



Chartered
Institute of
Taxation
Excellence in Taxation

The Chartered Tax Adviser Examination

May 2017

Suggested solutions

Inheritance Tax, Trusts & Estates

Advisory Paper

QUESTION 1

1) Income Tax:

No personal allowance is available. The executors are chargeable to Income Tax at the basic rate of 20% for savings and non-savings income and 10% for dividends.

2014/15

Source	Gross Income £	Tax deducted £
Rents	1,300	0
Interest 400 x 100/80	500	100
Dividends 900 x 100/90	1,000	100
Total	<u>2,800</u>	<u>200</u>
Income Tax		
@ 20%	1,800	360
@ 10%	<u>1,000</u>	<u>100</u>
	2,800	460
Deducted at source		<u>(200)</u>
Payable 31/01/2016		<u>260</u>

(payments on account do not apply)

Distributable income:

Gross	2,800
Income Tax	(460)
Expenses	<u>(1,000)</u>
Available for distribution	<u>1,340</u>

2015/16

Source	Gross Income £	Tax deducted £
Rents	7,800	0
Interest 160 x 100/80	200	40
Dividends 1,800 x 100/90	2,000	200
Total	<u>10,000</u>	<u>240</u>
Income Tax		
@ 20%	8,000	1,600
@ 10%	<u>2,000</u>	<u>200</u>
	10,000	1,800
Deducted		<u>(240)</u>
Payable 31/01/2017		<u>1,560</u>

Payments on account
Due for 2016/17:

Payable 31/01/2017	780
Payable 31/07/2017	780

Distributable income:

Gross	10,000
Income Tax	(1,800)
Expenses	(2,000)
Available for distribution	<u>6,200</u>

2016/17

Source	Gross Income £	Tax deducted £
Rents	2,600	0
Interest	1,340	0
Total	<u>3,940</u>	<u>0</u>

Income tax		
@ 20%	3,940	788
Less paid 31/01/2017		(780)
Payable 31/07/2017		<u>8</u>

Distributable income:

Gross	3,940
Income Tax	(788)
Expenses	(800)
Available for distribution	<u>2,352</u>

Capital Gains Tax (CGT)

The executors are entitled to the full annual exemption for the year of death and the following two tax years. They are chargeable to CGT at the higher rate of 28% for 2014/15 and 2015/16 and 20% (28% for residential property) for 2016/17.

2015/16

Share portfolio:

	£
Proceeds	135,000
Probate expenses*	(960)
Cost	<u>(120,000)</u>
Gain	<u>14,040</u>
Annual exemption	<u>(11,100)</u>
Chargeable gain	<u>2,940</u>
CGT @ 28%	<u>823</u>
payable 31/01/2017	

As legatee Vicky is deemed to acquire the rental property at its probate value and at the date of death. This is not a disposal for Capital Gains Tax.

*Under SP 2/04 i.e. 0.8% of probate value may be used.

2016/17

The estate qualifies for principal private residence relief (PPR) on The Gables as Vicky occupied it both before and after the deceased's death and is entitled to 75% of the proceeds of sale (s.225A TCGA 1992).

As she continued to occupy the property to within 18 months of its date of sale full relief is due.

The relief must be claimed by the executors.

2) R185s:

Estate admin expenses can be set against income in the way that is most beneficial to the taxpayer.

Vicky is deemed to receive income in 2015/16 equal to the lower of her income entitlement (for 2014/15 and 2015/16) and the capital value of the rental property appropriated to her in 2015/16.

2015/16	Total £	Non-Savings £	Savings £	Dividends £
Net income	5,655	5,430	225	0
Tax	1,414	1,358	56	0

The administration of the estate ended in 2016/17. Vicky is taxed on her share of the income for 2016/17 and Tom is taxed on his share of the income for the entire administration period having received no previous distributions.

