

The Chartered Institute of Taxation

Advanced Technical

Inheritance Tax, Trusts & Estates

May 2024

Suggested answers

1. Settlor

Income Tax (IT):

The trust is not settlor-interested under s.624 ITTOIA 2005 for IT as Jake is specifically excluded from benefitting from the trust and he is a widower.

This also prevents an IT charge on the settlor under s.720 ITA 2007 of the transfer of assets abroad (TOAA) provisions.

Capital Gains Tax (CGT):

Jake was UK resident on 1 June 2014, so he would have been subject to CGT at that time.

The property was his former principal private residence and so the gain would be covered by 100% principle private residence relief (PPR).

The US share portfolio only incurred a gain of £6,000, which, assuming no other gains in 2014/15, would fall within Jake's annual exemption (AE).

As the trust is non-UK resident for CGT (no UK resident trustees) a wider definition of settlor-interest applies under s.86 TCGA 1992. This includes the settlor's children and/or grandchildren as beneficiaries of the trust.

However, a charge under s.86 TCGA 1992 only applies to tax the gain directly on the settlor where they are both UK resident and UK domiciled in the year in which the gain arises. As Jake was not UK domiciled in 2023/24, he is not caught by s.86 TCGA 1992 in respect of the sale of the UK residential property on 31 March 2024.

Inheritance Tax (IHT):

Jake was non-UK domiciled and as such settlement of the US share portfolio is not a chargeable lifetime transfer (CLT) – it is excluded property.

The settlement of the UK property was covered by Jake's annual exemptions and nil rate band (NRB) of £325,000.

Jake retains no benefit in the property, and it is not therefore a gift with reservation of benefit (GWROB). The UK property does not form part of his estate for UK IHT.

Trustees:

CGT:

The trust is also non-UK resident for CGT (see above). This means that it is generally not chargeable to UK CGT.

There is an exception for gains arising in respect of UK land and property. Gains arising on UK residential property were brought into the charge to UK CGT on non-resident trustees with effect from 6 April 2015. Such gains are referred to as non-resident capital gains (NRCG).

There are three calculations to consider:

- 1) **The default method** based on the gain/loss using the rebased value on 6 April 2015.
- 2) **The time apportionment method** based on the total gain/loss apportioned to the period post 5 April 2015.
- 3) **The retrospective method** based on the total gain/loss.

Default method:

	£
Proceeds	475,000
Less MV @ 6/4/15	<u>(325,000)</u>
Gain before relief	150,000
PRR - note 1.	
((63+2+34+9)/108) x £150,000	<u>(150,000)</u>
Gain after reliefs	<u><u>£nil</u></u>

The trustees have a nil liability to NRCGT.

Note 1:

	Actual	Vacant	Deemed	Total
6 April 2015 to 30 June 2020	63 months			
1 July 2020 to 31 August 2020			2 months	
1 September 2020 to 30 June 2023	34 months			
1 July 2023 to 31 March 2024			9 months	
6 April 2015 to 31 March 2024				108 months

The default method automatically applies unless the trustees elect for an alternative method, which in this case is not required as the gain is fully covered by principal private residence relief. The retrospective method would only improve on this if it were to result in a loss, which it doesn't.

A NRCG return is required to be submitted to HMRC within 60 days of completion i.e. by 30 May 2024. This is the case even though there is no CGT payable.

S.86 and s.87 TCGA 1992 only apply to the gain not charged under NRCG which in this case is £nil. as the period up to 5 April 2015 is fully covered by principal private residence relief.

Beneficiaries:**IT:**

Where there is no IT charge on the settlor under s.720 ITA 2007, UK resident beneficiaries are instead subject to an IT charge under s.731 ITA 2007 on benefits they receive matched to relevant income.

The benefit of the use of the UK residential property is its market value rent less any rent paid to the trustees (nil).

