

**EXPLANATORY MEMORANDUM TO**  
**THE INHERITANCE TAX (MARKET MAKERS AND DISCOUNT HOUSES)**  
**REGULATIONS 2012**

**2012 No. 2903**

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs (HMRC) and is laid before House of Commons by Command of Her Majesty.

2. **Purpose of the instrument**

2.1 This instrument extends business property relief ("BPR") from Inheritance Tax ("IHT") to businesses carrying on the business of a market maker, within the definition given by the Markets in Financial Instruments Directive (2004/39/EC), in a regulated market of a European Economic Area ("EEA") member state. It makes similar provision in relation to interest on instalments in relation to companies. The instrument inserts new provisions into the Inheritance Act 1984 ("IHTA") and includes associated regulations for the purposes of those new provisions.

3. **Matters of special interest to the Select Committee on Statutory Instruments**

3.1 None

4. **Legislative Context**

4.1 For IHT there are restrictions on the location of a business and a requirement for UK institutional recognition in order for IHT to not apply to shares in the business. To protect against possible abuse there is also the requirement for the business to be recognised by either the London Stock Exchange or the London International Financial Futures and Options Exchange (LIFFE).

4.2 These requirements have been challenged by the European Commission through their pre-infraction inquiry system on the grounds the rules may impose restrictions on the freedom of establishment and the free movement of capital. These regulations therefore provide for BPR and relief from interest on instalments to apply to a business or company within any EEA state. This is the first use of the powers under sections 106(5) and 107(5) of the Finance Act 1986 ("FA 1986").

4.3 Section 106(5) of the FA 1986 gives the Commissioners for Revenue and Customs (“the Commissioners”) the power to amend section 105 of the IHTA so as to secure that section 105(3) does not apply to businesses of a description set out in regulations; and section 107(5) of the FA 1986 gives the Commissioners the power to amend section 234(3)(c) of the IHTA to secure that companies of a description set out in regulations fall within that subsection. These Regulations insert new section 105(4A), and amend section 234(4)(c) of the IHTA for those purposes.

4.4 The Regulations then set out descriptions of a business for the purposes of the new section 105(4A) and companies for the purposes of the new section 234(3)(c)(ii). The descriptions are of businesses/companies carrying on the business of a market maker, within the definition given by the Markets in Financial Instruments Directive (2004/39/EC). To safeguard against the potential for abuse, the Regulations include the requirement for the business or company to hold itself out at all normal times in compliance with the rules of a regulated market which has been notified to the Commission and is recognised as doing so by that regulated market.

## **5. Territorial Extent and Application**

5.1 This instrument applies to all of the United Kingdom.

## **6. European Convention on Human Rights**

6.1 The Commissioners for Her Majesty’s Revenue and Customs have made the following statement regarding Human Rights:

In our view the provisions of the Inheritance Tax (Market Makers and Discount Houses) Regulations 2012 are compatible with the Convention rights.

## **7. Policy background**

- *What is being done and why*

7.1 Unquoted shares are generally exempt from IHT; they qualify for Business Property Relief (BPR). This ensures that viable businesses are not put at risk by the need to fund an IHT bill out of illiquid assets. But, to focus the relief effectively and to prevent abuse, BPR is not due on shares in companies whose business involves dealing in securities, stocks and shares. Without such a restriction straightforward investments could be enveloped in a corporate wrapper and avoid IHT.

7.2 However, there are two types of companies that deal in financial instruments whose shares can qualify for BPR. These are companies whose business consists wholly as acting as a ‘market maker’ or ‘discount house’. In each case, the shares or securities held by the company, and offered at quoted prices, are closer to trading stock than investments.

7.3 For its shares to qualify for BPR a company acting as a market maker or discount house must carry out its business in the UK. And, if it is a market maker, must be recognised by one of two London-based exchanges, The London Stock Exchange or LIFFE.

7.4 The Commission assert our rules may dissuade UK residents to invest or participate in certain business activities in other EU/EEA States as BPR related to these activities located in other EU/EEA States do not qualify for our IHT relief.

7.5 The Regulations open up the existing tax treatment to businesses within EEA States, with the safeguard that they comply with the rules of a regulated market.

7.6 Although the Regulations widen the position from the UK to EEA States, the impact of the change is not expected to be significant.

- **Consolidation**

7.7 There are no relevant instruments to consolidate.

## **8. Consultation outcome**

8.1 HMRC held a four week consultation period to assure the technical content of the Regulations.

## **9. Guidance**

9.1 These Regulations widen a relief rather than imposing a new liability to tax or obligation. Guidance to explain the new provisions will be available through the HMRC website.

## **10. Impact**

10.1 The impact on business, charities or voluntary bodies is negligible.

10.2 The impact on the public sector is negligible.

10.3 A Tax Information and Impact Note was published alongside the draft legislation and is available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk).

## **11. Regulating small business**

11.1 The legislation does apply to small business.

11.2 Although market makers and discount houses may well be small business, the legislation does not impose additional regulatory burden. The commercial objective of such businesses already requires them to operate within a regulated market.

11.3 As the regulated market restriction is in place to protect against potential abuse, exempting smaller market makers from this restriction would create a loophole for possible abuse by smaller companies.

## **12. Monitoring & review**

12.1 This policy may be kept under review through communication with taxpayer groups affected by the measure.

## **13. Contact**

Theresa Merkaj at HMRC Tel: 020 7147 0104 or email: [theresa.merkaj@hmrc.gsi.gov.uk](mailto:theresa.merkaj@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.