

THE CHARTERED INSTITUTE OF TAXATION

APPLICATION AND PROFESSIONAL SKILLS

Inheritance Tax, Trusts & Estates

May 2021

TIME ALLOWED

3 HOURS 30 MINUTES

- In order to secure a pass in this exam, you will be required to demonstrate competence in each of three skills.

You will be assessed across your answer as a whole for Structure. A pass or fail grade will be awarded.

You will be assessed for competence in a number of broad topics for the following skills:

- Identification and Application
- Relevant Advice and Substantiated Conclusions

For each topic for each of these two skills, a grade will be awarded. The grades for those topics will be weighted and averaged to produce a final grade for each skill of 0, 1, 2, 3 or 4. A grade of 3 or 4 is required to demonstrate competence.

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- Scots Law candidates may provide answers referring to Land and Buildings Transaction Tax rather than Stamp Duty Land Tax.
- Except as set out below or indicated by additional information in the question, you may assume that 2020/21 legislation (including rates and allowances) continues to apply for 2021/22 and future years.

1) You MUST assume that the UK remains within the European Union.

2) You MUST ignore all temporary Covid related legislation including furlough, grants, loans and the reductions in VAT and SDLT rates.

Except in relation to points 1) and 2) above, candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.

- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

You are a tax manager in a firm of Chartered Tax Advisers. Following a meeting last week, your Tax Partner, Alison Clarke, has received an email (**EXHIBIT A**) from Richard Cresswell and Tara Marchant who are trustees of the Cresswell Family Settlement, a new client of your firm. The Cresswell Family Settlement was a lifetime trust created by Lady Lily Cresswell in 2014. The current trustees were not aware of the existence of the trust until recently as their elderly aunt and uncle were the original trustees.

Lily's death on 2 March 2019 has triggered a further Inheritance Tax charge which is now is overdue and one of the trust assets must be sold to fund the liability. In addition, the beneficiaries of the trust are approaching their respective 30th birthdays, after which the trust will cease.

Alison has asked you to review the email and the other documents provided by Richard and Tara (**EXHIBITS B and C**) and to prepare a draft report to the trustees addressing their concerns.

The following exhibits are provided to assist you:

EXHIBIT A: Email from Richard Cresswell to Alison Clarke on behalf of the trustees

EXHIBIT B: Valuation of assets held by the Cresswell Family Settlement

EXHIBIT C: Financial information for Cresswell Garden Centres Ltd

EXHIBIT D: Pre-seen information

Requirement:

Prepare a draft report to the trustees of the Cresswell Family Settlement, for review by Alison Clarke, which provides recommendations in relation to the sale of assets and advice on the tax issues arising on the cessation of the settlement.

Continued

Continuation

EXHIBIT A

Email from Richard Cresswell to Alison Clarke on behalf of the trustees

To: Alison Clarke <alison.clarke@abctax.co.uk>
From: Richard Cresswell <richard@cgc.co.uk>
Date: 1 May 2021 14:10
Subject: Cresswell Family Settlement

Dear Alison

Thank you for your time last week. Tara and I have discussed matters further and have detailed below our areas of concern.

As you know, we were not aware that the Cresswell Family Settlement existed until recently. Our mother, Lily, was always very private and never discussed her financial affairs with us. She only confided that a trust had been created to our Uncle Oliver and Aunt Violet. Amanda and Darcy have always declared the income from the assets that turned out to be held on trust on their own tax returns. Oliver administered the trust since its creation but both he and Violet retired as trustees in March this year due to ill health and Tara and I agreed to be appointed in their place. As requested, I enclose valuations of the trust assets which also include Oliver's notes (**EXHIBIT B**).

The solicitor dealing with our mother's estate has advised us that an Inheritance Tax liability of £70,500 (including interest charges calculated to the end of June 2021) was due on 30 September 2019, as Lily did not survive seven years from creating the trust. The trust bank account only holds a small balance, so we need to sell a trust asset to fund this.

The best option to raise the money quickly will be to sell either Bramble Cottage or the paddock. Bramble Cottage is in a terrible condition, but we think there will be considerable interest from property developers if it is listed in the next local property auction on 31 May 2021. Alternatively, the paddock could be sold to the neighbouring farmer, as he has always wanted to buy the land.

If Bramble Cottage is sold, the combined (VAT inclusive) auction house and legal fees will be 1.5% of the proceeds. If the paddock is sold, our solicitor will charge a flat fee of £500 (VAT inclusive) for the legal transfer. Either option will raise sufficient proceeds but obviously we have not factored in the tax consequences and need your assistance with this.

