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PERSONAL REPRESENTATIVE HELD PERSONALLY LIABLE FOR IHT

In the recent case of Harris v HMRC [2018] TC06448 the personal representative, who released a substantial amount of the estate's assets to the brother of the deceased who was a beneficiary of the estate, was held liable for inheritance tax (IHT) payable on the estate.

The liability of personal representatives for inheritance tax under the Inheritance Tax Act (IHTA) 1984 is relevant to this case, namely.

- Section 4 (IHTA 1984) provides that inheritance tax is charged on the death of an individual as if, immediately before the death, they had made a transfer of value equal to the value of their estate immediately before death.

- Section 200 (IHTA 1984) provides that the deceased's personal representatives (with limited exceptions) are liable for the inheritance tax arising on the deemed transfer on death.

- Section 216 (IHTA 1984) requires the personal representatives to deliver an inheritance tax account and pay any inheritance tax due before the Court issues the grant of representation to them. Where the estate includes land, the inheritance tax due on that land can be paid in ten equal annual instalments and, when the land is sold, any unpaid instalments will then become immediately payable.

Turning to the specific facts of the case in question:

Mr Harris was the appointed personal representative of the late Helena McDonald.

On 28 April 2013 he filed the inheritance tax account - form IHT400.

On 16 April 2014 HMRC opened an enquiry into the account and on 7 October 2015 issued a determination for £341,279 of IHT.

Mr Harris requested a statutory review of the determination and, in a letter dated 20 July 2016, was informed that the determination had been upheld. Mr Harris decided to appeal against this review decision on the grounds of insufficient funds.

Mr Harris had released a substantial amount of the estate's assets to the brother of the deceased, who was a beneficiary of the estate, on the understanding that the brother would settle the IHT but the brother returned home to Barbados without settling the IHT and Mr Harris was not able to contact him.

However, the First-tier Tribunal struck out the appeal as having no reasonable prospect of success. The fact that Mr Harris had transferred the assets of the estate to a beneficiary on the basis that the beneficiary would be responsible for payment of IHT, and was ignorant of his obligations as a personal representative to pay the IHT, was not a valid defence.

COMMENT

This case illustrates that personal representatives ought to be fully aware of their obligations when considering taking on this role. In particular, they should ensure they have sufficient funds to pay any IHT (and any other liabilities) before they make any distributions to beneficiaries.

OTS PUBLISHES PAPER ON SAVINGS INCOME: ROUTES TO SIMPLIFICATION

On 25 May the Office of Tax Simplification (OTS) published a 50-page paper entitled "Savings income: routes to simplification". As the OTS notes (without naming George Osborne), "Many of the issues have arisen because of a series of changes, each working well enough taken by itself but which together create significant complexity that is not easily resolved".

While the paper refers to "savings" in its title, confusingly it does not adopt the tax definition (ie. primarily interest), but looks across all investment income, including dividends and pension payments. The starting point for the paper is to note that "95% of people pay no tax on savings income", thanks to the starting rate for savings (SRS), personal savings allowance (PSA), dividend allowance (DA) and use of ISAs. However, in a statement repeated several times in the document, the OTS says that "the interactions between the rates and allowances is sufficiently complex at the margins that HMRC's self-assessment computer software has sometimes failed to get it right. It is proving to be very difficult to create an algorithm that calculates the tax correctly in all circumstances..."

The OTS floats a range of proposals for "further work", which suggests a more formal consultation may emerge in Mr Hammond's Autumn Budget. Despite some of the press stories, what the OTS has put forward is a long way from becoming law, if it ever does.

Much of the OTS review is focused on trying to overcome issues caused by the current combination of different tax rates, rate bands and allowances for interest and dividends, which is sufficiently complex that few taxpayers would be able to check their own calculation unaided.