The beneficiaries are therefore charged on the following amounts:

	Relevant income £	Benefit £	Beneficiary	Unmatched income c/f £	Cumulative Unmatched income £
2014/15	10/12 16,667	10/12 12,500	E/R/P	4,167	4,167
2015/16	20,000	15,000	E/R/P	5,000	9,167
2016/17	20,000	15,000	E/R/P	5,000	14,167
2017/18	20,000	15,000	E/R/P	5,000	19,167
2018/19	20,000	15,000	E/R/P	5,000	24,167
2019/20	20,000	18,000	E/R/P	2,000	26,167
2020/21	20,000	3/12 4,500	E/R/P		
		7/12 10,500	Phoebe	5,000	31,167
2021/22	20,000	18,000	Phoebe	2,000	33,167
2022/23	20,000	18,000	Phoebe	2,000	35,167
2023/24	20,000	3/12 4,500	Phoebe	15,500	50,667

The benefit is taxed as non-savings income (NSI) and without the benefit of the dividend or savings allowance. The unmatched income is carried forward against future benefits.

MARKING GUIDE

TOPIC	MARKS
Settlor:	
IT: Not settlor interested S.624/s.720. Specific exclusion from benefit/widower	1
CGT: UK resident on settlement, liable to UK CGT, 100% PRR, Gain on shares < AE/N/A i	1.5
CGT: non-resident trust, settlor-interested extended definition under s.86 – N/A as non-UK domiciled	1
IHT: US portfolio excluded property, UK property < 2xAE & NRB	1
IHT: No GWROB	0.5
Subtotal	5
Trustees:	
CGT: non-UK resident, generally not chargeable to UK CGT	0.5
CGT: UK land and property, residential property 6/4/15 >	0.5
CGT: 3 methods: Default method - rebasing 6/4/2015,	0.5
Time apportionment method – full gain/loss apportioned from 6 April 2015,	0.5
Retrospective method – full gain/loss	0.5
CGT: Calculation	
Basic Gain	1
PRR = Nil CGT	2
CGT: default method automatic unless election for non-default method - not required as default method results in nil charge as full PRR, would only use retrospective method if a loss	1.5
NRCG return 60 days of completion 30 May 2024, even where nil CGT payable	0.5
s.86/s.87 only applies to the gain not charged to NRCG – N/A	0.5
Subtotal	8
Beneficiaries:	
IT: No charge on settlor under s.720 therefore charge on beneficiaries under s.731, matching “benefit” to “relevant income”	1.5
IT: value of benefit = MV rent less paid	0.5
IT: E/R/P 2014/15 – 2020/21 (0.5 for pro-rata 2014/15, 0.5 full years 2015/16 – 2018/19, 0.5 full year 2019/20 (change of rental value), 0.5 for pro-rata 2020/21)	2
IT: Phoebe 2020/21 – 2023/24 (0.5 for pro-rata 2020/21, 0.5 for full years 2021/22 – 2022/23, 0.5 for pro-rata 2023/24)	1.5
Taxed as NSI, no savings or dividend allowance, C/f unmatched income against future benefits	1.5
Subtotal	7
TOTAL	20

2. FM Property GmbH is a non-UK resident close company having fewer than five participators. Gratuitous dispositions by close companies that result in a loss of value to the company are transfers of value for Inheritance Tax (IHT). Such transfers of value are attributed to each individual participator in accordance with their interest in the company.

A transfer of value by a close company is specifically prevented from being a potential exempt transfer (PET) and so is treated as an immediately chargeable lifetime transfer (CLT) made by the participator to whom it is attributed.

1 January 2020 - Transfer of UK commercial property, 50% to Jessie's husband and Gerard

	£	Jessie Mallon 25% £	Gerard Fagan 75% £
Transfer of value	900,000	225,000	675,000
Less Spouse exemption – Note 1		(225,000)	
		<u>Nil</u>	
Less increase in estate of participator – Note 2			(450,000)
Less Annual exemptions:			
2019/20			(3,000)
2018/19			(3,000)
CLT			<u>219,000</u>
Less Nil rate band – Note 3			(219,000)
Taxable			<u>nil</u>

Note 1:

Attributed transfers of value that increase the estate of the participator's spouse can benefit from the spouse exemption.

Note 2:

Any transfer of value attributed to the participator can be reduced by the corresponding increase in their own estate because of the transfer.

