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Death and taxes

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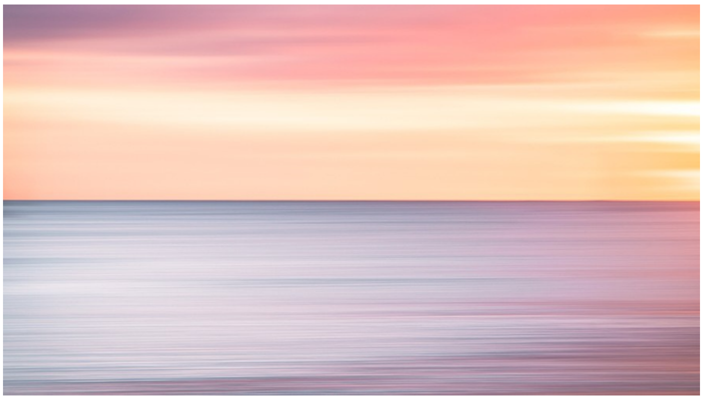

Benjamin Franklin may have been right to say that both death and taxes were unavoidable, but the future of tax on death is now up in the air!

The Office of Tax Simplification has been tasked by the Chancellor with reviewing inheritance tax and is currently assessing the comments that have been submitted by professionals and the general public, with a view to publishing its report in the Autumn. The aim of the review is to simplify the structure of inheritance tax and to reduce the distorting effect it has on taxpayers' investment decisions.

The survey sent out by the OTS suggests that they will focus on whether taxpayers have a good understanding of the rules and their practical impact. It has been confirmed that radical changes (such as the abolition of inheritance tax) are outside the scope of the exercise, despite the fact this was favoured by many early responders to the survey.

Perhaps not coincidentally, the Resolution Foundation has recently issued a report recommending that inheritance tax be replaced by a lifetime receipts tax, taxing the recipient of gifts rather than the donor or his or her estate. Each individual would have a lifetime allowance under which the first say £125,000 received by him or her would be free of tax. The balance over this would be taxed, probably at rates significantly lower than the current 40% inheritance tax rate.

This, says the author of the report, would give donors an incentive to spread their gifts more widely and could give younger family members the start they need to enable them to get onto the property ladder, and could also result in a reduction in the rate of tax. Other commentators have favoured replacing inheritance tax with a capital gains tax charge on death.

Though it seems unlikely that any of these radical options will be favoured in the immediate future, the fact that the Government has taken an initiative in this area accompanied by the relatively significant press coverage in recent months may mean some changes are to be expected.

Possible areas of change might be

- Amendments to Business and Agricultural Property Reliefs – these are expensive and the fact that they cover substantial number of AIM listed companies and tenanted farmland as well as owner managed businesses and working farmers means that they are seen by many not to be properly focussed.
- The abolition of some of the smaller annual reliefs, such as the annual small gifts exemption (of £250 per recipient) and gifts on marriage – the limits for which have not been increased since the 1980s. It would be nice to hope that this might be combined with an increase in the annual exemption of £3000 which has been at this level for nearly 40 years.
- Some further simplification of the rules taxing trusts which are extremely onerous and not justified by the amount raised.

Further initiatives in the medium term might address

- The newly introduced relief for residential property passing to descendants – again this is astonishingly complex and an increase in the general nil rate band would be much simpler to administer.
- Increases in the rate of tax on high value estates to help fund care costs – how to provide for an ageing population is something the Government needs to address and opinion polls suggest that this route might be acceptable to many voters.
- Even if a complete overhaul of the system is ruled out, the potentially exempt transfer regime (under which no tax is payable on outright gifts if the donor survives 7 years) must be vulnerable especially if there is a change of Government or a further downturn in the financial situation.

In the light of these risks, there is no time like the present for getting on with lifetime gifting, especially where property that benefits from Business and Agricultural Property Relief is involved.

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