



THREE COUNTIES

PROFESSIONAL BRIEFING

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IHT100

The revenue recently issued a consultation paper regarding the reporting limits for filing an IHT100 on discretionary trusts where there is no inheritance tax to pay. It is intended that the proposals will become law later this year, when the new limits will be backdated to **6 April 2007**.

There is no disadvantage in complying with the current limits. However, those who hope to make the most of any increase in the reporting limits can take advantage of the fact that an IHT100 does not need to be submitted until 12 months after the end of the month in which a discretionary trust is created.

The new reporting limits test will be based on the value of the gift before any deduction of any liabilities, exemptions or reliefs and most importantly for a discounted gift and income scheme, will be defined as the **undiscounted** amount of the gift. Under the proposals, the limits will be subject to change each year but for tax year 2007/2008, the chargeable transfer should not exceed £210,000, and the cumulative total of all chargeable transfers for the seven years preceding the current transfer, including the transfer, must not exceed £225,000.

Under the proposals, the IHT100 will not be required where the hypothetical value of the trust does not exceed £210,000 for 2007/2008. These proposals are subject to change depending on the comments the Revenue received during the consultation period. We will keep you updated on any developments.

Potentially exempt transfers (PETs)

Clients can still take advantage of the PET regime by executing a bare (absolute) trust for specific beneficiaries. Several providers offer a bare gift trust to take advantage of this very simple yet effective type of planning. They also offer a bare loan trust for those who wish to retain access to their capital.

Obviously, every client situation will differ and therefore it is essential to consider the client's income needs, availability to make gifts etc. before any recommendations are made.

More than one terminal gain in a tax year

There will be occasions when a client encashes more than one bond in the same tax year – perhaps as part of a comprehensive review of their investments. Advisers may find it useful to be aware that the application of the chargeable events regime is more complex than usual in these circumstances.

Furthermore, the final encashment of an incremented bond is sometimes treated in the same way as the encashment of multiple bonds in the same tax year. This article demonstrates the application of the chargeable event gain rules when more than one bond is encashed.

If an individual incurs two or more terminal gains on separate policies in the same tax year, the calculation of any additional income tax liability can become complicated. The first stage, however, is simply to add all the chargeable event gains together to obtain the 'aggregate gain' from all policies.

It follows that a higher rate taxpayer's position remains easy to determine. For an onshore bond, the policyholder has an additional liability to income tax of 20% of the total gains. For an offshore bond, where no credit is given for tax deemed to have been paid by the bond provider, the liability is 40% of the total gains.

However, the position is more complicated for a basic rate taxpayer who becomes a higher rate taxpayer because of the aggregated gains. This also applies to a client whose other income exceeds the basic rate threshold but who may be able to obtain a basic rate extension for pension contributions. It is then necessary to calculate the aggregate slice and the average number of relevant years.

Director's perks

Shareholding directors can normally choose the route(s) by which they extract profits from their business; for example using a combination of dividends, salary/bonus and pension contributions. Taking as much as possible as dividends has always been a popular strategy because it avoids paying employer and, to a lesser extent, employee national insurance contributions.

For many family businesses, the Arctic Systems case has complicated matters. The final judgement by the House of Lords is expected anytime now. It will be some time after this before the uncertainty is removed and we know how the Revenue intends to proceed – if indeed the appeal is unsuccessful.

For some clients we also need to bear in mind the Revenue's IR35 statement affecting directors of 'service companies'. The effect of IR35 is that dividend payments will tend to be ineffective as a means of reducing tax and NI liability where the individual is a director of a service company, an 'intermediary' firm X providing services to firm Y, but to all intents and purposes would otherwise be classed as an employer of firm Y.

In the meantime we should remember that the **director's 'perk'** of having control over the structure of his or her own remuneration package, is not limited to reducing the business' liability for NICs. Advisers also need to consider the impact on income and corporation tax liabilities – in addition of course to the personal circumstances and objectives of the director.

Key findings on Employee Benefits (based on a recent survey)

77% of employers feel responsible for employees' long term financial wellbeing.

72% do not measure the return on investment on pensions.

34% say they should educate staff on pensions but don't.

42% have considered introducing auto-enrolment to boost take up of their defined contribution pension scheme.

50% believe government proposals for 2012 for auto-enrolment and compulsory employer contributions of 3% will have no effect on their organisation's scheme(s).

10% plan to increase staff contributions to their staff scheme.

56% have made no changes to their scheme in light of age discrimination legislation.

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You should be aware that investment in securities involves risk. The value can fall as well as rise and you may not get back the full amount invested, particularly in the earlier years.

Taxation: All statements relating to taxation are based upon our understanding of the law and HM Revenue & Customs practice in force at the date of this report. There can be no guarantee that the tax position or proposed tax position at the time of investment will endure indefinitely.