Chartered Institute of Taxation

Excellence in Taxation

The Chartered Tax Adviser Examination

May 2018

Inheritance Tax, Trusts & Estates

Suggested solutions

1. SCOTT LINDEN

Our address

Your address

Date

Dear Mr Linden

The Estate of the Late Mr Joseph Linden

Following our meeting I have reviewed the potential Inheritance Tax (IHT) liability arising on your late father's estate and would advise you as follows:

If the estate is distributed in accordance with the Will, the IHT liability will be as follows:

Payable by	£	Due Date
The Executors	95,510	31 July 2018
Yourself in respect of property held jointly	88,163	31 July 2018
Yourself in respect of holiday cottage (GWR)	29,388	31 July 2018
Trustees of the Settlement	146,939	31 July 2018

Although it had been gifted to you, the holiday cottage is included in the calculation of the estate valuation and tax liability as your father continued to use it as he always had. This is known as a Gift with Reservation of Benefit (GWR) and any such assets are included at the market value at date of death.

You have indicated that your father wished to gift some of his estate to charity. If you, as his sole beneficiary, wish to honour this wish a Deed of Variation to make a charitable gift from the estate could be considered. The time limit for executing the Deed is two years from the date of death, and it must be made in writing and signed by you as the person who originally benefits under the Will. To be effective for IHT and Capital Gains Tax (CGT) it must also contain the appropriate statements which will then operate to provide that the estate is treated for IHT purposes as if the gift to charity was under the terms of your father's Will.

If the charitable gift is greater than 10% of the net personal estate the IHT rate will be reduced from 40% to 36%. A merger election can be made to join together any element of the estate for the purposes of calculating whether or not a charitable gift is sufficient to reduce the rate on those elements to 36%.

If the charitable gift is equal to or exceeds 10% of the net estate (after nil rate band) the whole estate can be aggregated, including the trust, and the reduced rate of 36% applied on the total estate. A gift of £90,000 will give a total IHT liability of £291,600, a tax saving of £68,400 making the cost of the gift only £21,600.

With a merger election the GWR in respect of the holiday cottage can also benefit from the lower 36% rate and is included in the total for calculating whether the 10% test is met. Without a merger election the GWR will be charged at the standard rate of 40% i.e. as it is a notional transfer of value it is not part of the free estate.

The time limit for a merger election is two years from the date of death. As Personal Representative, you will need to apply for the election on the general estate, you will also need to apply as owner of the joint property whilst the Trustees of the Linden Family 1986 Trust will need to make the application in respect of the settlement.

It is an HM Revenue and Customs requirement that charities are notified of the legacy being made to them. The details of the charities to which the donations are being made and copies of the executor's notification to the charities that the estate has been varied in their favour, and acknowledgement letters from the charities, must be provided to HM Revenue and Customs before the 36% rate is made available.

I enclose my detailed working for your information.

If you have any questions, please do not hesitate to contact me

Yours sincerely

A Green CTA

Estate of Joseph Linden

Inheritance Tax Liability Workings

ASSETS	**TOTAL**	**Executors**	**Survivorship**	**GWR**	**Settlement**
	£	£	£		£
Property	300,000		300,000		
Investments	200,000	200,000			
Cash	125,000	125,000			
Life interest	500,000				500,000
GWR (deemed part of estate)	100,000			100,000	
	1,225,000	325,000	300,000	100,000	500,000
Less NRB	(325,000)	(86,224)	(79,592)	(26,531)	(132,653)
Taxable estate	900,000	238,776	220,408	73,469	367,347
IHT @ 40%	360,000	95,510	88,163	29,388	146,939

* No RNRB available as none of the interest in the property is closely inherited

Merger election IHTA 1984 Schedule 1A section 7(1)

	£	
Total estate	1,225,000	
10% gift	(90,000)	10% of (£,1225,000-£325,000) £900,000
	1,135,000	
Less NRB	(325,000)	
Taxable estate	810,000	
IHT @ 36%	£291,600	Saving of £68,400. Cost of gift £21,600.

