

**The Chartered Institute of Taxation**

**Advanced Technical**

**Inheritance Tax, Trusts & Estates**

**November 2021**

**Suggested solutions**

## 1. TED

### 1) Setting up the trust

#### **Inheritance Tax (IHT):**

This would be an excluded property settlement as created by Ted, a non-UK domiciliary (note 1), comprising non-UK situs shares and cash. This would not be a chargeable transfer for IHT purposes.

Note 1:

Ted has a domicile of origin in the Isle-of-Man (IOM) and as he intends to return there, he has not acquired a UK domicile of choice.

Ted has been UK resident since March 2011, so he has not acquired UK deemed domicile status (resident <15 years).

#### **Capital Gains Tax (CGT):**

The gift to the trust would be a deemed disposal for CGT.

As Ted is taxed on the arising basis the gain would be within his 2021/22 CGT annual exempt amount.

#### **Trust residence:**

If UK resident it would be taxable on its worldwide income and gains.

If non-UK resident it would be taxable only on its UK income and any gains on UK land.

A trust is UK resident if either:

- a) All the trustees are UK resident, or
- b) At least one trustee is UK resident, and the settlor was either UK domiciled or UK resident at the time of the settlement creation.

If either Muriel or Ted were trustees, their UK residence status would cause the trust to be UK resident, it would therefore be preferable for the trustees to be non-UK resident e.g. Betty and John.

The trustees would need to be seen to be making independent decisions not simply rubber-stamping Ted's decisions otherwise the trust could be deemed to be UK-resident. Ted may therefore wish to make a non-binding letter of wishes setting out his requests to the trustees.

### 2) Ongoing tax liabilities:

#### **IHT:**

As an excluded property trust, no principal or exit charges would apply to its foreign situs assets.

The loan to Gordon would be a UK-situs trust asset. However, at the time of the trust's first 10-year anniversary (TYA) there would be less than the nil rate band outstanding (£80,000). Consequentially, although there would still be a reporting requirement, there would be nil IHT payable.

In the event that the trustees forgave any loan amount this would constitute a capital payment to Gordon triggering an exit charge. The charge would be nil irrespective of the timing of the loan

forgiveness given that as an excluded property the settlement, a 0% rate would be applied in the first 10 years and also following the first 10-year anniversary given the small loan amount outstanding at that date. There would be a reporting requirement within six months of the end of the month of exit.

**Income Tax (IT):**

As a non-UK resident trust, it would not be subject to UK IT on its foreign income.

Income distributions:

The non-UK resident beneficiaries i.e. Charlotte, David and Freddie would not be subject to UK IT on their income distributions.

Gordon (UK resident and domiciled – note 2) would be subject to UK IT on his income distribution. This would be taxed as foreign non-savings income at 20%, 40% or 45% as appropriate. No foreign tax credit relief would be available.

Loan:

Gordon would be receiving a trust benefit (interest-free loan). The benefit's capital value would be calculated by applying HMRC's official rate of interest to the outstanding loan.

Gordon would be subject to income tax under s.731 ITA 2007 to the extent that the benefit is matched with accumulated relevant income in the trust (i.e., undistributed income).

If the benefit should exceed the trust's "relevant income" the excess would be matched with the trust stockpiled gains (see below) and subject to CGT.

If the benefit should not exceed relevant income the unmatched "relevant income" would be carried forward.

Any capital payments or benefits provided to the non-UK resident beneficiaries would not be matched with "relevant income" and would not therefore reduce the pool balance carried forward each year.

**CGT:**

As the trust would be non-UK resident the trustees would not be subject to UK CGT except in relation to UK land (which it does not hold).

As the trust would not be "settlor-interested" for UK-CGT purposes, s.86 TCGA 1992 would not apply to assess the trust gains on Ted.

Gordon would be assessable under s.87 TCGA 1992 in respect of distributions or benefits which could be matched with the trust's stockpiled gains.

S.731 ITA 2007 and s.87 TCGA 1992 interact such that where a benefit is received from the trust which takes the form of a capital payment then it is matched first with relevant income, and to the extent that there is excess benefit, then matched with stockpiled gains (see above for IT).

As the benefit would be wholly matched against the trust income pool, any gains arising to the trustees would be "unmatched" and therefore carried forward to be matched against any future capital payments made to Gordon on a LIFO basis (since 6 April 2018 capital payments to non-UK resident beneficiaries are not "matched" with "trust gains" nor do they reduce the stockpile of gains in the trust to carry forward).