Note 3:

Nil rate band available £325,000 – used £219,000 = £106,000 to carry forward.

1 April 2021 - Transfer of German commercial property, 100% to Jessie's brother, Tim

	£	Jessie Mallon 25% £	Gerard Fagan 75% £
Transfer of value	1,850,000	462,500	1,387,500
Disregarded as excluded property – Note 1			(1,387,500)
			<u>Nil</u>
Less Annual exemptions:			
2020/21		(3,000)	
2019/20		(3,000)	
CLT		<u>456,500</u>	
Less Nil rate band – Note 2		(325,000)	
Taxable		<u>131,500</u>	
IHT payable x 20/80 – Note 3		32,875	
Gross CLT		<u>£489,375</u>	

Note 1:

Transfers of value of non-UK property attributed to non-UK domiciled individuals are disregarded as excluded property.

Note 2:

Nil rate band available £325,000 – used £325,000 = £nil to carry forward.

Note 3:

Grossing applies as the company is primarily liable to make payment of the IHT. If the company fails to make payment HMRC can seek payment from those who are secondarily liable. This is either the participator to whom the transfer of value is attributed i.e. Jessie, or the person benefitting from the transfer of value i.e. her brother Tim.

Payment was due on 31 October 2021.

1 January 2022 - Settlement of Gerard's shareholding on the Fagan Discretionary Trust.

	£	£
Transfer of value		<u>3,000,000</u>
Amount attributable to UK residential property – Note 1: (£1million - £111,111) / £4million x £3 million	666,667	
Less AEs:		
2021/22	(3,000)	
2020/21	(3,000)	
CLT	<u>660,667</u>	
Less Nil rate band – Note 2	(106,000)	
Taxable	<u>554,667</u>	
IHT payable x 20/80 – Note 3	<u>138,667</u>	
Gross CLT	<u><u>£799,334</u></u>	

Note 1:

Since 6 April 2017 UK residential property held by a non-UK domiciled individual through a non-UK envelope e.g. a non-UK company, is no longer excluded property.

The company must be a close company which FM Property GmbH is, and the non-UK domiciled individual must hold at least 5% of the shares, which Gerard does.

The value of the UK residential property held within such an envelope is therefore chargeable to UK IHT if the shares in that company are transferred by the non-UK domiciled individual to a trust as this is an immediately chargeable lifetime transfer.

Any liabilities of the company will be attributed to its assets pro-rata. The mortgage in respect of the UK residential properties is not therefore fully deducted from their value instead only £1 million/£4.5 million x £500,000 i.e. £111,111 is deductible.

Note 2:

Nil rate band b/fwd is £106,000.

Note 3:

Grossing applies as Gerard paid the tax on the CLT. Payment was due on 31 July 2022.

1 May 2024 – Death of Gerard Fagan:

Additional tax on transfer of shares to Fagan Discretionary Trust:

	£
Gross CLT	799,334
Less NRB – note 1	<u>(106,000)</u>
Taxable	693,334
IHT @ 40%	277,334
Taper relief – note 2	Nil
Less lifetime tax	<u>(138,667)</u>
IHT Payable – note 3	<u>£138,667</u>

Note 1:

Nil rate band b/fwd is £106,000.

Note 2:

Less than three years prior to death.

Note 3:

Payable by trustees – Michael and Nina, due 31 October 2024.

The death estate:

	£
Car	40,000
Chattels	5,000
Bank account (50%)	12,500
ISA	<u>20,250</u>
Total	77,750
Less funeral expense	<u>(1,000)</u>
Net estate	76,750
IHT @ 40% - note 1	£30,700

Note 1:

Nil rate band fully extinguished by transfer of share to the Fagan Discretionary settlement.

IHT payable by executors, due date 31 October 2024/delivery of IHT400 if earlier.

