These include the areas listed below:
- the practical operation of the reduced rate of Inheritance Tax which is available when a certain proportion of an estate is left to charity
 - the administration of life insurance products and pensions and the types of products available
 - technical aspects relating to trusts for example exit charges and the 10 yearly charges
 - the rules around reservation of benefit
- 3.54 While some of these areas will only be relevant to a small number of people, others, such as pensions, will be relevant to a larger number. There are both administrative and legislative complexities in these areas.

Comments made

- 3.55 The OTS has received representations which have highlighted several areas of complexity or uncertainty in these areas.
- 3.56 These include the practical operation of the reduced rate of Inheritance Tax which is available when 10% or more of an estate is left to charity.
- 3.57 The OTS has heard it is not straightforward to navigate these rules in ensuring that the estate is eligible when writing a will or to work out

⁵ <https://www.resolutionfoundation.org/publications/passing-on-options-for-reforming-inheritance-taxation/>

⁶ <https://www.ippr.org/research/publications/prosperity-and-justice-executive-summary>

whether the reduction can be claimed when administering an estate. The second report will look into the practical aspects of how to claim the relief.

- 3.58 The OTS has also heard that there are complexities in relation to the Inheritance Tax treatment and the administration of trusts, including pensions and insurance products held in trust. The changes to the taxation of trusts in 2006 have been criticised by some respondents as increasing complexity.
- 3.59 Some respondents have stated that the rules on giving a gift but retaining a benefit from the assets given away (the reservation of benefit rules), and the related pre-owned assets charge to income tax (POAT), are not well understood and known about by the public, while others have questioned whether POAT is still necessary. The POAT charge is an Inheritance Tax anti-avoidance provision.

Annex A

Scoping document

IHT General Simplification Review

Inheritance Tax (IHT) in its current form was introduced in 1986, replacing Capital Transfer Tax.

Since then, it has been subject to a continuous process of evolution and change. In addition, the economic and social landscape has changed. While fewer than 5% of estates are liable to IHT, there has been an increase in the number of people that think they may be within the scope of the tax. This is partly driven by increases in residential property prices, especially in London and the South East of England.

The Chancellor and the Financial Secretary to the Treasury have requested that the Office of Tax Simplification (OTS) carry out a review of a range of aspects of IHT and how it functions today, including its economic incidence, to identify simplification opportunities. The review will be consistent with the OTS's remit to provide advice on simplifying the tax system, with the Chancellor responsible for final decisions on tax policy.

The overall aim of the review will be to identify opportunities and develop recommendations for simplifying IHT from both a tax technical and an administrative standpoint. The OTS will work alongside HMRC's project on administrative changes for the clear majority of estates where there is no tax to pay.

The OTS will publish a report in the autumn of 2018 that:

- Provides an initial evaluation of aspects of the current IHT regime, and what they mean for taxpayers, HMRC and the Exchequer;
- Identifies opportunities for simplification of IHT supported by analysis and evidence; and
- Offers specific simplification recommendations for government to consider.

The OTS will provide a call for evidence early in 2018.

Scope of Review

The review will consider how key aspects of the current IHT system work and whether and how they might be simplified. This will include a combination of administrative and technical questions such as:

- The process around submitting IHT returns and paying any tax, including cases where it is clear from the outset that there will be no tax to pay;

- The various gifts rules including the annual threshold for gifts, small gifts and normal expenditure out of income as well as their interaction with each other and the wider IHT framework;
- Other administrative and practical issues around routine estate planning, compliance and disclosure, including relevant aspects of probate procedure, in particular in relation to situations which commonly arise;
- Complexities arising from the reliefs and their interaction with the wider tax framework;
- The scale and impact of any distortions to taxpayers' decisions, investments, asset prices or the timing of transactions because of the IHT rules, relevant aspects of the taxation of trusts, or interactions with other taxes such as Capital Gains Tax; and
- The perception of the complexity of the IHT rules amongst taxpayers, practitioners and industry bodies.

Further guidance for this review

In carrying out its review and developing its recommendations, the OTS should:

- Research widely among all stakeholders;
- Engage with HMRC's Administrative Burdens Advisory Board;
- Consider whether devolution of tax powers within the UK has implications and especially
- whether the Scottish legal system impacts any recommendations;
- Take account of relevant international experience;
- Consider the likely Exchequer implications of recommendations; and
- Be consistent with the principles for a good tax system, including fairness and efficiency.

A Consultative Committee will provide support and challenge.

Annex B

Consultative Committee

We are very grateful for the time and support of our Consultative Committee members.