S.87I TCGA 1992 is an anti-avoidance rule which means that if a capital payment should be made by the trustees to Charlotte, David or Freddie who then passed this on to Gordon, Gordon would be taxed on the trust gains as though the trustees had made the capital payment directly to him.

A supplementary charge would apply to the CGT arising on any gains matched to capital payments made outside the year of gain or the following year, being a minimum of 20% (year two), increasing by 10% each year to a maximum of 60% (year six).

### **Loan forgiveness**

To the extent that any amount of the loan to Gordon should be forgiven by the trustees at a future date, the amount forgiven would be treated in the same way as the loan benefit (above).

Note 2:

Gordon's domicile of origin is the IOM. He acquired a UK domicile of choice when he decided to live in the UK permanently.

## MARKING GUIDE

TOPIC	MARKS
<b>Setting up the trust:</b>	
<b>IHT:</b> Ted – non-domiciled (domicile of origin not displaced by domicile of choice, not deemed domicile), excluded property (non-UK-situs), no CLT (0.5 each)	1.5
<b>CGT:</b> Ted – arising basis < AE 2021/22	0.5
<b>Trust residence:</b> UK residence criteria (0.5), WW income & gains (0.5), not Muriel or Ted (0.5), non-UK R UK income/gains only (0.5) – Betty & John? (0.5)	2.5
Letter of wishes, anti-avoidance (deemed UK-R)	1
<b>PHS</b>	<b>0.5</b>
<b>Sub-total</b>	<b>6</b>
<b>Ongoing liabilities:</b>	
<b>IHT:</b> No principal or exit charges would apply on non-UK situs assets	0.5
Loan to Gordon = UK-situs asset	0.5
IHT principal charge – unlikely given repayment schedule (NRB available)	1
Exit charge to extent loan forgiven, reporting requirement only – nil IHT	1
<b>Income Tax:</b> Trust/non-UK R beneficiaries N/A (0.5 each)	1
Gordon = UK R & domiciled (0.5), –IT on cash as NSI (0.5). No foreign tax credit relief available (0.5)	1.5
s.731 ITA 2007 on “benefit” of loan 0.5, c/f pool 0.5, non-UK R future benefits not matched 0.5	1.5
<b>CGT:</b> Trust/Ted N/A – s.86 TCGA 1992 (0.5 each)	1
Gordon s.87 TCGA 1992, matching – loan (as for income) – 0.5, c/f excess benefits – 0.5, c/f unmatched gains LIFO 0.5, interaction s.731 ITA 2007 / s.87 TCGA 1992 (0.5) – loan benefit already fully matched against income (0.5), any gains c/f against future capital distributions (0.5)	3
non-UK R not matched, anti-avoidance s.87I, supplementary charge (0.5 each)	1.5
loan forgiveness – use of income pool/stockpiled gains (0.5), c/f excess benefit (if applicable) (0.5)	1
<b>PHS</b>	<b>0.5</b>
<b>Sub-total</b>	<b>14</b>
<b>TOTAL</b>	<b>20</b>

## 2. BARBARA WARDEN

### DISPOSAL OF SHARES IN AB LTD

Barbara personally holds more than 5% of the share capital of the company, which is 100% trading. She is an officer of the company meeting the minimum qualifying ownership period of two years. The trust is a qualifying interest in possession (QIIP) as it is an immediate post death interest (IPDI). The disposal of the shares by both Barbara and the trustees will therefore qualify for business asset disposal relief (BADR). The trustees do not need to hold 5% themselves as they may piggy-back on Barbara's entitlement.

The trustees' claim for relief will be a joint claim under s.169N TCGA 1992. Barbara needs to sign the claim as it will be her lifetime allowance of £1million that is used by the trustees.

Barbara's CGT liability will be £79,999 (Working A).

The CGT liability arising on the trustees will be £20,000 (Working B).

### WINDING UP OF THE TRUST

#### CGT

The beneficiaries of the trust would be absolutely entitled to trust assets as against the trustees. This would therefore be a chargeable disposal for CGT purposes.

The CGT arising on the appointment (Working C) would be payable by the trustees.

The trustees should withhold this amount from the cash due to the beneficiaries in order to fund the payment of the CGT.

To secure their position should there be any change in the CGT due as a result of any enquiry by HMRC, the trustees should either:

- 1) obtain indemnity from the beneficiaries for any additional tax that becomes due; or
- 2) place a legal charge over the properties transferred.

Alternatively, the trustees could request a post-transaction valuation check using form CG34 to secure HMRC agreement to the property values used.

On winding up, no holdover relief would be available under either s.165 TCGA 1992 as the trust assets are investments assets or s.260 TCGA 1992 as there is no immediate charge to IHT on that occasion (see below).

