

## CHAPTER 9

### APR AND BPR ON DEATH

#### 9.1 Death tax on chargeable lifetime transfers

In this chapter, we shall look at how we calculate death tax on a lifetime transfer, when the original gift was a gift of either agricultural or business property. We will start by looking at BPR and APR on chargeable lifetime transfers.

When an individual makes a gift of business property to a discretionary trust, **BPR has to be taken into account when calculating the lifetime tax**. BPR is given before annual exemptions in arriving at the chargeable lifetime transfer. If the donor dies within 7 years of making the gift to the discretionary trust, additional tax will be payable by the trustees. We need to deal with the BPR when calculating the tax on death.

Even if agricultural or business property relief was given on the lifetime transfer, it does not necessarily mean that the same relief will be available to the trustees on death. In **certain instances, APR or BPR given on a lifetime transfer will be withdrawn on the death** of the donor. This withdrawal of relief will most commonly occur if the **trustees sell or give away** the agricultural or business property before the donor dies.

As a general principle, in order for the trustees **to receive APR or BPR** to reduce the death tax, they **must have retained the property** until the death of the donor.

[IHTA 1984,  
s.113A](#)

A **withdrawal** of relief will also occur if the **property no longer qualifies for APR or BPR** at the time of the donor's death. For example, if a donor gives shares in an unquoted trading company to a discretionary trust, BPR at 100% will be available to reduce the value of the lifetime transfer. However if the **unlisted company subsequently becomes listed** on the Stock Exchange, the trustees will hold quoted shares at the date of the donor's death. In this instance BPR will be withdrawn as the trustees no longer own "relevant business property".

[IHTA 1984,  
s.113A](#)

There is one occasion when a sale of the assets by the trustees will **not lead to withdrawal** of business or agricultural property relief. If the trustees sell the assets, then **subsequently replace them within three years with other business or agricultural property**, BPR or APR is retained on the donor's death. In order to preserve the APR or BPR, the trustees must reinvest the whole of the original proceeds of sale.

[IHTA 1984,  
s.113B](#)

A **withdrawal** of BPR will **increase the tax payable** by the trustees on the donor's death. It will **not affect the original calculation of the lifetime tax**, which remains undisturbed.

**Illustration 1**

Michael owns a building which is used by a company under his control. In June 2005 he gave that building to a discretionary trust when it was worth £600,000. The transfer will qualify for 50% business property relief. After deducting two annual exemptions, Michael has a chargeable lifetime transfer of £294,000, subject to lifetime tax as below:

	£
Gift (June 2005)	600,000
Less: BPR @ 50%	<u>(300,000)</u>
	300,000
Less: AE 2005/06	(3,000)
Less: AE 2004/05	<u>(3,000)</u>
Chargeable lifetime transfer	294,000
Nil band 2005/06 (fully available)	<u>(275,000)</u>
Taxable	<u>19,000</u>
IHT @ 20% (paid by trustees)	<u>£3,800</u>

As you will see, BPR has been taken into account in calculating the lifetime tax.

In October 2008 the trustees sell the building. The sale proceeds are reinvested by the trustees into unit trusts. In May 2010, Michael died. We need to calculate additional tax on the CLT as a result of the donor's death within seven years, paying particular attention to the business property relief.

When calculating the death tax in May 2010, we start with the chargeable lifetime transfer which, after BPR and exemptions, was £294,000.

However as the building is not owned by the trustees at the date of the donor's death, any lifetime business property relief will be withdrawn on death. The sale of the building by the trustees will lead to a withdrawal of BPR, because the trustees did not reinvest their sale proceeds in other business property - they used the money to purchase unit trusts.

The way BPR is withdrawn on death is by increasing the chargeable transfer by the amount of the lifetime BPR given. Therefore the amount chargeable on the trustees at the date of death increases by £300,000, and is now £594,000.

Death tax - May 2010:	£
CLT	294,000
Add: BPR withdrawn (property not owned by trustees at date of donor's death)	<u>300,000</u>
Chargeable to IHT	<u>£594,000</u>

To calculate the additional tax on death, we deduct the nil band on death and multiply the excess by 40%. As there are more than three years between the date of the gift and the date of death, taper relief will be available.

Finally we can take a deduction for the lifetime tax paid on the original gift (£3,800) leaving additional tax payable by the trustees.

Chargeable to IHT	<u>£594,000</u>
£(594,000 - 325,000) @ 40%	107,600
Less: taper relief (4-5 years = 40%)	<u>(43,040)</u>
	64,560
Less: lifetime tax on CLT	<u>(3,800)</u>
Extra tax due	<u>£60,760</u>

The withdrawal of BPR on death has increased the tax payable by the trustees, but has had no effect on the original lifetime tax computation.

