Association of Taxation Technicians

Examination

May 2008

PAPER 4 – PART II

INHERITANCE TAX, TRUSTS & ESTATES

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

- You are required to answer **all** questions in Part I (printed separately) and Part II.
- The maximum number of marks for each question in Part II is shown in brackets.
- For Part II, start each answer on a new sheet of paper.
- All workings should be shown and made to the nearest month and pound unless the question requires otherwise.
- Marks are specifically allocated for good presentation.
- *There is an alternative part 5) of question 3 for Scots law candidates.*

1. One of the firm's senior partners has received the following letter:

Dear Mr Smith,

Your firm has acted for my daughter and her husband for a long time, and they have suggested that I write to you for some tax advice. I am a widower, aged 73, and would like to start some Inheritance Tax planning. I have made no gifts before now.

My only daughter and her husband are well established financially, so what I would like to do is start to make provision for my grandchildren. They are 15 and 18, and fairly sensible, but I wouldn't like them to immediately come into a lot of money.

What I want to do is to start to make provision for their future, and have it in mind to do the following:

1) Settle £500,000 cash into a UK discretionary trust, the potential beneficiaries of which will be my grandchildren. If this gives rise to any tax liability, I would like the trust to meet it.

2) In due course, gift into that trust my 15% holding in BL Trading Ltd, which runs a car repair and hire business. It's a profitable trading company; the directors turned down an offer for the group of £5 million last year, so I would say the shares are worth at least £600,000 to a third party. I acquired the shares on the death of my father in May 1986, when their probate value was £30,000.

I have two further questions. Firstly, I know the trustees will try and do a good job, but just in case, I would like to be able to step in and to retake an interest in the trust property. Secondly, a chap at the golf club told me that the clever thing to do would be to set up an offshore trust and do it like that. Would either of these plans work?

I look forward to meeting you.

Yours sincerely,

Barry Rose

The partner has a meeting with Mr Rose next week and has asked you to prepare a briefing memorandum on the course of action proposed. The partner has suggested that as the firm has been acting for the family for a very long time you can charge your time to the existing client code and there is no need to issue a new engagement letter.

You are required to prepare a memorandum in reply to the partner:

1) Explaining the Inheritance Tax and Capital Gains Tax implications of the transfers into the discretionary trust. Your answer should include any relevant calculations, discuss any beneficial elections and mention any future Inheritance Tax charges that the trust may suffer. (12)

2) Outlining the tax implications of the suggestions made by Mr Rose in the final paragraph of his letter. (4)

3) Explaining the basis upon which this client should be taken on by the firm. (4)

Total (20)

2. Assume that today's date is 27 February 2008.

Paul is a non-UK domiciled individual. He is single and has lived in the UK since February 1992.

He has become wealthy over the years as a result of running successful businesses, and investing wisely in assets that have increased in value.

He has approached you to act on his behalf as he feels that an Inheritance Tax review is now required.

His assets consist of the following:

A holiday home near his family in Torinoland, (in sterling)	£80,000
An offshore bank account in Torinoland (in sterling)	£64,050
A reversionary interest in a UK trust. This trust was set up by Paul's grandfather. The life interest was given to Paul's father. The capital will pass to Paul on his father's death.	The capital assets are currently worth £200,000. The reversionary interest has been valued at £50,000 at today's date.
305 quoted shares in Zebra-3 Ltd, a UK trading company.	The shares are quoted between £10.08 and £10.56.
1,500 unquoted shares in Huggy Ltd, his personal company, trading in the UK.	£725,000
A property currently let in the UK	£235,000
His home in the UK	£460,000
A UK bank account – an ISA	£1,480

Paul has previously made the following lifetime gifts:

	Date of gift	£
300 shares in Huggy Ltd, an unquoted trading company, to his brother, Nick, who has since sold these shares.	27 August 2002	93,000
£4,000 in cash to each of his three god-children	16 May 2003	12,000
A transfer of 500 shares in Huggy Ltd into a discretionary trust. (No Inheritance Tax was previously paid in relation to this transfer).	9 November 2005	230,000
£1,500 to his friend David, when he got married	9 May 2007	1,500

Paul is currently thinking about returning to Torinoland to look after his frail mother. Alternatively, he may decide to stay in the UK and make regular trips to Torinoland. He would like to know if this will affect his Inheritance Tax position in any way.

You are required to:

1) **Calculate Paul's Inheritance Tax liability assuming he dies on 27 February 2008.** (11)

2) **Explain the effects that:**

   (a) **staying in the UK; and**

   (b) **leaving the UK will have on Paul's Inheritance Tax position.** (4)

3) **Explain Paul's residence status for both Income Tax and Capital Gains Tax and confirm how he is chargeable to both taxes.** (5)

Total (20)

3. Edith died on 6 July 2007 aged 66. She left no will.

The personal representatives of her estate now have the task of completing the administration of the estate, including the final tax return for Edith.

No assets have been sold since Edith died, but the following information is available for the completion of the tax returns to the 5 April 2008.

<u>Net dividends from her GMS plc shares:</u>		£
Declared 16 March 2007	Paid 16 May 2007	585
Declared 16 May 2007	Paid 16 July 2007	630
Declared 16 October 2007	Paid 16 December 2007	675
Untaxed interest from Edith's capital of £20,000 in 8% loan stock	Paid 1 June 2007 Paid 1 December 2007	800 800
Net rental income		£1,581 per month
UK bank interest	Paid 30 April 2007	13,840
	Paid 30 October 2007	4,800
Edith's assessable trading profits for 2007/08 (to the date of death)		25,760
Edith's state pension		£87.30 per week
ISA interest	Paid 30 June 2007	960
	Paid 30 November 2007	980

You are required to:

1) **Calculate the Income Tax payable for both Edith and the period of administration for 2007/08.** (11)

2) **State the filing dates by which the tax returns for both Edith and her estate must be submitted to HM Revenue & Customs.** (1)

3) **State the due dates for making the balancing payments of Income Tax for 2007/08 and explain whether interest will be charged if the tax is paid late.** (2)

4) **Explain how any payments to a beneficiary on account of income during the administration period would be treated for tax purposes.** (2)

Edith's estate is valued at approximately £300,000 and her family are asking the personal representatives for distributions of the estate property to be made to them. However, before they do this, they would like your advice on how the estate should be distributed.

Edith left two adult children and four grandchildren, one of whom had been living with her for the last five years.

You are required to:

5) **(a) Explain how Edith's estate will be distributed under the Administration of Estates Act 1925.** (1)

(b) Explain, giving reasons, how the Inheritance (Provision for Family and Dependants) Act 1975 might affect your answer to part 5 (a) above. (3)

Scots law candidates should answer the following alternative part 5):

5) ***Succession to the estate of a deceased person under Scots law is regulated by four sets of rules, which are interrelated. State these four rules.*** (4)

Total (20)