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am Date of Examination

Tick box if you have answered in accordance with Scots Law

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Please tick which Advisory Paper you have attempted (if not already ticked below)

Taxation of Owner-Managed Businesses

Taxation of Individuals

VAT on UK Domestic Transactions, IPT & SDLT

VAT on Cross-Border Transactions & Customs Duties

Inheritance Tax, Trusts & Estates

Taxation of Major Corporates

Human Capital Taxes

Please tick here if you have used an extra answer booklet (ensure you attach your second answer booklet to the first using a treasury tag which will be provided).

Advisory

You must ensure that the Advisory Papers chosen are not the same as the corresponding Awareness Modules you have sat or will be sitting.

- For those candidates on the Indirect Tax Route you must sit the VAT on UK Domestic Transactions, IPT & SDLT Advisory Paper.
- For those candidates on the Indirect Tax Route you must sit the VAT on Cross-Border Transactions & Customs Duties Advisory Paper.

Instructions

Your script will be scanned electronically. Failure to comply with these instructions may lead to your script not being marked. You must:

- Complete the details on this page and in the booklet using BLACK or BLUE ballpoint pen only.
- Write on both sides of the page.
- Not write in the margin areas indicated.
- Start a new page for each question you answer and indicate the question number in the box provided at the top of each page.
- Not remove any pages from this answer booklet or damage it in any way.

Please do all of the above before the end of the examination.

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Scott Linder

Firm letterhead

Address

1 May 2018

Dear Scott

Inheritance tax liability arising as a result of your father's death
I have calculated the potential liability to inheritance tax (IHT) in appendix 1.

I note that Joseph gifted you a holiday cottage in 2008, but continued to use the cottage rent-free for a significant amount of time. This is a gift with reservation of benefit, and the tax treatment in this situation is to ~~to~~ include the cottage in Joseph's estate at death and pretend it was never gifted. This is because this results in a higher tax liability than if we allow it as a gift.

The life interest in the Linder Family 1986 Trust is a qualifying interest in possession as it arose before 22 March 2006. It forms part of Joseph's estate at death.

If part of the estate is left to charity, this legacy is exempt and would save IHT at 40% of the amount gifted. This can be achieved post-death through a deed of variation. The deed must be executed in writing and signed by yourself as beneficiary giving up part of their legacy, and must be done within two years of death. The charity must be notified of the gift.

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The deed must include a statement that s142 IHTA 1984 is to apply (this effectively rewrites the will).

If 10% of the net estate is left to charity, the remaining estate is eligible for the 36% rate of IHT to apply, saving further tax.

This is calculated on components, being in your case the free estate, the settled property component, and the gift with reservation. If 10% of ~~the~~ ^{the value} a component is left to charity, the 36% rate applies to that component. If sufficient is left ~~that~~ to charity that the amount exceeds 10% of more than one component, an election can be made to merge components.

The net value of the free estate component (after the nil rate band) is £433,180. Therefore if you left £43,318 to charity you would save IHT of £32,922.

Without making this variation on the current figures, the tax due is £348,000. This is due by 31 July 2018 or on submission of the IHT400 if earlier.

The tax in respect of the freehold property and the holiday cottage, as well as the tax payable by the trust, can be paid in installments over 10 years. The installments will be interest-bearing. I hope this is helpful

Yours sincerely

Tax adviser.

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Appendix 1

Estate at death

Freehold property (net of 10% tenanted discount)	270,000
Investments	200,000
Cash	<u>125,000</u>
	595,000
QIIP - Linder family 1986 Trust	500,000
GWR - holiday cottage	<u>100,000</u>
	1,195,000
Nil rate band	<u>(325,000)</u>
	870,000

IHT at 40% £348,000

Note: no residence nil rate band available as the Joseph's main residence is passing to a niece (ie. not a direct descendant).