Individual	Organisation
Stuart Adam	Institute for Fiscal Studies
Emma Chamberlain OBE	Pump Court Tax Chambers
Anne Fairpo	Temple Tax Chambers, Low Incomes Tax Reform Group, Judge in the First Tier Tax Tribunal
Zahra Kanani	Thackray Williams LLP
Sarah Kelsey	HM Revenue & Customs
Sue Moore	The Institute of Chartered Accountants in England and Wales
Jane Page	HM Treasury
Stephanie Parker	Creaseys LLP
Gill Steel	LawSkills Ltd
Anjula Thiru	HM Revenue & Customs

Annex C

Technical terms and acronyms

- **Agricultural property relief (APR)** – provides relief from Inheritance Tax on agricultural property, by reducing the value of the relievable property transferred by either 50% or 100%. See Chapter 3 for more detail about the conditions of the relief
- **AIM** – Alternative Investment Market
- **Beneficiary** – this may refer to the beneficiary of an estate or trust. It is a person who receives a benefit from the trust or estate, for example cash or assets that are distributed to that person
- **Business property relief (BPR)** – provides relief from Inheritance Tax on business assets, by reducing the value of the relievable property transferred by either 50% or 100%. See Chapter 3 for more detail about the conditions of the relief
- **Capital Gains Tax** – a tax on the gain or profit made when you dispose of an asset. Disposing of an asset includes selling it, giving it away, swapping it and getting compensation if it is lost or destroyed. Some assets are exempt, for example your main home, and your car. Capital gains tax is only chargeable on any gains above your tax-free allowance, which is called the annual exempt amount. This is currently £11,700
- **CTT** – Capital Transfer Tax
- **Chargeable event** – an event that may lead to a charge to Inheritance Tax, such as ten-year anniversary charges on trusts and chargeable lifetime transfers
- **Chargeable lifetime transfer** - immediately chargeable gifts during an individual's lifetime. This includes transfers to a company or a trust that add up to more than the NRB (currently £325,000) over any 7 year period. These are chargeable to Inheritance Tax at a rate of 20%. If the individual dies within 7 years, there may be a further charge to bring the rate up to a maximum of 40% depending on when the gift was given
- **Confirmation** – the Scottish equivalent of probate. Confirmation is a legal document from the court that allows an executor to administer and distribute an estate according to the wishes of the deceased or the law
- **Downsizing** – if the deceased sold, gave away or downsized to a less valuable home before they died, their estate may qualify for the residence NRB if they meet the following conditions: the person sold, gave away or

downsized to a less valuable home on or after 8 July 2015, the former home would have qualified for the additional threshold if they had kept it until they died, and their direct descendants inherit at least some of the estate

- **Estate** – an estate is comprised of all assets that were held by an individual before their death. This includes, cash, property, investments, business assets, vehicles and any pay-outs from life insurance policies
- **Excepted estate** – an estate where no Inheritance Tax is due, and certain other conditions are met, which means that the executor does not have to complete the long Inheritance Tax form, and can instead submit a short form. This includes estates below the NRB, and estates below £1 million where the estate is inherited by a spouse or civil partner, or charity, meaning no Inheritance Tax is due
- **Excepted settlement** – if the conditions are met for an excepted settlement, trustees are excused from submitting an IHT100 form at certain occasions, for example at 10 year anniversaries or when assets are taken out of the trust. To be an excepted settlement, the trust must meet certain conditions, including that the trustees are all UK resident. The value of the 'notional aggregate chargeable transfer' must also be considered, and if it is less than 80% of the NRB then the trust may be an excepted settlement. To calculate this is complex, and involves consideration of previous charges and related trusts
- **Executor** – the person or people who have responsibility for administering the estate, including dealing with any Inheritance Tax consequences and applying for probate. If a person does not leave a will, then someone can apply to be an 'administrator' of the estate. In this report we use 'executor' to embrace both roles
- **Failed potentially exempt transfer** – a gift given in the 7 years before death. The value of failed PETs may be subject to Inheritance Tax if they are above the available NRB. However, the rate of tax is tapered for gifts given between 7 and 3 years before death
- **Gift with reservation** - a gift made by an individual where that individual continues to use or benefit from the gifted property. If this is the case, then the gift is treated as part of their estate for Inheritance Tax purposes on death if the reservation of benefit occurred in the previous 7 years
- **HMCTS** – Her Majesty's Courts and Tribunals Service
- **HMRC** – Her Majesty's Revenue and Customs
- **HMT** – Her Majesty's Treasury
- **Individual executor** – an executor who is not a professional executor
- **Nil rate band (NRB)** - the value under which an estate is not chargeable to Inheritance Tax. The nil rate band is currently £325,000
- **Nil rate bands** – the NRB and the residence NRB, along with any that are available to be transferred

