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ACCA QUALIFICATION
COURSE NOTES

Paper F6

TAXATION (UK)
(FA 2011)

JUNE 2012 EXAMINATIONS

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P1 Governance, Risk & Ethics

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P6 Advanced Taxation (UK)

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SYLLABUS

1 Aim

To develop knowledge and skills relating to the tax system as applicable to individuals, single companies, and groups of companies.

2 Objectives

On successful completion of this paper candidates should be able to:

- Explain the operation and scope of the tax system
- Explain and compute the Income Tax liabilities of individuals
- Explain and compute the Corporation Tax liabilities of individual companies and groups of companies
- Explain and compute the Chargeable Gains arising on companies and individuals
- Explain and compute the Inheritance Tax liabilities of individuals
- Explain and compute the effect of National Insurance Contributions on employees, employers and the self employed
- Explain and compute the effects of Value Added Tax on incorporated and unincorporated businesses
- Identify and explain the obligations of taxpayers and/or their agents and the implications of non-compliance

3 Position of the paper in the overall syllabus

The syllabus for Paper F6, Taxation, introduces candidates to the subject of taxation and provides the core knowledge of the underlying principles and major technical areas of taxation as they affect the activities of individuals and businesses.

Candidates are introduced to the rationale behind and the functions of the tax system. The syllabus then considers the separate taxes that an accountant would need to have a detailed knowledge of, such as income tax from self-employment, employment and investments, the corporation tax liability of individual companies and groups of companies, the national insurance contribution liabilities of both employed and self employed persons, the value added tax liability of businesses, the chargeable gains arising on disposals of investments by both individuals and companies, and the inheritance tax liability of individuals.

Having covered the core areas of the basic taxes, candidates should be able to compute tax liabilities, explain the basis of their calculations, apply tax planning techniques for individuals and companies and identify the compliance issues for each major tax through a variety of business and personal scenarios and situations.

4 Detailed syllabus

4.1 The UK tax system

(a) The overall function and purpose of taxation in a modern economy
(b) Different types of taxes
(c) Principal sources of revenue law and practice
(d) Tax avoidance and tax evasion

4.2 Income tax liabilities

(a) The scope of income tax
(b) Income from employment
(c) Income from self-employment
(d) Property and investment income
(e) The comprehensive computation of taxable income and income tax liability
(f) The use of exemptions and reliefs in deferring and minimising income tax liabilities

4.3 Corporation tax liabilities

(a) The scope of corporation tax
(b) Taxable Total Profits
(c) The comprehensive computation of corporation tax liability

(d) The effect of a group corporate structure for corporation tax purposes

(e) The use of exemptions and reliefs in deferring and minimising corporation tax liabilities

4.4 Chargeable gains

(a) The scope of the taxation of capital gains

(b) The basic principles of computing gains and losses.

(c) Gains and losses on the disposal of movable and immovable property

(d) Gains and losses on the disposal of shares and securities

(e) The computation of capital gains tax payable by individuals

(f) The use of exemptions and reliefs in deferring and minimising tax liabilities arising on the disposal of capital assets

4.5 Inheritance tax

(a) The scope of inheritance tax

(b) The basic principles of computing transfers of value

(c) The liabilities arising on chargeable lifetime transfers and on the death of an individual

(d) The use of exemptions in deferring and minimising inheritance tax liabilities

(e) Payment of inheritance tax

4.6 National insurance contributions

(a) The scope of national insurance

(b) Class 1 and Class 1A contributions for employed persons

(c) Class 2 and Class 4 contributions for self employed persons

4.7 Value added tax

(a) The scope of value added tax (VAT)

(b) The VAT registration requirements

(c) The computation of VAT liabilities

(d) The effect of special schemes

(e) The effect of a group corporate structure for VAT purposes

(f) The VAT implications of imports and exports to European Union and non-European Union countries.

4.8 The obligations of taxpayers and/or their agents

(a) The systems for self-assessment and the making of returns

(b) The time limits for the submission of information, claims and payment of tax, including payments on account

(c) The procedures relating to enquiries, appeals and disputes

(d) Penalties for non-compliance

5 Approach to examining the syllabus

The syllabus is assessed by a three-hour paper-based examination. There will be 15 minutes reading and planning time given at the start of the exam.

Assessment: Taxation (GBR)

The paper will be predominantly computational and will have five questions, all of which will be compulsory.