Interest and dividends - streamlining the interaction of income tax rates and allowances

Suggestions include:

- Specifying the order in which allowances can be deducted (as the order of income is at present), to avoid issues with software calculating the tax due incorrectly, or taxpayers not making the best choice about the allocation of their allowances. The current law is that the allocation of personal allowances (and reliefs available against general income) should be made in the way which will result in the greatest reduction in the liability to tax. It is this optimisation which has triggered the HMRC self-assessment errors;

- Ending the current differential tax rates for dividend income (7.5%, 32.5% and 38.1%). The OTS suggests that if all taxable income was taxed at the same rates, it wouldn't matter how the personal allowance was used. It says making this change "would have the effect of increasing the amount of tax due from those who receive amounts of dividend income above the [£2,000] dividend allowance. It would also impact on the taxation of profit extracted as a salary or as a dividend, from family owned companies". Given the ongoing issues with NIC increases, IR35 and personal service companies, there is little doubt about the attraction of such an idea for the Treasury;

- Simplifying the income tax calculation by making the PSA and the DA true allowances or exemptions rather than just a nil rate of tax, a simplifying measure which it accepts would reduce Exchequer income. Income falling within the allowance would not need to be reported and would not count towards the individual's total income;

- Making savings interest completely exempt, either for basic rate taxpayers only, or for individuals with total income below a certain threshold, or for individuals over pension age. The OTS acknowledges that if an exemption were linked to the basic rate or an income threshold, this would also create a cliff edge. Equally, it would lessen any simplicity;

- Reducing the complexity arising from having two separate allowances by amalgamating the £5,000 SRS (which benefits fewer than 300,000 people) with the PSA, resulting in a combined allowance of £6,000 for basic rate taxpayers, or £5,500 for higher rate taxpayers. This would involve removing the condition attached to the SRS, which means its availability depends on an individual's non-savings income. Currently, this 0% tax band is only fully available where earned income (eg salary, benefits in kind, pensions, etc.) does not exceed the personal allowance, and it reduces to the extent that earned income does exceed the personal allowance. So, for example, if earned income is £12,000, the 0% starting rate for savings income reduces from £5,000 to £4,850;

- Considering whether trusts and personal representatives should be entitled to the PSA, as even modest estates will often receive interest on any cash deposit, meaning that income tax will need to be paid, with the accompanying administrative burdens on both the trustees/personal representatives and HMRC;

- A targeted extension to the ISA regime to allow larger sums to be transferred in cases where, for example, elderly people who had sold their family home to pay for long- term care could be encouraged to use their ISA allowances to protect themselves from the compliance burden of accounting for tax on the interest;

- Improving guidance on the taxation of savings income, using learning from the Financial Capability Unit where relevant. The OTS has started a project to take a strategic look at the approach to taxpayer guidance, in collaboration with work HMRC is itself doing to overhaul its 290 manuals. The OTS suggests that this should be an area of priority for HMRC; and

- Introducing a personal tax roadmap (to incorporate any plans for the taxation of savings and/or the consolidation of savings income rates and allowances, and the stages needed to get there) to allow people to plan their financial futures with a better level of certainty. This is effectively the OTS asking the Treasury to set out a long- term tax strategy, rather than make the yearly tweaks that have created the current situation.

Increase flexibility on ISAs

The OTS believes that ISAs have now become too complicated, with a variety of traps for the unwary.

Whilst a drop in ISA investment may simply be a result of low interest rates combined with the introduction of the PSA, the OTS considers that there is scope for a wider full review of the current ISA landscape, to make the regime simpler and more accessible.

Suggestions include:

- Allowing partial transfers of money invested in-year;

- Removing the requirement that an investor may only take out one ISA of each type per year, subject to the overall annual limit; and

- Extending the rule, that expired on 6 April 2018, allowing transfers from Help to Buy ISAs to LISAs without affecting the annual LISA allowance.

On LISAs, the OTS rightly observes that take-up “has been slower than predicted”, with only one provider offering a cash LISA. The OTS wants the 25% early withdrawal charge re-examined: it shares the FCA’s view that the effect of the charge is poorly understood and has been a deterrent to firms entering the market.

The OTS suggests that along with a full review of the current ISA landscape, to simplify the regime, further consideration should be given to how best to ensure that the LISA rules work effectively for unadvised savers.

Review rules on partial encashments from life insurance investment bonds

Will this review result in wholesale changes to bond taxation, or even lead to the ending of the 5% allowance? It’s unlikely.

