1. Pierre, who is resident in the UK but was born in France, owns a number of valuable paintings which are kept in a storage unit in Paris.

   1) Explain what is meant by the "lex situs" of a chattel and how it is determined.

   2) State the lex situs of Pierre's paintings and explain how this may impact on his Inheritance Tax liability on death. (You are not required to consider the tax position in France.) (4)

2. An "Age 18 to 25 trust" is a special trust which is given favourable Inheritance Tax treatment.

   Explain whether Inheritance Tax 10 year charges and exit charges apply to Age 18 to 25 trusts. (3)

3. Mrs Hardy makes gifts from her income to her children and grandchildren.

   State the two other conditions, besides being from her income, for Mrs Hardy's gifts to be treated as normal expenditure out of income, and state how such gifts are treated for Inheritance Tax purposes. (3)

4. Erik created the Collins Discretionary Trust on 2 January 2008 and settled £800,000 cash. This was his first chargeable lifetime transfer, and he paid the Inheritance Tax arising as a result of the transfer.

   On 31 March 2016 he also settled unquoted shares with a value of £200,000, again paying the Inheritance Tax arising as a result of the transfer.

   On 18 October 2016 the trustees made a distribution of unquoted shares with a value of £100,000 to a beneficiary.

   Calculate the Inheritance Tax exit charge arising on the distribution, assuming the beneficiary pays the tax. (4)

5. On 1 August 2014 Mr Singer settled a cello valued at £150,000 into the Symphony Interest Trust, and the trustees paid the resulting Inheritance Tax of £2,000. Mr Singer elected to hold over the capital gain of £30,000 which arose on the transfer.

   The trustees sold the cello for £100,000 on 26 November 2016 incurring auction fees of £1,300.

   1) Calculate the capital loss arising as a result of the trustees' disposal.

   2) Explain how the trustees are able to utilise the capital loss, assuming that they buy and sell musical instruments for beneficiaries of the trust on a regular basis. (3)

6. Jessica owns three of a set of five very valuable vases. Her husband owns the other two. On 16 February 2017 Jessica gave one of her vases to her daughter on her 30th birthday. The value of the vases at the date of the gift were as follows:

	£
One vase	50,000
Two vases	125,000
Three vases	300,000
Four vases	500,000
Five vases	800,000

Calculate Jessica's transfer of value for Inheritance Tax purposes. (3)

7. Dev created the Maxi Discretionary Trust on 19 September 2006 with £900,000 cash. This was his first chargeable lifetime transfer. On 19 September 2016 the trust fund was valued at £700,000. Each year the trustees retain income of £20,000, but do not accumulate it to capital.

Calculate, showing all your workings, the Inheritance Tax payable by the trustees as a result of the 10 year anniversary on 19 September 2016. (4)

8. Mark died on 7 February 2017. He was domiciled in the UK. Included in his death estate were a painting held in New York, valued at USD $50,000, and a 50% share of a holiday home in Cornwall which he owned jointly with his sister.

Explain how these assets will be valued in Mark's death estate for Inheritance Tax purposes. (3)

9. On 6 May 2016 Harold created a discretionary trust for the benefit of his wife; this was the only trust he had created and he was specifically excluded from benefitting from it.

In the year ended 5 April 2017, the trustees received rental income of £3,500 per month, and incurred repair expenses of £1,900 relating to the rental property.

Harold is now regretting not including himself as a beneficiary of the trust.

1) Calculate the Income Tax payable by the trustees for the year ended 5 April 2017.

2) Explain the Inheritance Tax implications if Harold had included himself as a beneficiary when he created the trust. (4)

10. Having made no lifetime gifts, Mairwen died on 2 December 2016 leaving the following estate to her sister:

	£
Main home	450,000
Shares in Doorknobs Trading Ltd	250,000
Factory used by Doorknobs Trading Ltd	200,000
Chattels, cash etc	100,000
Total	£1,000,000

Mairwen's shareholding in Doorknobs Trading Ltd, which she had held for 10 years, represents 65% of the total shares of the company. The factory had been used by Doorknobs Trading Ltd for the three years prior to Mairwen's death.

Calculate the Inheritance Tax payable as a result of Mairwen's death. (2)

11. The Campbell Discretionary Trust purchased an investment property for £300,000 on 1 October 2001. One year later, the trustees permitted Arnold, a beneficiary, to live in the property as his main residence, and he did so until 31 March 2008.