- Question one will focus on income tax and question two will focus on corporation tax. The two questions will be for a total of 55 marks, with one of the questions being for 30 marks and the other being for 25 marks.
- Question three will focus on chargeable gains (either personal or corporate) and will be for 15 marks.
- Questions four and five will be on any area of the syllabus, can cover more than one topic and will respectively be for 15 marks.

There will always be at a minimum of 10 marks on value added tax. These marks will normally be included within question one or question two, although there might be a separate question on value added tax.

National Insurance Contributions will not be examined as a separate question, but may be examined in any question involving income tax or corporation tax.

Groups and overseas aspects of corporation tax will be examined in question two or question five.

Questions one or two might include a small element of chargeable gains.

Any of the five questions might include the consideration of issues relating to the minimisation or deferral of tax liabilities.

Paper F6

TAX RATES AND ALLOWANCES

The following tax rates and allowances will be reproduced in the examination paper for Paper F6. In addition, other specific information necessary for candidates to answer individual questions will be given as part of the question. For example, in the case of corporate chargeable gains the relevant retail prices index for particular dates will be given.

Income Tax

		Normal rates	*Dividend rates*
		%	*%*
Basic rate	£1 – £35,000	20	10
Higher rate	£35,001 – £150,000	40	32.5
Additional rate	£150,001 and over	50	42.5

A starting rate of 10% applies to savings income where it falls within the first £2,560 of taxable income

Personal Allowance

	£
Personal allowance standard	7,475
Personal allowance aged 65–74	9,940
Personal allowance aged 75 and over	10,090
Income limit for age–related allowances	24,000
Income limit for standard allowances	100,000

Car Benefit Percentage

The base level of CO_2 emissions is 125 grams per kilometre.

A lower rate of 5% applies to cars with CO_2 emissions of 75 grams per kilometre or less and a rate of 10% applies to cars with CO_2 emissions of 76-120 grams per kilometre..

Car Fuel

The base figure for calculating the car fuel benefit is £18,800

Personal Pension Contribution Limits

The maximum contribution that can be made without evidence of earnings is £3,600.

Annual allowance £50,000

Authorised mileage allowances

All cars

up to 10,000 miles	45p
over 10,000 miles	25p

Capital Allowances

	%
Plant and machinery	
Annual Investment Allowance	
For the first £100,000 of expenditure per annum	100
General rate Pool	
Writing-down allowance	20
Special rate Pool	
Writing-down allowance	10
Motor cars	
CO_2 emissions up to 110 grams per kilometre	100
CO_2 emissions between 111 – 160 grams per kilometre	20
CO_2 emissions over 160 grams per kilometre	10

Corporation Tax

Financial year	*2009*	*2010*	*2011*
Small profits rate	21%	21%	20%
Main rate	28%	28%	26%
Lower limit	£300,000	£300,000	£300,000
Upper limit	£1,500,000	£1,500,000	£1,500,000
Standard fraction	7/400	7/400	3/200

Marginal Relief

Standard Fraction × (U – A) × N/A

Value Added Tax

Standard rate	20%
Registration limit	£73,000
Deregistration limit	£71,000

Rates of Interest

Official rate of interest:	4.0%
Rate of interest on underpaid tax:	3.0%
Rate of interest on overpaid tax:	0.5%

Capital Gains Tax

Individuals

Annual Exemption		£10,600
Rate of tax	– lower rate	18%
	– higer rate	28%
Entrepreneurs' relief	– lifetime limit	£10,000,000
	– Rate of tax	10%

Inheritance Tax

		%
Tax Rate:		
£1 – £325,000		Nil
Excess	– Death rate	40
	– Lifetime rate	20

Taper relief:

Years before death	*Percentage reduction* %
Over 3 but less than 4 years	20
Over 4 but less than 5 years	40
Over 5 but less than 6 years	60
Over 6 but less than 7 years	80

National Insurance (not contracted out rates)

	Annual		
Class 1	≤ £7,225	@	0%
Employee	[£7,226 – £42,475]	@	12%
	£42,476 and above	@	2%
Class 1			
Employer	≤ £7,072	@	0%
	£7,073 and above	@	13.8%
Class 1A			
Employer	13.8% × value of benefits		
Class 2	£2.50 per week		
	Annual		
Class 4	≤ £7,225	@	0%
	[£7,226 – £42,475]	@	9%
	£42,476 and above	@	2%

Calculations and workings need only be made to the nearest £.

All apportionments may be made to the nearest month.

All workings should be shown.

Chapter 1

THE UK TAX SYSTEM

Question 1 - 5

1 The overall function and purpose of taxation in a modern society

1.1 Economic factors

Spending by the government and the system of taxation impacts on the economy of a country.

