

OTS Report - Inheritance Tax Simplification

Earlier this year the Office of Tax Simplification was asked by the Chancellor of the Exchequer to conduct a wide review into inheritance tax (IHT), looking into it from both a technical and administrative standpoint. The report received a record amount of responses from a wide variety of people effected by IHT. Over 3000 responses made to an online survey, combined with a further 500 email responses and 100 written responses from experts responding to a call for evidence.

WHO ARE THE OFFICE OF TAX SIMPLIFICATION?

The OTS provide independent advice to the government and conduct inquiries into areas of the UK tax system that are complex and that would benefit from simplification to make it easier for the taxpayer, both individuals and businesses. They also look to reducing the administrative burden of interacting with the UK tax system; there was a large focus on administration issues in the IHT report, as even executors of estates that don't pay any IHT may be subjected to the burden of completing complex IHT forms.

WHAT DOES THE REPORT COVER?

The OTS's report is split into two parts, and the first part was published on 23rd November 2018. This first report is split into three chapters and covers the main issues that were raised with IHT:

- IHT administration process for executors
- Administration of other IHT charges such as PETs, chargeable lifetime transfers, and trust anniversary and exit charges.
- Other complex areas, including RNRB, lifetime gifting, businesses and farms, and the reduced IHT rate when part of an estate is left to charity.

Recommendations for simplification are offered on reducing the administrative burden on estates, but recommendations on more complex areas such as the residence NRB (RNRB), business and farm property, and lifetime gifting will not be made until the second report is published in Spring 2019.

SIMPLIFICATION OF THE IHT ADMINISTRATION PROCESS FOR EXECUTORS

According to the OTS report only 5% of estates actually pay IHT, but personal representatives for half of all deaths must complete IHT forms. According to the Office of National Statistics in the tax year 2015/16 there were 588,000 deaths with IHT payable on only 24,500 of those estates. IHT forms were completed for just under half of them.

The report considered the IHT forms, available guidance, communication with HMRC, the deadlines for payment of IHT, as well as non-IHT administrative matters.

[IHT Forms](#)

IHT forms need to be completed if probate is required, even if no IHT is due. There are two main forms; the short form (IHT205), and the long form or 'full inheritance tax account' (IHT400). The IHT forms must be completed and any IHT due paid before a grant of probate can be granted to allow the executor to administer the estate.

The OTS suggests that the short form is relatively straightforward, but the long form requires a disproportionate amount of information with the main form often needing to be supplemented with further pages to give more information e.g. where there is a claim for BPR, where the deceased was a beneficiary under a trust, or where they owned foreign assets.

Even though the short form may be simpler the task for a lay executor of establishing which is the correct form to use can be burdensome. The OTS finds that there is no straightforward process for directing an executor to the correct form.

Most forms can only be submitted by paper. The short form can be completed online but not by advisors. While the forms are all available online it is difficult to actually complete them digitally due to the format they use, this means that the majority of IHT forms are completed by hand. Proper digitisation of the forms could lead to less mistakes being made and a less time-consuming process.

The OTS's key recommendation is for the government to implement a fully integrated digital system for IHT that includes the ability to submit probate applications online. Interestingly changes to the probate application procedure were announced on the 1st November 2018, before the OTS's recommendations were published, and became law on the 27th November 2008. These changes were implemented by statutory instrument (The Non-Contentious Probate (Amendment) Rules 2018) and now allow for unrepresented applicants to submit probate applications online. This seems like it is already a step towards implementing an online system for estate administration to make the whole process smoother.

In the meantime, they suggest making changes to the current IHT forms and the guidance that supports them to clearly direct executors to the correct forms and to prepare them for being digitised. They also suggest implementing a new very short form for the simplest of estates that should be combined with a probate form, greatly reducing the administrative burden for simple estates where there is no IHT to pay.

[Guidance](#)

There are many government sources of guidance on how to complete the IHT forms and on IHT in general. Much of this guidance is provided in the form of notes accompanying the IHT400 and via HMRC's IHT Manual. The manual is publicly available but is actually HMRC's internal guidance notes, so the layout and terminology may be confusing to a layperson.

