

A higher burden

Simon McKie and Sharon McKie warn that the separate system of inheritance tax accounts and determinations can have serious and unexpected consequences for unwary advisers and their clients.

Those who deal regularly with self-assessment returns and only occasionally with submitting inheritance tax accounts, might easily assume that the self-assessment administrative system of returns, enquiries, information notices, assessments, limitation periods and appeals also applies, in essence, to this tax. It does not; inheritance tax has had its own administrative system, separate from the system that applies to the other major direct taxes, since it was introduced as capital transfer tax in 1974.

It is a system with significant differences from the self-assessment system and one that, in many respects, is weighted more heavily against the taxpayer and in favour of HMRC. Instead of returns it has accounts. It has no statute-based system of investigation equivalent to the enquiry provisions of self-assessment and it has no real equivalent to assessments, the function of which is only paralleled in part by 'determinations'. The limitation provisions applying to inheritance tax are also very different to those provided in respect of income tax and capital gains tax by TMA 1970, s 34, s 36 and s 36A.

Liability and payment

Liability to pay inheritance tax is governed by IHTA 1984, Pt VII (all statutory references are to this act unless otherwise stated). These provisions can impose liability on multiple persons in respect of the same occasions of charge.

Under self assessment there is no duty to pay tax, other than by way of deduction, in the absence of an assessment, whether it be a self assessment or an assessment by HMRC.

Key points

- Inheritance tax has its own administrative system, not to be confused with the self-assessment system for income tax.
- HMRC has the right 'to demand payment of an amount'.
- The Inland Revenue charge is imposed by IHTA 1984, s 237.
- The duty to deliver an inheritance tax account can apply to various persons.
- No limitation period applies if a loss of tax was deliberate.



For inheritance tax, in contrast, a duty to pay tax arises automatically on the expiration of a period after an event occurs which is chargeable to inheritance tax. The general rule is stated in s 226(1):

'The tax on the value transferred by a chargeable transfer shall be due six months after the end of the month in which the chargeable transfer is made or, in the case of a transfer made after 5 April and before 1 October in any year otherwise than on death, at the end of April in the next year.'

Specific provisions similarly make tax payable six months after the end of the month in which occur various specific occasions of charge or an event resulting in an increase in a charge (s 226(3), s 226(3A), s 226(3B) and s 226(3C) and s 226(4)).

Personal representatives are the only persons on whom a duty to pay inheritance tax is imposed by reference, not to the occurrence of an event which gives rise to a charge, but to the delivery of an account (see below) in respect of a chargeable event (s 226(2)).

Recovery of tax payable

So, although in general the duty to pay inheritance tax arises on the expiry of a period after the occurrence of an event creating a charge, s 226(5) provides:

'The board may in the first instance, and without prejudice to the recovery of the remainder of the tax, accept or demand payment of an amount by reference to the value stated in an account delivered to the board under s 216 or s 217 above.'

The consequence of the board having a right 'to demand payment of an amount' is not entirely clear. The intention seems to be to confer on HMRC a right to recover the amount demanded but, read literally, the provision does not do that. No doubt the courts would remedy the inadequacies of the drafting by applying a looser, purposive construction of this provision.

In general, under s 242, the board may proceed to recover inheritance tax from a person only when it has been agreed in writing with that person or has been determined and specified in a determination. In the latter case, recovery proceedings cannot be taken if the determination is under appeal. This gives, by a different route, a similar result to income tax and capital gains tax provisions under which a liability to pay arises only in respect of an assessment which has either been made by the taxpayer or agreed with him or which has become final either because it has not been appealed or it has been determined by the tribunal or the court.

The Inland Revenue charge

If any inheritance tax, or interest thereon, is payable and is 'for the time being unpaid', a charge in favour of HMRC is imposed by s 237 for the amount unpaid on:

- (a) 'any property to the value of which the value transferred is wholly or partly attributable; and
- (b) where the chargeable transfer is made by the making of a settlement or is made under Part III of this act, any property comprised in the settlement.'

