



Practical Tax People

Association of
Taxation Technicians

May 2015 Examination

PAPER 5

Inheritance Tax, Trusts & Estates

Part I Suggested Solutions

1.	Terry's death:			
		£	£	
	Total value of Terry's death estate		400,000	
	Spouse exemption on ½ estate		<u>(200,000)</u>	½
	Chargeable estate		200,000	
	Nil rate band at death (2007/08)	300,000		½
	Less: used against PET	<u>(20,000)</u>		½
	Available nil rate band		<u>(280,000)</u>	
	Unused nil rate band on Terry's death		<u>80,000</u>	½
	Catherine's death:		£	
	Death estate:			
	Chargeable estate		800,000	
	Less nil rate band		<u>(325,000)</u>	½
	Less transferable nil rate band:			
	26.67%* x £325,000		<u>(86,678)</u>	½
	Taxable estate		<u>388,322</u>	
	Inheritance Tax at 40%		<u>155,329</u>	½
	* 80,000/300,000 x 100% = 26.67%			½
	Total			(4)
2.	2013/14:		£	
	Shares in ABC Ltd			
	Disposal proceeds		19,000	
	Less: probate value		<u>(12,000)</u>	
	Chargeable gain		7,000	½
	CGT Annual Exemption – restricted to gain		<u>(7,000)</u>	½
	Taxable gain		<u>nil</u>	
	2014/15:		£	
	Shares in DEF Ltd			
	Disposal proceeds		48,000	
	Less: probate value		<u>(40,000)</u>	
	Chargeable gain		8,000	½
	CGT Annual Exemption*		<u>(nil)</u>	½
	Taxable gain		<u>8,000</u>	
	Capital Gains Tax at 28%		<u>2,240</u>	½
	No tax liability on gilts – exempt asset			½
	*CGT Annual exemption only given in first three tax years, including tax year of death.			
	Total			(3)

3. Principal Charge:			
	£	£	
Trust value at 27 October 2014:			
Shares in Ice plc	580,000		
Investment property	<u>345,000</u>		
		925,000	
Nil rate band 2014/15		<u>(325,000)</u>	½
		<u>600,000</u>	
Notional tax at 20%		120,000	½
Effective rate (120,000/925,000 * 100%)		12.973%	½
Actual rate:			
12.973% x 30%		3.892%	½
Inheritance Tax arising:			
Tax on shares in Ice plc: 580,000 x 3.892%	22,574		½
Tax on investment property: £345,000 x 3.892% x (40 - 27)/40	<u>4,364</u>		½
		<u>26,938</u>	
NB Quarters expired before property added – 27 Oct 2004 to 12 Sept 2011 = 27			½

The submission deadline for form IHT100 is 6 months after the end of the month of the chargeable event, being 30 April 2015 (1/2).

Note - Rate of tax shown to 3 decimal places. Credit given for different rounding of rate.

Total (4)

4. Exit charge arising on distribution:			
	£		
Trust value at 27 October 2014:		925,000	
Nil rate band 2020/21		<u>(350,000)</u>	½
		<u>575,000</u>	
Notional tax at 20%		115,000	½
Effective rate (115,000/925,000 * 100%)		12.432%	½
Actual rate:			
12.432% x 30%		3.730%	½
Inheritance Tax arising:			
£395,000 x 3.730% x 22/40		<u>8,103</u>	½
NB Quarters between 10 year anniversary and exit - 27 October 2014 – 12 May 2020 = 22 complete quarters			½
Total			(3)

5. **Income Tax calculation:**

	Dividend (£)	
Dividends (£6,000 x 100/90)	6,667	½
Income Tax payable:		
£1,000 x 10%	100	½
£5,667 x 37.5%	<u>2,125</u>	½
Total tax	2,225	
Less dividend tax credit	<u>(667)</u>	½
Tax paid by trustees	<u>1,558</u>	
Tax pool working:		
Tax pool b/fwd	950	½
Add tax paid in year	<u>1,558</u>	½
	2,508	
Less tax credit on distribution:		
£1,650 x 45/55	<u>(1,350)</u>	1
Tax pool c/fwd to 2015/16	<u>1,158</u>	

Total **(4)**

6. Capital gains should be calculated and reported to HM Revenue & Customs on the trust's annual self-assessment tax return. (1/2), known as SA900 (1/2).

There is usually no need to report a capital gain if it is within the trust's annual exemption (1/2). If, however, the disposal proceeds are more than four times the value of the annual exemption the disposal must be reported even if no gain arises (1/2).

In order to claim a capital loss the disposal should be reported on a tax return (1/2).

