

Briefing document

HMRC consultation on trust taxation

Introduction

On 7 November 2018 HMRC launched a consultation on the taxation of trusts. The consultation is broad in nature, and HMRC intend to consider trust taxation as a whole. At this early stage of the consultation, HMRC have summarised the government's policy principles underlying the review, and some specific areas of taxation which they would like to consider.

The consultation closes on 30 January 2019. Once the government have considered the responses they have received, a further consultation will be held on a specific proposal for reform. The consultation document does not specify a date from which any changes will be implemented.

Our view

Trust taxation can be complicated, and so any simplification would be welcome. However, substantial changes have been made to the taxation of trusts in recent years, particularly non-UK trusts, and so a period of stability would also be welcome.

The government's policy principles

The consultation document summarises the policy principles underpinning the review, which are:

- **Transparency** – so as to prevent the ownership of funds or assets being hidden, and so that HMRC can ensure that trusts do not offer the opportunity to avoid or evade UK taxation.
- **Fairness and neutrality** – Trust taxation should be fiscally neutral, and so neither encourage nor discourage use of trusts. In particular, trusts should not offer tax avoidance opportunities.
- **Simplicity** – Of both taxation and administration. Specifically, the administration associated with trusts should not act as a disincentive to use of trusts, in circumstances where using a trust is appropriate. In addition, the administrative processes in place should serve to reduce the risk of error.

Transparency

The UK has various registers which require beneficial ownership to be recorded. At present, due to the application of the EU's Fourth Money Laundering Directive (4MLD), trusts that have a liability to one of a number of specified UK taxes and which meet certain other requirements must provide 'beneficial ownership' information to HMRC. HMRC then retains this information on a non-publicly available register. The information required goes beyond information relating to beneficiaries and when they may or may not benefit from the trust and also, for example, requires details of the settlor to be disclosed to HMRC for recording on the register.

The existing trust register is expected to be expanded by March 2020 in order to comply with the EU's Fifth Money Laundering Directive (5MLD). This will substantially increase the number of trusts that need to register, as the registration requirements will also encompass trusts that do not have a UK tax liability. 5MLD is broad in nature and its implementation will also affect other types of entity, such as companies. The implementation of 5MLD into UK law will be subject to a separate consultation over winter 2018/19, so details of the revised register are not included in the trust taxation consultation document.

In addition to the above, beneficial ownership information is increasingly being shared internationally. This includes, for example, the Common Reporting Standard, under which over 100 jurisdictions have agreed to share information, and the requirement under 5MLD for the EU Member States' beneficial ownership registers to be interconnected by March 2021. These points are not part of the current consultation.

Taxation of trusts: points of consideration

Scope of UK taxation

UK resident trusts are within the scope of taxation on worldwide income and gains. Trusts are UK resident if, either, all of the trustees are UK resident, or if at least one trustee is UK resident and the settlor was UK resident and/or UK domiciled when the trust was established or property added.

Non-UK resident trustees are, broadly, subject to taxation on UK income and certain capital gains, such as gains arising on disposal of UK residential property (and also non-residential UK property, from April 2019).

The government seeks views on whether the current system is appropriate, though acknowledges that any changes would fundamentally change trust taxation policy, so change would only be warranted if it constitutes a significant improvement over the current system.

Use of non-UK trusts

The government would like to understand why trusts are used, and, specifically, why an individual who is UK resident and/or UK domiciled might choose to use a non-UK resident trust instead of a UK resident one. Views are therefore sought on this point, with specific reference to whether non-UK resident trusts may be used for tax avoidance or evasion purposes.

Taxation and neutrality

As noted, it is government policy for trust taxation to be neutral. The key question here is: neutral compared to what? The position if the settlor had retained personal ownership of the settled assets or the position if assets were given outright to beneficiaries? If the latter, how would this be determined in cases where trustees have discretion over which of the beneficiaries, if any, benefit from the trust?

This point will be considered as part of the consultation, with specific reference to:

- Nil rate band trusts, where individuals settle amounts up to the available nil rate band into trust every seven years (i.e. the maximum amount that can be given to trusts without an immediate inheritance tax charge arising, in the absence of other reliefs and exemptions).
- Inheritance tax charges payable by affected trustees every ten years. HMRC consulted on simplifying this area of trust taxation in recent years, but no substantive changes were made.
- Trusts created under a will, to which some or all of the property an individual held on death is added.
- Private residence relief for capital gains tax, which is available to trustees where a trust property is occupied by a trust beneficiary as their only or main residence and certain other conditions are met. There is no requirement for the proceeds on disposal of the property to be used for the benefit of the individual who occupied the property as a home, and it is this which HMRC wish to consider.
- Trust management expenses, which may be deductible for income tax purposes.
- The taxation of capital receipts received by trustees, compared to the income tax position of income receipts and or amounts received by beneficiaries personally.
- Trusts and transactions which are declared void by the courts, which may occur in certain circumstances, such as where a mistake was made when a trust was set up.

Administration

HMRC are also considering ways in which trust administration could be made simpler, particularly for trusts with a low level of income or for inheritance tax reporting of ten year charges payable by trusts.

Find out more...

This note reflects the law in force as at 7 November 2018, and HMRC consultation document entitled The Taxation of Trusts: A Review, published on the same date. Please be aware that this note does not cover all aspects of this subject. To find out more about any aspect of the above, please discuss with your usual Deloitte contact. If you do not have a usual contact, please contact Patricia Mock (pmock@deloitte.co.uk).

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