This is still called, despite the Inland Revenue having been replaced by HMRC in 2005, an 'Inland Revenue charge'. The charge does not extend to a debt due for penalties imposed by HMRC and there is no requirement for the department to register such a charge (*Howarth's Executors v CIR* [1997] SSCD 162).

It will be seen that the charge for unpaid inheritance tax on the value transferred by a chargeable transfer is imposed on property to the value of which the value transferred is wholly or partly attributable (emphasis added). The result is that real property and interests in real property in a deceased person's free estate, which are comprised in the chargeable transfer on the deceased's death and subject to the Inland Revenue charge, are subject to this for the whole of the unpaid inheritance tax on the chargeable transfer arising from the deceased's death, including any such tax in respect of personal or moveable property which is not itself subject to the Inland Revenue charge.

If the chargeable transfer is made on death, personal or moveable property situated in the UK which was beneficially owned by the deceased immediately before his death and which vests in his personal representatives is not subject to the charge (s 237(3)).

A purchaser of personal property situated in the UK, or of any property situated outside the UK, takes it free from the Inland Revenue charge if they had no notice of the facts giving rise to the charge (s 238(1)(c)).

In the case of a potentially exempt transfer which becomes chargeable on the death of the transferor within seven years of the transfer, the charge does not apply to property to which the transfer was wholly or partly attributable, or to an interest in any such property, if the property or interest has been disposed of to a purchaser before the transferor's death. If such property has been otherwise disposed of before the death of the transferor, property that at the death represents such property or an interest in that property is subject to the charge (s 237(3A)).

If property subject to a charge is disposed of to a purchaser in circumstances where the charge does not cease, the charge ceases six years after the later of either:

- the date on which the tax became due; or
- the date on which a full and proper account of the property was first delivered to the board in connection with the transfer concerned (s 238(2)).

Accounts

The primary duty to deliver an inheritance tax account is imposed, under s 216(1), on various persons who are liable to inheritance tax. But if there is delay in obtaining a grant of representation (or a confirmation) for a deceased estate the duty may also fall, under s 216(2), on the person beneficially entitled to the property, or to an interest in possession in it, or who is a potential beneficiary of the property. If a duty arises under s 216(2), the persons having to deliver an account under s 216(1) are not relieved of that duty.

Investigations

As we have said, the legislation does not contain a statutory power for HMRC to raise an enquiry into an inheritance tax return as is provided by TMA 1970, s 9 for the self-assessment regime. To identify inheritance tax charges that have either not been the subject of an account or have been understated, HMRC uses information which it obtains from its general activities, from informal requests for information and under the information powers conferred by FA 2008, Sch 36.

It should be noted that the terminology in respect of such inheritance tax matters is different from that of self assessment. The self-assessment regime uses the term 'enquiry' whereas this word does not appear in IHTA 1984. HMRC's *Inheritance Tax Manual* uses the terms 'enquiry' and 'investigation' interchangeably and also refers to 'compliance checks'. In this article we use the term 'investigation' to refer to all active steps that HMRC takes to determine whether a charge to inheritance tax has arisen which has either not been the subject of an account or which has been understated in an account and, if so, the amount of that charge.

HMRC has woken up to the fact that a large amount of revenue can be raised from investigating inheritance tax accounts. According to a response to a Freedom of Information Act request made by the wealth management firm Quilters in 2019, in recent years HMRC has opened about 5,500 such investigations each year. Because about 22,000 estates were charged to inheritance tax in 2018-19, this indicates that about a quarter of all chargeable occasions are subject to active investigation.

HMRC says that every inheritance tax account received is risk assessed (see IHTM29031) by a risk assessor and the department distinguishes between what it calls 'compliance checks' and 'enquiry cases'. According to the manual at IHTM29011, 'enquiry cases' are those where the risk assessors have decided that they need to:

- 'question the veracity of one or more aspects of an account;
- identify omissions from an account;
- ask for an account to be submitted where this has not been done within the time limit and [they] have information that suggests a tax charge arises.'