IHT is payable by:

Scott 202,393

Trust 145,607

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Notes for meeting with Cereia Cooper

A trust set up by Cereia for the benefit of Philip would be settlor-interested for income tax purposes. The income received by the trust would be taxed as though it arose to Cereia directly. If Philip was excluded from benefit but James was a beneficiary, the trust is a parental settlement for a minor child. Anti-avoidance means any income distributed to James would be taxed as arising to Cereia.

For CGT purposes, if either Philip or James can benefit then the trust is settlor-interested. Any gains arising would be taxed on Cereia as under s86 TCGA 1992. Cereia would be able to set off personal losses and her annual exemption.

For IHT, the gift into trust is a CLT. Assuming she has made no previous CLTs, the IHT charge arising is $\frac{21,000}{22,500}$ if she pays the tax herself. The rate is 20% if the trust pays and 25% if she pays.

The trust would be a relevant property trust and would be subject to principal charges and exit charges.

A chargeable gain arises on transfer into trust as this is a disposal to a connected person. The deemed proceeds are market value. A gain cannot be deferred using gift relief if the trust is settlor-interested. The gain arising is £195,000 giving a CGT charge of £51,436 (charged at 28% after deduction of

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£11,300 annual exemption as the properties are residential).

The attribution of income to the settlor under settlor-interested trusts can be avoided under a "motive" exemption, i.e. if the settlor can show that the motive of putting property into trust was not to avoid tax. However in practice this is notoriously difficult to obtain.

Alternatively the rental properties could be gifted outright to Philip. This gift is exempt from IHT under spousal exemption, and for CGT purposes no gain arises on transfer between spouses.

Philip would be taxed on the income going forward in his own name. He has no taxable income and so the rental income would all be taxed at basic rate of 20% rather than higher rate 45% as it is in Cereia's hands. Potentially some income would fall in Phillip's personal allowance and save further tax. The tax saving would be $25\% \times 35,000 = £8,750$.

If Cereia wants to put the properties into trust, CGT savings would be obtained by gifting the three properties in different tax years to utilise annual exemptions, This would also save IHT in the same way.

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	Cecelia could also gift a half share in the properties to	
	Philip before both Cecelia and Philip gift into trust.	

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Trusts for the disabled

Reasons for setting up a trust for the disabled

- To ensure adequate provision for a ^{disabled} relative on your death
- To protect assets where the disabled beneficiary does not have capacity to hold assets in their own right
- To self-settle in order to protect assets, and provide income.
- Where a disabled beneficiary has means-tested benefits, income from a discretionary trust does not affect these benefits as the beneficiary does not have a right to the income.

Who can set up such a trust

- Anyone can set up a trust for the benefit of a beneficiary who is currently disabled.
- Can be set up for the settlor's own benefit if they expect to become disabled in the future.

Definition of disabled person

- As defined in Sch 1A to Finance Act 2005
- In receipt of disability living allowance (or other specified benefits) or
- A person who by reason of mental disorder under the Mental Health Act is incapable of administering their own affairs.

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Conditions that the trust must meet

- If income/^{or capital} is distributed from the trust, it must be applied for the benefit of the disabled beneficiary (during their lifetime).
- There is an annual limit of income which can be applied other than for the disabled beneficiary (eg. for trustees expenses) which is the lower of 3% of the capital value of settled property and £3000.

Conditions that the beneficiary must meet

- For IHT, must be currently (or expected to be for self-settlement) a disabled person per Sch 1A FA 2005.
- For income tax and CGT, the beneficiary must meet the definition of a "vulnerable beneficiary".

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Tax treatment

The trust is treated as though it is a qualifying interest in possession.

For IHT, the gift into trust is a PET. If the settlor survives seven years, no IHT charge arises. In the case of self-settling, the transfer is not a PET or a CGT, there is no transfer of value.

On the beneficiary's death the value of the trust forms part of their estate. There are no principal charges or exit charges.