Total **MAX (2)**

The deadline for submitting the self-assessment tax return is 31 January following the end of the tax year if filing online (1/2) or 31 October if submitting a paper version (1/2). The payment date for CGT liabilities is 31 January following the end of the tax year in which the liability arose. (1/2)

Credit will be given for other valid comments.

Total **OVERALL MAX (3)**

7. Inheritance Tax liability on death

	£	£	
Family home	2,000,000		
Loan for agricultural land*	<u>(300,000)</u>		½
		1,700,000	
Agricultural land	400,000		
APR @ 100%	<u>(400,000)</u>		½
		nil	
Shares in KO Ltd	500,000		
Loan taken out for KO shares**	<u>(400,000)</u>		½
	100,000		
BPR @ 100%	<u>(100,000)</u>		½
		nil	
Cash and personal possessions		<u>350,000</u>	
Chargeable estate		2,050,000	
Nil rate band		<u>(325,000)</u>	½
		<u>1,725,000</u>	
Inheritance Tax on death @ 40%		<u>690,000</u>	½

* The secured loan on the family home used to acquire the agricultural land can be deducted from the value of the family home as it was arranged prior to 6 April 2013 (1/2)

** In contrast, the loan taken out to acquire the KO Ltd shares must first be deducted from the value of the shares, even though the loan was secured on the family home, as it was arranged after 6 April 2013. (1/2)

Total (4)

8. As a UK domiciled individual, his estate would be liable to UK IHT on his worldwide assets (1/2).

Having acquired a domicile of choice elsewhere, the deemed domicile rules will apply to the individual (1/2). These rules state that an individual is deemed domiciled in the UK for IHT purposes (1/2) if at any point in the previous three years they were actually domiciled in the UK (1/2). This means that the individual will continue to be liable to IHT on their worldwide assets for three years after they lost their UK domicile (1/2).

Once the individual is no longer caught by the deemed domicile rules, they will only be liable to IHT on their UK assets. (1/2).

Credit will be given for any other valid comments.

Total MAX (2)

9. Where property qualifies for interest-free instalments no interest accrues on the unpaid balance of tax (1/2). Instead, interest will only be charged if the instalments themselves are paid late (1/2).

The instalments are payable in 10 equal amounts (1/2), paid annually (1/2). The first instalment is payable on the usual payment date, i.e. 6 months after the end of the month of death (1/2). The balance of the tax can, however, be settled at any time (1/2). If the qualifying property is sold by the new owner whilst tax remains outstanding, the unpaid balance of tax becomes payable in full at the point of sale (1/2).

Total **MAX (3)**

10.	1)	Rancho Ltd	£	
		Transfer of value	800,000	
		IHT payable @ 20/80%	200,000	1

NB tax rate is grossed up as Rancho Ltd, being the Transferor, is primarily liable for the tax

2)	Participators		£	
	Michael	$88\% \times \text{£}800,000 \times 20/80\% =$	176,000	1/2
	Hussein	$8\% \times \text{£}800,000 \times 20/80\% =$	16,000	1/2
	Linda	No secondary liability as owns <5% shares		1

Total **(3)**

11. **Step 1 – calculate 10% charity threshold** **(3 marks)**

	£	£	
Gross estate		1,600,000	
Less reliefs/exemptions:			
Spouse Exemption		(900,000)	1/2
Business property relief		<u>(200,000)</u>	1/2
		500,000	
Nil rate band at death	325,000		1/2
Chargeable lifetime transfers	<u>(125,000)</u>		1/2
		<u>(200,000)</u>	
Baseline amount/10% threshold		<u>300,000</u>	1/2
Baseline amount x 10%		<u>30,000</u>	1/2

Charity gift of £50,000 is in excess of this amount so 36% rate applies.

Step 2 – calculate tax on death estate **(1 mark)**

Baseline amount b/fwd		300,000	
Less charity exemption		<u>(50,000)</u>	1/2
Taxable estate		<u>250,000</u>	
IHT @ 36% reduced rate		<u>90,000</u>	1/2

Total **(4)**

12. The executors were aware the capital gain should have been included in the 2012/13 tax return but chose not to do so. It is likely that HM Revenue & Customs will consider the error to be deliberate but not concealed, as the executors did not falsify accounts or documents. (1)

The disclosure to HM Revenue & Customs has been prompted (1/2), so the minimum penalty that can apply is 35% (1/2) and the maximum penalty that can apply is 70% (1/2) of the potential lost revenue (1/2).

Factors HM Revenue & Customs may take into account when determining any reduction in the maximum level of penalty are cooperation from the executors in assisting to calculate the additional tax payable (1/2) and access to records (1/2).

Total

MAX (3)