MARKING GUIDE

TOPIC	MARKS
Close company:	
Identification, attribution, CLT	1.5
1 January 2020:	
Attribution 25%/75%	0.5
Spouse exemption – Jessie	1
Deduct increase in estate of participator – Gerard	1
Annual exemptions x 2, CLT, nil rate band	1.5
1 April 2021:	
Attribution 25%/75%	PAG
Excluded property disregard	1
Annual exemptions x 2 (PAG), CLT (PAG), nil rate band, taxable	1
IHT single grossing, Gross CLT	1
Payment primary liability company, secondary liability Jessie/Tim, due date	1.5
Transfer into trust:	
1 January 2022:	
Post 6/4/17 rule – UK residential property, non-UK domiciled, enveloped non-UK, close company >= 5% participation, no longer excluded property	2
Transfer to trust CLT, attribution of UK residential property value as proportion of share value, pro-rata apportionment of creditors against UK residential property	1.5
AEs x 2, CLT (PAG), residual NRB, Taxable	1
IHT – single grossing – payable by Gerard as settlor, gross CLT (PAG), due date	1.5
Death:	
15 April 2024:	
Additional IHT on death – 1 January 2022 transfer:	
IHT @ 40%, nil taper, deduct lifetime tax, payable by trustees, due date	2
Death estate:	
Net estate, IHT @ 40%, payable by executors, due date	2
TOTAL	20

3. 1) IHT on Paulette's death:

Death Estate:

	£	£
Free Estate ("General" property) – Note 1		435,862
Survivorship property – Note 2		550,000
Settled Property		<u>400,000</u>
Gross estate		1,385,862
Less funeral expenses		(5,000)
Less costs relating to Spanish Property - Note 3		<u>(7,543)</u>
Net Estate		1,373,319
Spouse exemption – Note 4		<u>(973,319)</u>
Chargeable estate		400,000
NRB/TNRB – Note 5	(325,000)	
RNRB/TRNRB – Note 6	<u>(0)</u>	
		<u>(325,000)</u>
Taxable		<u>£75,000</u>
IHT @ 40%		<u>£30,000</u>

Note 1:

Rental property – tenancy in common with Rory and Bernice. As there is an unrelated third party Paulette's undivided share, whilst still valued with Bernice's undivided share and 50% applied to arrive at the value of Paulette's share this will not produce a higher value than if it had been valued separately. A 10% discount is appropriate. Paulette's share of the rental property is therefore £75,000 (£250,000/3 @ 90%).

The Sterling value of the Spanish property is €175,000/1.16 = £150,862.

Paulette's free estate also comprised personal chattels and ISAs.

Total free estate is £75,000 + £150,862 + £10,000 + £160,000 + £40,000 = £435,862.

Note 2:

Oaktrees – joint tenant with Bernice = related property. Paulette's share is £900,000/2 = £450,000.

Total assets held jointly are £450,000 + (£200,000/2) = £550,000.

Note 3:

Restricted to 5% of the Spanish Property value i.e. £7,543.

Note 4:

Under the Intestacy rules William is not "issue" as he is neither Paulette's natural son, nor legally adopted. Paulette's free estate therefore passes to her spouse Bernice.

The funeral and Spanish Property expenses are deducted from the free estate restricting the spouse exemption to £423,319.

The property held jointly passes by survivorship to Bernice and attracts the spouse exemption of £550,000.

Total spouse exemption is £423,319 + £550,000 = £973,319.

Note 5:

Paulette's full NRB is available as she has made no cumulative lifetime transfers. She is not entitled to a TNRB as she has not previously been married or in a civil partnership.

Note 6:

No RNRB (or TRNRB) is available as Oaktrees does not pass to direct lineal descendants.

2) Reduced rate of IHT:

The taxable estate plus any donation = baseline amount. This can be calculated as $£75,000 \times 100/90 = £83,333$.

10% of the baseline amount is £8,333 = the optimum charitable donation.

To benefit from the reduced rate of 36% on the entire taxable estate an election to combine components should be made.

All components will then benefit from the reduced rate saving £3,000 of IHT.

If no election is made, only the component(s) from which the donation is made, will benefit from the reduced rate of IHT. As this is currently the free estate which will benefit from the spousal exemption already reducing its IHT to nil, this will be of no practical benefit.

