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IHT, Trusts and Estates

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BUDGET 2018 COVERAGE PROVIDED BY TOLLEY®GUIDANCE

The tax industry is renowned for its complexity and its speed of change. The annual budget brings a whole new set of rules, which tax practitioners need to grasp swiftly in order to advise clients. The Tolley®Guidance writers have put together their expert analysis and commentary on Budget 2018 to help you understand what the changes mean to you and your clients.

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Normally Chancellors relish the prospect of delivering a budget – it is an opportunity to make a mark as a great tax reformer and to show off their conjuring skills with announcements to wrong-foot the opposition. But the run up to today's speech felt very different. Expectations were deliberately being dampened down. Was it going to be just a holding exercise, with the 'real' budget to be announced post-Brexit? Indeed, did the Chancellor want to deliver a Budget at all? Some people thought that he wanted to postpone it until the spring, but was trapped by his own decision a couple of years ago to move to an Autumn Budget. So, we were waiting with more than the usual amount of anticipation when he stood up to speak at 3:30.

For a man whose job is widely said to be on the line, his delivery was assured and he had the command of the House of Commons. He threw in several light-hearted comments – I can't imagine many of his predecessors coming up with the line "Fiscal Phil says fiscal rules OK", let alone making a series of increasingly laboured jokes about public lavatories: what would Gladstone have said?! He painted a very positive picture of the public finances, and was able to say that "austerity was coming to an end", not, you will notice, that it has actually ended.

So, what did he say about tax?

The biggest headline will be the proposal for a tax on digital services. It is intended to be restricted to only established tech giants and will be subject to consultation coming into effect in 2020, subject to no new international agreement being introduced before then.

The massive increase in the annual investment allowance to £1m was a big surprise, and comes with a reform of capital allowances to give a measure of relief for some commercial buildings, but at the expense of some of the existing allowances for plant and machinery. The small print of this will be important. Business owners will breathe a sigh of relief that entrepreneur's relief is to remain, although in future it will be necessary to own the business for two years to qualify for relief. That is a reasonable compromise.

Large and medium-sized businesses will also have to get to grips with new rules when they engage workers through personal service companies, but at least these are not going to be introduced until 2020, and there will be a period of consultation – it will be critically important to get the details right.

Home owners will not be faced with capital gains tax on selling their private residences, although there is a tightening up of the rules where property has been let or where there is an overlap between buying one house and selling another.

The major announcement for income tax payers was the bringing forward of the personal allowance and higher rate threshold a year earlier than expected. So, the personal allowance will be £12,500 and the higher rate threshold will be £50,000 from April 2019. Those are substantial changes and will have an impact on almost all taxpayers.

There was more meat in this Budget than we might have expected. As ever though, the detail will be important, and I'll leave the analysis of that to our resident Tolley experts who have worked indefatigably through the evening and night to deliver insight on not only what the statements are, but also what they mean to you and your clients. We are also very fortunate to have a wider team of editors and technicians supporting us and making it all possible. We hope you find the commentary useful and informative.



Andrew Hubbard

Andrew is Editor-in-Chief of New Tolley and Taxation magazine and a consultant at RSM. Andrew initially trained as an inspector of taxes before joining the accountancy profession. He has worked in a 'big four' environment and was a partner in BDO Hayward and then Tenon before joining RSM and LexisNexis. He is also past president of both ATT and CIOT as well as an accomplished musician.

OUR EXPERT WRITERS:



PAULINE LONSDALE,
Inheritance Tax Manager,
Tolley

Pauline joined Tolley in 2012 as writer and editor for the IHT, Trusts and Estates module of Tolley®Guidance. She has been an independent practitioner for many years engaged in personal tax, trusts and estates work. In addition to advising her own clients, she acts as consultant to solicitors and accountants, focusing on finding practical solutions to a broad range of private client problems. She now divides her time between her own tax practice and Tolley®Guidance.