Taxation policies have been used to influence economic factors such as employment levels, inflation and imports/exports

Taxation policies are also used to direct economic behaviours of individuals and businesses. For example they encourage individual saving habits (Individual Savings Accounts), and giving to charity (Gift Aid Scheme).

Further they may discourage motoring (fuel duties), smoking & alcohol (duties and taxes) and environmental pollution (landfill tax).

As government objectives change, taxation policies may be altered accordingly.

1.2 Social justice

The taxation system accumulates and redistributes wealth within a country.

Different taxes have different social effects.

(a) Progressive taxation:

As income rises the proportion of taxation raised also rises, for example UK income tax

(b) Regressive taxation

As income rises the proportion of taxation paid falls, for example, tax on cigarettes is the same regardless of the level of income of the purchaser, so as income rises it represents a lower proportion of income.

(c) Proportional taxation

As income rises the proportion of tax remains constant, for example Latvian/Lithuanian income tax

(d) Ad Valorem principle

A tax calculated as a percentage of the value of the item, for example Value Added Tax

2 Types of taxes

Income Tax	Payable by individuals on most income
National Insurance Contributions	Payable by individuals who are employed or self employed and businesses in relation to their employees
Capital Gains Tax	Payable by individuals on the disposal of capital assets
Inheritance Tax	Payable by individuals on lifetime and death transfers of assets.
Corporation Tax	Payable by companies on income and chargeable gains
Value Added Tax (VAT)	Payable by the final consumer on purchases of most goods and services

3 Direct and indirect taxation

3.1 Direct taxation

Taxes are paid directly to the Government, based on income and profit.

Examples are:

- Income tax
- Corporation tax
- Capital gains tax
- Inheritance tax

3.2 Indirect taxation

Taxes are collected via an intermediary who passes them on to the government for example:

- VAT where the consumer pays VAT to a supplier, who then pays to the government

4 Structure of the UK tax system

4.1 HM Revenue and Customs (HMRC)

The treasury formally imposes and collects taxation. The management of the treasury is the responsibility of the Chancellor of the Exchequer. The administration function for the collection of tax is undertaken by HMRC

4.2 Commissioners

At the head of HMRC are the commissioners whose duties are:

(a) to implement statue law

(b) oversee the process of UK tax administration

The main body of HMRC is divided into District offices and accounting and payment offices

4.3 District Offices

The Commissioner appoints Officers of HMRC to implement the day to day work of HMRC

4.4 Accounts and payment offices

These concentrate on the collection and payment of tax.

5 Sources of tax law

5.1 Tax legislation / statutes

Adherence is mandatory. It is updated every year by the annual Finance Act.

The Government may issue Statutory Instruments which are detailed notes on an area of tax legislation.

5.2 Case law

This refers to decisions made in tax cases. The rulings in the courts are binding and so provide guidance on the interpretation of tax legislation.

5.3 HMRC guidance

This is issued due to the complexity of the legislation

(a)	Statements of practice	–	sets out how HMRC intend to apply the law
(b)	Extra statutory concessions	–	sets out circumstances in which HMRC will not apply the strict letter of the law where it would be unfair.
(c)	Internal guidance manuals	–	HMRC's own manuals which are available to the public
(d)	Press releases	–	provide details of a specific tax issue, for example, used to communicate the information stated in the annual budget
(e)	Pamphlets	–	provide explanations of various tax issues in non technical language

6 The interaction of the UK tax system and overseas tax systems

6.1 Other countries

The UK has entered into Double Tax Treaties with various countries. These contain rules which prevent income and gains being taxed twice, but may include a non-discrimination provision preventing a non-resident individual from being treated less favourably than a resident individual.

Where there is no double tax treaty the UK system will allow relief for double tax.

6.2 The European Union

The aim of the EU is to remove barriers and distortions due to different economic and political policies imposed in different member states.

Although EU members do not have to align their tax systems, members can agree to jointly enact specific laws known as Directives. The most important example is VAT, as EU members have aligned their policies according to EU legislation but the members do not need to align the rate.

Cases have been brought before the European Court of Justice regarding the discrimination of non-residents, some of which have led to a change in UK tax law.

7 Tax avoidance and tax evasion

7.1 Tax evasion

Any action taken to evade taxes by illegal means, for example

(a) suppressing information - failing to declare taxable income to HMRC

(b) providing false information - claiming expenses that have not occurred

Tax evasion carries a risk of fines and/or imprisonment

7.2 Tax avoidance

Any legal method of reducing your tax burden, for example taking advantage of an Individual Savings Account or making best use of available allowances, exemptions and reliefs..