MARKING GUIDE

TOPIC	MARKS
Letter to Personal Representatives	
Responsibility for paying tax. PR's. Joint tenant. GWR. Trustees. Due date (0.5 each)	2.0
Tax liabilities – calculation	
Four elements to estate calculation. General, Survivorship, GWR, Settlement	1.0
Allocation of Nil Rate Band	1.0
No residential nil rate band available interest not closely inherited.	1.0
Tax @ 40%	0.5
Deed of variation	1.0
Time limit	0.5
Statement variation has effect for IHT/CGT. Read back into the will.	1.0
Merger election	1.0
Who makes the claim	1.0
Time limit	0.5
10% Gift by general estate calculated by reference to the total estate	1.0
36% liability total estate	0.5
Saving to the estate, cost of gift to charity (0.5 each)	1.0
Acknowledgement from Charity required for HMRC	1.0
GWR included in Merger election only. Reallocation of NRB to include GWR	1.0
TOTAL	**15.0**

2. GENEA COOPER

1) Notes for meeting with Genea and Philip Cooper.

a) Genea and Philip are connected persons and James is a minor. Multiple tax consequences and compliance responsibilities operate to negate any tax advantage.

Income Tax (IT)

b) Philip as a beneficiary is a connected person (as spouse of the Settlor) irrespective of whether an interest in possession (IIP) or discretionary trust. As such it will be settlor interested trust (SIT).

c) As a SIT all income arising under the settlement, will ultimately be assessed on Genea but with credit for the tax paid by the trust.

d) The trustees will have a liability to tax at basic rate or lower savings rate if an interest in possession and on the first £1,000 of income if a discretionary trust with the balance charged at 45% (for non-dividend income). If due to onward assessment of that income on Genea there is a repayment of IT, or reduction of liability, Genea will need to reimburse the trustees by returning the repayment/reduction to the trust

e) Irrespective of the trust type, the trustees will need to complete a trust return, disclosing the settlor interest and providing Genea with an R185 detailing the trust income/tax credit. Genea will be required to report this on her personal self-assessment return.

f) Trust income actually paid to Philip either as the life tenant or discretionary beneficiary will be treated as franked by a non-repayable tax credit sufficient to discharge any further liability in the beneficiary's hands but they will not be able to claim any tax repayments.

g) A trust, irrespective of trust type, which benefits a minor child of the settlor is a parental settlement. In the case of an IIP trust in James favour the income will be assessable on Genea as it arises until James reaches majority at age 18. With a discretionary trust, the income of the trust will be assessable on Genea to the extent that trust income or capital is applied for James' benefit.

Capital Gains Tax (CGT)

h) Any trust, irrespective of trust type, in favour of Philip will be settlor interested for CGT purposes.

i) The rules in respect of minor children such as James are wider for CGT than IT and the mere possibility of benefit by James, even as a discretionary beneficiary, will be sufficient to be caught by the CGT rules for SITs.

j) The transfer of the property into the trust will crystallise a CGT charge of £51,436 (£415,000 - £220,000 - £11,300 = £183,700 @ 28% = £51,436) payable by Genea through her self-assessment return.

k) A transfer to a SIT cannot benefit from holdover relief under s.260 TCGA 1992 (nor under s.165 TCGA 1992 even if the asset is a qualifying business asset which is not the case here).

l) CGT arising on trust assets will remain the responsibility of the Trustees.

Inheritance Tax (IHT)

m) A trust, irrespective of trust type, created by Genea for Philip's benefit will be a relevant property trust for IHT purposes. The transfer to it of the property portfolio will be treated as a chargeable lifetime transfer made by Genea. Assuming that she has made no other chargeable lifetime transfers in the previous seven years, this will give rise to an IHT liability at 20% on the value transferred in excess of the available nil-rate band. However, as Genea will need pay the entry charge due to lack of liquid assets available in the trust, this will result in an effective rate of 25% calculated as follows:

£415,000 - £325,000 = £90,000
£90,000 x100/80 = £112,500
£112,500 @ 20% = £22,500

This will also be the case if for a trust, irrespective of trust type, created for the benefit of James.

The trust, irrespective of trust type, will be subject to the compliance rules for relevant property trusts for IHT, namely, reporting 10-year principal anniversaries and proportional exit charges, and account for and pay any liabilities to IHT arising.

2) Outright gift to Philip

o) For IT, Philip will have a beneficial interest in the property portfolio and the income will be assessable directly on him. Care should be taken over where the income is paid and purpose for which used since if Genea should be seen to be benefitting from the income it may still be assessable on her.

p) For CGT this will be a nil gain/nil loss transfer as a spousal gift and thus will be CGT neutral.

q) For IHT, this will be covered by the spousal exemption and thus will be IHT neutral.