The 5% allowance has had a number of close calls over the years, most recently following Lobler v HMRC in which the judge severely criticised the taxation regime on partial surrenders. HMRC

suggested a range of alternative tax treatments, but eventually settled on a new process instead, due to the small number of policyholders who find themselves in the position of having a gain on part surrender which is 'wholly disproportionate'. Affected taxpayers may now apply to HMRC for adjustments to be made on a just and reasonable basis.

The OTS report states that HMRC has only received around 15 applications since the new process was introduced in 2017. Nevertheless, the OTS considers it would have been preferable for the legislation not to result in disproportionate gains.

It suggests that an administrative option to simplify the tax treatment of partial withdrawals without substantially changing the tax calculation would be to mandate a 'vertical' calculation (the actual profit on each segment) in cases where the withdrawal exceeded the cumulative 5% allowances. Although it acknowledges that encashing segments in this way would cause a tax charge to arise in circumstances where 'horizontal' encashments (where only the excess above 5% is taxable) would not.

The OTS believes that this area of savings taxation warrants further review once the new system has bedded down.

Of course, you may recall that the OTS suggested similar simplifications in an earlier review, and eventually recommended, in 2011, that the 5% rule be retained, saying at the time: "The relief is a substantial simplification for HMRC, individual investors and insurance companies, and any replacement is likely to be at least as complex."

The taxation of withdrawals from personal pensions

The OTS has reviewed the change that was brought in at the point of pension freedoms whereby those without a valid tax code with the pension provider are taxed using an emergency tax code on a month one basis. This generally results in an overpayment of tax which needs to be reclaimed either immediately, by the completion of a form, or through the use of the PAYE system. The OTS observes that whilst this practice is there to ensure that HMRC isn't chasing for additional payments, the lack of understanding by consumers can cause problems with planning. In addition, it also notes that although HMRC states it pays the tax back within seven days of the claim the industry isn't experiencing that as a whole.

The taxation of lump sums from deferred state pensions

The OTS has reviewed the way in which deferred state pension lump sums are taxed. It observes that the taxation of the lump sum is determined by the top rate of tax the consumer is paying in the year that they claim the lump sum and this may or may not reflect the tax that should have been paid had the income been taken instead. They also note that tax reducers, such as Gift Aid, do not have an impact on these calculations.

Overall it notes that it is a complex area and needs reviewing to make it clearer to the consumer.

COMMENT

The OTS has identified a number of areas where simplification or streamlining should be considered and says that it "considers it important not to make piecemeal changes, which risk adding further layers of complexity". On past performance, it looks unlikely its wish will be granted.

And as it acknowledges that some of its suggestions would have an Exchequer cost that is currently unquantified, it will remain to be seen how much of this will be taken forward by Government.

PENSION TRANSFERS

In mid-May The Pensions Regulator (TRP) issued a Freedom of Information (FoI) release on DB transfers in the year to 31 March 2018. This FoI request represented a request for an update on data issued a year earlier, also under FoI. The TPR data was solely on transfers *from* DB schemes, so included DB to DB transfers (although these are rare given that just 14% of DB schemes were open in March 2017, according to TPR).

Shortly afterwards the *Financial Times* issued fresh FoI data on transfers, looking specifically at DB to DC transfers. The information was provided by the FCA. The latest figures are more insightful than TPR's which related "to transfers in the 12 month period covered by the reporting schemes' most recent annual report and accounts relative to the effective date of the schemes' submission of information to TPR" and so had a built in time lag. According to the FCA:

- In 2017, £20.8bn was transferred from DB to DC schemes. The corresponding figure for 2016 was £7.9bn, meaning the 2017 increase was 163%.
- The number of actual DB to DC transfers also rose, but at a slower rate. There were 92,000 in 2017, against 61,000 in 2016 – a 51% increase.
- By simple mathematics, the average DB to DC transfer in 2017 was £226,000 against £129,500 in 2016, a 75% increase.