#### INHERITANCE TAX (IHT)

The appointment of assets to Barbara in satisfaction of the value of her life interest would not be a transfer of value for IHT purposes. The assets would form part of her estate both before and after the appointment.

The appointment of assets to James would be a \*potentially exempt transfer (PET) deemed made by Barbara. The assets would pass out of Barbara's estate and into James'.

The £3,000 annual exemption (AE) and that of the previous year may be available to the trustees to reduce the value of the PET. Barbara must give notice to the trustees within six months confirming their availability and the trustees' entitlement to the same.

If Barbara did not survive the appointment to James by at least seven years, the trustees would be primarily liable for any IHT arising on the failed PET. James, as remainderman, would have secondary liability to the extent of his share of the trust assets.

The maximum potential IHT liability should be calculated (Working D) and the trustees should hold that sum in reserve for seven years.

Alternatively, the trustees should obtain further indemnity from James or place a further legal charge over his property.

James should consider taking out a life insurance policy to cover his potential liability.

Taper relief would be available after three years to mitigate the potential IHT due.

## CONCLUSION

As can be seen above for an immediate charge to CGT of £215,000 there is the possibility of avoiding an IHT charge of £595,600 on Barbara's death.

Barbara would retain sufficient income for her needs without the accumulation of surplus income.

James would receive a large proportion of his inheritance and the income therefrom sooner rather than having to wait until Barbara's death.

On Barbara's death, James would not benefit from the CGT free uplift on the assets already appointed to him but would receive this on the commercial property retained by Barbara if this were to pass to him under Barbara's Will.

As the cash appointed to Barbara would have been fully utilised to pay the CGT on the property this would not increase her estate.

### Working A: Sale of shares - Barbara

Sale proceeds £800,000 less cost £10 = £799,990. CGT payable £799,990 @ 10% = £79,999.

Barbara's annual exemption has already been used by Barbara against gains taxable at higher rates of CGT.

### Working B: Sale of shares - trustees

Sale proceeds £240,000 less cost £40,000 = £200,000. CGT payable as follows:

£200,000 @ 10%	£	<u>20,000</u>
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The trust annual exemption has already been used.

### Working C: Capital gains tax liability

Assets	Probate Value	Market Value	Chargeable gain	Rate	CGT
	£	£	£	%	£
Cash (Note 1)		220,000	N/A	N/A	N/A
UK Commercial property (let)	160,000	360,000	200,000	20	40,000
UK residential property (let)	300,000	600,000	300,000	28	84,000
Investment portfolio		1,215,000	455,000	20	91,000
Total		<u>£2,395,000</u>			<u>£215,000</u>

Note 1:

Proceeds of AB Ltd £240,000 – CGT payable (Working B) £20,000 = £220,000.

**Barbara:**

Appropriation:

	£
Commercial property	360,000
Cash	40,000
Less CGT	<u>(40,000)</u>
Net assets received	<u>£360,000</u>

**James:**

Appropriation:

	£
Residential property	600,000
Investment portfolio	1,215,000
Cash	180,000
Less CGT	<u>(175,000)</u>
Net assets received	<u>£1,820,000</u>

**Working D:** Potential IHT liability arising on failed PET:

$(£1,820,000 - £6,000 (\text{AE} \times 2) - £325,000 (\text{nil rate band (NRB)}) = £1,489,000 @ 40\% = £595,600.$

Barbara has made no previous lifetime transfers to utilise her NRB.

She will not be entitled to a transferable nil rate band (TNRB) from her husband Anthony as he fully utilised this on his prior death.

Residence Nil Rate Band (RNRB)/Transferable Residence Nil Rate Band (TRNRB) will not be available as it will be a lifetime transfer.

## MARKING GUIDE

TOPIC	MARKS
<b>CGT on sale of AB Ltd</b>	
Disposal of shares qualifying for BADR. Barbara Working A (1), trustees Working B (1) Net Proceeds available for distribution after CGT (0.5)	2.5
Requirements met - minimum holding and qualifying ownership period – via Barbara (1), Trust IIP, Joint claim by Barbara and trustees (1), trust use of Barbara's lifetime allowance of £1 million (0.5)	2.5
Subtotal	5
<b>Winding up of Trust:</b>	
<b>CGT</b>	
Absolute entitlement as against trustees = CGT	1
Working C – CGT £215,000 (0.5 each element exc. cash)	1.5
Net appropriation (after CGT 1) Barbara, 2) James (0.5 each)	1
CGT liability of trustees – withholding cash to pay, indemnity/charge as security for increase in liability, CG34 (0.5 each, max 1)	1
No holdover s.165/s.260 TCGA 1992	1
<b>IHT</b>	
Barbara no transfer of value	0.5
James – PET by Barbara (0.5), Barbara's AE available (and PY) (1), Barbara notice in writing & timing (0.5)	2
Trustees primarily liable for IHT on failed PET, then secondary liability = remainderman (0.5 each)	1
Calculation potential IHT based on Barbara's cumulative totals – working D – net appropriation (1), full NRB, nil TNRB, no RNRB/TRNRB on lifetime transfer, @ 40% (0.5 each)	3
Trustees withholding cash to pay, indemnity/charge as security for increase in liability/additional liability (0.5 each, max 1), James – life insurance policy (0.5)	1.5
Possibility of taper after 3 years	0.5
Conclusion – higher skills	1
Subtotal	15
<b>TOTAL</b>	<b>20</b>