Vicky

2016/17	Total £	Non-Savings £	Savings £	Dividends £
Net income	1,764	1,560	204	0
Tax	441	390	51	0

Tom

2016/17	Total £	Non-Savings £	Savings £	Dividends £
Net income	2,473	2,330	143	0
Tax	618	582	36	0

MARKING GUIDE

TOPIC	MARKS
Income Tax:	
No personal allowance available to executors	0.5
Interest and dividend gross up 2014/15, 2015/16	1
Interest gross 2016/17	0.5
Tax @ 20%/10% as appropriate	1
Tax deducted at source/notional tax on dividends 2014/15, 2015/16	1
Due dates of payment	1
Distributable income – less expenses	0.5
Capital Gains Tax:	
Rental Property not a disposal for CGT purposes, beneficiary takes at probate value	0.5
Share Portfolio:	
Sale proceeds net of probate expenses SP 2/04	1
Deduct probate value	0.5
Full annual Exemption, narrative on rules (0.5 each)	1
CGT @ 28%, due date (0.5 each)	1
The Gables:	
100% PPR, S.225A TCGA 1992 rules, must be claimed	1.5
Sub-Total	11
R185s:	
Vicky 2015/16 – rental property distribution	1
75% 2014/15 + 2015/16 assessable on Vicky in 2015/16	1
Vicky and Tom 2016/17 – end of administration period	1
Vicky 75% 2016/17 income, Tom 25% all years	1
Sub-Total	4
TOTAL	15

QUESTION 2

Draft Inheritance Tax (IHT) Computations on the death of Harold Hardy:

PET to Stan

	£	£
Harold's nil rate band (NRB)		325,000
Transferable nil rate band (TNRB)*		<u>325,000</u>
Total NRB available		650,000
PET	150,000	
Annual Exemption (AE) 2010/11	(3,000)	
AE 2009/10	<u>(3,000)</u>	
Net PET	144,000	
NRB utilised	<u>(144,000)</u>	(144,000)
Chargeable	<u>0</u>	
NRB carried forward		<u>506,000</u>

*available on a failed PET/CLT on death of second spouse

PET to Molly

	£	£
NRB brought forward		506,000
PET	150,000	
AE 2011/12	(3,000)	
Net PET	<u>147,000</u>	
NRB utilised	<u>(147,000)</u>	(147,000)
Chargeable	<u>0</u>	
NRB carried forward		<u>359,000</u>

Chargeable Lifetime Transfer (CLT) to Discretionary Trust

NRB brought forward		359,000
CLT	800,000	
AE 2012/13	(3,000)	
Net CLT	<u>797,000</u>	(359,000)
NRB utilised	<u>(359,000)</u>	
Chargeable	<u>438,000</u>	
NRB carried forward		<u>0</u>
IHT @ 40%	175,200	
Less taper relief (175,200 x 40%)**	<u>(70,080)</u>	
Total	105,120	
Less previously paid by trustees (see below)	<u>(94,400)</u>	
Payable by trustees 30/09/2017	<u>10,720</u>	

**The transfer took place between four and five years before death.

IHT previously paid by the trustees:

	£	£
Harold's NRB		325,000
CLT	800,000	
AE 2012/13	(3,000)	
Net CLT	<u>797,000</u>	
NRB utilised	<u>(325,000)</u>	(325,000)
Chargeable	<u>472,000</u>	
NRB carried forward		<u>0</u>

IHT @ 20%	<u>94,400</u>
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The annual payment of accountancy fees can be exempted as normal expenditure out of income (NEOI).

PET to Heather

	£
PET	150,000
Gift in Consideration of marriage *	(5,000)
AE 2013/14	<u>(3,000)</u>
Chargeable	<u>142,000</u>

IHT @ 40%	56,800
Less taper relief (56,800 x 20%)**	<u>(11,360)</u>
Payable by Heather 30/09/2017	<u>45,440</u>

*by parent of one party to the marriage.