Outright gift to James (bare trust as James is a minor).

r) For IT, this will be a parental settlement and the income would be assessable on Genea until James reaches majority after which he would be assessed personally. With current rental income of £35,000 the £100 de-minimis threshold, by which the income is ignored, will not apply.

s) For CGT, the gift would be a chargeable disposal by Genea without the benefit of holdover relief. CGT on the future sale of the properties would however be assessable on James, utilising his personal annual exemption and basic rate band. Gifting the individual properties over several tax years will maximise use of annual exemptions and spread the CGT cost.

t) For IHT, this would be a PET and Genea would need to survive the gift by seven years for it to gain full exemption.

MARKING GUIDE

TOPIC	MARKS
Identify settlor interested trust for IT irrespective of type – Philip	0.5
Income tax assessed on Genea	0.5
James – minor – must be provision made for him – IIP or Discretionary payment of income	1.0
Trust responsible for returning and paying the tax, income retains source for settlor R185, personal tax return entry, return of repayments required (0.5 each, max 2)	2.0
Highest rate of tax for non-settlor beneficiary, no repayment of tax credit	0.5
Settlor interested trust – CGT – irrespective of type – Philip	0.5
CGT rules wider than for IT in respect of minor children – as for Philip	0.5
CGT arising on transfer in – calculation	1.0
No holdover relief available,	0.5
Trustees responsible for Capital gains arising within the trust	0.5
Relevant property trust, non-qualifying IIP	0.5
Lifetime inheritance tax charge, calculation, grossing up – no liquid funds	1.5
Trust - 10 year charges and exit charges	0.5
Subtotal	10.0
Alternatives. Outright Gift to Philip	0.5
IT on Philip - beneficial interest	1.0
CGT Nil gain nil loss	0.5
IHT spousal exemption,	0.5
Outright gift to James	0.5
IT settlor interest to James majority (as trust)	0.5
CGT (as trust), James on future sale, split gift to use annual exemption	1.0
IHT – PET	0.5
Subtotal	5.0
TOTAL	**15.0**

3. TRUSTS FOR THE DISABLED

1. Reasons for Setting up a trust for the disabled or Disabled Person's Interest (DPI)

Financial support.
Tax mitigation.
To protect the vulnerability of the beneficiary.
To preserve/enable entitlement to income related state benefits (if the trust is discretionary and not self-settled)
(The list is not-exhaustive)

2. Who is able to set up the Trust?

Anyone – e.g. parents/relatives/friends

Self-settlement (including in anticipation of losing mental/physical capacity (Inheritance tax only))

3. The Definition of a Disabled Person (DP) for this purpose

A person who by reason of a mental disorder within the meaning of the Mental Health Act 1983 is incapable of administering his/her property or managing his/her affairs.
Or
A person who qualifies under a "benefits test" i.e. is in receipt or eligible for one of the following benefits:

1) increased disablement pension
2) attendance allowance
3) care component of disability living allowance (DLA) (highest or middle rate) or mobility component of DLA (higher rate) *
4) personal independence payment (PIP) *
5) armed forces independence payment

* Post 6 April 2014.

4. Qualifying conditions - Trust

Income Tax (IT)/Capital Gains Tax (CGT):

Legislation introduced in 2005 for trusts for "vulnerable beneficiaries" defined as:

Disabled Person (DP) (above)
Beneficiaries under the age of 18 years, at least one of whose parents have died*

*not the subject of this training session

Whilst the DP is alive or until termination of the trust the trust property must be applied for the DP; and
The DP is entitled to all the income from the trust, or alternatively, if there is no "interest in possession (IIP)", no other beneficiary is entitled to have any trust income applied for their benefit;

Non-disabled beneficiaries may have trust capital applied for their benefit up to a maximum of £3,000 (or 3% of the value of the trust capital if lower) per tax year.