- **OTS – Office of Tax Simplification**
- **Potentially exempt transfers (PET)** - are gifts from individuals to other individuals (and some specific types of trust) that are not generally counted towards the value of an estate for Inheritance Tax purposes if they are given more than seven years before death
- **Pre-owned assets charge (POAT)** – this is an annual income tax charge on benefits received by a former owner of property. The charge is applied to individuals who owned assets and then disposed of them but continue to receive a benefit from them. It applies to land, household and personal goods and intangible property or cash, stocks, shares and insurance products. It will not apply if the property that the individual retains a benefit from is still counted as part of their estate and so subject to Inheritance Tax
- **Probate** – the granting of probate gives a person the legal right to deal with someone's estate after their death. If the person left a will, then you apply for a grant of probate, if the person did not leave a will then you apply for letters of administration. Sometimes probate will not be needed, for example if the assets in the estate are all jointly held, or if the organisations that hold the estates assets do not require probate to obtain access to them. Each organisation has its own limit and processes
- **Professional executor** – individuals can appoint a professional executor such as a solicitor, bank or an accountant. They will take on the responsibility of administering the estate and are usually specialists at doing so. Professional executors are paid to take on this role
- **Residence nil rate band (residence NRB)** – this is an amount additional to the NRB, available where an estate includes a home, either in whole or in part, that is passed on to the deceased's direct descendants (for example children or grandchildren). The amount available is currently a maximum of £125,000, but will increase each tax year to reach £175,000 by tax year 2020 to 2021. The amount available will be the lower of the value of the home (or part of a home) or the maximum residence NRB available. For estates valued over £2 million, the maximum residence NRB available will be reduced by £1 for every £2 above that amount
- **Reservation of benefit** – someone who continues to reserve a benefit in property they have gifted
- **Transferable nil rate band (transferable NRB)** - the NRB is transferable between spouses and civil partners, when not fully used on the first spouse or civil partner's death
- **Transferable residence nil rate band (transferable residence NRB)** – the residence NRB is transferable between spouses and civil partners, when not fully used on the first spouse or civil partners death
- **Trust Inheritance Tax regime:** when trusts are referred to within this document, we generally mean discretionary trusts unless otherwise stated
 - **10 year charges** – certain trusts may be charged Inheritance Tax on every 10 year anniversary since the trust started. There is a complex

calculation to work out the amount of tax due on each 10 year anniversary, using an effective rate, broadly calculated as if a chargeable lifetime transfer of the value of the relevant property in the trust were made by the settlor, taking into account their total chargeable lifetime transfers in the seven years leading up to the creation of the trust. This value is set against the NRB available, which is currently £325,000. No relief for BPR/APR is available in establishing this effective rate. The effective rate is then applied on the net value of the property in the trust, meaning a deduction of any reliefs or exemptions can be claimed, at this point in the calculation. Trusts are eligible to claim many of the same reliefs as estates on death

- **Exit charges** - there may be an Inheritance Tax charge when assets are taken out of a trust, for example when they are distributed to beneficiaries or when the trust comes to an end. This is known as an exit charge. Not all payments out of a trust give rise to an exit charge, but when they do, the calculation to work out any Inheritance Tax due is complex. As with the 10 yearly charge, there is no set single rate applied to the value of the property exiting, but again an effective rate is calculated