The second area of concern is that my daughter Amanda will be 30 years old on 18 September 2021 and Tara's daughter, Darcy will be 30 years old on 21 May 2023, after which the trust will end. Please would you clarify the tax issues we should be aware of in relation to this and if there is any action we need to take before Amanda's birthday?

Amanda and Darcy have agreed to pay the tax due when the trust ends as they have each received a sizeable cash legacy from their grandmother. However, we do not want either of them to be left in a position where the tax liabilities from the trust consume most of their inheritance. They both plan to keep the shares in the company as they want the ownership to stay within the family and they are also happy to keep the rental assets as long-term investments.

Finally, we should tell you about the changes made to the business (Cresswell Garden Centres Ltd) over the past few years as this may be relevant. As you know, the company was not in a healthy financial position when our mother died. She had a strong view on how the business should be run and always insisted that plants and bulbs would be the only products on sale. She refused to allow any gardening related products, other merchandise or food and drinks to be sold and she resisted online sales until 2012.

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Continuation

In Summer 2019 we undertook a major overhaul of the business and decided to reduce the floor space in each store dedicated to our own stock down to about 60% of the total area. We now only stock the most unusual varieties of plants and bulbs, but we have not cut staff numbers as we want to maintain the best levels of customer service.

The remaining area in each centre is now let to third-party retailers who sell items such as outdoor clothing and shoes, art and craft materials, gardening equipment and furniture. Part of the area in each centre is also let to a well-known bakery chain who run an in-store café on the premises.

We have been amazed at the increase in customers visiting each site and the demand for our specialist plants and bulbs means we have been able to increase prices. The increase in profits in such a short space of time has exceeded our expectations and Tara and I wish that we had persuaded our mother to make these changes years ago.

Enclosed is some financial information prepared by the company accountant, which he says will be of use to you (**EXHIBIT C**).

We look forward to hearing from you shortly regarding our queries.

Yours sincerely

Richard Cresswell
On behalf of the trustees of the Cresswell Family Settlement

Continued

Continuation

EXHIBIT B

Valuation of assets held by the Cresswell Family Settlement

<u>Assets settled</u>	<u>Lily's acquisition price</u> £	<u>Value on 12 August 2014</u> £	<u>Apportioned Inheritance tax (see note 3)</u> £	<u>Current value</u> £
300 ordinary shares in Cresswell Garden Centres Ltd	See note 1) below	2,400,000	£nil	2,625,000
Wilton House, Oxfordshire (inherited from Percy in 2001)	420,000	1,335,000	269,000	1,500,000
Bramble Cottage, Oxfordshire (purchased by Lily in 2003)	72,000	80,000	16,000	99,000
The paddock, Oxfordshire (10 acres of land purchased by Lily in 2010)	150,000	70,000	14,000	94,000
Trust bank account	n/a	5,000	1,000	3,800

Oliver Knight's notes

- 1) Lily held 1,000 ordinary shares in Cresswell Garden Centres Ltd on 12 August 2014. She acquired 500 shares for £500 on incorporation in 1973 and she inherited 500 shares from Percy. Probate value of the 500 shares on 7 May 2001 was £7.5 million.
- 2) HMRC have agreed that Inheritance Tax Business Property Relief at 100% was available on the shares in Cresswell Garden Centres Ltd on Percy's death, at the date of transfer to the trustees of the Cresswell Family Settlement and on Lily's death.
- 3) Inheritance tax of £233,000 was due on the creation of the Cresswell Family Settlement. The trustees paid this liability in instalments over a five year period.

The apportioned Inheritance Tax figures shown above relate to the combined total of the tax payable on the creation of the trust and the additional tax payable by the trustees on Lily's death (but not the late payment interest), apportioned across the trust assets.

- 4) Where the relief was available, Lily claimed capital gains holdover relief on the assets transferred into the trust.
- 5) When Lily bought the paddock, she thought that planning permission could be obtained to construct several residential properties on the site. By 2014, it was discovered that the surrounding hedgerow was the nesting place for a rare species of bird, so planning permission would never be granted. Lily transferred the paddock into the trust at this point and the trustees immediately let the land to a local arable farmer who has used the additional land to grow his crops ever since.