**The transfer took place between three and four years before death.

PETs to Stan, Molly and Heather

	£
PET	10,000
AE 2016/17 (3,000 / 3)	(1,000)
AE 2015/16 (3,000 / 3)	<u>(1,000)</u>
Chargeable	<u>8,000</u>

IHT @ 40%	3,200
Less taper relief***	<u>(0)</u>
Payable by each of Stan, Molly and Heather 30/09/2017	<u>3,200</u>

***No TR is due as the transfers are within three years of death.

The death estate

	£
Residence	700,000
Painting	500,000
Less conditional Exemption (CE)	(500,000)
Cash	500,000
Less funeral expenses	<u>(10,000)</u>
Chargeable free estate	<u>1,190,000</u>

IHT @ 40%	<u>476,000</u>
Payable by the executors 30/09/2017 (or upon submission of the IHT account if earlier)	

MEMO

To: The Senior Tax Partner
From: Mr A Tax Advisor
Date: May 2017

National Heritage Property

General requirements:

Conditional exemption (CE) is a relief from Inheritance Tax (IHT) on designated National Heritage Property.

It is dependent on the nature of the property and the eligibility of the transfer made.

There are six categories of property as follows:

- (a) Pre-eminent object – of national, scientific, historic or artistic interest (not producing an income)
- (aa) including a collection or group of objects which together are pre-eminent
- (b) Land – Outstanding scenic, historical or scientific interest
- (c) Building – Outstanding historic or architectural interest
- (d) Land – essential for the protection and character of amenities at (c)
- (e) Objects – historically associated with (c)

The relief is subject to a formal claim which must identify the asset, state why the asset should be designated and include an undertaking to care for the asset in the UK, to make the asset available to the public (including advertising its availability and providing access without prior appointment at least some of the time e.g. by open viewing or at a public gallery or museum) and to retain the asset for such purposes i.e. confirm that there is no current intention to sell.

The time limit for a claim is two years from the date of the chargeable event subject to extension at HMRCs discretion.

Providing public access for a reasonable entry charge is allowed.

The relief is available on death, a chargeable lifetime transfer (CLT) and on a failed potentially exempt transfer (PET).

Relief is available on a CLT subject to the transferor (and/or spouse) being beneficially entitled to the property in the immediately preceding six years or having inherited the property whilst conditionally exempt.

Absolute exemption is available on a gift or sale by private treaty to certain public bodies specifically set up for the purposes of holding such property on trust for the benefit of the public. These are listed at Schedule 3 IHTA 1984.

Once a claim has been accepted and the asset designated as Heritage Property, unless the CE becomes absolute such as on either of the two events specified above, the relief is subject to either a replacement undertaking (in the case of a PET or exempt transfer to ensure the delivery and futurity of the undertaking) or to a full claim and new undertaking (on a chargeable lifetime transfer or on death).

CE is withdrawn and IHT becomes payable if the property is subsequently sold (other than to a public body mentioned above), gifted to someone who does not replace the undertaking or in the event of a material breach of the agreed terms of the undertaking.

Stan's current position:

Harold's painting falls within category (a).

Stan needs to make a claim within two years of Harold's death to include an undertaking as above to preserve the CE.

Stan's future options:

Stan's future options fall into two categories:

- 1) Those that incur an immediate charge of the IHT conditionally exempted based on the market value at the time of the event:
 - a) Sell on the open market
 - b) Gift or bequeath to someone who does not replace his undertaking or make a new claim as appropriate
 - c) Materially breach the undertaking i.e. by making it unavailable to the public or permanently removing it from the UK.

- 2) Those that preserve or pass on the CE or make it absolute
 - a) Gift (either a PET, exempt transfer or CLT) to someone who replaces his undertaking (or makes a new claim in the case of a CLT).
 - b) Gift to a Schedule 3 IHTA 1984 listed body, in which case the CE becomes absolute.
 - c) Sale by private treaty to a schedule 3 IHTA 1984 listed body, in which case the CE becomes absolute.
 - d) Offering the property in lieu of a liability to IHT under the Acceptance in Lieu scheme (AIL).*

*not in the syllabus, but credit available.