Annex D

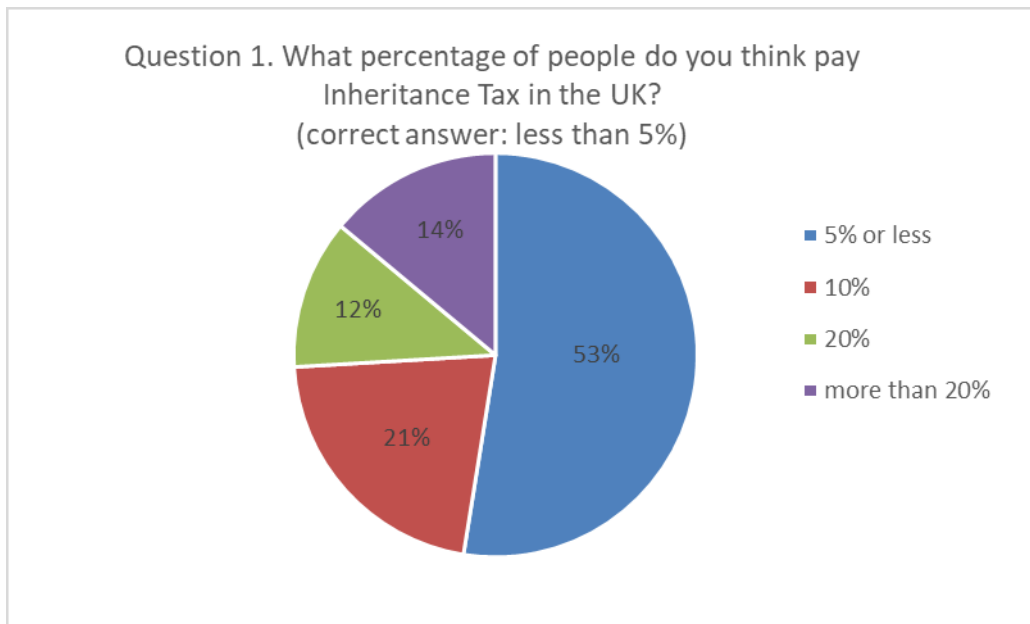
Survey findings

The OTS survey on Inheritance Tax was published on the OTS's website and various newspapers provided a link to it. It is important to highlight that the OTS survey was open to all who wished to take part, and as the respondents were only those who chose to complete the survey, it did not form a representative sample of society. This means that the survey findings are not generalised to the wider population and self-selection bias could distort the findings. The OTS received nearly 3000 responses to the survey.

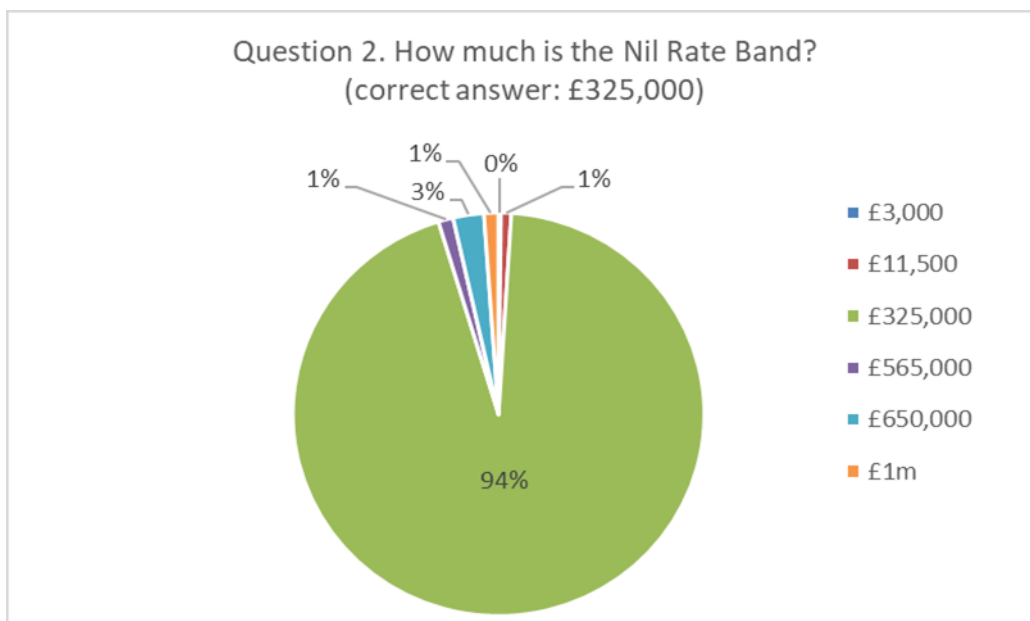
The key messages drawn from the survey are as follows:

- over a quarter of respondents thought that 20% or more people have to pay Inheritance Tax (729 out of total of 2811 responses)
- 38% of respondents (who did not use an adviser) recalled spending 50 hours or more on estate administration (339 out of a total of 889 responses)
- understanding and completing the relevant forms, and obtaining probate were the two most commonly cited processes which took the longest to undertake. (424 out of a total of 877 responses)
- 65% of respondents who did not use an adviser and 50% of those who had, felt that they still had to provide lots of information despite no Inheritance Tax being due (519 out of a total of 799 responses who did not use an adviser & 274 out of 545 responses who did)
- only 11% of respondents who did not use an adviser recalled finding the process simple and user friendly (87 out of a total of 799 responses)
- only a quarter of respondents recalled receiving an acknowledgement from HMRC that their paperwork had been received (198 out of a total of 799 responses)
- 61% of respondents stated that they were unaware how long it would take HMRC to respond once they had submitted their form (507 out of a total of 836 responses)
- the most commonly cited reason for making an amendment to a form (whether an adviser was used or not) was to adjust for assets which had not previously been identified (140 out of a total of 1007 responses)
- from the survey only 12% of respondents (who didn't use an adviser) said that they had submitted forms electronically to HMRC (97 out of a total of 840 responses)
- of those who used an adviser, 35% said that they had done so because of the complexity of the estate (112 out of a total of 317 responses) and over half, 56%, said that they used an adviser because they were concerned about making a mistake (178 out of a total of 317 responses)