The term is also used to describe tax schemes that utilise loopholes in the tax legislation.

HMRC have introduced new disclosure obligations regarding tax avoidance schemes.

8 Professional and ethical guidance

Accountants often act for taxpayers in dealings with HMRC.

Their duties and responsibilities should be towards both clients and HMRC

8.1 The accountant must uphold standards of the ACCA that is

(a) to adopt an ethical approach to work, employers and clients

(b) acknowledge the professional duty to society as a whole

(c) maintain an objective outlook

(d) provided professional high standards of service, conduct and performance at all times.

8.2 The ACCA "Code of Ethics and Conduct"

The ACCA "Code of Ethics and Conduct" sets out five fundamental principles which members should adhere to meet these expectations, namely:

(a) Integrity

(b) Objectivity

(c) Professional competence and due care

(d) Confidentiality

(e) Professional behaviour

Example 1

Identify which tax applies to the following situations and state whether it is a direct or indirect tax

(a) A sole trader earns £100,000 profit in a year

(b) A company has profit of £250,000 in a year and employes 30 employees

(c) An individual sells an antique table for £100,000 which cost £40,000 eight years ago

(d) A business buys raw materials from a supplier

(e) A company sells a factory for £750,000 bought for £250,000 three years ago

(f) An individual dies and bequeaths their estate death of £1,000,000 to their children

Chapter 2

INCOME TAX COMPUTATION

Question 1, 4 or 5

1 Introduction

Compulsory question 1 is an income tax question. It is likely to contain most sources of taxable income and require an income tax computation to be prepared. However, there may be also be marks available for dealing with trading losses, pensions, national insurance contributions, and the residence status of an individual.

There are two main parts to the computation, firstly the computation of Taxable Income and secondly the calculation of the Income Tax Liability and/or Income Tax Payable thereon.

The Taxable Income will also be divided into three possible analysis columns, Dividend income, Savings Income which is interest income and Non-Savings Income which will be made up of employment income, trading profits of the self-employed and property income. This analysis is required as different tax rates may apply to the different types of income.

2 Computation of Taxable Income

An Income Tax Computation is prepared for each taxpayer and records the income to be taxed for that individual for a Tax Year. The Tax Year runs from April 6 to following April 5. The Tax Year 2011/12 runs fro April 6, 2011 to April 5, 2012. Therefore each source of income requires its own basis of assessment to determine how much income is to be assessed to tax in each such year.

Proforma income tax computation for 2011/12

	Non-savings income	*Savings income*	*Dividends*	*Total*
	£	£	£	£
Trading Profit	X			X
Less Trading Loss relief – brought forward	(X)			(X)
	X			X
Employment Income	X			X
Property Income	X			X
Dividends from UK companies × 100/90			X	X
Building society interest × 100/80		X		X
Bank deposit interest × 100/80		X		X
Other interest - gross		X		X
TOTAL INCOME	X	X	X	X
Less				
Qualifying interest	(X)			(X)
Trading Loss reliefs	(X)			(X)
NET INCOME	X	X	X	X
Less: Personal Allowance	(X)			(X)
TAXABLE INCOME	X	X	X	X

2.1 Exempt Income

The following sources of income are exempt from income tax

(a) Interest or bonuses on National Savings & Investment Certificates

(b) Interest and dividends within an Individual Savings Account [ISA]

(c) Gaming, lottery and premium bond winnings

2.2 Tax liability and Tax Payable

Having calculated the taxable income, the examiner could ask for one of two things:

(a) Tax liability = income tax on taxable income

(b) Tax payable = tax liability
LESS
tax already deducted at source, for example, Pay As You Earn (PAYE) on employment income and tax credits on interest received net.

2.3 Taxation of non-savings income.

Non-savings income is taxed at the following rates:

£1 to £35,000	20%	(basic rate)
£35,001 – 150,000	40%	(higher rate)
£150,001 +	50%	(additional rate)

Non-savings income consists of:

(a) Trading Profit - see chapters 4-8

(b) Employment Income - see chapter 9

(c) Property Income - see chapter 3

Example 1

Mr Smith is a single man who has been working for many years and earns a salary of £50,000 per annum (PAYE £10,010).

Calculate the income tax payable for Mr Smith in 2011/12?