MARKING GUIDE

TOPIC	MARKS
Inheritance Tax computations:	
PET to Stan – NRB/TNRB utilisation, 2 x annual exemption (0.5 each) max 1.5	1.5
PET to Molly – 1 x annual exemption	0.5
Discretionary Trust	
1 x annual exemption	0.5
IHT @ 40%	0.5
Taper relief	0.5
Deduction of tax previously paid @ 20%	1
Person liable for tax and due date	0.5
NEOI for accountancy fees	0.5
PET to Heather	
Gift in consideration of marriage, 1 x annual exemption (0.5 each)	1
Taper relief	0.5
IHT @ 40%, person liable	0.5
PET to Stan, Molly & Heather	
2 x annual exemption (shared), no taper relief (0.5 each)	1
IHT @ 40%, persons liable	0.5
Death Estate	
Net of CE, IHT @ 40%	0.5
Person liable	0.5
Sub-total	10
National Heritage Property – CE	
6 Categories (0.5 per set of categories i.e. (a) & (aa), (b) and (c),(d) & (e))	1.5
Claim – 2 year time limit (with discretionary extension)	0.5
Claim requirements – ID (0.5), why (0.5), undertaking (1), retention (0.5)	2.5
Eligible transfers – including on death (0.5 each) max 1	1
Replacement / new claim depending on type of transfer	1
Stan's current situation – category, new claim required	1
Stan's options and IHT consequences – continuing CE, absolute – 2 ways within syllabus, recall charge - 3 ways (0.5 each, max 2.5)	2.5
Sub-Total	10
TOTAL	20

QUESTION 3

Mrs R Smith
The Midlands

May 2017

Dear Rebecca

Further to our recent meeting I can advise you further as follows:

Gift with reservation of benefit (GWR)

Inheritance Tax (IHT)

Where an individual disposes of a property by way of gift, a GWR will arise where either the donee does not assume bona fide possession and enjoyment of the property or the gifted property is not enjoyed to the entire exclusion of the donor.

The GWR rules will apply to the gift of the holiday cottage to Matthew as you continue to use the property on a regular basis and do not pay market rent for that use. For IHT purposes the holiday cottage is deemed to form part of your estate on death.

The gifts made to your daughters will fall out of charge after September 2017.

Assuming the current market value to be the value chargeable on your death, Matthew would then have a maximum liability to IHT (assuming you died post September 2017 but before 5 April 2018) as follows:

	£
Residence	450,000
Cash	250,000
Holiday Cottage (reserved benefit)	320,000
Total	<u>1,020,000</u>
Less Nil Rate Band (NRB)	(325,000)
Less Residence nil rate band (RNRB)*	<u>(100,000)</u>
	<u>595,000</u>
IHT @ 40%	<u><u>238,000</u></u>
Payable by Matthew	
£238,000x£320,000/£1,020,000	<u><u>74,667</u></u>

*From 6 April 2017 the RNRB is set at £100,000 and is increased by £25,000 per year reaching a maximum of £175,000 in 2020/21. This applies where the residence of the deceased is bequeathed to lineal descendants.

If you ceased to use the holiday cottage or started to pay full market rent of £9,600 to Matthew this would terminate the GWR. Termination of a GWR during your lifetime would itself constitute a deemed potentially exempt transfer (PET) which you would need to survive for a further seven years for this to fall outside your estate.

If you do not survive the requisite seven years the deemed PET to Matthew would benefit from the NRB reducing his liability to IHT to nil. The burden of tax would then fall wholly on the death estate. If you do survive seven years, the deemed PET falls out of charge and the NRB would then become available against your remaining death estate, which taking the residence nil rate band to be £175,000 at that point would reduce the executors' liability to IHT to just £80,000.

Income Tax (IT)

There are no IT implications arising from your reserved benefit in the holiday cottage. If you paid full market rent to Matthew to bring the reserved benefit to an end that rent would be treated as Matthew's income and assessable upon him as such.

Capital gains Tax (CGT)

The market value at the date of original gift is Matthew's base cost for CGT i.e. £280,000 and he would not benefit from the CGT free market value uplift to £320,000 as would normally be the case on death. Ownership for CGT purposes has already passed to Matthew.

The deemed PET on cessation of the GWROB has no effect for CGT purposes.

Pre-Owned Assets Tax (POAT) – your gifts of cash to Mandy and Karen

POAT applies where, in any year of assessment an individual occupies land and either the disposal condition or contribution condition are satisfied. However, POAT does not apply if the gift is already caught under GWR.