Responses to survey quiz¹

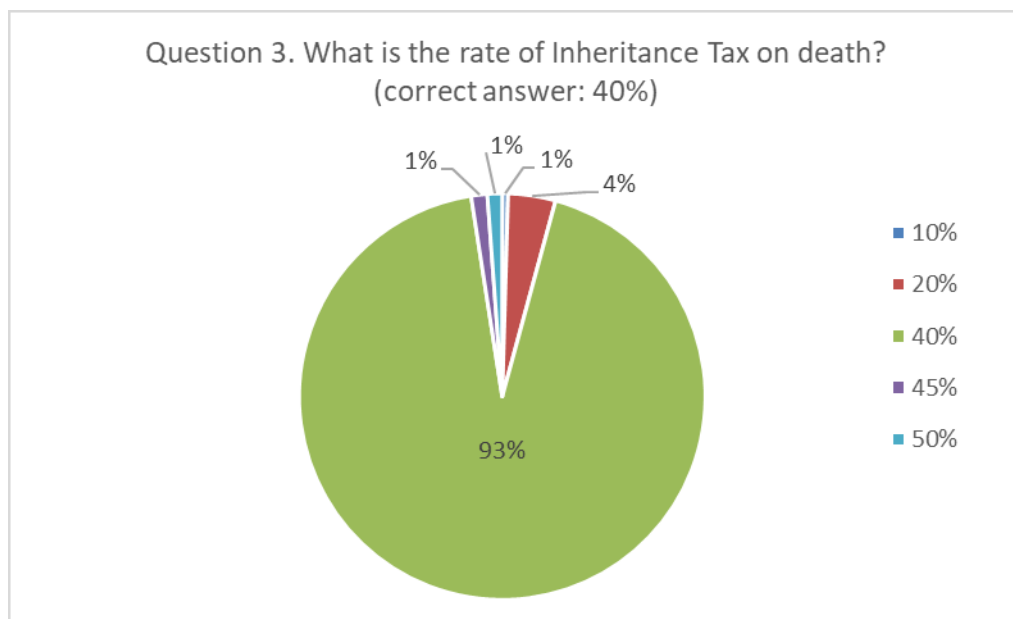


Total number of respondents: 2811

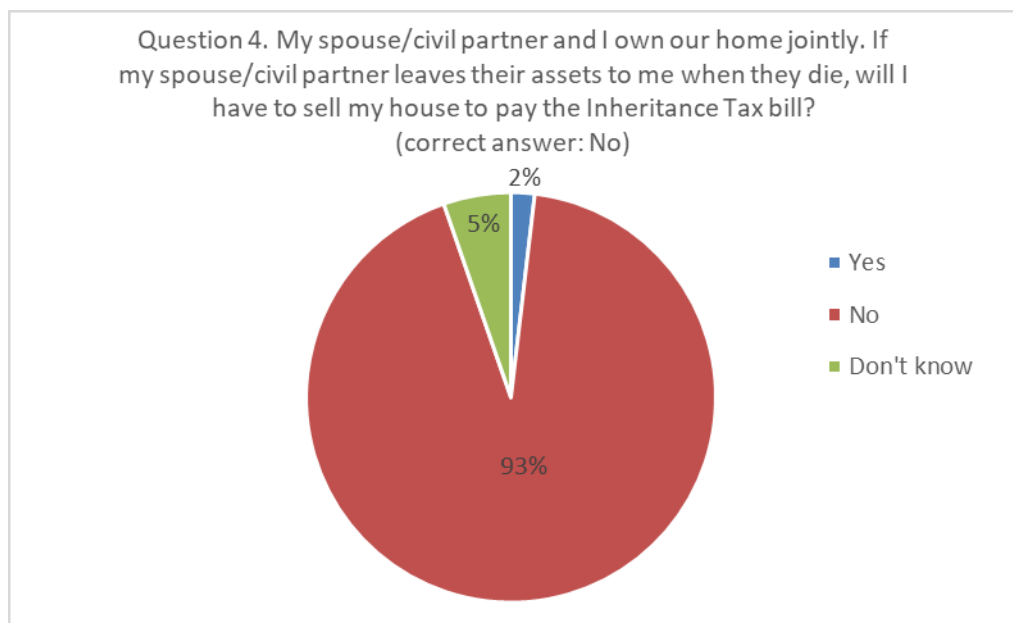


Total number of respondents: 2813

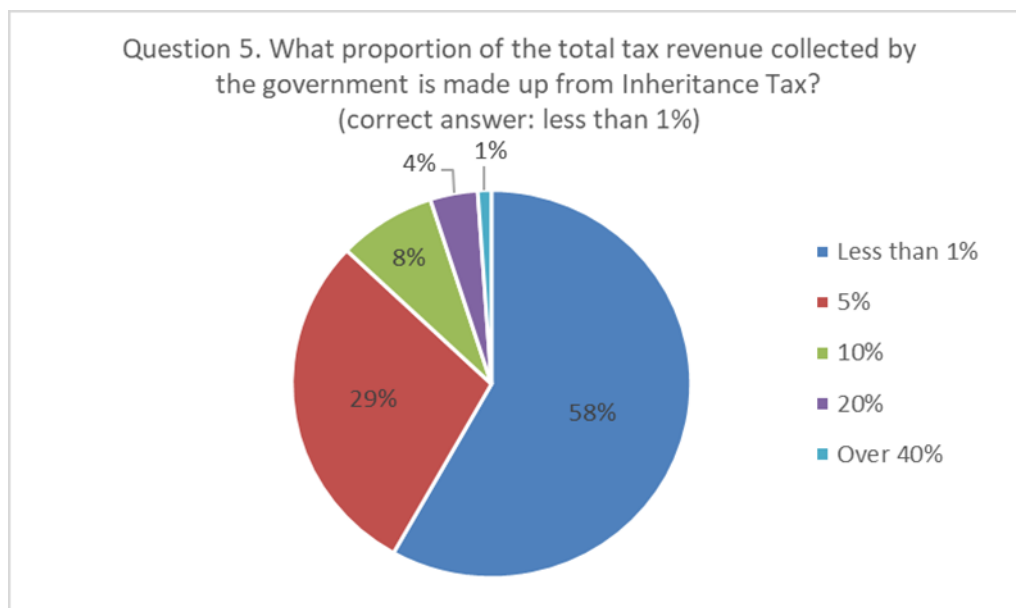
¹ Where appropriate, subject to rounding to reach 100%



