



The Chartered Tax Adviser Examination

November 2002

PAPER IIB

TAXATION OF INDIVIDUALS, TRUSTS AND ESTATES

TIME ALLOWED - 3 HOURS

Candidates should answer all six questions set.

Start each answer on a fresh sheet.

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.

Candidates who answer the law part of this paper in accordance with Scots law or Northern Ireland law should tick the appropriate box on the front of the answer folder.

1. For the tax year 2001/02 Mr McIntyre, aged 50, a UK resident, ordinarily resident and domiciled and married individual, had the following:

<u>Income</u>	£
Schedule D Case I taxable partnership profit share	24,000
UK dividends net received	810
UK bank interest net received	1,100
Non-UK dividends net received (foreign tax deducted at source of £420)	2,000
Chargeable event gain (UK non-qualifying policy owned for two years)	2,000
 <u>Outgoings</u>	
Personal pension plan contribution paid (net)	2,365
Interest paid on loan to contribute partnership capital	3,000
EIS investment	800
Gift Aid payment made	1,000

You are required to calculate Mr McIntyre's Income Tax payable for 2001/02.

(10)

2. The finance director of a client company has contacted you. He wishes to ensure that benefits provided to the four directors of the company, who each own 25%, are properly taxed. He has provided the following information:

Tax Status

All directors are UK resident, ordinarily resident, domiciled and perform all their duties in the UK.

School Fees

The company made a payment to the school of £15,000 to settle the school fees due on one of the director's children.

Bonus

The directors were voted a bonus of £50,000. As the company had cash temporarily invested in some gilt stocks it transferred these to the directors in settlement of the amount due to them.

Loan to a Director

The company set up an employee benefit trust many years ago. The trustees have lent £100,000 interest free, repayable on demand, to a director. The loan is not in breach of the Companies Act. The money was lent to enable the director to buy an investment property that is let on commercial terms to unconnected persons.

You are required to draft a letter for issue to the finance director, which explains, for each of the items described:

- 1) **The Income Tax consequences.** (5)
- 2) **The PAYE consequences.** (5)
- 3) **The National Insurance consequences.** (5)

Total (15)

3. Inheritance Tax is charged on a chargeable transfer. In order to determine if a chargeable transfer has occurred it is necessary to understand the following basic concepts:

- Disposition
- Transfer of value
- Exempt transfer of value
- Potentially exempt transfer of value

One of your clients, an insurance company, is anxious to ensure that its financial advisers have a basic grasp of these concepts: in particular they must be made aware of the various exclusions and exemptions that are provided under Inheritance Tax law.

You are required to prepare a technical note that provides a summary of each of the basic concepts and identifies the more important exclusions and exemptions.

(15)

4. Mr Wood, a UK domiciled individual, died on 5 February 2002. The following information is held.

- 1) On 10 December 1996 he gifted £100,000 cash to one of his children. He made no other lifetime transfers.
- 2) Mr Wood is survived by a widow and two children.
- 3) His main residence and contents were worth £200,000.
- 4) He owned the following investments:
 - (a) 30,000 shares in Kellan plc quoted at 150p – 201p;
 - (b) 12,500 shares in Anderson plc quoted at 135p – 179p (special bargains had been done at 135p and 155p);
 - (c) Bank account balance of £25,000 (excluding interest accrued of £1,250);
 - (d) French villa worth £250,000 which has borrowings of £150,000 secured on it.

He was one of two partners in a computer services consultancy business set up four years ago. The total value of the business, at time of death, was £350,000. The remaining partner exercised an option, given under the partnership agreement, to buy Mr Wood's partnership share from his estate for 50% of the death value.

Mr Wood had a life interest inherited on his father's death on 10 November 1998. His father's estate at death was £230,000, of which £50,000 (net of taxes) related to the trust fund in which his father had the life interest. Inheritance Tax of £23,000 was paid on the father's estate. The trust fund was worth £125,000 on Mr Wood's death, when it passed to his brother.

The terms of Mr Wood's will are that the house, its contents and the French villa are left to his widow. The younger child was given a tax free legacy of £40,000 and the residue was left to the older child.

You are required to:

- 1) **Calculate the Inheritance Tax payable as a result of Mr Wood's death.** (13)
- 2) **Calculate how much the widow and each child will receive.** (3)
- 3) **Briefly describe the duties of a personal representative (*executor in Scotland*).** (4)

Total (20)

5. On 12 September 1994 Bill's employer, Fattening Snacks Ltd, granted him options over 6,000 shares under an unapproved share option scheme. This represented less than 1% of the company. The market value at the time of grant was £2.00 per share and the exercise price was £1.20 per share. The options were exercisable at any time between one and seven years from the date of grant.

On 28 August 1996 Bill exercised options over 4,000 shares at which time the market value of the shares was £3.20 per share. On 25 October 1999 he exercised the remaining 2,000 options at which time the market value of the shares was £4.30 per share.

On 10 May 2001 Bill transferred 4,000 shares to Susan, his wife, who is aged 50. On 8 July 2001 the entire company was sold to a quoted company for £25.00 per share. At all times, Fattening Snacks Ltd was an unquoted trading company and both Bill and Susan were UK resident, ordinarily resident and domiciled.

In 2001/02 Susan received:

	£
Premium bond prize	1,000
Winnings from bet on the Grand National	300
Dividend income from Fattening Snacks Ltd (net)	6,000

In previous years Susan was a housewife and had no income.

You are required to:

- 1) **Calculate Susan's Capital Gains Tax liability for 2001/02.** (11)
- 2) **In the context of taper relief for an individual owning 15% of the share capital, describe what is meant by a "qualifying company".** (6)
- 3) **In point form, detail SIX matters that a company should consider before issuing shares.** (3)

Total (20)

6. Robert and James

Brothers Robert and James own Barleymow Farm as joint tenants (*Owners in Common in Scotland*). They let the farm land and each lives with his family in one of the two farmhouses. Robert and his family live in East House and James and his family live in West House. They were bequeathed the farm on their father's death on 20 November 1996 at which time East House was worth £350,000 and West House was worth £320,000. James and his family have decided that they will move out of the area and therefore West House will be sold for £500,000 on 20 November 2002. Robert will use his proceeds of £250,000 from the sale of West House to purchase James' share of East House. East House is currently worth £600,000.

Harold and Agnes

Harold and Agnes purchased Manor House as joint tenants on 10 January 1992 for £300,000. The grounds are in two parts:

- 1) The house, garden and paddock which includes a garage block, a summer house and a swimming pool. This covers an area of two hectares and is bounded by a road to the front, and walls to the sides and rear. Beyond each of the three perimeter walls are the gardens of neighbours' houses. The paddock is used for grazing the family's miniature pony and covers an area of approximately a half hectare at the end of the garden and is separated by a three bar corral style fence. When they purchased the house the paddock area was a part of the lawn.
- 2) A front garden and river mooring across the road from the house. This covers 0.2 hectares and has been a part of the property since 1865.

Agnes' mother has been lodging with them for the last three years paying £500 per month in rent.

They are thinking of moving and have received separate offers of £120,000 for the front garden and mooring and £800,000 for the remainder of the property. Assume that both transactions will occur before 6 April 2003.

You are required to:

- 1) **Discuss the Capital Gains Tax implications of each of the above scenarios.** (17)
- 2) **Explain the concept of judicial precedent.** (3)

Total (20)