As Bernice has no entitlement to the settled property component, she is unable to re-direct funds from this component to charity. The election therefore effectively extends the benefit of the IHT saving from the charitable legacy made by the free estate to the settled property component.

All “appropriate persons” need to make the election - the administrators of the free estate and the trustees of the Grisham family trust.

The election must be made within two years of death by 31 March 2026.

MARKING GUIDE

TOPIC	MARKS
Death estate:	
Free estate “general component” Valuation of TIC, Sterling value of Spanish property, other assets, total	1.5
Survivorship property component Oaktrees – related property value, joint bank account, total	1
Settled property component.	0.5
Deductions from “general” component – funeral expenses, Spanish property expenses (restricted)	1
Intestacy rules – no issue, all to Bernice as spouse	1
Spouse exemption, NRB (no TNRB, RNRB, TRNRB), IHT @ 40%	2
Reduced rate of IHT 36%:	
Baseline amount – gross up for charity donation, 10% - optimum donation to Charity	0.5
IHT saving, election to combine components, why	1.5
Appropriate persons, time limit	1
TOTAL	10

4. 1) Capital Gains Tax (CGT) liability to date of death:

Carry back loss against previous three years on a last in first out (LIFO) basis:

	2023/24	2022/23	2021/22	2020/21
Gain/(loss) £	(22,000)	18,000	14,000	35,000
Annual exemption (AE)		(12,300)	(12,300)	(12,300)
Gain before relief		5,700	1,700	22,700
Loss utilisation	22,000	(5,700)	(1,700)	(14,600)
Taxable gain		0	0	8,100
CGT @ 20%		0	0	1,620
Less already paid @ 20%		(1,140)	(340)	(4,540)
Overpaid	(4,400)	(1,140)	(340)	(2,920)

2) Estate rate of Inheritance Tax (IHT) on the death estate:

	£
Valued assets – note 1	1,620,000
Accrued interest – note 2	180
CGT overpayment – note 3	
	<u>4,400</u>
Gross estate	1,624,580
funeral expenses	<u>(5,000)</u>
Net chargeable estate	1,619,580
Nil rate band (NRB) – note 4	<u>(325,000)</u>
Taxable estate	<u>£1,294,580</u>
IHT @ 40%	<u>£517,832</u>
Estate rate £517,832/£1,619,580 x 100	31.9732%

Note 1:

The valuation of shares in ABC Plc will be cum-div. No adjustment to the valuation is therefore required.

Note 2:

Accrued interest is an asset on death included in the death estate net of the basic savings rate of Income Tax (IT) - £225 x 0.80 = £180.

Note 3:

The overpayment of CGT is an asset of the death estate.

Note 4:

Full NRB is available as there have been no lifetime transfers in the seven years before death. No residence NRB is available as the sole beneficiary of Constance's estate is her niece. No transferable NRB is available as Constance never married.

3) IT & CGT liability for the administration period

	NSI £	SI £	DI £	Total IT due £
Rents (note 1)	36,000			
Interest FRB (note 2)		400		
Interest BS Account (note 2)		250		
Dividends ABC Plc (note 2) (£2,000+£1,800+£1,800)			5,600	
Dividends ISA (note 3)			0	
Total	<u>36,000</u>	<u>650</u>	<u>5,600</u>	
IHT loan interest – (note 4)	<u>(3,000)</u>			
Taxable	33,000	650	5,600	
IT @ 20%/8.75%	<u>(6,600)</u>	<u>(130)</u>	<u>(490)</u>	<u>7,220</u>
Net distributable income	<u>£26,400</u>	<u>£520</u>	<u>£5,110</u>	

The sale of the ISA on 31 January 2024 was within three years of death and before the end of the administration period. It is therefore exempt.

There is no CGT on the transfer of assets to Jane on 28 February 2024, which she received at their probate value.

The gain on the sale of the residential let on 31 March 2024 is as follows:

	£
Proceeds	610,000
Probate value	(600,000)
Probate expenses - £8,000 x £600,000/£1,624,580 (note 5)	(2,955)
Net gain	7,045
AE – note 6	(6,000)
Taxable gain	£1,045
CGT @ 28%	£293

Note 1:

Cash basis - $9/12 \times £48,000 = £36,000$.