For income tax the income is taxed as an IP. This makes use of the beneficiary's personal allowance & marginal rates of tax.

Gains are charged to CGT in the trust as normal for a discretionary trust.

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Report to: Trustees of Kelsby 2003 Trust

From: Tax adviser

Date: 1 May 2018

Subject: CGT and IHT implications of appointments from the Kelsby 2003 Trust.

I set out below the implications to tax of beneficiaries Victoria and Hollie reaching the age of 28 and receiving capital from the Kelsby 2003 Trust.

The Kelsby 2003 Trust has been a relevant property trust since 5 April 2008. It is subject to charges to inheritance tax on principal charges (on each tenth anniversary of the trust's creation) and exit charges on distributions of capital.

Appointment to Victoria

On Victoria attaining 28, she is entitled to a one third share of the trust assets. We assume that on Hollie attaining 28, she received her shares and cash, and therefore Victoria is entitled to half the sum remaining at 4 July 2018. She therefore receives:

Freehold property	108,333	$\frac{1}{3}$ of value
Shares	80,000	
Cash	12,500	

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The distribution gives rise to an exit charge for IHT. This is calculated - using the rate from the previous principal charge in May 2013 and applying it to the distribution, adjusting for the number of quarters since the principal charge:

$$\text{Exit charge} = 3.111\% \times \frac{20}{40} \times 200,833 = \underline{\pounds 3,124.}$$

~~the~~ This assumes that Victoria pays the charge.

The appointment of trust assets gives rise to a capital gain as the trustees and beneficiary are connected persons. The gain is charged on the trustees. Where there is a charge to IHT, the gain can be deferred under s200 TCGA 1992. The beneficiary acquires the assets at the trust's base cost. This will apply to the investment portfolio & Victoria will acquire the shares at £50,000 base cost.

There is no CGT on cash.

However under *Croome v. Appleby*, where an indivisible asset is distributed, the gain does not arise until the whole property has been distributed. This will apply to the investment property.

The gain will not arise until Louise becomes 28 as until this point the property cannot actually leave the trust. At this time in 2025 the gain will not be able to be deferred as for Victoria there will be no charge to IHT.

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We note that Victoria is considering moving to Australia. If assets are distributed while she is non-resident, there is no gift relief available and the CGT charge will be $(80,000 - 11,300) \times 20\% = \text{£}13,740$.
(gain) AC

If the assets are distributed before Victoria becomes non-resident, she will be required to pay a CGT exit charge on moving to Australia, based on the value of the shares at that time.

The trustees are required to file an IHT100 form on distribution of the assets, with the calculation of the exit charge. This must be filed within 6 months of the end of the month of distribution, i.e. by 31 Jan 2019.

The capital gain is reported on the trust's tax return for 2018/19, which must be filed by 31 Jan 2020.

Payments of both taxes are due with the return.

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Appointment of Hollie's share

An exit charge arose on the distribution to Hollie in 2016.

This should be calculated as:

$$\text{Value distributed} = \frac{725,000}{3} = 241,667$$

$$241,667 \times 3.111\% \times \frac{10}{40} = \underline{\underline{£1,880}}$$

This is now around 22 months late and therefore interest and penalties will be due. The IHT100 form should be completed as soon as possible.

A gift relief claim can ^{not} still be made in respect of the shares gain. You have until 31 Jan one year after the date the CGT return is due, i.e. for the gain in tax year 15/16 you have until 31 Jan 2018.

However no gain should have arisen on the freehold property and so the return submitted can be amended up to two years following submission.

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IHT payable on death of Chris Holt 2 May 2017

Lifetime gifts

1) CLT 5 Sep 2011

BPR is withdrawn on death as the trustees no longer own the relevant business property.

Gift 700,000

NRB (325,000)

375,000

IHT at 40% 150,000

Taper relief 60% (90,000) 5-6 years

60,000 payable by Trustees

2) PET 7 Apr 2012

APR withdrawn as David no longer owns the land.