3 Savings income and Dividend Income

Savings income is interest income and is received either gross or net of deduction of basic rate tax at source

3.1 Types of taxed savings income

(a) Building society interest

(b) Bank deposit interest

(c) Company debenture interest

Most building society interest, bank deposit interest and company debenture interest is received by individuals net of 20% income tax deducted at source. This tax credit is refundable if the amount deducted at source exceeds the Tax Liability of the taxpayer.

3.2 Interest received Gross:

(a) National Savings Bank Interest

(b) Government Stock Interest (Gilts, Treasury Stock, Exchequer stock)

3.3 Basis of assessment

Savings income is assessed in the tax year that it is received.

3.4 Dividend Income

Dividends are included on the computation on a basis of actual amounts received in the Tax Year. The figure is also grossed up but now at a rate of 100/90 for what is a notional tax credit of 10%. In this case no actual tax is deducted at source by the company paying the dividend nor then paid over to HMRC. As no tax has actually been paid no repayment can therefore arise if this credit exceeds the Tax Liability. For this reason the notional tax credit on dividends is always deducted first.

3.5 Calculation of tax on all savings income and all dividend income

(a) Interest received net and dividends must be grossed up for inclusion in the income tax computation

- interest received net is grossed up by $^{100}/_{80}$
- dividends are grossed up by $^{100}/_{90}$

(b) Interest received (including interest received gross) is included in the saving income column of the computation, dividends received are included in the dividend column

(c) Any deductions in the income tax computation (personal allowance and/or reliefs) are deducted first from non-savings income, then savings income, then dividend income hence the order in which the analysis columns are listed.

(d) Non-savings income is treated as the first slice of taxable income to be taxed followed by savings income then dividend income. The total of this tax is the Tax Liability of the taxpayer

(e) Tax suffered as source is deducted from the tax liability in order to arrive at tax payable.

(f) If there is no liability, the tax suffered on interest and PAYE may be repaid, but tax suffered on dividends is not repayable.

(g) The different types of income are taxed as follows and in this order:

Non Savings	£1 to £35,000	20%
	£35,001 – 150,000	40%
	£150,001 +	50%
Savings	• Savings income is taxed in the same way as non-savings income, however a starting rate of tax of 10% will apply to the first £2,560 of savings income in the following circumstance: The 10% rate only applies where savings income falls within the first £2,560 of taxable income.	
	• If the first £2,560 consists of non-savings income then the 10% rate will not apply.	
	•	
Dividends	• After considering non savings and savings income the dividend tax rates are: £1 – £35,000 @ 10%; £35,001 – £150,000 @ 32½ %; £150,001 + @ 42½ %	

EXAMPLE 2

Billy earned trading profit of £25,000 and received bank deposit interest of £8,000 in 2011/12

Calculate Billy's income tax payable in 2011/12

Example 3

Recalculate Billy's income tax payable, assuming the bank deposit interest is £16,000

Example 4

Molly receives bank interest of £16,000 and no other income in 2011/12.

Calculate Molly's income tax payable in 2011/12

Example 5

Rework the example of Molly, assuming she receives trading profit of £8,000 in addition to the bank interest.

Example 6

Daisy earned a salary of £15,000 (PAYE £1,505), received £8,000 bank deposit interest and dividend income of £1,800 in 2011/12

Calculate Daisy's income tax payable for 2011/12

Example 7

Recalculate Daisy's income tax payable, assuming Daisy earned a salary of £35,000 (PAYE £5,705) and received bank deposit interest of £9,600. Dividend income received remains at £1,800.

4 Personal allowances

All individuals are entitled to a tax free amount - this is £7,475 for 2011/12, but may be higher for elderly tax payers or lower for individuals with income exceeding £100,000.

- The standard personal allowance for 2011/12 is £7,475. However if an individuals adjusted net income exceeds £100,000 then the personal allowance is reduced by:

  1/2 × [Adjusted net income – £100,000]

- Once adjusted net income ≥ £114,950 the personal allowance is reduced to NIl.
- Net income is total income less qualifying interest payments and trading loss reliefs (see later).
- Adjusted net income is Net income less gross personal person contributions and less gross gift aid payments (see later).

Example 8

Mike earned employment income of £108,000 in 2011/12 of which £33,130 was deducted at source under PAYE in 2011/12.

Calculate Mike's income tax payable for 2011/12.

Example 9

Ken earned trading income of £130,000, received bank interest of £32,000 and dividend income of £32,400 in 2011/12.

Calculate Ken's income tax payable for 2011/12.