Inheritance Tax (IHT):

Under S.89B 1(a) – 1(b) IHTA 1984:

Post 9 March 1981 settlement / self-settlement in anticipation of disability post 21 March 2006
During the lifetime of the DP there is no IIP in the settled property i.e. it is a discretionary trust;

Under S.89B 1(c) IHTA 1984:

Post 21 March 2006 entitlement to an IIP

Under S.89B 1(d) IHTA 1984:

Self-settlement post 21 March 2006 on IIP in anticipation of disability

Any property that is applied during the lifetime of the DP must be applied for the benefit of that beneficiary (subject to the £3,000/3% rule above). ^^

^^for property settled before 17 July 2013 up to half of that property is able to be applied for non-disabled beneficiaries.

5. Qualifying Conditions - Beneficiary

Income Tax (IT)/Capital Gains Tax (CGT):

A beneficiary who is a "disabled person" as defined (see above)

Inheritance Tax (IHT):

The criteria for a person to qualify as a DP is the same as for IT and CGT (above).

In addition, a DP (for IHT purposes only) also includes a settlor who transfers or settles their own property into a trust for themselves at a time when they have a condition which it is reasonable to expect will lead to their becoming a DP.

(For a DP to qualify under this heading the terms of the trust must provide that during the lifetime of the settlor/beneficiary, no other beneficiary can benefit from the trust property).

6. Tax treatment

IT & CGT treatment of trust for "vulnerable" beneficiaries including a DPI:

The trustees and the beneficiary can jointly make a "vulnerable person election" using form VPE1. If no election is made then the trust is taxed using normal trust rules.

The election is irrevocable.

The election comes to an end when the beneficiary ceases to qualify as a vulnerable beneficiary. The trustees must inform HMRC.

The election must be made no later than 12 months after the normal filing date for the first trust return for which it is to have effect.

Once in place the trustees can make a decision each tax year whether or not to claim for "Special tax treatment" to apply to the trust income and/or gains. This claim is made on the self-assessment trust tax return and applies to both IT and CGT for the year in question, there is no mix and matching of the rules.

The claim allows the trustees to effectively stand in the shoes of the beneficiary and be taxed as if the beneficiary had received the trust income or made the trust gains personally, thereby achieving a lower tax liability.

Any discretionary trust income actually distributed to a discretionary beneficiary (to which normal distribution rules apply) can result in an increase in the liability to tax on the trustees by 1) being taken into account in the alternate calculation for purposes of the election and 2) having an adverse effect on the tax pool resulting in a tax pool charge on the trustees. For these reasons the trustees have the option to elect for special tax treatment not to apply.

A settlor interested trust is automatically taxed on the settlor for IT purposes but still qualifies for special CGT treatment (from 6 April 2008 onwards).

Special CGT and IT treatment does not apply in the year of death of the DP.

IHT treatment of a DPI:

A DPI is not subject to the ten year anniversary charge or the exit charge but is taxed as though it were a qualifying IIP i.e. it is aggregated with the DPs estate on death.

Transfers into a DPI during a settlor’s lifetime (non-self-settled) will be a potential exempt transfer (PET).

Transfers into a DPI during a settlor’s lifetime (self-settled) is not treated as a transfer of value and is IHT neutral.

There are no special rules for the IHT due by the estate in respect of a DPI trust created on death.

MARKING GUIDE

TOPIC	MARKS
Reasons for setting up a DPI (0.5 each max 1)	1
Who – others, self, (in anticipation of disability IHT only) (0.5 each)	1.5
Conditions:	
Trust (IT, CGT & IHT): applied for benefit of DP only, de-minimis	1
Trust (IT & CGT): IIP or no income other	0.5
Trust (IHT): DT / post 22 March 2006 IIP, no income other	0.5
Beneficiary (IT, CGT & IHT):	
Mental disorder – Mental Health Act 1983, incapable	1
"benefits test" in receipt of or eligible (0.5) – examples (0.5 each – max 1.5)	2
Beneficiary (IHT only): anticipatory self-settlement, no benefit others during lifetime	1
IT/CGT treatment:	
VPE1, joint election, 12 months > 31/1 > 5/4, irrevocable, cessation (0.5 each max 2)	2
Annual claim for special IT/CGT treatment. Effect, choice	1.5
Settlor interest exclusion IT	0.5
No special CGT treatment year of death DP	0.5
IHT Treatment:	
No TYC/exit charge, part of DP estate	1
Transfers in lifetime (PET), death estate normal rules apply	1
TOTAL	**15**

4. THE KEBBY 2003 TRUST

Report for the Trustees of the Kebby 2003 Trust

You have requested advice in respect of the Capital Gains Tax (CGT) and Inheritance Tax (IHT) implications of Victoria's absolute entitlement to her share of the trust on attaining age 28.