Gift 500,000 NO NRB remedy

IHT at 40% 200,000

Taper relief 60% (120,000) 5-6 years

80,000 payable by David.

3) PET 30 Apr 2012

This gift gets APR as it is occupied for agricultural purposes (the farm is run from the house).

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Death Estate

Holt Contracting Ltd (N1)		780,000
BPR 100%		(780,000)

50% The Barn (N2)

50 acres farmland (N3) 2,495,000

APR 100% x agricultural value (550,000)

BPR 50% on uplift (N4) (972,500) 972,500

~~1,945,000~~

Cash & chattels 185,000

Partnership share 200,000

BPR 100% (200,000)

(No NRB remaining, no RNRB as house to wife) 1,157,500

IHT at 40% £ 463,000

Suffered by David as sole beneficiary.

N1. Valued under related property valuation

$$\frac{26}{51} \times \text{£}1.53\text{m} = 780,000$$

51

† Unlisted trading co shares \Rightarrow BPR at 100%.

N2. Passes by survivorship to wife - exempt & not via executors

$$\text{N3. Market value of land} = \text{£}2\text{m} + \frac{45}{50} \times \text{£}550,000 = \text{£}2,495,000$$

N4. BPR given at 50% on assets used in a partnership in which you are a partner.

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2) Post-mortem reliefs available

Where land is sold at a loss to an unconnected party post-death, relief can be claimed. The development land which was valued at £2m in the IHT comp would give rise to a loss of £200,000 if sold for £1.8m.

This loss can be deducted from the value in the IHT comp before the application of BPR and APR.

This relief is available for losses made on land in the four years commencing on the date of death.

The allowable loss is reduced if any purchases of land are made in the period beginning with the date of death and ending 4 months after the last sale of land in the three years following the date of death.

A claim must be made for the relief within four years of the end of the three years after death (i.e. within seven years of death).

There is no relief available for sales to connected persons such as Michael (by virtue of being partner in the same partnership). (and by being a grandchild of Chris).

~~Note the loss~~

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Note that IHT in respect of the farmland can be paid in installments and these will be interest free as the land attracts APR.

The installment option ceases where land is sold and the IHT becomes due at this point.

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1) Income tax due for trust 2017/18

	Non-savings	Savings	Dividends
	7,800	4,320	7,200
Tax			
1,000	20%	200	
6,800	45%	1,360	
4,320	45%	1,944	
7,200	38.1%	<u>2,743</u>	
		6,247	
less paid at source		<u>(720)</u>	
		5,527	due 31 Jan 2019

If income is distributed to Charlotte, as she was under 18 for part of the year she is a minor beneficiary of a parental settlement and any income distributed to her is taxed as Emily. This will be at higher rates due to her being a HTRP.

Acc Undistributed income which arose more than 5 years before the ten year charge date is included in the principal charge. Income in this category totals £33,160. However the charge is less than 6%. therefore income should not be distributed to the beneficiaries in excess of their basic rate bands.

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The income distribution assume is £45,000^{gross} to Julie.

R185 - Julie.

Net tax

Trust income

45,24,750

20,250.

R185 - Charlotte - no distributions.

Tax pool

Brought forward

38,658

11 year

6,247

On distributions

(20,250)

c/f.

12,161

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2) Principal charge 1 April 2018

Income distribution on UFO basis - does not affect the charge

Current value of trust

Shares 330,000

Rental prop 160,000

Undistributed income > 5 yrs old 33,160

523,160

NRB 325,000

Less Settlers transfers (100,000)

Less exits from trust (50,000)

(175,000)

348,160

Notional IHT 20% 69,632

ER 13.31%

AR on original prop 3.99%

on added prop $\frac{40-28}{40}$ 1.198%

Charge = 3.99% x 363,160 14,490

1.198% x 160,000 1,917

16,407

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