5 Personal age allowances

- A person aged 65 or above (at any time in the tax year) receives an age allowance of £9,940 instead of the standard personal allowance of £7,475
- A person aged 75 or over (at any time in the tax year) receives an age allowance of £10,090 instead of the standard personal allowance of £7,475
- However where adjusted net Income exceeds £24,000, the age allowance is restricted by ½ [Adjusted Net Income – 24,000] until it is reduced to a minimum of the standard personal allowance £7,475
- There will be a further reduction if adjusted net income exceeds £100,000.
- Regardless of a persons age, no personal allowances will be available where adjusted net income ≥ £114,950

Example 10

Tony has adjusted net income of £25,000 in 2011/12. He is 68 years old.

Calculate the personal age allowance Tony is entitled to.

Example 11

Recalculate the age allowance assuming Tony's adjusted net income is £30,000 in 2011/12

Example 12

James is 71 years old in 2011/12. He earned trading profit of £102,000 and receives bank interest of £3,200 in 2011/12.

Calculate James's income tax payable for 2011/12.

6 Reliefs

6.1 Reliefs are tax deductible

The only reliefs examinable at Paper F6 are

(a) qualifying interest

(b) loss reliefs

6.2 Qualifying interest is:

(a) On a loan to purchase an interest in a partnership or a contribution to the partnership of capital or a loan

(b) On a loan to purchase plant or machinery used in the business, by a partner

(c) On a loan to purchase plant and machinery by an employee if used in the performance of duties

(d) On a loan to purchase an interest in a close company

6.3 Loss reliefs

These will be explained in chapter 7.

EXAMPLE 13

Kathy has trading profit of £50,000 in 2011/12 and paid £1,000 interest on a loan to purchase plant & machinery used in the business of her partnership.

Calculate Kathy's income tax liability for 2011/12

7 Payments to charity under the Gift Aid System

7.1 Basic rate taxpayers

Payments to charity under Gift aid are treated as being paid net of the basic rate tax (20%). For a basic rate taxpayer tax relief at the basic rate is automatically obtained as payments are made to the charity net of basic rate relief being given at source ie to give a charity £100 the taxpayer need only make a gift aid payment of £80 and the charity will be able to claim back from HMRC the basic rate tax of £20 thereon collected by HMRC from the taxpayer's income. Therefore the donation is not deducted in the calculation of Taxable Income, but see note below on restriction of personal allowance.

7.2 Higher rate tax payer

For higher rate taxpayers, 40% tax relief is given as follows:

(a) 20% at source

(b) 20% through the income tax computation, obtained by extending the basic rate band by the **gross donation** (so that more income is taxed at 20% and less at 40%)

The taxpayer can elect to treat the gift aid payment as if made in the previous year, ie a payment made by 31 January 2012 can be treated as if paid in tax year 2010/11.

7.3 Additional rate tax payer

For additional rate taxpayers, 50% tax relief is given as follows:

(a) 20% at source

(b) 30% through the income tax computation by extending both the basic rate band and additional rate band by the gross donation (so that more income is taxed at 20% and less at 50%)

The same treatment as gift aid payments will also apply to payments made by individuals into their Personal Pension Scheme (see chapter 10)

See also earlier note 4 on page 10 that both the gross gift aid payments and personal pension contributions are deducted in arriving at the adjusted net income figure used to restrict the personal allowance of the taxpayer.

Example 14

Elliot has trading profit of £48,000 in 2011/12. He paid £1,600 to charity under the gift aid system.

Calculate Elliot's income tax liability for 2011/12

Example 15

Thomas earned £160,000 trading profit in 2011/12. In the tax year he paid £6,400 to charity under the gift aid scheme.

Calculate Thomas's income tax liability for 2011/12.

Example 16

Kerry earned £102,000 trading profit in 2011/12. In addition she received bank interest of £3,200 and dividend income of £2,700. She paid interest of £3,000 on a loan to contribute capital into a partnership of which she is a partner. She made a payment of £4,800 to charity under the gift aid scheme.

Calculate Kerry's income tax payable for 2011/12.

8 Jointly owned assets of a married couple, or by a couple in a civil partnership

Spouses and civil partners are taxed as two separate people. Each spouse / civil partner has their own Income Tax Computation and includes within it their own taxable income and is entitled to a personal allowance or an age related personal allowance depending on his or her own age and income

8.1 Joint property

When spouses/civil partners own income generating assets jointly, it is assumed that they are entitled to equal shares of the income and it is split accordingly on a 50:50 basis between them.

However they may make a joint election to HMRC to split the income according to their actual ownership shares, (except in the case of jointly held bank or building society accounts).