### 3. JONTY FELDSPAR

Calculation of the Inheritance Tax (IHT) arising on Jonty's death:

	£
Free estate	480,000
"annuity slice" - Note 1	<u>568,182</u>
Total	1,048,182
Less nil rate band (NRB) – Note 2	<u>(325,000)</u>
Balance	<u>£723,182</u>
IHT @ 40% due 30 April 2022 (or date IHT400 submitted if earlier)	<u>£289,273</u>
Payable by the administrator (Debbie) – Note 3:	<u>£132,468</u>
£480,000/£1,048,182 x £289,273	<u>£132,468</u>
Payable by the trustees:	<u>£156,805</u>
£568,182/£1,048,182 x £289,273	<u>£156,805</u>
Distribution:	£
Debbie £480,000 - £132,468 - Note 3	347,532
Trustees £568,182 - £156,805	411,377
HMRC	<u>289,273</u>
Total	<u>£1,048,182</u>

Note 1:

Jonty was entitled to a "free of tax" annuity of £20,000 from the Myles Feldspar Will Trust. This equated to a gross annuity (based on a current basic rate band of 20%) of £25,000 (£20,000 x 100/80).

As Jonty became entitled to the annuity on his brother's death the annuity represented a qualifying interest in possession (QIIP) and its capital value is aggregated with his death estate for IHT purposes.

The capital value of the annuity therefore needs to be valued at the date of Jonty's death.

S.50(2) IHTA 1984 provides that the value of his interest in the trust is the capital required to provide the annuity – the "annuity slice". The total value of the trust assets is apportioned between the deceased annuitant and the other beneficiaries according to their respective income entitlements. This is usually based on the income of the tax year prior to the annuitant's death.

The value of the trust assets was £1.5 million and the income for 2020/21 was £66,000.

The "annuity slice" is therefore valued at £568,182 (£1.5million x £25,000/£66,000).

Note 2:

Jonty had made no potentially exempt transfers nor chargeable lifetime transfers in the seven years prior to his death. He therefore had his full nil rate band (NRB) available.

He was never married and so the transferable nil rate band (TRNB) is not available.

He had no lineal descendants and so the residence nil rate band (RNRB) is not available in respect of his private residence.

Note 3:

Jonty died intestate. Under the intestacy rules Debbie is entitled to his estate as he has no surviving spouse nor children, his parents predeceased him and Debbie's father (his only sibling) also predeceased him. Debbie therefore inherits her father's entitlement per stirpes.

Scots Law:

Jonty died intestate under Scots law. As there is no surviving spouse, children or cohabitant there are no legal, prior or cohabitants rights to be considered. Under Scots statutory rules of intestacy (Succession (Scotland) Act 1964) Debbie therefore inherits as her father's representative per stirpes as both he (Jonty's only sibling) and both of Jonty's parents, have predeceased him.

IHT on the private residence may be paid by 10 equal annual instalments by the administrators of the estate.

The first instalment would be due on the normal due date of 30 April 2022.

A claim for the instalment option would need to be made within the form IHT400.

The instalments are interest bearing and interest will be charged from the original due date to date of payment.

The amount eligible for instalments is £110,390 (£400,000/£1,048,182 x £289,273).

As Debbie is the sole beneficiary of the free estate, she will be the administrator and so no indemnity or charge over the property is required.