One of the main issues the OTS identified with the published guidance is that it is sometimes inconsistent, with the terminology used in the IHT400 notes sometimes being completely different from that used on GOV.uk. The guidance and manuals are also difficult to navigate making it difficult to actually find the information required.

They identify many gaps in the guidance, mainly information about timescales, an executor's obligations, information retention for executors, and what can be done where there aren't enough liquid assets in an estate to pay the IHT.

The OTS concluded that a general review of all of the IHT guidance is required to address these issues. The guidance should be updated to remove inconsistencies and be generally easier to follow. The public would also benefit from worked examples throughout the guidance, even for simple estate where there is no IHT, and an IHT calculator. The OTS suggest that updated guidance would also benefit HMRC by freeing up resources currently used on corresponding with members of the public who are confused about IHT and the forms.

[Communication with HMRC](#)

Communication with HMRC could be improved. Currently weeks or months can pass without any response from HMRC after forms or correspondence has been submitted. This can be unnerving for executors especially if they have not dealt with probate or IHT in the past.

In April 2018 HMRC began trialing a 12-week response period for inquiries into IHT forms. HMRC will now write to an executor within 12 weeks of their submission of the IHT400 to confirm whether they have any enquires. This should remove some worry for executors, who can now assume that if HMRC have not contacted them within 12 weeks no enquires will be made so they can carry on with the administration.

Currently no receipts are issued for the payment of IHT automatically, though HMRC will issue a receipt if one is requested. The OTS found that HMRC's system for issuing receipts is manual so issues them in all cases would be too labour intensive and time consuming. Evidence suggests that receiving a receipt for IHT would be reassuring for executors, so the OTS recommends HMRC considers a system of automated receipts to address this.

[Payment Deadlines & Probate](#)

Under the current system the deadline for payment of IHT is 6 months from the month of death, and the deadline for issuing IHT forms is 12 months. The grant of probate giving the executors the legal authority to deal with the deceased's assets cannot be granted until the IHT forms are submitted and any IHT due is paid.

The OTS suggest that having two separate deadlines causes confusion and this could be simplified by making the deadline for IHT payment and submission of the IHT forms the same. It seems pointless to have a tax payment deadline that is shorter than the reporting deadline.

The report also uncovered a general opinion that a 6-month deadline to pay IHT is not enough and more time may be required to calculate the tax due, especially on more complex estates. 10% of estates paid IHT outside of the 6-month deadline. The two main reasons they identified for 6 months not being long enough are:

- Administration is not top priority when a relative or close friend has died – often the executor will be someone who is closely affected by the deceased's passing.

- Gathering information is time consuming and difficult – especially considering that this is likely to be the first time acting as an executor if they are not a professional.

Sometimes the probate process can be confusing and frustrating for executors. In some cases, the executors can't access the information they need to complete the forms and pay the IHT because they don't have a grant of probate, but they can't obtain the grant until they have paid the IHT. This leads to a circular and frustrating experience for a lay executor. If they are then forced to make estimates to complete the forms this further increases the administrative burden on executors as they will then need to go back and make adjustments once they can access the deceased's full information.

A further point of frustration for executors is the funding gap. The IHT needs to be paid before they can apply for the grant, but the grant is often needed to access the assets to pay the IHT. While there are ways to deal with this as some banks will release assets to pay the IHT, and others will provide loans to executors, this can be difficult to arrange and there are often high interest rates associated with the loans.

The address this the OTS recommends allowing executors to obtain probate without submitting an IHT form, or at least on submitting a simple form, if the estate is a low value estate and no IHT is due. They also suggest considering a method of confirming an executor's status before the grant is issued to allow them to access and gather all of the information they need prior to the issue of a grant.

ADMINISTRATION OF OTHER IHT CHARGES

The second chapter of the report considers IHT charges that occur during an individual's lifetime or during the lifetime of certain trusts. IHT charges may occur in lifetime on the following events:

- chargeable lifetime transfers, including 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

Reporting to HMRC that IHT is due because of a trust or other chargeable event is done via a separate form, the IHT100. This form is made up of an 8-page base form and various supplementary forms depending on what additional information is required. The form caters to differing roles as the person responsible for completing it varies depending on the reason the form has to be completed. This makes it too complex and it is accused of overcomplicating matters by trying to cater to too many scenarios at once.