The contribution condition applies if the individual has directly or indirectly provided any of the consideration given by another person for an acquisition of an interest in the land. The contribution condition therefore applies to the gifts of cash to both Mandy and Karen.

Where there is limited occupation of less than two weeks unattended or less than four weeks along with the donee, POAT will not apply. This is also the case where occupation is limited by domestic purpose e.g. babysitting. You do not meet the strict time exemptions but it could be argued that your occupation is exempt by falling under the domestic purpose rule (babysitting).

However, if that argument failed the de-minimis rules for land would need to be considered. These exempt the POAT charge if the pro-rated annual rental value is less than £5,000. The pro-rated annual rental values are as follows:

Mandy	$4/52 \times £1,200 \times 12 = £1,108.$
Karen	$10/52 \times £1,500 \times 12 = £3,462.$

The de-minimis is therefore met in both cases.

Where there is an unforeseen change in the donor's circumstances and they occupy land as reasonable provision by the donee for the donor's care and maintenance due to infirmity POAT is disregarded. You should not therefore be subject to a charge to POAT on moving into Karen's house during your treatment and subsequent convalescence, however once you are in remission POAT will apply unless you return to your own residence or pay the full market rent to Karen.

I hope the above to be of some use to you and look forward to hearing from you again soon.

Yours sincerely
Mrs A Tax Advisor

MARKING GUIDE

TOPIC	MARKS
Reservation of Benefit:	
Inheritance Tax:	
Identification of GWR circumstance applicable to the holiday cottage	1
Inclusion in death estate	0.5
Single NRB	0.5
RNRB, lineal descendants	1
IHT @ 40%	0.5
Apportionment, payable by Matthew	1
Deemed PET, cessation of occupation, market value rent	1
Reduced IHT if survive 7 years post deemed PET	0.5
Income Tax:	
No effect of GWROB	0.5
Deemed PET via rental chargeable on Matthew	0.5
Capital Gains Tax:	
Base cost for Matthew (no market value uplift on death), date of acquisition	1.5
No effect of deemed GWROB	0.5
Sub Total	9
POAT	
Disposal/Contribution conditions - contribution condition satisfied	1.5
Limited occupation consideration	2
De-minimis, pro-rata	1
Calculation Mandy (0.5), Karen (0.5)	1
Disregard for change of circumstance	0.5
Sub-Total	6
TOTAL	15

QUESTION 4

An Address
Anytown

Simon Baker
Somewhere

May 2017

Dear Simon,

Trusts, including those for disabled or vulnerable beneficiaries

In your specific situation we discussed that trusts are likely to be very useful for you, William, and Charles, as either now or in the future it will be necessary for someone else to make decisions regarding the assets. This letter sets out the circumstances in which a trust can be set up for a disabled beneficiary and provides specific advice on your situation.

Trusts

The Inheritance Tax (IHT) regime for discretionary trusts, and some life interest trusts consists of an entry charge, principal (10 yearly) charges and exit charges. Where particular conditions are met a trust may be exempted from such charges and this would be the case for a trust created for a disabled person.

An immediate post death interest trust such as the one that owns the house you have the right to live in is an example of a life interest trust that would not suffer 10 yearly or exit charges. Instead the asset is treated as if within the beneficiary's estate (in this instance your estate) on their death. A trust for a disabled person is dealt with in the same manner.

Disabled beneficiary

A disabled person is defined for this purpose as a person meeting certain criteria i.e. 'a person who by reason of a mental disorder within the meaning of the Mental Health Act 1983 is incapable of administering his or her property or managing his or her affairs'. This is likely to be the case for William now, and for you in the future. A second criterion is that a person is in receipt of disability living allowance by virtue of entitlement to the care component at the highest or middle rate, or the mobility component at the higher rate. This is likely to apply to Charles in the future.

Assets settled into trust for your own use

You could 'self-settle' into a qualifying disabled person's trust (place property into trust for your own benefit), as you have a medical condition that is expected to lead to you meeting the definition of a disabled person at some future time. That trust could be either an interest in possession trust where you are the sole life tenant, or a discretionary trust capable of being used only for your benefit during your lifetime.

