Is it Safe Yet?

Mark McLaughlin looks at the time limits for HMRC to collect inheritance tax underpayments.

Taxpayers generally seek finality in their tax affairs as soon as possible, so that they need not worry about unwelcome HMRC enquiries and the possibility of unexpected tax liabilities.

The tax system provides some degree of finality, including time limits for HMRC to issue tax assessments. For example, for income tax and capital gains tax (CGT) purposes, there are four main time limits for HMRC to issue assessments:

• a normal time limit of four years after the end of the tax year to which it relates (TMA 1970, 34(1));

• a six-year time limit where a loss of tax has been brought about carelessly;

• a 12-year time limit where the lost tax involves an offshore matter or an offshore transfer which makes the lost tax significantly harder to identify (TMA 1970, s 36A); and

• a 20-year time limit where the taxpayer brought about the loss of tax deliberately (TMA 1970, s 36(1), (1A)).

There are also four, six and 20-year assessment time limits for corporation tax purposes (FA 1998, Sch 18, para 46).

Aside from discovery, it is sometimes overlooked that where a taxpayer fails to notify HMRC of chargeability to income tax or CGT, the time limit is 20 years after the end of the relevant tax year; the normal four and six-year time limits do not apply (TMA 1970, s 36(1A)(b)).

Is that clear?

The inheritance tax (IHT) compliance regime differs significantly to self- assessment compliance for income tax and CGT purposes.

Achieving finality in respect of an individual’s estate on death normally involves applying to HMRC for a ‘clearance certificate’ on a form IHT30 (which can be downloaded from HMRC’s website: tinyurl.com/HMRC-IHT30).

If HMRC gives clearance, it normally discharges the taxpayer from further liability to tax on the assets specified in the certificate (but see below).

The application can only be submitted when the person liable for the IHT is sure (to the best of their knowledge) that there will be no further changes to the asset values submitted to HMRC,

and that all material facts have been disclosed. The person(s) who are liable for IHT will normally be the personal representatives for property passing under the deceased's will or intestacy, or trustees for property in a settlement. They will generally need to wait at least two years from the transfer, although HMRC have discretion to consider a clearance application within the two-year period (IHTA 1984, s 239).

However, HMRC's policy is to refuse to give clearance in respect of an immediately chargeable lifetime transfer, as the subsequent death of the transferor may bring failed potentially exempt transfers into cumulation (see HMRC's Inheritance Tax manual at IHTM40011).

In addition, HMRC will treat an application for a clearance certificate as

premature unless all the following conditions are satisfied (see IHTM40101):

• the value of the property to which the application relates is finalised.

• all the tax on that property has been paid, or is being paid by instalments.

• the value of all aggregable property (e.g., joint property, qualifying interests in possession in settled property and gifts) is finalised.

• the applicant has no potential liability to tax in respect of gifts.

Whilst a clearance certificate means that the taxpayer will not normally have to pay any further tax on the transfer disclosed in the certificate, it will not provide taxpayers with protection from HMRC collecting additional IHT in certain circumstances. These include where there has been fraud or a failure to disclose material facts (IHTA 1984, s 239(4)), such as where there is evidence to suggest that proper consideration was

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IHT time limits

In terms of IHT time limits and finality, the general rule is that there is no liability to pay additional IHT on any property after four years from the later of the date on which the payment (or for instalments, the last payment) was made and accepted, and the date on which the tax (or the last instalment) became due where the tax attributable to that property was paid in accordance with an IHT account delivered to HMRC and the payment was made and accepted in full satisfaction of the IHT (IHTA 1984, s 240(2)).

However, there are exceptions to this general rule for what the IHT legislation describes as 'underpayments', which broadly means a loss of IHT. If the loss was brought about carelessly, the time limit for bringing proceedings to recover any additional IHT is six years. The term 'carelessly' is defined as a failure to take reasonable care to avoid the loss.

Furthermore, if an error is subsequently found in information submitted to HMRC and reasonable steps are not taken to inform HMRC, any loss of tax brought about by the inaccuracy is treated as having been brought about carelessly (IHTA 1984, s 240A(3)).

An extended time limit of 12 years applies to IHT underpayments involving an offshore matter, or an offshore transfer that makes the lost tax significantly harder to identify (IHTA 1984, s 240B). These provisions are broadly similar to the extended time limit provisions for income tax and CGT purposes. This 12-year time limit for IHT purposes overrides the normal four or six-year time limits.

However, it does not apply to an offshore tax loss where a longer time limit applies. A longer time limit applies if the loss of tax was brought about deliberately; in those cases, the time limit is extended to 20 years.

There's no limit Although not expressly stated in the legislation, HMRC considers that there is scope to collect IHT underpayments beyond even the 20-year time limit.

The normal IHT time limits apply where a return has been submitted to HMRC, and payment has been made in full satisfaction of the IHT attributable to the return. Where no IHT return has been submitted, the normal time limits are extended to 20 years from the date of the chargeable transfer. This time limit applies if the loss of tax was not brought about deliberately by the person liable for the tax, or by a person acting on their behalf such as an agent (IHTA 1984, s 240(6), (7)).

However, it is implicit from the legislation that if no IHT return was submitted and the loss of tax was brought about deliberately, there is no time limit for HMRC to recover the tax underpayment.

Furthermore, HMRC's guidance points out that a 20-year time limit generally applies if an IHT return was submitted but the return omitted an asset, where there is consequently an unpaid IHT liability in respect of that asset. However, if the omission (and so the loss of tax) was deliberate, there is no time limit for the recovery of the unpaid tax (see IHTM30462).

Proceed with caution

Consequently, great care is needed when submitting IHT returns. If an IHT return has been overlooked, or if an asset was omitted from an IHT return that was submitted some time ago, consider the position carefully. This is particularly important if HMRC are seeking to proceed on

the basis that the non- submission of the return or the asset omission was deliberate, since it could have far-reaching implications.

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