Victoria

Victoria will become absolutely entitled to a 50% share in the trust capital on 4 July 2018. Based on the estimated valuations provided, the assets to be appointed will be:

	£
Freehold Property	162,500
Investment portfolio	80,000
Cash	12,500
Total	255,000

IHT

The appointment of assets to Victoria will trigger an IHT exit charge calculated with reference to the rate established at the last ten year anniversary in May 2013 scaled back for complete quarters elapsed since that date. The IHT charge and IHT forms must be paid/submitted to HM Revenue and Customs by six months from the end of the month in which the event occurred thus by 31 January 2019.

The exit charge arising on the appointment is:

£255,000 x 20/40 x 3.111% = £3,967.

This sum should be deducted from the cash funds being appointed to Victoria.

CGT

Victoria's entitlement to her share of the trust capital will be a chargeable event for CGT purposes and should be reported on the Trust's 2018/19 self-assessment return which must be submitted to HM Revenue and Customs (HMRC) by 31 October 2019 (paper) or 31 January 2020 (online). The tax is due for payment by 31 January 2020.

Investment portfolio

If the share of the portfolio is sold with the cash distributed, the Trustees will be liable for any CGT arising. If the portfolio share is transferred in specie, this will still be a chargeable event for CGT however, as this will also be a chargeable event for IHT purposes there is an option to claim s.260 TCGA 1992 holdover relief. This operates to defer recognition of the gain with Victoria receiving the investments at their original cost (see calculations below).

The Trustees and Victoria will need to make a joint holdover relief claim. The time limit for making the claim is four years from the end of the year in which the transfer takes place i.e. by 5 April 2023.

Freehold property

Under the rule established in Crowe v Appleby, an indivisible asset such as land is not treated as disposed of for CGT purposes until all the beneficiaries have become absolutely entitled to their share. Accordingly, even though Victoria will receive a share of the property on reaching age 28 (as did Hollie) recognition of the chargeable event for

CGT purposes will be postponed until the whole property has vested when Louise reaches age 28 in September 2025. At this stage only the gain relating to Louise's share will be eligible for a holdover relief claim as it will be the only part of the transaction with an IHT chargeable event occurring at the same time.

Possible move overseas

If Victoria becomes non-UK tax resident within six years of the end of the year in which the appointment is made the holdover relief claim will be clawed back by HMRC and the original CGT liability (treated as arising in that year of clawback) will become payable, as if no deferral had been claimed.

Hollie

IHT

The IHT return reporting the exit charge due in respect of the appointment of assets to Hollie on her 28th birthday has not been completed, nor has the IHT been paid

The assets transferred to Hollie were:

	£
Freehold Property	150,000
Investment portfolio	75,000
Cash	16,667
Total	241,667

The exit charge due was:

£241,667 x 10/40 x 3.111% = £1,880.

The IHT forms and tax payment were due by 31 July 2016. There will be late filing penalties in respect of the return and interest due on the late payment.

The exit charge was not deducted from the funds paid to Hollie therefore unless Hollie agrees to meet the payment due the value of the assets appointed will need to be grossed up and the IHT recalculated accordingly.

CGT

Hollie will have received her share of the property on attaining age 28, however, as with Victoria's position described above, recognition of the chargeable event will be postponed until Louise becomes absolutely entitled to her share.

As the investments were transferred to Hollie rather than being sold, the Trustees can make a joint holdover relief claim with Hollie to defer the gain as you are still within time to do so. However, if Hollie does not consent to the holdover relief claim the trustees will be liable for the CGT which will be treated as arising in 2015/16.

If a claim is made Hollie's base cost going forward will be the same as Victoria's i.e. £50,000 (see below).

Workings

Without a Holdover relief claim, the potential CGT liabilities for the Trustees are as follows:

		Hollie		Victoria
		£		£
Market value	18 Jan 2016	75,000	4 July 2018	80,000
Cost	14 May 2003	(50,000)	14 May 2003	(50,000)
Gain		25,000		30,000
Annual exemption		(5,550)		(5,650)
Chargeable gain		19,450		24,350
CGT payable	28%	5,446	20%	4,870

With a holdover relief claim the gain is deferred and Hollie's and Victoria's respective base costs going forward will be £50,000 each instead of the market value of the date of their respective appointments.