## 9.2 Effect on donor's cumulative total

[IHTA 1984,  
s. 113A\(2\)](#)

When APR or BPR is withdrawn on a chargeable lifetime transfer - for instance as a result of a sale by the trustees - the original transfer will remain on the donor's "clock" for IHT purposes.

The **original figure in the donor's cumulative total is not affected by any subsequent withdrawal** of BPR at death.

### Illustration 2

In the above illustration, in June 2005 Michael made a chargeable lifetime transfer (after BPR and exemptions) of £294,000. Even though the BPR was withdrawn when calculating the death tax payable by the trustees, this original transfer of £294,000 remains on Michael's "clock" for cumulation purposes.

Therefore, if Michael made another lifetime transfer after June 2005 (e.g. a PET before death) when calculating the tax on this PET we need to take account of Michael's brought forward total, which here would be £294,000.

Let us assume Michael made a PET in July 2008 (after annual exemptions) of £50,000. The PET would be chargeable on Michael's death in May 2010.

To calculate the tax we start with the nil band at the date of death of £325,000. Michael's chargeable transfers in the seven years before the gift are £294,000. This is what we mean by the original transfer remaining on the donor's "clock". £31,000 of the nil band remains, leaving £19,000 of the PET to be charged to inheritance tax.

	£	£
PET (July 2008)		50,000

Nil band at death	325,000	
Less: chargeable transfers in 7 years before PET (i.e. original CLT June 2005)	<u>(294,000)</u>	
Nil band remaining		<u>(31,000)</u>
Taxable on death		<u>£19,000</u>
IHT @ 40% (no taper relief)		<u>£7,600</u>

### 9.3 Death tax on potentially exempt transfers

When an individual makes a gift of business or agricultural property to another individual - i.e. he makes a **PET** for IHT purposes - we **ignore the APR or BPR during the lifetime** of the donor. This is for the simple reason that there is **no lifetime tax on a PET**, so the amount of any APR or BPR does not need to be considered.

We only need to think about the effect of APR or BPR if the PET becomes chargeable as a result of the donor's death within seven years.

As a general principle, if the **donee has retained** the agricultural or business property at the date of the donor's death, when calculating the donee's death tax we would **give an appropriate amount of APR or BPR**.

If the **donee had sold the property** before the death of the donor, **no BPR or APR will be available to reduce the death tax**. BPR or APR will be retained if the donee sells the original property and uses the whole of the sale proceeds in purchasing a replacement.

Similarly if the **assets no longer qualify** as relevant business or agricultural property at the donor's death - for example if unquoted shares become listed on the Stock Exchange - **BPR will be denied** on death. Note here we are not taking away any APR or BPR previously given. No APR or BPR is actually given against a PET whilst the donor is alive. At the point of death, we simply make a decision as to whether any APR or BPR is or is not available.

**Illustration 3**

Laura owns 10,000 shares in James Ltd, an unquoted trading company. In August 2005, Laura gave the shares to her son when they were worth £500,000. This gift is a PET for IHT purposes. The gift will potentially qualify for BPR, depending on what the son does with Laura's shares.

The PET **will use** any available annual exemptions, despite the fact the transfers of unquoted shares qualify for 100% BPR.

As this is a PET, there is no lifetime tax to consider. There is no point in allocating BPR against the value of the transfer. BPR only needs to be considered if Laura dies within seven years of the gift.

In July 2008, Laura's son sells 8,000 shares in James Ltd for £600,000. He uses the money to buy a house.

In June 2010 Laura dies. The PET in August 2005 now becomes a chargeable transfer, and Laura's son has a possible IHT liability. We will explore the availability of BPR in calculating this death tax.

BPR will only be available on the shares retained by the son at the date of Laura's death. The son sold 8,000 of the 10,000 shares in July 2008. Therefore he has retained 2,000 shares out of the 10,000 originally gifted. Therefore 2/10ths of the value of the initial transfer will qualify for BPR.

	£
PET = chargeable on death	500,000
Less: BPR on shares retained by son at donor's death	
$\frac{2000}{10000} \times £500,000 \times 100\%$	<u>(100,000)</u>
	400,000
Less: AEs x 2	<u>(6,000)</u>
Chargeable to IHT	<u>394,000</u>

As this was Laura's only lifetime transfer, the full nil band of £325,000 will be available on death. As there are just under 5 years between the date of gift and the date of death, this tax can be reduced by 40% taper relief.

Chargeable on death	<u>£394,000</u>
Tax £(394,000 - 325,000) @ 40%	27,600
Less: taper relief (4-5 years = 40%)	<u>(11,040)</u>
Tax payable by donee (son)	<u>16,560</u>

Therefore if a donee receives a gift of business property from a donor, for tax planning purposes it is important that the donee does not sell the property until after the donor has died. In this instance, the sale of the shares by Laura's son in July 2008 has had the effect of generating a substantial IHT charge on Laura's death.