Pauline is a member of the ICAEW, CIOT and STEP. She sits on the STEP Practice Committee and spent some time as a tutor for the STEP Diploma programme.



RICHARD WHITAKER,
IHT, TolleyAdvance Manager,
Tolley

Richard joined LexisNexis in March 2017, after working at a variety of small, regional and national law firms as a private client solicitor. During his time in practice, Richard covered the whole spectrum of private client work although, more recently, his work focussed on wealth protection and inheritance tax planning. Since moving to Tolley, he has retained his links to law and is an examiner for the Equity and Trusts module of the GDL.

Prior to his legal career, Richard spent 12 years in the Army as a musician and soldier, travelling the world (including an operational tour of Kosovo).

Richard is a full member of the Society of Trust and Estate Practitioners.

Budget 2018 – IHT, Trusts and Estates overview

The Chancellor, Philip Hammond, delivered his [2018 Budget](#) on 29 October 2018. Finance Bill 2018/2019 will be published on 7 November 2018 and is expected to receive Royal Assent before the start of the 2019/20 tax year.

Residence nil rate band

Legislation will be introduced in Finance Bill 2018/19 to amend certain details of the operation of the residence nil rate band (RNRB). The changes take effect for deaths on or after Budget day, 29 October 2018. The RNRB is an addition to the basic nil rate band which further reduces the inheritance tax payable on death. It provides relief for the devolution of the value of residential property to direct descendants in tightly prescribed circumstances. It is not surprising that the very complex provisions have thrown up some doubtful or unanticipated results.

[IHTA 1984, ss 8D-8M](#)

See the [Residence nil rate band – main provisions](#) and the [Residence nil rate band – trusts, downsizing and lifetime gifts](#) guidance notes for full details of how the relief works.

Downsizing

The downsizing provisions were inserted so that those who had downsized (or completely disposed of their residence), prior to death, were not penalised. Unfortunately, the rules have proved confusing, often involving cumbersome calculations. One inconsistency that is the target of today's announcement is the definition of rules for calculating the 'lost relievable amount' at [IHTA 1984, s 8FE](#).

When calculating the lost relievable amount, reference is made to VT, which is the value of the chargeable transfer made on death (Step 2 at [IHTA 1984, s 8FE\(9\)](#)). However, no allowance is made for any value that passes to an exempt beneficiary, such as the spouse (as this is not a chargeable transfer).

This has the effect that, where some or all of the estate is left to a spouse, the VT is nil and thus, the percentage at Step 2 is 0%. The knock-on effect is that the lost relievable amount may be higher than it should have been.

The government presumably intends to amend the wording of Step 2 at [IHTA 1984, s 8FE\(9\)](#) with a view to tweaking the use of VT by including exempt transfers into the value of the estate.

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Gifts with reservation

The second proposed amendment is to the legislation at [IHTA 1984, s 8J](#) in relation to gifts with reservation. The general rule is that lifetime gifts do not benefit from the RNRB. However, if a person has made a lifetime gift with reservation (GWR), the property is taxed as part of his estate on death. The consequence of this fiction (ie that the property is included in the death estate) is that a GWR **will** benefit from the RNRB if the recipient of the gift is a direct descendant. As far as the RNRB is concerned, it should make no difference whether, for example, a parent gives his child his residence during his lifetime as a GWR or on death. And if the deceased gives his property to a person who is not a lineal descendant, it will be taxed as part of his estate without the benefit of the RNRB.

This is the intention of the law and is HMRC's view of it as confirmed by [IHTM46033](#). However, a problem has apparently been identified with the definition of 'inherited' which requires an amendment. The aim of the amendment is to ensure that a residence which is a GWR will only be treated as being inherited by a direct descendant if it became immediately comprised in the descendant's estate as a result of the original gift. That is in fact our interpretation of the law as it stands. We shall have to await the publication of the Finance Bill to discover how the wording is perceived to be deficient.

[IHTA 1984, s 8J\(6\)](#)

See [IHT: changes to Residence Nil Rate Band](#).