Total number of respondents: 2809



Total number of respondents: 2797

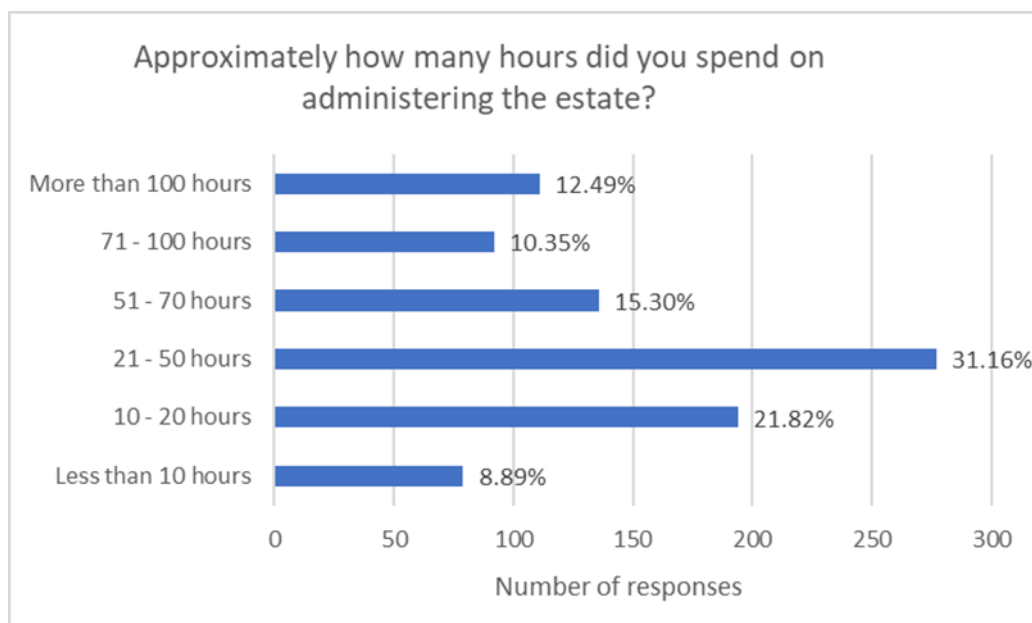


Total number of respondents: 2804

Survey responses relevant to the administration of Inheritance Tax where people did not use an adviser