Questions to be asked

HMRC says the main purpose of an investigation into an inheritance tax account 'is to make sure that significant amounts of tax are not lost as a result of errors, omissions, under-valuations or improper claims for relief' (IHTM09021). HMRC's directions to its staff (IHTM09022) are that 'if a case is selected for further investigation you should not simply check the accuracy of the information provided in the account. You should also check other information sources to try to build up a picture of the transferor and their financial affairs as a whole to identify any potential errors, omissions, under-valuations, tax avoidance and tax evasion.'

At IHTM09052, the manual goes on to direct that HMRC officers 'should frame [their] questions carefully so that the taxpayers are clear about precisely what information [they] need and all information is requested at the outset. Questions should be phrased in such a way that they can, if necessary, be lifted to form the basis of a [FA 2008, Sch 36] information notice.'

In practice, questions are rarely 'carefully' framed although it is true that the questions from information requests are often copied uncritically into Sch 36 information notices causing severe difficulties for taxpayers who take seriously their statutory duty to comply with those notices.

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HMRC's 'compliance check'

In its *Trusts and Estates Newsletter: Special Edition: April 2018*, HMRC announced that it will notify taxpayers within 14 weeks of receiving an account if it is to carry out what it calls a 'compliance check'. It states that in 'some straightforward cases' the department will not need to look at the account in any more detail after sending its initial calculation of the inheritance tax chargeable. Written notice will be given within one to two weeks if this is to be the case or if an account is going to be looked at in more detail.

HMRC states: 'If you have not heard from us by [14 weeks after the submission of an account] you can assume we do not have any questions to ask about the information and values you have [given]...'

Rather unhelpfully, it goes on to say: 'It is up to you to decide how to administer the estate, but you may choose to distribute some of the assets now.'

It is sometimes thought erroneously that this has the effect of placing a time limitation on information requests or even on the issue of determinations. It does not. There is no practical prospect that a judicial review application would be successful in stopping HMRC from requiring further information or from issuing or applying a determination in respect of an event which is the subject of an incorrect account by establishing that a taxpayer had relied on these statements.

Obtaining information

FA 2008, Sch 36 para 63 governs the provision of information for a large range of taxes including inheritance tax. HMRC may serve a notice requiring a person to provide information or to produce a document as long as 'the information or document is reasonably required by the officer for the purpose of checking the taxpayer's tax position' (Sch 36 para 1).

Schedule 36 para 2 provides a similar power to obtain information from third parties.

The term 'tax position' is very broadly defined (Sch 36 para 64) and means: 'In relation to a person ... the person's position as regards any tax, including the person's position as regards:

- (a) past, present and future liability to pay any tax;
- (b) penalties and other amounts that have been paid, or are or may be payable, by or to the person in connection with any tax; and
- (c) claims, elections, applications and notices that have been or may be made or given in connection with the person's liability to pay any tax; and references to a person's position as regards a particular tax (however expressed) are to be interpreted accordingly.'

An information notice 'for the purpose of checking the tax position of a person who has died' must be made within four years of the person's death (Sch 36 para 22). There is no restriction within Sch 36 as to the age of the information or documents which a person may be required to produce except that para 20 imposes an internal administrative review in respect of notices to provide documents that are more than six years old. Schedule 36 para 18 provides that: 'An information notice only requires a person to produce a document if it is in the person's possession or power.'

The general requirement that the information or document must be 'reasonably required for the purpose of checking [a] taxpayer's position' has the result that information concerning chargeability to tax which cannot give rise to a recoverable liability cannot be within the scope of the power. For this reason, time limits on assessment (to income tax or capital gains tax) or recovery (inheritance tax) place an indirect limitation of time on the information that can be required under Sch 36 paras 1 and 2.

Notices of determination

Section 221(1) provides: 'Where it appears to the board that a transfer of value has been made or where a claim under this act is made to the board in connection with a transfer of value, the board may give notice in writing to any person who appears to the board to be the transferor or the claimant or to be liable for any of the tax chargeable on the value transferred, stating that they have determined the matters specified in the notice.'