Excluded property trusts

Since the extension of the deemed domicile rules, particularly in relation to "formerly domiciled residents", the definition of excluded property trusts has become more pertinent. See the [Application of the deemed domicile rules](#) guidance note.

[IHTA 1984, s 48\(3\)](#)

The current law provides that property comprised in a settlement situated outside the UK is excluded property if the settlor was domiciled outside the UK when the settlement was made. Accepted HMRC practice is to treat additions to the settlement as not excluded property if the settlor had become UK domiciled or deemed domiciled when the additions were made. See [IHTM04272](#).

This treatment is not explicitly laid down in statute however. As indicated in the Overview of Tax Legislation and Rates [OOTLAR](#) at para 2.21, it is proposed that Finance Bill 2019/20 will amend the legislation to confirm that assets

added to trusts after the settlor has become UK-domiciled or deemed domiciled will not be designated as excluded property. Consequently, the settlement as a whole will include a combination of excluded and non-excluded property.

It is also proposed that transfers between trusts that occur after Royal Assent of Finance Bill 2019/20 will be subject to additional excluded property tests, as yet unspecified.

Taxation of trusts – simplification

Trust practitioners may remember that we were promised a consultation on simplifying the taxation of trusts in last year's [Autumn Budget 2017](#). Our Budget [news article](#) last year included some comments and predictions on the proposal. This year's [OOTLAR](#) at para 2.3 simply repeats the proposal with no further details provided.

Trusts capital gains – private residence relief

In his Budget speech, the Chancellor announced a restriction on the availability of CGT private residence relief for individuals. The specific aspects targeted are letting relief and the deemed occupation for the final 18-month period of ownership. See [OOTLAR](#) at para 2.2. The proposals are:

- > to restrict letting relief to situations where the tenant shared occupation with the owner, and
- > to reduce the final tax exempt period to nine months

These changes will take effect from April 2020. The government will consult on the detail of the changes.

These proposals will also apply to the CGT liability of trustees where a beneficiary occupies a residential property under the terms of the trust. See the [Private residence relief](#) guidance note. Where, for example, a trust property has been occupied by a beneficiary for only part of the ownership period, relief will not be extended by a period of letting.

When the final period exemption was reduced from 36 months to 18 months in 2014, the more generous 36-month exemption was retained for disabled persons and those moving to a care home. In the latest proposals, the longer period of 36 months will again be retained for those people, and it is expected that it will apply equally to trust gains where the beneficiary qualifies.

Charities

Two small changes were made affecting charities and philanthropists.

The small trading exemption limit allows charities to raise (within limits) an amount of tax-free income from activities that are not related to their primary function. The example given by the government is of a charity selling Christmas cards.

Charities whose income falls between £20,001 and £200,000 can receive tax-free income that is 25% of the charity's turnover. This band will be increased to between £32,000 and £320,000 (with no change in the 25% rate).

A charity whose charitable income is below £20,000 can currently raise £5,000 tax-free income that is not related to their 'primary purpose'. This will be raised to £32,000 and £8,000 respectively.

At the other end of the scale, those charities whose charitable income is over £200,000 can currently raise £50,000 tax-free non-primary income. This will be raised to £320,000 and £80,000 respectively.

In short, the new bands and rates are:

ANNUAL CHARITY INCOME	MAXIMUM NON-PRIMARY INCOME
Under £32,000	£8,000
£32,000–£320,000	25% of income
Over £320,000	£80,000

The changes will come into effect from 1 April 2019 for corporation tax and 6 April 2019 for income tax.

The Gift Aid Small Donations Scheme (GASDS) was introduced to allow individuals to make small donations to charity without the need to fill in a Gift Aid declaration form. The current limit of £20 has been increased to £30, to bring it on a par with the contactless payments limit.

See [Increases to charities' small trading exemption limits](#) and [Gift Aid Small Donations Scheme](#).

For further information on Gift Aid, see the [Gifting cash and assets to charity](#) guidance note.

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