Note 2:

Receipts basis - dividend dated 1 May 2024 attributable to Jane.

Note 3:

Exempt.

Note 4:

Allowable as a deduction. Against NSI in priority to SI or dividends.

Note 5:

SP2/04 - allowable probate costs based on gross value of estate £1 million - £5 million = £8,000.

Note 6:

Full AE available in the year of death and following two tax years. AE 2023/24 is £6,000.

R185 entries - Jane:

2023/24

Jane received capital distributions in 2023/24 exceeding the estate income received. Income is deemed to be distributed in priority to capital so the entire net distributable income for 2023/24 is deemed to have been distributed in 2023/24:

	NSI £	SI £	DI £
Net income	26,400	520	5,110
Tax credit	(6,600)	(130)	(490)

2024/25

Nil – no estate income arose in the period 6 April 2024 to 30 April 2024 (cessation of the administration period).

Higher rate tax adjustment for income subject to IHT:

Net pre-death income x estate rate = $£180 \times 31.9732\% = £58$

Gross up IHT at basic rate = $£58 \times 100/80 = £73$

MARKING GUIDE

TOPIC	MARKS
IT, CGT to date of death.	
CGT – c/b 3 years, LIFO	1
Gain after AE, 2022/23, 2021/22, 2020/21	1.5
Loss utilisation 2022/23, 2021/22, 2020/21	1.5
Revised tax payable, less paid = net overpayment (shortcut full loss utilisation x 20% gets full credit)	1
Subtotal	5
Estate rate:	
Valued assets – no adjustment for dividend (valuation cum-div) - add accrued income, CGT overpayment	2
Funeral expenses, net chargeable estate	1
NRB, IHT @ 40%, estate rate	2
Subtotal	5
IT, CGT admin period, R185 entries, HRT adj. s.669	
Rents cash basis	0.5
Interest, Dividends receipts basis excluding 1/5/24 dividend, ISA exempt	1
Deduct loan interest from NSI in priority	0.5
Tax @ 20%/8.75%	1
CGT – N/A distributed assets, ISA exempt	1
CGT calc – probate value, probate expenses, AE, CGT @ 28%	2
R185 – Jane – 2023/24 capital distribution exceeds income 2023/24 – all	2
R185 – Jane – 2024/25 nil – no income to end of admin period	0.5
Net pre death income x estate rate	1
Gross up	0.5
Subtotal	10
TOTAL	20

5. 1) Trust income Tax liability

The trust is a mixed trust for Income Tax as it was a qualifying interest in possession (QIIP) up to Mary's death on 6 June 2023 and a discretionary trust (DT) after her death. This means that the income apportioned to the period before her death will be taxable at the basic rate and that apportioned to the period after her death at the rate applicable to trusts (RAT).

The trust management expenses (TMEs) are also apportioned and are only deductible from the income apportioned to the period after Mary's death in calculating the Income Tax.

The TMEs apportioned to the period before Mary's death are however deducted in arriving at the distributable income available to Mary.

	Discretionary NSI	QIIP NSI	Discretionary SI	QIIP SI	TMEs	Total
	£	£	£	£	£	£
Rent	20,000					
Interest				1,750		
Less income subject to QIIP 2/12	(3,333)	3,333		(292)	292	
TMEs x 10/12 x 100/80				(521)		
Income liable to tax at RAT	16,667			937		
Tax on income subject to RAT						
£1,000 @ 20%		(200)				
(£16,667 - £1,000) @ 45%	£15,667	(7,050)				
£937 @ 45%				(422)		
£521 @ 20%					(104)	7,776
Tax on income subject to QIIP						
£3,333 @ 20%		(667)				
£292 @ 20%					(58)	725
Total Tax						£8,501
Net income subject to RAT	£9,417			£515		
TMEs x 2/12				(83)		
Net distributable income (QIIP)		£2,666		£151		
Tax Pool:					£	
B/f					0	
Add total tax paid					7,776	
Less tax paid on expenses					(104)	
Less tax credit on distribution to Tom £5,000 x 45/55					(4,091)	
C/f					£3,581	

R185s – 2023/24

R185 – Tom	Net £	Tax £
	5,000	4,091
R185 – Mary	Net £	Tax £
NSI	2,666	667
SI	151	38

2) Exit Charge

The 10-year anniversary (TYA) of the trust is 24 May 2024, based on Peter's date of death as the original settlor.