The rules allows couples to rearrange joint income between them to better use their personal allowance and lower tax rates thereby reducing their overall tax liabilities

Note, for shares held in a husband and wife (or civil partner) company, dividends are always divided according to the exact proportion to which each is actually entitled to, it is never assumed that it is in equal proportions.

The 50:50 rule may also be used to reduce income tax liabilities where a higher rate taxpayer currently owns outright an income producing asset while their spouse is not fully using either their personal allowance or basic rate band. A transfer of a nominal amount of the capital ownership eg 5% would allow 50% of the income to be assessed on the spouse! Clearly if the taxpayer was happy to transfer the entire ownership of the asset to the spouse then an even greater amount of tax would be saved!

Example 17

Elton is a higher rate taxpayer (Adjusted net income is ≤ £100,000). This includes £20,000 of rental income on a property owned entirely by Elton on which he pays tax at 40%, a tax liability therefore of £8,000. David his civil partner has no income.

Discuss the way Elton and David could reduce their income tax liabilities

9 Status of an individual in the UK and the effect of their liability to UK income tax

9.1 Definitions

- **Resident in the UK**
  - If an individual is physically present in the UK for 183 days or more in the tax year they are resident in the UK for the whole of the tax year.
  - If an individual is physically present for 91 days or more on average over the previous 4 tax years they will become resident from the start of the fifth tax year.
  - An individual entering the UK to stay permanently (at least 2 years) is resident from the day they enter the UK
  - An individual who is resident and leaves the UK, must be absent for a complete tax year in order to lose their residence status, unless they are leaving permanently to set up home overseas then they lose their residence status when they leave the UK
- **Ordinary Resident**
  - Ordinary resident status is based on where one normally and habitually resides and obtained once an individual has been resident for 3 years
  - An individual entering the UK to stay permanently (at least 3 years) will be ordinary resident immediately
  - If their intention is stay less than 3 years but they do stay then they become ordinarily resident from the third anniversary of arrival, or from the start of that tax year where it appeared obvious their intention was to stay permanently
  - An individual who is ordinary resident and leaves the UK, must be absent for three complete tax years to lose their ordinarily resident status unless they are leaving permanently then they will lose their ordinarily resident status from the day they leave the country

9.2 Implications for Income Tax

- **Non resident** – Taxed on UK income only
- **Resident (but not ordinarily resident)** – UK income and can elect to have overseas income taxed on a remittance basis if the individual pays a £30,000 tax charge under some circumstances.
- **Resident and ordinarily resident** – worldwide income on an arising basis

For exam purposes, any income tax computations will assume the individual is assessed on worldwide income.

Note: However the definitions of resident and ordinarily resident could be tested in a written question

Chapter 3

PROPERTY INCOME AND INVESTMENTS – INDIVIDUALS

Question 1, 2, 4 or 5

1 Income liable

The following income is liable to assessment under Property Income:

(a) rents under any lease or tenancy agreement

(b) premium received on the grant of a short lease

1.1 Basis of assessment

Income from land and buildings is computed as if the letting of the property were a business, and the amount assessable under property income will be the rental business profits for the individual in the tax year.

Accounts should be drawn up using the accruals basis. Any expenses payable for the same period can be deducted. Capital expenditure is not allowable.

EXAMPLE 1

Jim bought a property and rented it out for the first time on 1 July 2011. The rent of £6,000 per annum is paid alternatively (1) quarterly in advance (2) quarterly in arrears, or (3) annually in advance.
He paid allowable expenses of £300 in November 2011 for redecoration and £500 in May 2012 for repairs completed in March 2012.

Calculate the Property Income for 2011/12.

1.2 Allowable deductions

(a) To be allowable expenses must have been incurred wholly and exclusively in connection with the business for example

- insurance
- agents' fees
- other management expenses, for example cleaning expenses
- repairs
- interest on a loan to purchase the property

(b) Capital expenditure is not allowable.