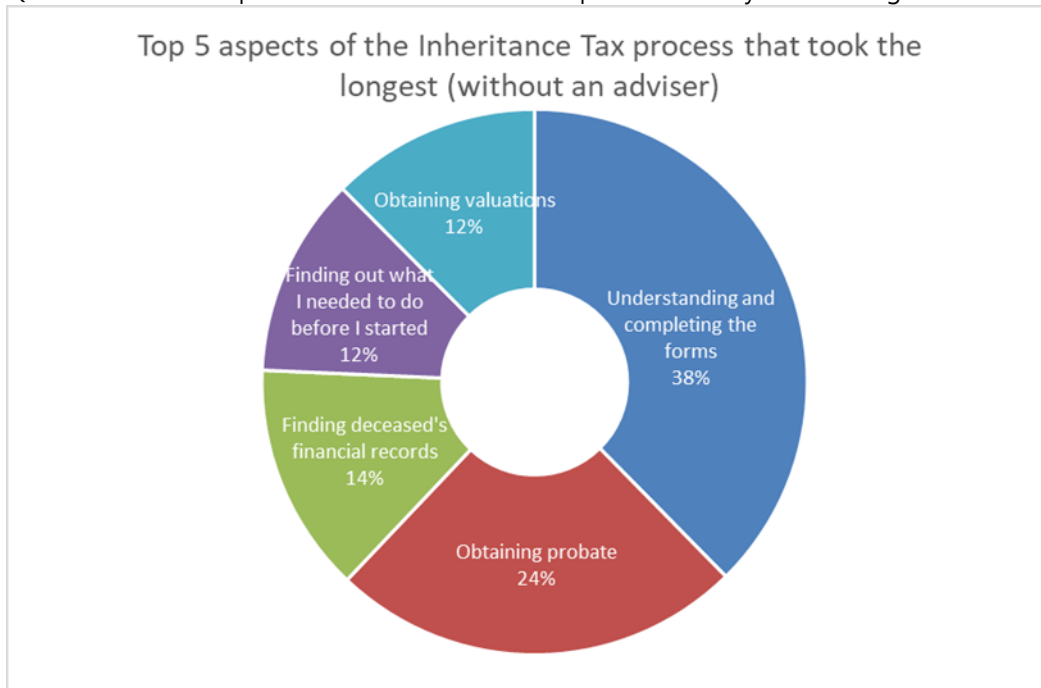
The following charts show the some of the responses of people who administered an estate without using an adviser

Question: Approximately how many hours in total did you spend on administering the estate? For example, on completing forms or finding financial records.