There would be no immediate IHT charge on creation but on your death IHT would be due on any remaining trust funds as if you had owned them directly. Therefore setting up such a trust for yourself would be IHT neutral.

William

William already meets the definition of a disabled person and you could establish a disabled person's trust for his benefit meeting the conditions set out above. It would be preferable for you to establish the Trust whilst you have full capacity so that it is already in place when you may no longer be able to manage William's affairs.

The gift into trust would be treated as a 'potentially exempt transfer' (PET) and would not attract an IHT charge unless you died within seven years. In that case the gift would utilise the unused nil rate band available on your death with the excess subject to an IHT charge payable by the trustees.

The value of the Trust fund on William's death would be treated as part of his estate for IHT purposes.

Charles

Charles does not currently meet the definition of a disabled person and there is no certainty that he is likely meet this definition whilst you have the mental capacity to set up a trust for his benefit. Unfortunately there is no provision to establish a disabled person's trust for anyone who is expected to become disabled other than under the 'self-settlement' provisions.

You could consider gifting money to a third person who would establish a disabled person's trust for Charles when he meets the necessary conditions. However, this is not recommended.

You could leave funds to establish a trust for Charles on your death when it is more likely he would meet the definition of a disabled person. The funds would suffer a charge of up to 40% on your death but would not suffer ongoing 10 yearly/exit charges.

You could give Charles money now which he could settle on trust for himself. Such a lifetime gift by you would be a PET and would be outside your estate if you survive for seven years from the date of the gift.

The order in which trusts are created (and/or direct gifts made) may affect the amount of IHT payable. I would be happy to advise on this further when you have thought more about the specific amounts you may wish to give.

IHT payable in the current situation and under proposals suggested above

I have set out below some outline calculations which reflect the IHT consequences of these proposals.

1. IHT position if you spend the £300,000 you think you will need before you die, and do nothing with the rest of the money:

IPDI trust	£700,000
Free estate	£1,200,000
Nil rate band	<u>(£325,000)</u>
Chargeable	<u>£1,575,000</u>
Tax at 40%	£630,000

2. Effect of settling a disabled trust for William:

If you settle a disabled trust for William, and survive seven years, then no IHT would be payable on that portion of the money on your death. This would save 40% on any funds settled into trust.

3. Effect of gifting monies to Charles:

If you gave some money to Charles, and survived seven years, then no IHT would be payable on that portion of the money on your death.

In both instances, IHT would, however, be payable on the death of the respective child, but as they are likely to spend the money during their lifetime that is a lesser consideration.

If you died within seven years of any all or all of these transactions, then IHT would be payable. It would be borne at the greatest rate on the latest transaction, due to the operation of the nil rate band on the death calculation, but the overall tax burden would not exceed the position had no gifts had been made, and assuming you survive at least three years from the date of a gift, the overall tax would be lower.

I would be happy to provide more detailed calculations when you have had time to think about this and decide further on any gifts you wish to make.

Please let me know if you would like any further information.

Yours sincerely
X Adviser

MARKING GUIDE

TOPIC	MARKS
Presentation	1
Brief introduction about trusts	1.5
Comment on IPDI trust	1
Disabled trust definition and reference to William	2
Disabled trust effect	1
Self settlement	1.5
William – disabled trust	1.5
Implications of death of disabled beneficiary	1
Implications of death of Simon within seven years	1
Mention order of trusts is important	1
Charles – problems – cannot settle a disabled trust for someone who is not yet disabled	2
Charles – solutions including trust on death or immediate gift now	2.5
Indications of the IHT payable in the current situation and under proposed transactions	3
TOTAL	20

QUESTION 5

Training notes on domicile

General

Domicile is a concept under UK (English and Welsh, Scottish, and Northern Ireland) general law, and UK tax law adapts it bringing in concepts such as deemed and elective domicile. An individual can only have one domicile at a given time and that domicile is within a place governed by a single system of law.

Domicile of origin

An individual inherits their domicile at birth (domicile of origin) from their father if their parents are married, otherwise from their mother. An individual may change domicile (domicile of choice) but the domicile of origin always revives if the domicile of choice is lost without a new domicile being acquired.