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Continuation

EXHIBIT C

Financial information for Cresswell Garden Centres Ltd

<u>Balance sheet information</u>	<u>31 March 2021</u>		<u>31 March 2020</u>	
	£	£	£	£
Fixed assets				
Land and buildings	3,600,000		3,600,000	
Investment property	2,400,000		2,400,000	
Plant and machinery (note 1)	<u>202,000</u>		<u>236,000</u>	
		6,202,000		6,236,000
Current assets				
Stocks	595,000		580,000	
Debtors	85,000		25,000	
Cash in bank and in hand	<u>103,000</u>		<u>125,000</u>	
	783,000		730,000	
Creditors: amounts falling due within one year	<u>(315,000)</u>		<u>(285,000)</u>	
Net current assets		<u>468,000</u>		<u>445,000</u>
Net assets		<u>6,670,000</u>		<u>6,681,000</u>

<u>Profit and loss information</u>	<u>y/e 31 March</u>	<u>y/e 31 March</u>
	<u>2021</u>	<u>2020</u>
	£	£
Turnover:		
Plant and bulb sales	2,170,000	2,260,000
Letting floor space	<u>1,820,000</u>	<u>1,305,000</u>
Total	<u>3,990,000</u>	<u>3,565,000</u>
Profit:		
Plant and bulb sales	988,000	904,000
Letting floor space	<u>1,116,000</u>	<u>985,650</u>
Total	<u>2,104,000</u>	<u>1,889,650</u>

Average number of employees during the financial year

	<u>y/e 31 March 2021</u>	<u>y/e 31 March 2020</u>
Retail staff (note 2)	26	25
Lettings staff (note 3)	2	2
Total	28	27

Accountant's notes

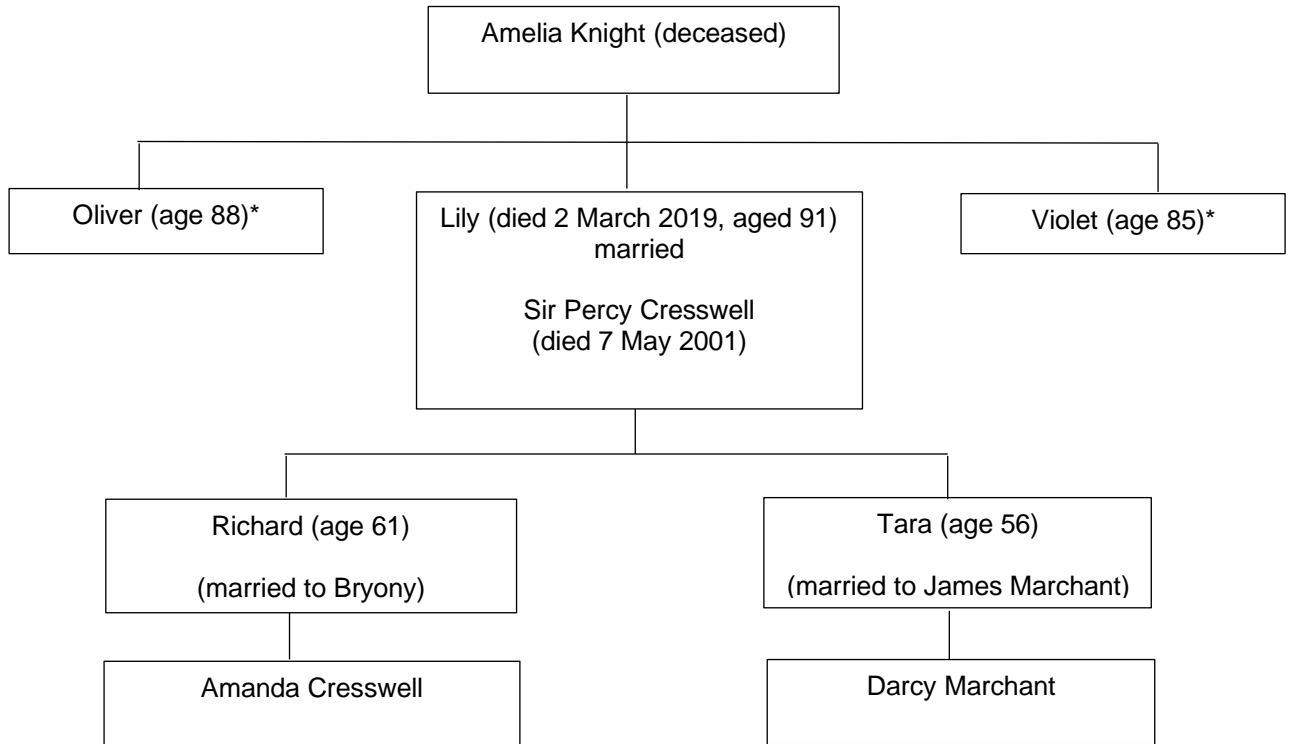
- 1) Plant and machinery is made up of fixtures, shelving and fittings and tills for plant and bulb sales areas only. The third-party retailers who rent floor space from the company provide their own shop fixtures and fittings.
- 2) The company's retail staff work on the shop floor of each garden centre as sales assistants dealing with plant and bulb sales only. The third-party retailers provide their own staff and their sales are dealt with separately by these staff and go through their own tills.
- 3) The company employs two administration staff who deal solely with issues relating to the third-party lettings. They deal with matters such as maintenance contracts, cleaning of the let areas, leases and rent collection.