MARKING GUIDE

TOPIC	MARKS
Victoria	
IHT - Value of Estate appointed	1.0
Chargeable event for IHT Exit/Proportional charge	0.5
Filing deadline IHT100 – 6 months from end of month	0.5
Due date for tax 31 Jan 2019	0.5
Calculation of exit charge, Relevant fraction	1.0
IHT paid from exiting funds	0.5
CGT – chargeable event	0.5
Gains reported on SA return	0.5
Due date for payment of CGT	0.5
Trustees liable for gain	0.5
Investments - Holdover relief claim s260, made jointly, time limit 4 years from end of year, defers the gain (0.5 each)	2.0
Property – Crowe v Appleby – awareness of rule	1.0
Indivisible asset. Not disposed of for CGT	1.0
CGT deferred until Louise reaches 28	1.0
Only Louise eligible for holdover claim	1.0
Non-UK resident within 6 years of claim – clawback of deferred gain	1.0
Base cost with holdover	0.5
Report layout	0.5
Sub-total	14.0
Hollie	
IHT exit charge on 28th birthday	0.5
Value of assets appointed	1.0
Exit charge calculation	1.0
Due date, interest and penalties	0.5
IHT paid from exiting funds, or grossed up	0.5
No CGT liability on property, holdover on investments	1.0
Hold over still in time	0.5
Calculation of potential CGT liability for trustees	1.0
Subtotal	6.0
TOTAL	**20.0**

5. CHRIS HOLT

1) Inheritance Tax (IHT):

Lifetime Transfers:

The trustees:

5/9/11

Chargeable Lifetime Transfer (CLT) of shares when made but 100% Business Property Relief (BPR) applied such that nil tax paid on creation.

As the trust was wound up in favour of David on 5 April 2015 the trustees no longer own the property and cannot therefore meet the additional conditions required to qualify for BPR at the date of death of the transferor.

IHT becomes chargeable on the trustees as follows:

	£
Shares	700,000
Less Nil Rate Band (NRB)	(325,000)
	375,000
IHT @ 40%	150,000
Less Taper relief (TR) – 60% (Note 1)	(90,000)
Due and payable by trustees (on 30 November 2017)	
	60,000

This does not affect the cumulative total carried forward i.e. this remains at nil.

Note 1
Between five and six years before date of death.

David:

7/4/12

Failed PET of Farmland:

The farmland qualified for APR (at 100%) on transfer from Chris to David as it was owned by Chris and used in the farming business in which Chris was a partner. It similarly would have qualified for BPR (at 50%) had there been a premium on the property at that time.

David no longer owns the farmland and so the gift does not meet the additional conditions for it to qualify for APR or BPR on Chris's death.

As David gifted the farmland to Michael no proceeds were received that were capable of reinvestment, even if Michael had made payment or part payment for the land this would not be an arm's length transaction and so the replacement property provisions cannot apply.

	£
Land	500,000
Less Nil Rate Band (NRB)	(325,000)
	175,000
IHT @ 40%	70,000
Less TR – 60% (Note 1)	(42,000)
Due and payable by David on 30 November 2017	28,000

Note 1
Between five and six years before date of death.

30/4/12

Failed Potentially Exempt Transfer (PET) of Farmhouse:

The farmhouse qualified for 100% APR on the date of gift.

As related property the value of the gift of the 50% share from Chris to David was £100,000.

The farmhouse was still owned by David at Chris's death, the farmhouse remains occupied for the purposes of agriculture by David and Michael. It is common occupation that is important not common ownership ("The Hanson case" (2013)).

100% APR therefore also applies on Chris's death.

The death estate:

Joint assets:	£
The Barn (Note 1)	160,000
Spouse exemption	(160,000)
Chargeable	0
Free estate:	
Unquoted shares (Note 1) (W1)	780,000
BPR 100%	(780,000)
Farmland (Note 2) (W2)	2,495,000
APR (100%)	(550,000)
BPR (50%) (W3)	(972,500)
Partnership share	200,000
BPR (100%)	(200,000)
Cash & Chattels	185,000
Chargeable	1,157,500
IHT @ 40% due and payable by executors on 30 November 2017	463,000

Note 1
Related property

Note 2
Development value

W1
26/51 x £1,530,000 = £780,000.