#### MARKING GUIDE

TOPIC	MARKS
<b>IHT Liability:</b>	
"free of tax" annuity – gross up (0.5), "annuity slice" QIIP (0.5), calculation (1)	2
NRB, no RNRB, TNRB, TRNRB (no PETs/CLTs, no spouse, no lineal descendants) (0.5 each)	2
IHT @ 40%, due date (0.5 each)	1
Payable by administrator (Debbie), calculation – no security required (0.5 each)	1.5
Payable by trustees, calculation (0.5 each)	1
Distribution of estate – Debbie (0.5), trustees (0.5), IHT (0.5) max 1	1
Intestacy rules – no spouse, children, living parents, Debbie per stirpes from entitlement of Myles (predeceased sibling) = applicable for both E&W and Scots law	1
Instalment option applicable to private residence	0.5
<b>TOTAL</b>	<b>10</b>

#### 4. HENRY COTTERILL

Inheritance Tax (IHT) on lifetime gifts and on Henry Cotterill's death:

	Lifetime IHT	IHT on Death	Seven-year cumulation	Nil Rate Band (NRB) (Lifetime)	NRB on Death (Note 1)
		£		£	£
1 <u>10 February 2011</u>		>7yrs N/A	11 Feb 2004		
Cash 2011 settlement	250,000				
Annual exemption (AE) 10/11	(3,000)				
AE 09/10	(3,000)				
NRB				325,000	325,000
Value of CLT	244,000				
NRB utilisation	(244,000)			(244,000)	(244,000)
NRB c/f (Note 2)				£81,000	£81,000
2 <u>14 April 2016</u>			15 Apr 2009		
Gift of shares to 2016 trust	980,000	980,000			
Business property relief (Note 3)	(980,000)		-		
AE 16/17					
AE 15/16					
Value of CLT	-				
NRB utilisation	-				
		(81,000)			
NRB c/f (Note 2)				£81,000	£81,000
Value on death	899,000				
IHT at 40%	359,600				
Taper relief (TR) at 60% (5-6 years)	(215,760)				
<b>IHT due 31 March 2022</b>				<b>£</b>	<b>143,840</b>
<b>Payable by trustees</b>					
3 <u>23 June 2016</u>			24 Jun 2009		
Gift of shares to charity	1,050,000	1,050,000			
Charitable exemption	(1,050,000)	(1,050,000)			
Value on death	-	-			

4	<u>5 August 2016</u>		6 Aug 2009
	Gift to granddaughter on marriage	10,000	10,000
	Marriage exemption	(2,500)	(2,500)
	AE 16/17	(3,000)	(3,000)
	AE 15/16	(3,000)	(3,000)
	NRB utilisation		(1,500)
	Value of PET	1,500	NIL
	Value of failed PET on death		-
	NRB c/f		81,000
			79,500
5	<u>20 March 2018</u>		21 Mar 2011
	Gift of trading premises	300,000	300,000
	Business property relief (Note 4)	(150,000)	-
	AE 17/18	(3,000)	(3,000)
	NRB reinstated > 7 years		244,000
	Available NRB		244,000
	NRB utilisation		325,000
	Value of PET	147,000	323,500
	Value of failed PET on death		(297,000)
	NRB c/f		325,000
			26,500
6	<u>5 November 2018</u>		6 Nov 2011
	Gift of land	350,000	350,000
	APR (Note 5)	(75,000)	-
	AE 18/19	(3,000)	(3,000)
	NRB utilisation		(26,500)
	Value of PET	272,000	(26,500)
	Value of failed PET on death		320,500
	NRB c/f		325,000
	IHT at 40%	128,200	0
	TR @ 0% < 3years	-	
	<b>IHT due 31 March 2022</b>	<b>£128,200</b>	

**Payable by Philip**

Death Estate 28 September 2021 (Note 6)	5,765,000
BPR (Note 3)	-
Chargeable estate	
	5,765,000
<b>IHT @ 40% due 31 March 2022</b>	<b>£2,306,000</b>
<b>Payable by executors</b>	

Note 1:

No transferable nil rate band available against lifetime transfers chargeable on death/death estate.

No residence nil rate band/transferable residence nil rate band available as the death estate is valued in excess of £2.35 million.

Note 2:

Original value of CLT (post BPR) counted for purposes of NRB to be carried forward.

Note 3:

The original gift on 14 April 2016 qualified for 100% BPR as this was of shares in an unquoted trading company.

At the date of Henry's death there was a binding contract for sale of the shares which negates BPR under s.113 IHTA 1984 both in respect of the lifetime gift and of the shares held by Henry at the date of his death.

Note 4:

The original gift qualified for 50% BPR as Henry was a majority shareholder of an unquoted trading company in which the property was used. At the date of Henry's death, the property was retained by Flora but no longer qualified as "relevant business property" in her hands. She held no shares in the company. Relief is therefore negated under s113A(3)(b) IHTA 1984.