Continuation

EXHIBIT D

Pre-seen information

Family Tree



* both Oliver and Violet are married with children and grandchildren of their own who are not shown on the family tree.

Permanent File Information

Client name

Trustees of the Cresswell Family Settlement

Settlor

Lady Lily Cresswell (deceased)

Trustees

Original trustees: Oliver Knight and Violet Taylor
Current trustees: Richard Cresswell and Tara Marchant

Date of creation

12 August 2014

Beneficiaries

Amanda Cresswell
Darcy Marchant

Continued

Continuation

Trust background information

Lady Lily Cresswell, a widow, was UK resident and domiciled in England. Her husband, Sir Percy Cresswell, left his entire estate to her on his death.

Lily created her only trust, the Cresswell Family Settlement, on 12 August 2014 for the benefit of her two grandchildren, Amanda Cresswell and Darcy Marchant. The Inheritance Tax due on creation was paid by the trustees.

The original trustees were Lily's brother, Oliver and her sister, Violet. They retired as trustees in March 2021 when it was agreed that Lily's children, Richard and Tara, should take over.

All members of the family are higher rate taxpayers, resident in the UK and domiciled in England.

Assets settled on trust (no changes since creation)

300 ordinary shares in Cresswell Garden Centres Ltd.

Wilton House, Oxfordshire (a large residential five bedroom property, currently let).

Bramble Cottage, Oxfordshire (a two bedroom residential property in a poor state of repair, habitable but currently unoccupied).

10 acre paddock, Oxfordshire (the land is currently let to a local arable farmer who uses it for growing additional crops).

Cash held in a non-interest bearing current account.

Information relating to Cresswell Garden Centres Ltd

Lily and Percy were keen gardeners and in 1973 they turned their hobby into a business, setting up an unquoted company, Cresswell Garden Centres Ltd.

The total issued share capital of the company is 1,000 ordinary shares. Lily was the majority shareholder, holding the remaining 700 shares in the company following the gift to the Cresswell Family Settlement, until her death.

Richard and Tara have been employed by Cresswell Garden Centres Ltd since the early 1990s, but none of the other family members shown above works in the business.

Lily did not allow Richard and Tara to have much say in running the business during her lifetime. As a result, the company's profits have declined over the past 20 years, mainly because Lily resisted their attempts to introduce new products and other retailers into the garden centres.

Summary of terms of trust

The income from the trust fund is to be paid to the beneficiaries in equal shares.

The trustees have the power to advance in whole or in part, as they think fit, the presumptive capital entitlement of a beneficiary by deed prior to him or her attaining the age of 30 years.

In default of an exercise of the above power, each beneficiary will become absolutely entitled to an equal share of the trust fund when they attain the age of 30 years.

In the event that none of the beneficiaries attain the age of 30 years, the trust fund will be held absolutely for any surviving issue of Amelia Knight who have attained the age of 30 years at the end of the trust period.

Continuation

Lady Lily Cresswell's estate

Lily's net estate was valued at £14.5 million. Under the terms of her Will, she left a tax-free legacy of £150,000 to each of Amanda and Darcy and the residue of her estate to Richard and Tara equally.

Other than creating the Cresswell Family Settlement, Lily's only lifetime transfers were as follows:

- 1) 6 April annually (commencing on 6 April 2005) – £1,500 to Amanda and £1,500 to Darcy which utilised her Inheritance Tax annual exemption.
- 2) 5 May 2014 – gift of Sandy Villa, a holiday home, valued at £205,000 to Richard.
- 3) 10 July 2014 – gift of Highbury House, an investment property, valued at £206,000 to Tara.

Grant of Probate was issued to the executors on 1 March 2021.

Engagement letter

The firm's GDPR compliant engagement letter was signed by the trustees on 20 April 2021 covering tax compliance and advisory services.