Domicile of dependence

While a child is under 16, their domicile changes with that of their father, if their parents were married at the time of their birth or have subsequently married, and assuming the child has a home with the father. Otherwise the child's domicile changes with that of their mother.

Domicile of choice

From age 16, an individual may acquire a domicile of choice. This requires tax residence in the jurisdiction of choice and an intention to remain there permanently and indefinitely.

Deemed domicile

For IHT purposes there is also the concept of 'deemed domicile'. A person is deemed to be domiciled in the UK at a particular time if:

- (a) he was actually domiciled in the UK within the three years immediately preceding the particular time, or
- (b) he was resident in the UK in not less than 17 of the 20 years of assessment ending with the year of assessment in which the particular time falls.

Furthermore it is possible for a person to elect to be deemed domicile in the UK for IHT purposes which is useful to enable unrestricted spouse exemption to be received. They can do this if:

- (a) during the period of seven years ending with the date on which the election is made, the person had a spouse or civil partner who was domiciled in the UK or
- (b) the spouse of the person making the election has died and, at any time within the period of seven years ending with the date of death, that spouse was domiciled in the UK.

Under condition (b) the election may be made within prescribed time limits by the person's personal representatives.

Tax effect of domicile

Domicile is relevant for Income Tax (IT), Capital Gains Tax (CGT) and Inheritance Tax (IHT).

A person who is not domiciled in the UK is entitled to access the 'remittance' basis of taxation for income and capital gains tax purposes,

An individual who is neither domiciled in the UK, nor deemed or elected UK domiciled, is subject to IHT on UK situs assets only.

Examples

An individual who has a UK domicile of origin and emigrates abroad permanently is likely to change their domicile by acquiring a domicile of choice in the new jurisdiction. However, they will continue to be deemed domiciled in the UK for IHT purposes until the relevant amount of time has passed. The burden of asserting the change of domicile is on the person who asserts the change.

If an individual who has a UK domicile of origin emigrated to Australia acquiring a domicile of choice there, but later took up temporary residence in France no longer intending to live in Australia or the UK, but without wishing to live in France permanently, their UK domicile of origin would revive. This would remain the case until they took up residence somewhere else and formed the intention to stay there permanently and indefinitely thereby acquiring a domicile of choice in that new location.

Trusts

A lifetime trust comprising non UK situs assets settled by a non-UK domiciled (or deemed/elective domicile) individual is called an excluded property trust. Such a trust is not subject to IHT entry charges, principal (10 yearly) charges or exit charges, on non-UK situs assets, even if the settlor subsequently becomes domiciled or deemed domiciled in the UK. Excluded property rules supersede gift with reservation rules for settlor interested trusts.

A lifetime trust settled by an individual who is deemed domiciled in the UK is a relevant property trust. Regardless of whether the assets are located in the UK or not, the trust would be subject to an entry charge (broadly speaking, 20% tax on assets settled that exceed the nil rate band), principal charges (a charge of 6% of the asset value in excess of the nil rate band, levied every 10 years) and exit charges (a pro-rated charge similar to the principal charge on capital leaving the trust).

It is therefore of considerable benefit to set up a trust with non-UK situs assets before becoming deemed domiciled in the UK, as a trust set up after that point would be subject to IHT entry charges, principal charges and exit charges.

MARKING GUIDE

TOPIC	MARKS
General concept	
Domicile of origin including mother's where relevant and reversion	1.
Dependence	1
Choice including burden of proof	1.
Tax effect – which taxes, what effect, concept of deemed domicile	2
Emigration example	1.5
Loss of domicile of choice example	1.5
Trusts	2
TOTAL	10

QUESTION 6

Estate of Rosemary Jones Lifetime transfers

April 2014

During life this was a potentially exempt transfer with no IHT due. As death was within seven years of the transfer this then became chargeable.