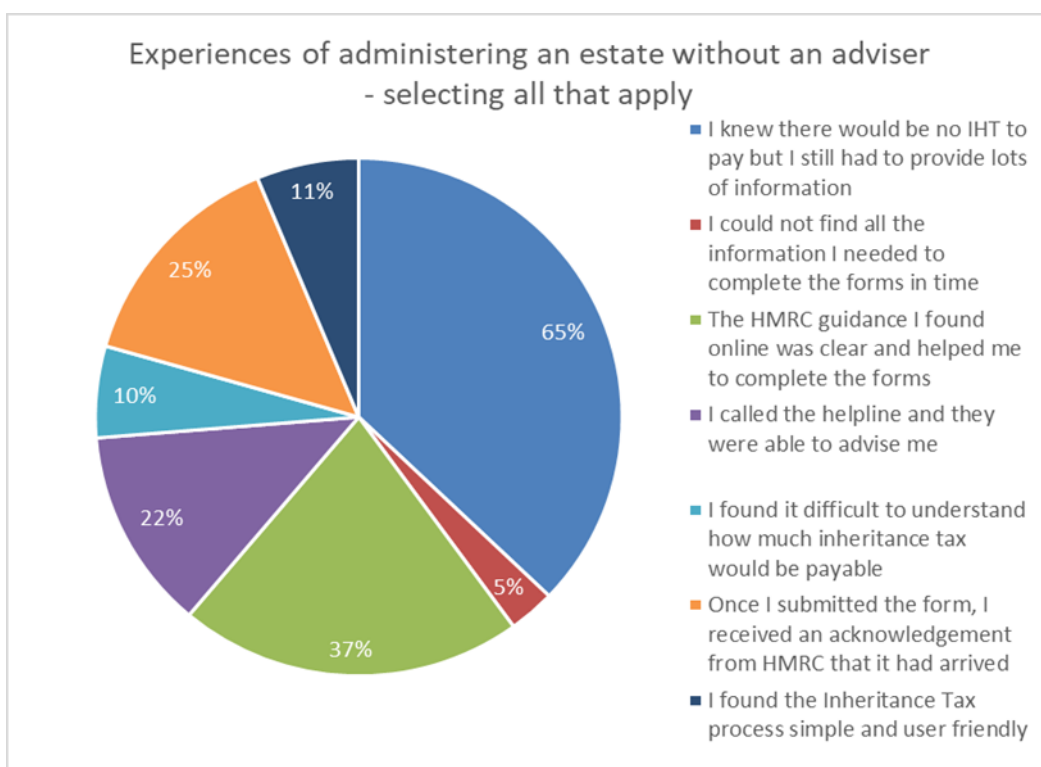
Total number of respondents: 889

Question: What aspect of the Inheritance Tax process took you the longest?



Total number of respondents: 877

Question: Experiences of administering an estate without an adviser – select all that apply



Total number of respondents: 799

Annex E

Organisations consulted

The OTS have listed below the wide range of organisations who gave their time to provide evidence to this review. The OTS are grateful to these organisations and the large number of individuals who gave their time to provide evidence. Individual names have not been published here.

Apologies are given to any organisations that have been inadvertently omitted.

1825 Financial Planning	Central Association of Agricultural Valuers
Aegon	Charity Tax Group
Age UK	Chaverys
Agricultural Law Association	Cheviot Holiday Cottages
AJ Bell	Chartered Institute of Taxation
Art Fund	Country Landowners Association
Association of Accounting Technicians	Department for Environment, Food & Rural Affairs
Associations of Lloyd's Members	Duncan & Toplis Ltd
Association of Tax Technicians	DWF LLP
BDO LLP	Eaton Manor Country Estate
Beacon Hill Far Holidays	Estates Business Group
Belle Grove Barns	EY
Bircham Dyson Bell	Family Education Trust
Bishop Fleming	Field House Farm Cottages
Blankney Estates Ltd	Field Seymour Parkes LLP
Boodle Hatfield LLP	Forsters LLP
Bosinver Farm Cottages	Gillespie Macandrew LLP
Bourne Leisure Ltd	Grant Thornton LLP
Broomhill Manor Country Estate Ltd	Grosvenor Estate
Burness Paull LLP	Group Risk Development
Canada Life	Hargreaves Lansdown
Cancer Research UK	Higher Menadew Farm Cottages

Carswell Group	Higher Wiscombe Ltd
Historic Houses	Personal Finance Group of the Sheffield U3A
HM Revenue & Customs	Philanthropy Impact
HM Treasury	Pitt Farm Holiday Cottages
Hunters	Plover Ltd
Institute of Chartered Accountants in England and Wales	Professional Association of Self Caterers
Institute for Family Business	PwC
Institute of Directors	Remember A Charity
Institute of Fundraising	Rosehill Lodges
Institute of Legacy Management	Royal London
Insuring Change	Royds Withy King
Investment & Life Assurance Group	RSM UK Tax and Accounting Ltd
Jane Clayton & Company Ltd	Saffery Champness
Johnston Carmichael LLP	Salvation Army
Kerridge End Holiday Cottages	Scottish Land and Estates
Kilik & Co	South West Tourism Alliance
Kings Court Trust Ltd	St James's Place Wealth Management
Knowle Farm	Society of Trusts and Estates Practitioners
Llanfendigaid Estate	Tenant Farmers Association
London Stock Exchange Group	The Association of British Insurers
Low Incomes Tax Reform Group	The Institute of Chartered Accountants of Scotland
Manx Insurance Association	The Law Society of England and Wales
Michelmores LLP	The Law Society of Scotland
Mills & Reeve LLP	The TaxPayers' Alliance
My Country Houses Ltd	Tourism Management Institute
National Council for Voluntary Organisations	UJIA
National Farmers Union	University of Birmingham
Octopus Investments	Valuation Office Agency
OHL Ltd	Wedlake Bell LLP
Old Mutual Wealth	Wheeldon Trees Farm
Opes Tax	Wrigleys Solicitors LLP
Penningtons Manches LLP	