Note 5:

The original gift qualified for 100% APR on its agricultural value as Henry had inherited the land from his wife who had owned it since 1978 and therefore satisfied the seven year ownership period under s.120 IHTA 1984. At the time of the gift the land had been let for agricultural purposes for 10 years.

Philip had sold the land prior to Henry's death and had not replaced it. APR was no longer due despite it having been let for agricultural purposes during Philip's ownership.

N.B. Philip could acquire replacement property within three years of selling the original property i.e. by 31 January 2024 (or enter into a binding contract for purchase of replacement property within that time) in order to retain entitlement to APR. This would have to be for the entire consideration received i.e. proceeds less any professional costs less any CGT due.

IHT corrective form C4 would then need to be completed to claim the relief.

Note 6:

Henry's 60% holding is valued using the related property rules as he gifted a 20% holding to the Old Donkeys of Northumberland (a registered UK charity) and the charity still held these shares at the date of his death less than five years later. The value used is therefore £3.02 million x 60/80 = £2,265,000.

The estate value is therefore:

$$\text{£3,500,000} + \text{£2,265,000} = \text{£5,765,000}$$

## MARKING GUIDE

TOPIC		MARKS
Gift 1	2 x AE, Value of CLT, Use of NRB, NRB c/f (original value of CLT used)	2
Gift 2	<i>Life tax</i>	
	Value	0.5
	Recognise fully covered by BPR	0.5
	<i>Death tax</i>	
	BPR withdrawn	0.5
	2 x AE not applied as HMRC practice not to disturb	0.5
	IHT calculated at 40%	0.5
	Taper calculated at 60%	0.5
	Due date and payable by trustees	1
Gift 3	Value	0.5
	Gift to charity exempt on life and death	0.5
Gift 4	Marriage exemption life and death calcs	0.5
	<i>Life tax</i>	
	2 x AE	0.5
	<i>Death</i>	
	2 AE not reallocated to earlier gift	0.5
	Nil rate band set against	0.5
	NRB c/f	0.5
Gift 5	<i>Life tax</i>	
	BPR at 50%	0.5
	1 AE	0.5
	<i>Death</i>	
	Withdrawal of BPR	0.5
	Reinstatement of NRB gift 1 (>7 years)	0.5
	NRB set against	0.5
	NRB c/f	0.5
Gift 6	<i>Life</i>	
	MV with APR on ag value only	1
	1 AE	0.5
	<i>Death</i>	
	Withdrawal of APR, potential claim for reinv < 3 yrs of sale, form of claim, entire proceeds	2
	NRB set against	0.5
	NRB c/f	0.5
	IHT at 40%	0.5
	Payable by Philip	0.5
Death	Related property value	0.5
	Nil BPR	0.5
	IHT @ 40%	0.5
	Payable by executors	0.5
<b>TOTAL</b>		<b>20</b>

## 5. DEMELZA JOHNS

1) The trust satisfies the conditions of s.71D(6) IHTA 1984 i.e. it is an 18-25 trust:

- There is entitlement to income and capital at age 25 years
- The class of beneficiaries was closed before 5 April 2008 i.e. the trust is for the named beneficiaries Lily and Bess only.

### Inheritance tax consequences

	<u>Bess's share</u>
	<u>1 September</u>
	<u>2021</u>
	£
Initial value of whole fund	970,000
NRB at exit	(325,000)
Settlor's chargeable transfers in seven years prior	200,000
	<hr/>
	845,000
Notional IHT £845,000 x 20%	169,000
Effective rate = notional/Initial Value	17.423%
Actual rate = 17.423% x 30% x 28/40	3.659%
<b>Exit charge- Bess: £524,500 x actual rate</b>	<b>£19,191</b>

### Capital gains tax

The appointment of an asset from an 18-25 (or s71D) trust will trigger a CGT charge as it is a disposal by the trustees.

Because there is an IHT charge at the same time the gain can be held over under s.260 TCGA 1992 and no immediate charge to CGT arises. The transferee must agree to the hold over.

### Properties

On the original appointment to Lily, the commercial property and residential property will not have been disposed of by the trustees for CGT purposes. The two properties are undivided shares of a property, and so the case of *Crowe v Appleby* (1975) applies.

Where there is an undivided share of land, until the last beneficiary becomes absolutely entitled any interim beneficiaries are not considered to have become absolutely entitled to the asset as against the trustees.

As the trust is now terminated by the appointment to Bess, both Bess and Lily become absolutely entitled to their share in the properties.

The entirety of the properties are now treated as having been disposed of.