#### 9.4 Effect on cumulative total

We need to consider the effect that a denial of BPR will have on the donor's cumulative total. In the case of PETs, the new figure - i.e. the **amount of the PET ultimately charged to inheritance tax - goes on to the donor's IHT clock for cumulation purposes.**

##### Illustration 4

In the previous example, Laura made a gift of shares to her son in August 2005.

Laura died in June 2010 such that this PET became chargeable. As the son had retained 20% of the shares, £100,000 of BPR was given on death. After taking two annual exemptions, a PET of £394,000 was chargeable on death. It is this figure that will cumulated for inheritance tax purposes.

Therefore if Laura was to have made another lifetime gift between August 2005 and the date of death, when calculating tax on death her seven year cumulative total will be £394,000.

Therefore when calculating any IHT payable by the donee of a later gift, we would look back seven years and see that this previous transfer had utilised the whole of Laura's nil band.

**This is a very important distinction.**

When BPR is withdrawn on a chargeable lifetime transfer, the original transfer remains on the clock for cumulation purposes.

However in the case of a potentially exempt transfer, when BPR is denied on death it is this **new** figure - i.e. the amount chargeable to inheritance tax - that goes into the donor's cumulative total.

#### 9.5 Miscellaneous points

As a general rule, the donee must hold relevant business property at the date of the donor's death if BPR is to be given when calculating death tax. This does **not** apply if the original gift was shares in a **quoted trading company.**

For example, assume a taxpayer has a 51% holding in a quoted company (Q Plc). The donor gave a **1% holding** in the company to a discretionary trust.

When calculating tax on this chargeable lifetime transfer, BPR would be due at a rate of **50%** because the donor had made a transfer out of a **controlling holding in a quoted trading company**.

The donor dies and additional tax is payable by the trustees. What the trustees actually **own** at the donor's death is a **1% holding** of shares in Q plc. A 1% holding of shares in a quoted trading company is **not** relevant business property for BPR purposes. However, when calculating the additional tax on death, **none of the BPR will be withdrawn because the original gift was shares in a quoted trading company**.

[IHTA 1984,  
s. 113A\(3A\)](#)

### Example 1

Paul made the following lifetime gifts:

May 2003	1,000 shares in Widget Co Ltd to his son. The shares were worth £120,000 at date of gift
August 2004	£228,000 cash to discretionary trust.

Paul's son sold all the Widget Co Ltd shares in July 2008. Paul died on 20 April 2010.

**Calculate the IHT due as a result of Paul's death.**

### Example 2

Samantha gave her 1% holding of shares in ABC Ltd to a discretionary trust in November 2008. The shares were worth £340,000 at the date of the gift.

ABC Ltd became listed on the Stock Exchange in 2009. Samantha died in September 2010.

**Calculate the tax payable by the trustees on Samantha's death.**

**Answer 1**

- (i) Gift to son (May 2003)

	£
Gift	<u>120,000</u>
PET	
Potential BPR	
Uses AEs for 2003/04 & 2002/03	

- (ii) Gift to discretionary trust (August 2004)

	£
Gift	228,000
Less: AE 2004/05	<u>(3,000)</u>
CLT	225,000
Nil band 2004/05 (fully available)	<u>(263,000)</u>
Taxable	<u>Nil</u>

Note: the PET in May 2003 does not use up the nil band as it is not a chargeable transfer at this point.

Death tax:

- (i) PET (May 2003)  
 Chargeable on death  
 No BPR available as son sold all of the shares before donor's death.

	£
Gift	120,000
Less: BPR (denied)	<u>Nil</u>
	120,000
Less: AE 2003/04	(3,000)
Less: AE 2002/03	<u>(3,000)</u>
Chargeable transfer	114,000
Nil band at death (fully available)	<u>(325,000)</u>
Taxable	<u>Nil</u>

No tax payable by donee (son)

## (ii) CLT (August 2004)

	£	£
CLT		225,000
Nil band at death	325,000	
Less: chargeable transfers		
7 years before CLT (= PET May 2003)	<u>(114,000)</u>	
Nil band remaining		<u>(211,000)</u>
Taxable		<u>£14,000</u>
IHT @ 40%		5,600
Less: taper relief (5-6 years = 60%)		<u>(3,360)</u>
Payable by trustees		<u><b>2,240</b></u>

## Note:

The "new" PET (i.e. after BPR denied on death) is on the donor's "clock" for cumulation. It therefore uses up part of the nil band when calculating death tax on the CLT.

**Answer 2**

No lifetime tax on CLT - 100% BPR

BPR withdrawn on death - shares no longer "relevant business property".

	£
Original CLT	Nil
Add: BPR withdrawn on death	340,000
Less: AEs x 2	<u>(6,000)</u>
Chargeable on death	<u>334,000</u>
IHT £(334,000 - 325,000) @ 40%	<u><b>£3,600</b></u>
No taper relief as < 3 years	