Section 221(2) provides that the matters which may be specified in a notice of determination are all or any of the following:

- (a) 'the date of the transfer;
- (b) the value transferred and the value of any property to which the value transferred is wholly or partly attributable;

- (c) the transferor;
- (d) the tax chargeable (if any) and the persons who are liable for the whole or part of it;
- (e) the amount of any payment made in excess of the tax for which a person is liable and the date from which and the rate at which tax or any repayment of tax overpaid carries interest; and
- (f) any other matter that appears to the board to be relevant for the purposes of this act.'

Section 221(5) says that unless the notice of determination is either varied by agreement, or is the subject of an appeal, it 'shall be conclusive for the purposes of this act against the person on whom the notice is served; and if the notice is served on the transferor and specifies a determination of the value transferred by the transfer of value or previous transfers of value, the determination, so far as relevant to the tax chargeable in respect of later transfers of value (whether or not made by the transferor) shall be conclusive also against any other person, subject however to any adjustment under section 240 or 241 below [which concern underpayments and overpayments]'

In effect, HMRC can either collect inheritance tax in accordance with an account or it can raise a determination where it believes that this tax is chargeable whether or not an account has been delivered. Any such determination can be the subject of an appeal by the taxpayer to the tribunal and from there to the courts.

Limitation periods

There is no time limit on HMRC's power to issue a notice of determination.

Time limits do operate on HMRC's power to recover tax. If tax attributable to the value of any property is paid under an account duly delivered to the board and the payment has been made and accepted in satisfaction of the tax, proceedings to recover any additional tax may only be commenced within:

- 20 years of the payment of the tax in respect of a case involving a loss of tax brought about deliberately by a person liable for the tax (another 20-year period may apply in cases concerning the general anti-abuse rule) (s 240(5));
- six years of the payment of the tax if the loss of tax is brought about carelessly but not deliberately (s 240(4)); and
- four years of the payment of the tax if the loss of tax has been brought about otherwise (s 240(2)).

A loss of tax is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss (s 240A(2)).

If no account has been delivered, or the property by reference to which tax is chargeable has been omitted from an account, there is no limitation period if the loss of tax has been brought

about deliberately and it is 20 years otherwise (s 240(6) and (7)). This is more onerous than the equivalent limitation period in respect of assessments to income tax and capital gains tax.

An example

The absence of comprehensive limitation provisions coupled with the provisions imposing the Inland Revenue charge can result in an inheritance tax liability emerging after decades and being charged on assets, the owners of which have been previously unaware of the liability. Perhaps we should conclude with the following example as a warning of what can happen in practice.

In 1993, Rupert settled a house ('Misfortune Manor') and farmland on discretionary trusts. The land qualified for 100% agriculture property relief but Misfortune Manor did not. Rupert was aware of that, but chose to regard it as if it did. Thinking, erroneously, that if all the property settled were wholly exempt he would have no duty to submit an account, he did not do so, with the result that he failed to account for inheritance tax chargeable on the transfer into the settlement.

In 2002, the trustees exercised a power to advance the trust property to Rupert's daughter, Hortensia, at which point the trustees claimed agricultural property relief on the farmland, but not on Misfortune Manor as was correct. The farmland was sold and Hortensia gave Misfortune Manor to her son, Henry, who lived in it until 2010 when he sold it and bought a rental property ('Let House').

In 2017, many years after Rupert's death, HMRC issued a notice of determination in respect of the settlement of Misfortune Manor in 1993 on the basis that the loss of tax due to Rupert's failure to submit an account was caused deliberately so that there was no limitation on HMRC's power to recover the inheritance tax chargeable on the settlement.

Under s 237, until Misfortune Manor was sold in 2010, it had been subject to the Inland Revenue charge. On the sale, that charge transferred to the sale proceeds and, when these were applied by Henry in acquiring Let House, transferred again to that property.

To Henry's dismay, in 2018, a quarter of a century after the settlement, HMRC began proceedings to enforce the charge and to collect, with interest, the unpaid inheritance tax. ●

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Planning point

Do you have processes in place to determine whether HMRC has the power to recover tax? Do not assume that the same rules apply for inheritance tax as they do for income tax. In some cases there is no limit to how far back HMRC can go to recover inheritance tax.

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