W2
£2 million + (45/50 x £550,000) = £2,495,000.

W3
£2 million – (5/50 x £550,000) = £1,945,000 x 50% = £972,500.

2) **Post Mortem reliefs:**

There are three post mortem reliefs from IHT of which only two are relevant in this case:

- Related property
- Land and property

Common conditions for related property and land and property reliefs are as follows:

- Both reliefs must be claimed within the permitted timeframe.
- The sales must be made by appropriate person, as defined, being the person liable for the IHT attributable to the value of the property disposed. This is usually the personal representatives but it may also be for instance be a specific legatee who bears the tax.

Related property:

S.176 IHTA 1984 provides relief for sales made within three years of the death as a separate interest for less than the related property valuation.

The property must have originally been valued under the related property provisions.

The sale must be at arm's length and freely negotiated at the time of sale.

The sale must not be made in conjunction with the sale of the related property or other property with which it was valued.

There must be no connection between the vendor and the purchaser.

The seller must not be able to re-acquire the property.

The relief is not in the form of the lower sale price but rather the independent valuation at the date of death.

In the case of the sale to Michael of the 26% shareholding in the contracting company relief is precluded as David, as beneficiary of Chris's estate, is connected with his son Michael.

Land and Property:

Relief is available for sales of land at less than its date of death value within four years of the date of death under S.190 – 198 IHTA 1984.

The relief is a fall in value relief (as above). This is based on gross proceeds before incidental costs of sale.

Sales in the fourth year are only taken into account if they are at a loss, otherwise all qualifying sales of land in the first three years after death are aggregated.

Certain sales are excluded from relief being:

Those to a person (or spouse, civil partner, child or remoter issue of a person) beneficially entitled to or having an interest in possession of the asset at any time between the date of death and sale.

Those where the loss is below the de-minimis amount of less that the lower of £1,000 or 5% of the value on death.

Sales of land which attract 100% APR and/or BPR.

In this case the land sold to Michael is excluded by 1) him being the child of David and 2) it benefitting from APR at 100%.

The only land available for the relief is therefore the sale of the development land at a loss of £2 million - £1.8 million = £200,000. Relief will be restricted by APR/BPR available.

MARKING GUIDE

TOPIC	MARKS
Inheritance Tax:	
Trustees:	
CLT- 100% BPR	0.5
Change of ownership – additional conditions for BPR unable to be satisfied by trustees	0.5
Trust NRB, IHT @ 40%, TR, payable by trustees 30/11/17	2
No effect on cumulative total carried forward	0.5
David:	
Farmland:	
PET – 100% APR, 50% BPR	0.5
Change of ownership – additional conditions not satisfied by David	0.5
Replacement property – No proceeds/Non-arm's length transaction excludes	0.5
NRB, IHT @ 40%, TR, payable by David 30/11/17	2
Farmhouse:	
PET – 100% APR, related property value	0.5
Retained ownership and remains in occupation for purposes of agriculture "the Hanson case" (2013), 100% APR on death	1
Death estate:	
Barn – related property, spouse exemption	0.5
Unquoted shares – related property, 100% BPR	0.5
Farmland – development value, 100% APR, 50% BPR	1
Partnership share – 100% BPR	0.5
IHT @ 40%, payable by executors 30/11/17	1
Sub-Total	**12**
Post Mortem Reliefs:	
ID two relevant reliefs	0.5
Common conditions	0.5
Related property – individual conditions (0.5 each, max 2.5)	2.5
Connected person exclusion from relief	0.5
Land and property – individual conditions (0.5 each, max 2)	2
Child/100% APR exclusion – land sold to Michael	1
Relief available development land only, restricted by APR/BPR	1
Sub-Total	**8**
Total	**20**

6. THE HEGARTY DISCRETIONARY SETTLEMENT

1) Optimum Income Distribution

With effect from 6 April 2014, un-accumulated income which arose more than five years before the ten-year anniversary is to be regarded as relevant property at the time of the ten year anniversary for purposes of calculating the ten year charge.

In order to avoid any of the undistributed income being included as relevant property at the ten year anniversary £33,160 (being the undistributed income that arose in the five year period ended 31 March 2013) needed to have been distributed by 31 March 2018.