However, S.80 IHTA 1984 applies because Mary, as the spouse of the original settlor, had a qualifying interest in possession (QIIP) but on her death the property became held on discretionary trust (DT) thereby passing into the relevant property trust regime.

The effect of s.80 IHTA 1984 is that Mary is treated as the settlor of the relevant property trust (RPT) on her death 6 June 2023. It is Mary's lifetime gifting cumulation that is used when calculating the effective rate for the exit charge.

In addition, the initial value of the trust is the value on Mary's death, after deducting Inheritance Tax paid by the trustees of £448,000 i.e. the "conversion" amount, not that originally settled.

The exit charge requires adjustment for the reduced number of full/part quarters in the period from Mary's death to reflect that the property was only relevant property from Mary's death.

The calculation is therefore as follows:

Exit charge before the first principal charge:

	£	£
Initial value of relevant property on "conversion" from QIIP to RPT = MV @ Mary's death – IHT paid by trustees		757,000
Nil rate band at date of exit 30/4/2024	325,000	
Less settlor's cumulative total in seven years before conversion	<u>(240,000)</u>	
Nil band remaining		<u>(85,000)</u>
		672,000
Notional IHT x 20%		134,400
Effective rate $\text{£}134,400/\text{£}757,000 \times 100$		17.754%
Actual rate $\times 30\% \times (n-x)/40$		0.399%
Grossed up $0.399/(100-0.399) \times 100$		0.401%
Exit charge = $\text{£}30,000 \times 0.401\%$		£120

n = completed quarters between commencement and exit = 39

X = completed quarters between commencement and "conversion" = 36

MARKING GUIDE

TOPIC	MARKS
Income Tax:	
Identification of mixed trust, QIIP/DT – apportionment requirement	0.5
TME apportionment – deducted for IT RAT, deducted from distributable income – QIIP	1
Calculation – deduct 2/12 QIIP to calculate RAT, TME grossed up	0.5
Tax - £1,000 @ 20%, balance @ 45%, TMEs @ 20% (not deducted from income for distribution)	1.5
Add tax on QIIP @ 20%, total IT	0.5
Distributable income subject to RAT	0.5
Deduct 2/12 x TMEs to arrive at distributable income for QIIP	0.5
Tax Pool – nil b/f (previously a QIIP), add tax paid of income subject to RAT exc. Tax on TMEs, deduct 45% tax credit on distribution to Tom, c/f	2
Tom – net £5,000, Tax x 45/55	0.5
Mary – net £2,666, £151 x 20/80	0.5
Subtotal	8
Exit:	
ID s.80 IHTA 1984, spouse of settlor QIIP, DT on death	1
Effect of s.80 IHTA 1984 – Mary settlor, Mary’s cumulative total for purposes of ER, MV @ date of death less IHT = “conversion” amount used in calculation of exit, reduced number of quarters for period before RPT	1.5
Exit calc – “conversion” value, NRB – cumulative total, IHT @ 20%, ER	2
Exit calc – AR x 30% x (n-x)/40, n=commencement to exit, x = commencement to conversion	1.5
Exit calc - AR gross up – trustees pay tax, exit charge x £30,000 distribution	1
Subtotal	7
TOTAL	15

6. Lifetime gifts:

1 May 2017

The gift was spouse exempt.

1 November 2017, 1 December 2021 and 1 February 2022

The land and barns had been owned by Richard for seven years at the date of each gift (ownership condition met).

The land and barns were used for the purposes of agriculture by a farming partnership of which Richard was a partner on a post 1 September 1995 tenancy so 100% agricultural property relief (APR) applies to the agricultural value (AV) on all gifts.