The property was then unoccupied for two years until Sarah, another beneficiary, was permitted to occupy the property as her main residence from 1 April 2010.

The trustees disposed of the property on 1 October 2016 for £950,000, having made other chargeable disposals to utilise their annual exemption for the year.

Calculate the Capital Gains Tax payable by the trustees in respect of the disposal of the investment property. (4)

12. Lachlan died in August 2015 having been resident and domiciled in the UK all his life. The executors of his estate have made the following disposals of estate assets:

	Date of sale	Proceeds	Probate value
		£	£
Painting	February 2016	49,000	72,000
Shares in Invest plc	March 2016	Nil – to beneficiary under terms of will	61,500
Residential investment property	September 2016	229,000	181,000

The executors incurred costs of £1,200 in establishing the title to the investment property.

Calculate the Capital Gains Tax payable by the executors for each relevant tax year. (3)

November 2017 Examination

PAPER 5 PART II

Inheritance Tax, Trusts & Estates

TIME ALLOWED – 3 ¼ HOURS
(for Part I and Part II)

- The first 15 minutes of the three and a quarter hour exam is designated as reading time. You then have three hours to answer both the Part I and Part II questions.
- During the 15 minutes reading time, you may read and annotate your Part II question paper**.** You may also read the legislation.
- You are **NOT** permitted to open the Part I question and answer booklet until the Presiding Officer says the 15 minutes reading time is over. Calculators may not be used during reading time.
- The Presiding Officer will inform you when you can start writing your answers.
- You are required to answer **all Part II** questions in the Part II answer booklet.
- Please start each answer on a fresh page and do not write in the margins.
- All workings should be shown and made to the nearest month and pound unless the question requires otherwise.
- There is an alternative part in question 2 for Scots Law candidates.

Part II

Write your answers in the Part II answer booklet.

Marks are specifically allocated for appropriate presentation.

1. Rosie is 75 and owned a rental property with a market value of £975,000. She had bought the property in July 1989 for £395,000 and in November 1994 had converted the basement at a cost of £204,000.

   On 1 March 2017, she sold the property to her daughter Honeysuckle's interest in possession trust. This trust was created by Honeysuckle's father. The trustees advised Rosie that they could only afford to pay £750,000 and she was prepared to accept this price.

   Rosie did not make any other disposals in 2016/17 and pays higher rate tax. A holdover relief claim will be made in respect of this disposal and the trustees have agreed to pay any Inheritance Tax due.

   In 2011/12 Rosie created a trust for her niece and the chargeable lifetime transfer totalled £155,000. This is currently the only trust created by Rosie.

   Rosie would like to create two new trusts for Honeysuckle and has questioned whether these should be created now, or on her death. She also mentioned that she would be reluctant to report the creation of any new trusts to HM Revenue & Customs at present.

   You are required to:

   1) **Calculate the Capital Gains Tax payable by Rosie for 2016/17.** (3)

   2) **Calculate the Inheritance Tax payable by the trustees on the sale of the rental property to Honeysuckle's interest in possession trust.** (3)

   3) **Explain the differences in the tax treatment of an interest in possession trust created during a settlor's lifetime compared to one created on death.** (4)

   4) **Explain briefly how Inheritance Tax relevant property calculations are affected by the same settlor making additions to two or more existing trusts on the same day.** (1)

   5) **Define a resulting trust and give two examples when such a trust may occur.** (3)

   6) **State the action to be taken by a member of the Association of Taxation Technicians when a client is reluctant to disclose aspects of their tax affairs to HM Revenue & Customs.** (2)

   Total (16)

2. The executors of Damien Grey received the following income from the date of his death on 2 October 2016 to the end of the period of administration on 17 November 2017:

	2016/17	2017/18
	£	£
Rental income, after expenses	7,385	
Bank Interest	3,600	2,400
Dividends		3,000

The executors took out a loan of £20,000 on 1 November 2016 to pay the Inheritance Tax liability. The interest rate incurred was 3.9% per annum. The loan was repaid on 30 March 2017.

Damien had no immediate relatives and left his entire estate to his lifelong friend, Hector.

The estate assets comprised:

	Probate value
	£
Rental property	325,000
Bank account	125,500
Shares in a limited company	30,000
Stamp collection	8,000

The executors have never dealt with an estate before and have queried their responsibilities, including when they will need to pay the estate's Income Tax and when the tax return(s) will need to be submitted to HM Revenue & Customs.