As Emily created the settlement when her daughters were both minors it was a parental settlement and she would have been assessed at (higher rate) on any income distributed to them before the age of 18 (or marriage beyond the age of 16) to the extent that income exceeded £100 per annum.

Julie is 21 and Charlotte reached age 18 on 15 September 2017. In order to avoid any of the income being assessed at higher rate on Emily, (or to the extent of income in excess of the personal allowance and basic rate band on either of Julie or Charlotte) the income should have been distributed 50% to Julie (at any time before 31 March 2018) and 50% to Charlotte (between 15 September 2017 and 31 March 2018).

R185 Entries (each of Julie & Charlotte):

R185 (Trust income)
Year to 5 April 2018

	£
Net income distribution	16,580
Tax credit x 45/55	13,565

Note: credit will be given for any combination that covers the personal allowances of each beneficiary without exceeding the basic rate band of either.

Tax Pool:

	£
B/fwd	38,658
Additions:	
Non-savings – £1,000 @ 20%	200
Non-savings – £6,800 @ 45%	3,060
Savings – £3,600 @ 45%	1,620
Dividends – £7,200 @ 38.1%	2,743
Available to frank distributions	46,281
Tax on distributions (above x 2)	(27,130)
C/fwd	19,151

2) Ten Year Anniversary (TYA) Charge:

Current value:

The value of the relevant property at the ten year anniversary (net of Agricultural Property Relief (APR)/Business Property Relief (BPR)) was as follows:

	£
Share portfolio	330,000
Cash (Note 1)	0
Property	160,000
Undistributed income (Note 2)	0
	490,000

Note 1
The capital within the current account had already been distributed to Julie and Charlotte. The current account comprised only undistributed income.

Note 2
In accordance with the answer at 1) above there is no undistributed income to be taken into account on the TYA on the assumption that it has all been paid out prior to 31 March 2018.

There are no related trusts to consider.

Previous cumulative total:

	£
Personal cumulative total	100,000
Previous exits in the last ten years (Note 1)	50,000
	150,000

Note 1
The beneficiaries paid any tax due on the respective capital appointments made on their 18th birthdays and thus there is no requirement to gross up.

The Principal Charge:		£
Value on trust fund Transfer		490,000
Nil rate band at anniversary date	325,000	
Capital distributions	(150,000)	
Balance of nil rate band		(175,000)
Taxable		315,000
Notional Tax @ 20%		63,000
Effective rate £63,000/£490,000		12.857%
Actual rate 3/10 x 12.857%		3.857%
Principal Charge £490,000 x 3.857%		18,899
Less relief for added property (note 1)		(4320)
IHT due by trustees' payable by 31 October 2018.		14,579

Note 1 - Relief for added property:

	£
Added property	160,000
No of complete quarters before added property became relevant property	28
Relief £160,000 x 28/40 x 3.857%	4,320

MARKING GUIDE

TOPIC	MARKS
Optimum distribution, R185s & Tax Pool:	
Amount of undistributed income to be distributed – 5 year rule (1.5), no reduction, consider formal accumulation, timing, to whom, parental settlement consideration, personal allowance, tax bands (1/2 each max 2.5)	4
R185s - undistributed income disregarded for TYC = net, tax x 45/55 x 2, any combination that fully utilises personal allowance of both beneficiaries and does not exceed basic rate band of either	1
Tax Pool:	
Basic rate	0.5
Higher rate by savings/non-savings & dividend @ 45%/38.1% as appropriate	1
Tax on distributions	0.5
Sub-Total	7
Ten year anniversary:	
Current value of relevant property (excluding undistributed income, cash distributed to Julie & Charlotte before ten year anniversary)	2
Previous cumulative total (including cash distributed to Julie & Charlotte before ten year anniversary)	1
Available nil rate band remaining after previous cumulative total	0.5
Notional tax – current value of relevant property – NRB x 20%	1
Effective rate – notional tax / current value of relevant property	0.5
Actual rate - x 3/10	0.5
Principal charge – current value of relevant property x actual rate	0.5
Identify Added Property value	0.5
No of complete quarters before became added property (n)	0.5
Fraction (n)/40	0.5
Calculate relief – added property value x (n)/40 x actual rate	0.5
Sub-total	**8**
TOTAL	**15**