In their report the OTS even quoted STEP as saying the IHT100 is not fit for purposes as it has never been updated to take account of changes made by the Finance Act 2006. They also go on to say that the form complicates the calculation of what is already an overly complex tax.

The issue of confusion over who is responsible for reporting a gift to HMRC when a PET fails and becomes chargeable was also raised. Although formally it is the responsibility of the recipient of the gift to report it via the IHT100, in practice the deceased's executors often report it on their IHT forms.

When the form is being completed by trustees the signature requirement for the IHT100 is inconsistent with other areas of the tax system. The IHT100 must be signed by all trustees, which can cause delays if it is difficult or inconvenient for all trustees to meet and sign the form together. In other areas of the tax system where there are multiple trustees a principal acting trustee is nominated who can sign and complete forms on behalf of all trustees.

On the topic of trustees, there are occasions where the IHT100 must be completed even where no IHT is due. The OTS suggest that HMRC review the requirement for trustees to submit a form where no IHT is due.

Their other recommendations largely mirror those for the IHT forms discussed in the earlier chapter. Mainly simplifying and updating the form and moving towards an online system instead. A further addition they recommend to the proposed online system would be a calculator that works out the IHT due for the taxpayer, removing the need for them to do complex calculations and reducing the volume of mistakes made.

OTHER AREAS OF COMPLEXITY

The third chapter discussed other areas of complexity in the IHT system. No recommendations were made on these topics as these will be covered in the second report due to be published in Spring 2019. Instead this section collected the comments and evidence that the OTS has received.

The NRB was discussed here, and in their report the OTS stated that the ordinary NRB and transferable NRB is generally well understood. The complications come mainly, and perhaps unsurprisingly, from the RNRB and TRNRB. This has been criticised since before its introduction on 6 April 2017 as being overly complicated and disadvantageous to those who do not have children as it only applies to a person who dies leaving an interest in a qualifying residence to a 'direct descendant'. The RNRB is also further complicated by the downsizing provisions, aimed at helping individuals who have sold their property or downsized. The OTS comment that many respondents suggested that the RNRB should simply be removed and the NRB increased.

Lifetime gifts were also addressed, as were the various reliefs and exemptions. The OTS highlighted comments received about the complexity of the exemptions available and the fact that many are either not well known or not very well understood.

The limits for the £3000 annual exemption, £250 small gift exemption, and the exemption for gifts on marriage have not increased since IHT was introduced. This has been presented as a criticism of the system.

There are uncertainties surrounding the evidence that executors are required to supply to HMRC for various types of lifetime gift. The administration of maintaining records was also described in the report as 'problematic'.

BPR and APR are due to be discussed in the second report. The main criticisms this report raised were the favourable treatment of certain businesses over others, paying special attention to furnished holiday lettings and the discrepancy in how they are treated for IHT purposes and how they are treated for income tax and CGT purposes and the difficulties with the wholly or mainly test.

To qualify for BPR certain criteria must be met. One such criteria is that the business must not wholly or mainly consist of holding investments, however this 'wholly or mainly' test is not clearly defined in legislation. According to responses the OTS received this test can be challenging to apply and cause uncertainty for business owners.

In the Spring 2019 report the OTS are also going to consider more technical elements of the IHT system, including the reduced rate of IHT where a proportion of an estate is left to charity, the administration of life insurance and pension products, exit and anniversary charges on trusts, and the rules on gifts with reservation of benefit.

CONCLUSION

This month's CPD paper has been only a summary of the OTS report into IHT and their key recommendations. A follow up paper will be issued in the Spring once the second report has been published. For a deeper understanding of the recommendations on simplifying IHT and the administration process we would recommend all members read the OTS report in full. The full report, including an executive summary, can be found here:

<https://www.gov.uk/government/publications/office-of-tax-simplification-inheritance-tax-review>

Important Reminder:

These notes are produced solely for the benefit of SWW members when completing the December 2018 CPD test to gain 1 hour of structured CPD towards their annual quota. The notes do not represent legal advice and no reliance can be made on the content of the notes in any or individual specific client circumstances. Having read the notes members should cement their understanding by considering further reading around the subject – cases details can be found by searching the case references using BAILII or GOOGLE.