THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Inheritance Tax, Trusts & Estates

May 2021

TIME ALLOWED

3 HOURS 30 MINUTES

- 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.

1. Fiona Davey, aged 52, was born in the UK, to UK domiciled parents but emigrated to Australia with her parents and brother 50 years ago. She acquired a domicile of dependence in Australia and now considers herself Australian domiciled.

   Fiona is being seconded by her Australian employer to the UK on a three-year contract. She will start her UK role and become UK resident on 1 January 2022 but intends to return home to Australia once the contract comes to an end.

   Fiona set up a discretionary trust on 1 March 2013 after the death of her husband. Fiona is a trustee together with her brother who is Australian resident and domiciled. The beneficiaries are Fiona and her two adult children.

   The trust's assets consist of an investment portfolio and cash. The portfolio contains some UK situs investments that produce UK dividend income each year.

   Fiona has never received any income or capital distributions from the trust and views the trust as being primarily established for the benefit of her children.

   Requirement:

   Explain the Income Tax, Capital Gains Tax and Inheritance Tax implications in relation to the trust for Fiona and the trustees whilst she is UK resident and advise what steps could be taken to mitigate any UK tax. (15)

2. Farida Ashar, who is UK resident and domiciled, has recently been diagnosed with a degenerative disease and she anticipates that her health will deteriorate rapidly in the next few years.

   Farida plans to retire, sell her business and use the net proceeds (after paying any Capital Gains Tax) to set up a trust for herself to protect her assets in the future.

   Requirement:

   Explain the specific circumstances in which such a trust can be created including the immediate and ongoing tax implications of doing so. (10)

3. The Jones Trust was settled on 5 January 1986 by Lionel Jones, a UK resident and domiciled individual. Lionel has not settled any other trusts or made any other gifts. The beneficiaries of the trust are Lionel's grandchildren who are:

Harry, born 21 May 1985
Beth, born 6 October 1990
Mae, born 4 November 1992

Under the terms of the trust, the trustees may distribute income and capital at their discretion. However, when the grandchildren each attain the age of 30 years old they become entitled to a life interest in their one third of the trust fund.

On 6 July 2015, a capital distribution of £20,000 was made to Harry on which he paid the tax. On 5 January 2016, the trust's assets were worth £950,000. None of the trust's assets qualified for Business Property Relief.

The income of the trust for the 2020/21 tax year was as follows:

	<u>6/4/20 - 5/10/20</u>	<u>6/10/20 - 5/4/21</u>
	£	£
Bank Interest	96	99
Dividends	18,000	21,000
Treasury stock	2,000	-
Accrued income scheme charge	275	-

Trust management expenses attributable to and met from income were £900.

The trustees sold the following assets in the 2020/21 tax year:

<u>Asset</u>	<u>Proceeds</u>	<u>Cost</u>
	£	£
Holding of 5% Treasury Stock	5,500	5,000
Shares in Sweets plc	18,231	5,757

On 6 April 2020, the tax pool brought forward was £2,200.

On 6 August 2020, the trustees made a capital distribution of £20,000 to Beth, subject to her meeting any tax liability thereon.

On 10 September 2020, the trustees made an income distribution of £5,000 to Mae.

Requirement:

1) **Calculate the Income Tax and Capital Gains Tax liabilities of the trustees for 2020/21.** (11)

2) **Prepare the appropriate R185's.** (5)

3) **Calculate the Inheritance Tax liability, if any, arising on the capital distribution to Beth.** (4)

Total (20)

4. The Barker family are considering Inheritance Tax planning. William Barker is in good health but his wife, Mary Barker has recently been diagnosed with a terminal illness and has a life expectancy of 12-18 months. William and Mary are concerned about the value of their estate and would like to gift assets to reduce the Inheritance Tax exposure on death.

William and Mary have two adult sons, Henry and John and a daughter, Susan. Henry currently lives abroad and is not UK resident but he has always indicated his desire to live in the family home, Briar Wood, on his permanent return to the UK.

On 1 September 2010, William gave each of his three children £300,000.

On 1 December 2017, William and Mary sold their second home for £600,000. They gifted the proceeds equally to their three children.

William and Mary's main residence, Briar Wood is worth £2.4 million. The property is owned as joint tenants.

They would like to gift one third of the property to Henry and it is proposed that Henry would buy the remaining two thirds at its full market value of £1.6 million. William and Mary would then gift the £1.6 million proceeds to John and Susan equally.

William and Mary would initially continue to occupy Briar Wood. In approximately five years, Henry plans to return permanently to the UK and live in Briar Wood. At that time, William would move out of Briar Wood and into a smaller nearby property which he intends to purchase.

Henry has not spent any of the money gifted by his parents and could use these funds, together with a mortgage, to purchase the two third share of Briar Wood. Alternatively, he could entirely fund the purchase with a mortgage.