	Lily £	Bess £	Total £
<u>Residential property</u>			
Market value	250,000	250,000	500,000
Base cost	(100,000)	(100,000)	(200,000)
Gain	150,000	150,000	300,000
Holdover relief (note 1)		(150,000)	(150,000)
Annual exemption (note 2)	(3,075)		(3,075)
	146,925	-	146,925
Tax at 28%	<b>41,139</b>	-	<b>41,139</b>
<u>Commercial property</u>			
Market value	190,000	190,000	380,000
Base cost	(125,000)	(125,000)	(250,000)
Gain	65,000	65,000	130,000
Holdover relief (note 1)	-	(65,000)	(65,000)
Annual exemption	-	-	-
Tax at 20%	<b>13,000</b>	-	<b>13,000</b>

**Note 1:**

Holdover under s260 is available on Bess's share as there is a charge to IHT.

**Note 2:**

AE = trust annual exemption 20/21 (£6,150), divided by 2 as the settlor has made two settlements = £3,075. Set off here as maximises tax charged at 20%.

**Cash**

No gain accrues on the transfer of the cash.

**Shares**

The share portfolio is standing at a gain of £60,000-£52,000 = £8,000. Holdover relief will be available under s260 in respect of the gain, reducing Bess's base cost to £52,000 (plus the IHT exit charge attributable to the shares) on a future disposal. The claim will be made on a holding by holding basis.

- 2) The CGT position will be different on each half share.

Lily

Lily's gain would be calculated as half of the proceeds of sale (less incidental costs of disposal) less her base cost of £250,000, being the market value of the asset when it was received by her from the trustees. She would also be able to deduct any enhancement costs incurred by her since she received the property.

Assuming that Lily has lived there throughout as her principal private residence (PPR), any gain on disposal will qualify for relief and be exempt.

Therefore no CGT will be due on disposal.

Bess

Bess's gain would be calculated as half of the proceeds of sale (less incidental costs of disposal) less her base cost of £100,000. This being market value of £250,000 at the date of appointment less the gain heldover on appointment to Bess of £150,000.

She would also be able to deduct any enhancement costs incurred by her since she received the property.

A deduction will also be available under s260(7) for the IHT attributed to the asset, being £250,000/£524,500 x £19,191 = £9,147

No PPR relief would be available on the disposal because holdover relief was claimed on the transfer to Bess (s226A TCGA 1992).

Bess's annual exemption of £12,300 would be available to offset against the gain.

Any remaining gain will be mainly taxed at the residential property rate of 28%.

## MARKING GUIDE

TOPIC		MARKS
IHT	Bess's appointment	
	Initial value	0.5
	Less NRB	0.5
	Less previous gift	0.5
	Notional IHT at 20%	0.5
	Effective rate	0.5
	Actual rate calculation	0.5
	n/40 reducer	0.5
	applied to transfer value	0.5
CGT	appointment triggers a CGT charge as disposal by the trustees	0.5
	Accompanying IHT charge - s.260 TCGA 1992 holdover available and no immediate charge to CGT arises.	0.5
	recognise Crowe v Appleby (1975) applies – undivided share of land all disposed of at date of Bess disposal (ie not previously disposed). Applies to residential and commercial properties	1
	<u>Residential property gain</u> – calculation	0.5
	AE calculation and offset against residential gain on Lily's share	1
	Lily – no holdover as no IHT charge	0.5
	Tax at 28%	0.5
	Bess's share - Holdover under s260 is available (mark given above)	
	<u>Commercial property gain</u> – calculation	0.5
	Lily's share no holdover (mark given above)	
	Taxed at 20%	0.5
	Bess's share - Holdover under s260 is available (mark given above)	
	<u>Cash</u> - No gain accrues on the transfer of the cash	0.5
	<u>Shares</u> - calculation of gain	0.5
	Holdover relief claim available	0.5
<b>Subtotal</b>		<b>11</b>
b.	Lily – half of proceeds less costs of disposal less base cost less enhancements	0.5
	Lily - Principal private residence relief is available in full –	0.5
	Bess – calculation of gain as half of proceeds less costs of disposal less base cost less enhancements (mark given above for basic computation)	
	Bess - Base cost is market value at receipt less the holdover claim	1
	Bess: deduction for IHT suffered on transfer s260(7) - $250k/524,500 \times 19,191 = £9,147$ or description of how the deduction is arrived at	0.5
	Bess: Principal private residence relief is not available because holdover relief was claimed on the transfer to Bess (s226A TCGA 1992)	1
	@28% or 18% (residential rate)	0.5
<b>Subtotal</b>		<b>4</b>
<b>TOTAL</b>		<b>15</b>

## 6. KESHAV MAVJI

### Post-mortem relief

There are two possible relevant claims for post-mortem relief available to the executors.