They have also enquired about professional fees for advice and assistance with administering the estate.

You are required to:

1) **Calculate the Income Tax payable by the executors for the periods ended 5 April 2017 and 17 November 2017, assuming 2016/17 rates of tax apply to both years.** (3)

2) **Calculate the R185 entries for 2016/17 assuming the executors transfer Damien's stamp collection to Hector on 31 March 2017.** (1)

3) **Calculate the R185 entries for 2017/18 when Damian's remaining assets are transferred to Hector on 17 November 2017.** (2)

4) **Identify the dates on which Income Tax payments and tax return(s) are due in 2018.** (2)

5) **Explain how an executor differs from an administrator.** (3)

[*Alternative for Scots Law candidates:*

Explain how an executor-nominate differs from an executor-dative. *(3)****]***

6) **State how and why a member of the Association of Taxation Technicians should document an agreed fee charging structure with a client and give three examples of possible fee arrangements.** (3)

Total (14)

3. Matthew Sampson died on 6 February 2017. His estate comprised the following assets and liabilities:

	£	
Family home in Dorset	450,000	Left to his wife, Mary
Cottage in Wiltshire	70,000	Left to his son, Sam
Cash and small chattels	5,000	Left to his son, Sam
Income tax to the date of death	6,300	
Funeral costs	5,000	
General probate costs	7,000	

In December 2012 Matthew settled his farmland, Premium Bonds and other investments into trust for the benefit of his son, Sam. At the time the farmland was settled, the agricultural value which qualified for 100% agricultural property relief, was agreed at £950,000. Inheritance Tax of £104,750 was paid on the transfer by Matthew and the gross chargeable lifetime transfer was calculated as £848,750.

In February 2016 the trustees sold the farmland as Sam showed no interest in farming. With the proceeds they immediately purchased a small rental property portfolio.

Matthew's wife, Mary, is considering using a deed of variation to gift a 25% share of the family home to Sam. She is also thinking about updating her own will, but is confused about the different types of legacies that she could include.

You are required to:

1) **Calculate, showing all your workings, the Inheritance Tax payable by the trustees as a result of Matthew's death.** (3)

2) **Calculate the Inheritance Tax payable on the estate and state when it will be payable.** (3)

3) **Explain briefly the conditions for Mary's estate to qualify for the maximum Residence Nil Rate Band and explain whether she will receive an increase due to Matthew's death.** (3)

4) **Explain the tax effects if Mary decides to gift a 25% share in the family home to Sam using a Deed of Variation.** (3)

5) **Describe, with examples, three types of legacy that can be included in a will.** (3)

Total (15)

4. Following an initial client meeting with Emily Light, you have been given the following file note relating to a discretionary trust she created for her grandchildren:

File Note 30 March 2017
To: Tax department
From: A Partner
Subject: Client meeting notes re the Emily Light Grandchildren Discretionary Trust

	2016/17
	£
Bank interest received	3,000
Rents received from residential letting	12,480
Letting agent fees paid	2,850
Service charges paid	820
Buildings insurance	310
Dividends received	6,300
Trust management expenses paid	333

As at 30 March 2017, Emily had three other settlements which were created in previous years. A further settlement was terminated in June 2016.

The tax pool brought forward as at 6 April 2016 totalled £1,173.

Emily would like to give her eldest grandson, Freddie, funds to help with university fees and thinks £10,000 should be sufficient.

In order to fund school fees for the younger grandchildren, on 2 February 2017, the trustees sold 10,000 of quoted shares, realising sale proceeds of £37,000 and incurring selling costs of £500. The shares were valued at £2.35 per share when they were settled by Emily on the creation of the trust.

Other matters

Emily has mentioned that one of her grandchildren (who is a beneficiary of one of the other settlements) has been arguing with the trustees that they are in breach of their responsibilities, as he believes they have not given him the trust funds to which he is entitled.

You are required to:

1) Calculate the trust's Income Tax liability for 2016/17. (5)

2) Explain the tax consequences for both the trustees and for Freddie of £10,000 being paid to him as an income distribution compared to a capital distribution. (4)

3) Calculate the tax pool as at 5 April 2017, assuming the trustees made an income distribution to Freddie of £10,000 on 31 March 2017. (2)

4) Calculate the trust's Capital Gains Tax liability for 2016/17. (2)

5) Define a breach of trust and briefly explain one of the remedies available to the beneficiaries. (2)

Total (15)