1 February 2022

As the market value (MV) exceeds AV, 50% business property relief (BPR) is available on the balance of £860,000 (£1 million - £140,000) = £430,000 as the land is owned outside the partnership by Richard. APR is given in priority to BPR.

On Richard's death:

The gifted property must be retained by the donee and qualify for APR/BPR in their hands. For APR there must also be continuing occupation for the purposes of agriculture, and for BPR continuing use in a trading business carried on by the transferee otherwise APR/BPR are withdrawn. If the property is sold full proceeds must be applied in acquiring other qualifying assets "replacement property" within three years.

1 November 2017

Original PET = 100% APR.

It also qualified for BPR (of nil as APR was given in priority).

The barns and land (excluding the eight acres sold and not reinvested in BPR or APR assets) continued to be used in the partnership carried on by Ethan and Chloe and will qualify for 50% BPR, as these are owned by Ethan personally.

	£	
BPR – barns £50,000 (50%)		25,000
BPR – land £220,000 x 12/20 (50%)		66,000

1 December 2021

The land continued to be used by the farming partnership - 100% APR applies.

1 February 2022

The land continued to be used by the farming partnership - 100% APR and 50% BPR continue to apply, as originally.

Richard's death estate

Richard's partnership share passed to Ethan and benefits from 100% BPR.

The balance of Richard's death estate passed to Deidre and is therefore covered by the spouse exemption.

Deidre's death

100 acres – received as lifetime gift from Richard.

This had been owned by Deidre for seven years and was occupied for agricultural purposes first by the partnership, then subsequently by Ethan and will qualify for 100% APR. The AV and MV are the same.

Farmhouse and 100 acres – received on Richard's death.

Deidre does not meet the seven-year ownership condition for tenanted land independently. However, she inherited the property on Richard's death and as his spouse their ownership period is combined. She therefore qualifies for 100% APR if the occupation condition is also met.

The farmhouse and 100 acres were occupied by Richard for the purposes of agriculture up to his death and so met the occupation condition up to that point. These assets continued to be occupied for the purposes of agriculture by Ethan following Richard's death and so would continue to meet the occupation condition.

It is assumed that the "character appropriate" test was met in relation to the farmhouse as the agricultural tie means that the AV is the same as the MV because the farmhouse can only be used for the purposes of agriculture. 100% APR is applied against the full £400,000.

The Cottage – received on Richard's death.

Ownership condition met (as above).

Although it would have qualified for 100% APR on Richard's death had it not been spouse exempt (formerly occupied by a retired farmworker and only recently having become vacant), the cottage will not qualify on Deidre's death as she lived there. The occupation condition was not therefore met as Deidre was not involved in farming and the cottage was not therefore in occupation for the purposes of agriculture.

MARKING GUIDE

TOPIC	MARKS
Lifetime gifts:	
On original transfers:	
1/5/17 – spouse exempt	0.5
1/11/17, 1/12/21, 1/2/22 – 100% APR agricultural purposes – post 1995 tenancy	1.5
Rationale: Seven-year ownership condition met; occupation condition met – partnership of which owner a partner	1.5
1/2/22 – 50% BPR on balance, held outside partnership, APR in priority	1.5
On Richards death:	
Retained by donee (continuing ownership condition)	0.5
Continued occupation purposes of agriculture (APR), use in business of donee (BPR):	1
Replacement property within three years of sale	0.5
1/11/17 – 50% BPR on barns and 12 acres of land (8 sold, not reinvested), held outside partnership	1
Rationale: BPR on original gift (nil, APR priority), continued business use in hands of transferee	1.5
1/12/21 – 100% APR – continued occupation	0.5
1/2/22 – 100% APR/50% BPR – continued occupation/use	1
Richard’s death estate – BPR partnership capital account, spouse exemption	1
Deidre’s death:	
100 acres lifetime gift 1/5/17 – seven years ownership condition met; occupation condition met – 100% APR	1
Farmhouse & 100 acres – combined period of ownership – spouse on death, occupation condition met – AV = MV, 100% APR	1.5
Cottage – occupation condition not met	0.5
TOTAL	15