	£
Transfer	300,000
Less Annual Exemption 13/14	(3,000)
Less Annual Exemption 12/13	(3,000)
	<hr/>
	294,000
Less nil rate band	(294,000)
Chargeable	<hr/>
	0

March 2015

During life this was a potentially exempt transfer with no IHT due. As death was within seven years of the transfer this then became chargeable. At the time of the gift the shares qualified for business property relief, however as they are now listed on the London Stock Exchange this is no longer the case.

	£
Transfer	60,000
Less annual exemption 14/15	(3,000)
Less nil rate band	(31,000)
	<hr/>
Chargeable	26,000
IHT at 40%	10,400

IHT is payable by John.

June 2015

During life this was a potentially exempt transfer with no IHT due. As death was within seven years of the transfer this then became chargeable. At the time of the gift the shares qualified for business property relief, however half of those shares have now been sold this is no longer fully the case. The value of the original gift of the shares that have been sold becomes chargeable. Reinvestment of the proceeds in agricultural property does not preserve the original BPR.

	£
Transfer	100,000
Less annual exemption 15/16	(3,000)
Less business property relief	(50,000)
Less nil rate band	0
	<hr/>
Chargeable	47,000
IHT at 40%	18,800

IHT is payable by John

September 2015

At the time of the gift this was a chargeable lifetime transfer which partially qualified for business property relief. As all of the shares have been sold they no longer qualify for business property relief. However, as

	£
Transfer	250,000
Less business property relief	<u>(200,000)</u>
	50,000
Less nil rate band	<u>(325,000)</u>
Chargeable	0

During lifetime no IHT was therefore due.

On death the nil rate band is no longer available and the business property relief is removed as not all the proceeds were re-invested:

	£
Transfer	<u>250,000</u>
IHT at 40%	100,000

IHT is due by the trustees.

December 2015 – gift by company

During life this was a chargeable lifetime transfer (of the £50,000 undervalue) by Rosemary, however it was fully covered by the nil rate band at the time so no IHT was due. On death this is no longer the case.

	£
Transfer	50,000
Less nil rate band	<u>-</u>
Chargeable	50,000
IHT at 40%	20,000

IHT is payable by John.

December 2015 – gift to Max

During life this was a potentially exempt transfer which would have otherwise qualified for business property relief. On death this became chargeable, however business property relief is still available as Max held the shares, which still qualified until his death. No IHT is therefore due.

Death estate

	£
House	700,000
Cash	50,000
Buy to let property	350,000
Discount for tenancy (Note 1)	(35,000)
Painting	20,000
Land (Note 2)	100,000
Business Property Relief	(100,000)
Business (Note 3)	250,000
Business Property Relief	(250,000)
X Ltd (Note 4)	<u>300,000</u>
Total	<u>1,385,000</u>
Nil rate band fully utilised	
IHT at 40%	554,000
Quick succession relief*	<u>(1,680)</u>
Tax due	552,320

*Quick succession relief is available on the painting as it was inherited three years before and IHT was paid on that transfer. The relief available is:

$\text{£}14,000/\text{£}20,000 \times \text{£}6,000 \times 40\%$ (as death was between three and four years earlier).

£1,680 of relief is available.

IHT is due by the executors and borne by the legatee, Jennifer.

Note 1

As the property is tenanted, a discount of 10% has been given against open market value.

Note 2

As the land has been used in a business by Rosemary for the two years prior to her death, full business property relief is available. It does not matter that the use changed during the two year period.

Note 3

As the business was owned and run for over two years prior to death, full business property relief is available.

Note 4

As the main activity of X Ltd is holding investments, no BPR is available.

MARKING GUIDE

TOPIC	MARKS
April 2014 PET	1.5
March 2015 PET , comment on BPR, and person liable for tax	2
June 2015 PET , comment on BPR, comments on APR replacement, calculation of partial relief and person liable for tax	3
September 2015 lifetime calculation	1
September 2015 death calculation and BPR comment including reinvestment	3
December 2015 CLT – lifetime comment	1
December 2015 - death tax	1
December 2015 BPR PET	2
Death Estate – Correct assets and calculation	1
Quick Succession relief	1.5
Valuation of tenanted property (mark for any sensible discount)	0.5
Comment on land BPR	1
Comment on BPR for X Ltd and owner managed business	1.5
TOTAL	20