COMMENT

The sharp rise in average transfer values is puzzling. While transfer values did rise between 2016 and 2017, according to Xafinity, the increase was of the order of 15%. It is not a British Steel effect either, as this is reported to have involved 2,600 transfers worth £1.1bn (an average of £423,000), hardly enough to make a significant change in the overall average.

NEW FUEL RATES FOR COMPANY CARS

HMRC has announced the new fuel rates for company cars applicable to all journeys from 1 June 2018 until further notice.

The rates per mile are based on fuel prices and adjusted miles per gallon figures.

For one month from the date of the change, employers may use either the previous or the latest rates. They may make or require supplementary payments, but are under no obligation to do either. Hybrid cars are treated as either petrol or diesel cars for this purpose.

Rates from 1 June 2018:

Engine size	Petrol	LPG	Engine size	Diesel
1,400 cc or less	11p	7p	1,600 or less	10p
1,401cc to 2,000cc	14p	9p	1,601cc to 2,000cc	11p
Over 2,000cc	22p	14p	Over 2,000cc	13p

UNIVERSAL CREDIT FOR THE SELF-EMPLOYED

According to the latest Office for National Statistics figures around 4.8 million people are self-employed in the UK. This represents 15% of the workforce.

The Office for Budget Responsibility expects around 700,000 self-employed claimants will be supported by Universal Credit once it is fully rolled out in 2022.

The main changes for the self-employed are:

- the introduction of a Minimum Income Floor (MIF) – an assumed level of income used to calculate Universal Credit entitlements;

- a ‘Start up Period’ for newly self-employed claimants of one year, during which the Minimum Income Floor does not apply; and

- an increased role for Jobcentre Plus in determining whether claimants are gainfully self-employed for Universal Credit purposes and supporting them during their first year in business. (A claimant is gainfully self-employed if self-employment is their main employment and if it is regular, organised and carried on in expectation of profit). Jobcentre Plus is introducing specially-trained self-employment specialist Work Coaches to better assess and support claimants.

One issue the report didn’t tackle was pension contributions. The Low Incomes Tax Reform Group has been calling for the Government to re-define the MIF so as to allow for the deduction of self-employed pension contributions.

Currently, both employed and self-employed claimants can deduct certain pension contributions in arriving at the net income figure on which their Universal Credit is calculated. However, whilst there is no limit on the amount of pension contributions that can be deducted by employed claimants, for self-employed claimants if such contributions take their net income below the MIF level, they will be treated as if their income was equal to the MIF. This means the self-employed don’t receive the same recognition for pension contributions as their employed counterparts.

FAILING TO PREVENT CRIMINAL FACILITATION OF TAX EVASION

HMRC has updated its guidance covering processes and procedures that a business can put in place to limit the risk of its representatives criminally facilitating tax evasion – the corporate offence of

criminally facilitating tax evasion. The guidance is based around six principles:

- risk assessment - the relevant body assesses the nature and extent of its exposure to the risk of those who act in the capacity of a person associated with it criminally facilitating tax evasion offences and the risk assessment is documented and kept under review;
- proportionality of procedures - reasonable procedures will be proportionate to the risk the relevant body faces. This will depend on the nature, scale and complexity of the relevant body's activities, taking account of the level of control and supervision the organisation is able to exercise over a particular person acting on its behalf, and the proximity of the person to the relevant body;
- top-level commitment - the top-level management of a relevant body should be committed to preventing persons acting in the capacity of a person associated with it from engaging in criminal facilitation of tax evasion. They should foster a culture within the relevant body in which activity intended to facilitate tax evasion is never acceptable;
- due diligence - the organisation applies due diligence procedures, taking an appropriate and risk-based approach, in respect of persons who perform or will perform services on behalf of the organisation, in order to mitigate identified risks;
- communication and training - the organisation seeks to ensure that its prevention policies and procedures are communicated, embedded and understood throughout the organisation, through internal and external communication, including training. This is proportionate to the risk to which the organisation assesses that it is exposed; and
- monitoring and review - the organisation monitors and reviews its preventative procedures and makes improvements where necessary.

INCOME WITHDRAWAL RATE FOR JUNE 2018

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in June 2018 is 1.75%.