Requirement:

Explain the Inheritance Tax implications of the family's proposals making suggestions on how this could be improved, and of Henry's plans for funding the purchase. (15)

5. Cameron Davies, UK resident and domiciled, died on 5 July 2019. Under the terms of his Will, he left his entire estate (worth £950,000 gross) to his two children, Eliza and Edward in equal shares. The administration period is ongoing, and the Executors received the following income in 2019/20 and 2020/21:

	2019/20	2020/21
	£	£
Dividend income	7,000	10,000
Dividends from ISA portfolio	3,000	5,000
Bank interest*	3,500	2,500
Interest from ISA portfolio	800	1,000
Property income (rental property only)	20,000	30,000

*The 2019/20 interest includes £1,500 from a fixed term bond which matured on 30 June 2019. As a result of an administrative error, this interest was not paid until 31 July 2019.

The expenses incurred by the Executors were:

	2019/20	2020/21
	£	£
Interest on loan to pay Inheritance Tax^	2,000	6,000
Allowable expenditure on sale of rental property	nil	5,000
Administration expenses attributable to income	750	1,500

^Paid in four equal instalments on 31 March, 30 June, 30 September, and 31 December 2020. The loan was taken out on 30 November 2019.

At the date of his death, Cameron held 100,000 shares in LCJ plc, which had a probate value of £250,000. The cost of obtaining probate was £500. The following LCJ plc share transactions occurred during 2019/20 and 2020/21:

Date	Transaction	Detail	Proceeds	Cost
			£	£
30 September 2019	Sale	50,000 shares	135,000	
31 October 2019	Rights issue	One share for each share held on 31 August 2019		£2 per share
30 November 2019	Bonus issue	Two shares for each share held on 1 November 2019		Nil paid
31 March 2021	Sale	The remaining shares	335,000	

Cameron owned two properties at death, his main residence, and a rental property. Each property had a probate value of £200,000 and cost £450 to obtain probate.

Cameron had unused capital losses of £7,000 at the date of his death. The ISA portfolio was sold on 28 February 2021 and realised capital gains of £22,000. The rental property was sold on 5 April 2021 for £275,000.

The Executors made payments to Eliza on 1 April 2020 and 1 April 2021 of £5,000 and £20,000 respectively. The main residence was transferred to Edward on 28 February 2021 when it was valued at £240,000.

Requirements:

1) Calculate the Executors' Income Tax and Capital Gains Tax liabilities for 2019/20 and 2020/21 and state the due dates of payment. (14)

2) State the 2019/20 and 2020/21 R185 entries for the beneficiaries. (6)

Total (20)

6. Adam Salter is a 66-year-old retired business owner who is concerned about the Inheritance Tax payable on his death. Adam is widowed and has two children, James (aged 32) and Holly (aged 34). All are UK resident and domiciled.

Adam was married to Moira (UK domiciled) who died on 1 October 2007 when the nil rate band was £300,000. Under the terms of Moira's Will, she left pecuniary legacies to James and Holly of £75,000 each and the residue of her estate to Adam absolutely. The value of Moira's gross estate was £500,000, which included her half share of the family home.

Adam owns 75 £1 ordinary shares out of 100 £1 ordinary issued share capital in Salt & Pepper Ltd, which runs a kitchen accessories store in the local town. Adam paid £1 per share in December 2000 when the company was incorporated. The 75 shares have a current market value of £1.32 million (20% discount applied).

On 1 May 2017, Adam created the Salter Discretionary Trust for the benefit of his children and remoter issue into which he transferred 25 £1 shares in Salt & Pepper Ltd. The value of Adam's shares (100 shares) before the transfer was £2 million. The value of Adam's shares after the transfer (75 shares) was £1.2 million (again, 20% discount applied). The agreed market value for the disposal was £250,000. The 25 shares have a current market value of £275,000 (50% discount applied).

The Salt & Pepper Ltd balance sheets at 30 April 2017 and 30 April 2021 have been analysed by his accountant as follows:

	Year ended 30 April 2017	Year ended 30 April 2021
	£	£
Surplus Cash	200,000	330,000
Trading assets (net of liabilities)	1,500,000	1,600,000

Adam and the trustees are considering selling all of the shares in Salt & Pepper Ltd, which has recently been valued as a whole at £2.2million. The proceeds are to be split equally according to the percentage shareholding.

Adam's other assets consist of the following:

	£
Main Residence	500,000
ISAs	150,000
Bank accounts	150,000
Personal chattels	50,000

Adam has made no other gifts during his lifetime.

Under the terms of Adam's Will, the residue of his estate passes to James and Holly absolutely in equal shares.

Requirements:

1) Calculate Adam's and the trustees' current exposure to Inheritance Tax if Adam were to die before any sale of shares is agreed.

(10)

2) Calculate Adam's and the trustees' exposure to Inheritance Tax once the shares are sold and explain how this could be mitigated. (10)

Total (20)