These are claims under s179 (Quoted shares/open ended investment companies) and s176 IHTA 1984 (related property) and are set out below.

#### Quoted shares/open ended investment companies (OEIC)

IHT relief is available if the executors sell quoted shares or OEIC shares at a loss within 12 months of the date of death.

The loss will reduce the value of the estate for IHT purposes and will generate an IHT refund where IHT has been paid.

The sales of all quoted /OEIC shares in the 12-month period must be considered even if they stand at a profit and this will be netted off against the loss.

Any purchases of quoted /OEIC shares within two months after the last sale made within the 12-month period will restrict the loss.

Gross proceeds should be used, and sales costs ignored.

Available claim under s179:

	Valuation £	Proceeds £	profit/(loss) £
Underhill plc	256,000	150,000	(106,000)
Big Bank plc	127,888	130,000	2,112
Pharmaceutical plc	49,078	55,000	5,922
Net loss	<hr/> <u>£(97,966)</u>		

IHT refund due £97,966 x 40% = £39,186.

Notes:

1. The shareholding in the family investment companies are not quoted and so are excluded from the claim.
2. Telecom plc was sold more than 12 months after death and so is also excluded

#### Related Property – s176

A claim under this section is available where assets have been valued under the related property rules in s161 IHTA 1984 and are sold within three years of death. There are two further conditions for a claim - the assets must be sold to an unconnected third party and the gross proceeds of sale must be less than the original value charged to IHT. For the purpose of the claim, each asset is looked at in isolation.

Wind in the Trees Ltd:

There is no claim available as the gross proceeds of sale exceed the related property value i.e. £380,000 / 2 = £190,000 < £200,000.

Sand and Leaves Ltd:

The claim will be permitted as the gross proceeds of sale (£450,000) are lower than the related property value (£1.4 million/2). The latter value of £700,000 will be replaced with the non-related property value of £600,000 at the date of death but the loss on sale is not relevant.

The IHT refund will be £700,000 - £600,000 = £100,000) @ 40% = £40,000.

**R185 entries for Annie and Girish – year ended 5 April 2021:**

	Gross income	Tax deducted	Net income	Expenses	Distributable Income	Distribution to Girish*	Distribution to Annie	Income C/f
	£	£	£	£	£	£	£	£
Rents	20,777	(4,155)	16,622		16,622	8,311	8,311	0
Interest	3,782	(756)	3,026		3,026	1,189	1,513	324
Dividends	12,189	(914)	11,275	(2,500)	8,775		4,176	4,599
Total			£30,923			£9,500	£14,000	£4,923
				Net Tax Credit				
				£	£			
Girish	Non-Savings	8,311	2,078					
	Savings	1,189	297					
	Dividends	0	0					
				Net Tax Credit				
				£	£			
Annie	Non savings	8,311	2,078					
	Savings	1,513	378					
	Dividends	4,176	339					

\*Capital distribution to Girish of Keshav's jewellery is matched to available income

## MARKING GUIDE

TOPIC		MARKS
PM reliefs	<u>Recognition of s179 claim</u>	0.5
	Conditions: quoted shares including OEIC's – Underhill plc	0.5
	Within 12 months of DoD	0.5
	Include those sold at a profit and netted off	0.5
	Gross proceeds (i.e. ignore costs)	0.5
	Calculation	1
	Amount of IHT refund due	0.5
	<u>Recognition of s176 claim</u>	0.5
	Conditions: where asset valued with other asset (ie related property)	0.5
	And asset is sold within 3 years of death	0.5
	And gross proceeds is less than the amount previously charged to IHT – no claim on Wind in Trees as gross proceeds is the metric to be used, not net	1
	Claim on asset by asset basis – ie only on Sand & Leaves Ltd – no account taken of Wind in the Trees Ltd	0.5
	Replaces the value in estate/loss not relevant	0.5
	Quantification/calculation	1
	IHT refund due	0.5
Subtotal		9
R185s		
	Net income by source for distribution after tax 20%/7.5%	1
	(Set off of expenses against net income NB expense set off in dividend/non dividend order unless rationale explained for alternative treatment)	0.5
	Each source divided equally between beneficiaries and deduction therefore limited to 50%	0.5
	Deduction from non-savings first then savings then dividend	1
	Girish – capital treatment as income; R185 shows £9.5k distribution	1
	Annie – R185 shows distribution of £14k	0.5
	Tax credits on all types of income $\times 20/80 / \times 7.5/92.5$	1
	Distributable income c/f	0.5
Subtotal		6
<b>TOTAL</b>		<b>15</b>