- Repairs are allowable revenue expenses.
- Improvements are capital and therefore disallowed

(c) Capital allowances may be claimed for expenditure on plant and machinery used for the maintenance of the property

(d) If the lettings are furnished, tax relief is usually given for the furniture and furnishings by a 10% wear and tear allowance, calculated as:

$$10\% \times \text{rental income}$$

or, if the landlord pays council tax, water rates or business rates on the property:

$$10\% \times (\text{rental income} - \text{council tax / business rates} - \text{water rates})$$

(e) Relief is available for expenditure incurred before letting commenced, under the pre-trading expenditure rules. ie expenditure incurred up to 7 years prior to renting - the revenue expenses are treated as incurring on day one of the letting business

EXAMPLE 2

Sid owns a furnished property that is let out at an annual rent of £3,600, payable monthly in advance. During the year 2011/12 he incurred the following expenditure:

May 2011	Construction of a garage, replacing the car port	£2,000
June 2011	Insurance for year from 1 July 2011 (insurance for the previous year to 30 June was £420)	£480
November 2011	Drain clearance	£380
May 2012	Redecoration (work completed in March 2012)	£750

The tenant vacated the property during June 2011 without having paid the rent due for June. Sid was unable to trace the defaulting tenant, but managed to let the property to new tenants from 1 July 2011.

Calculate the Property Income for 2011/12 assuming that Sid claims the 10% wear and tear allowance.

2 Property losses

If total expenses exceed total rental income, the property income assessment is **nil** and the excess property loss is carried forward and offset against future property income only.

3 Furnished holiday lettings

There are special rules for furnished holiday lettings.

The letting is treated as if it were a trade. This means that, although the income is taxed as income from a UK property business some of, the provisions which apply to actual trades also apply to furnished holiday lettings as follows:

(a) Capital allowances are available on furniture instead of the wear and tear allowance

(b) Income qualifies as earnings for pension relief (see chapter 10)

(c) Capital gains tax rollover relief, gift relief and entrepreneurs' relief are all available.

The profit or loss is computed for tax years on an accruals basis. Losses may only be carried forward against future profits from furnished holiday lettings

The lettings must be of UK or European Economic Area furnished accommodation made on a commercial basis with a view to the realisation of profit. In addition the following conditions must also be satisfied:

(d) The accommodation must be available to let for at least 140 days in the tax year.

(e) The accommodation must actually be let for at least 70 days in the year

(f) No one person occupies the property for more than 31 consecutive days. If one or more persons does occupy the property for more than 31 consecutive days then these periods of long letting must not exceed 155 days in the year

4 Rent a Room relief

If an individual lets a room or rooms, furnished, in his or her main residence as living accommodation then gross rents up to £4,250 p.a. are exempt.

The exemption may be ignored if the tax payer wants to generate a loss where expenses exceed income, or where actual expenses exceed £4,250.

If gross rent exceed £4,250 p.a. the tax payer may choose to assess as follows:

(a) Ordinary calculation

Gross rent	X
Less: expenses	(X)
Wear & tear allowance	(X)
Property Income	X

(b) Alternative calculation (election)

Gross rent	X
Less: rent a room relief	(4,250)
Property Income	X

The election must be made for 2011/12 by 31 January 2014 and stays in force until it is revoked.

Example 3

Barbara rents a room in her main residence. Gross rents are £85 per week and expenses amount to £120

Calculate Barbara's Property Income and state the due date for any relevant election.

5 Lease premiums on grant of short lease (50 years or less)

5.1 Introduction

(a) When a tenant takes on a new lease he may be required to pay a one-off premium in addition to the annual rent. If the lease is for less than 50 years, part of the premium is assessed on the landlord as property income, the remainder is treated as a capital receipt.

The treatment of the capital receipt is outside the syllabus

(b) The amount of the premium assessed as Property Income is:

$$P \times \frac{51 - n}{50}$$

Where: P = total premium

n = duration of lease in years

EXAMPLE 4

Bill grants Richard a lease to a shop on 30 June 2011
Annual rent £5,000 due on 1 July 2011
Term 20 years
Premium £60,000

Calculate the Property Income assessment for Bill in 2011/12

5.2 Trading Profit deduction for traders

Where a trader has paid a premium for a short lease he may deduct the following annual amount against his Trading profit in each of the year's of the lease in which the property is used in the trade. This is in addition to any rent paid:

$$= \frac{\text{Property Income assessment on landlord}}{\text{Life of lease}} \text{ p.a.}$$

Example 5

Using example 4 above, show the relief available to Richard for the premium paid.

6 Individual Savings Accounts (ISA's)

6.1 ISA's are the most common form of tax efficient investment. An ISA can be opened by any individual aged 18 or over who is resident and ordinarily resident in the UK (although a cash ISA can be opened by an individual aged 16 or over)

The main advantages of ISAs are:

(a) Income is free of income tax

(b) Disposals of investments within an ISA are free from capital gains tax

(c) No minimum holding period - withdrawals can be made at any time

6.2 Components of an ISA

(a) Cash - for example in a bank account

(b) Stocks and shares listed anywhere in the world

6.3 Subscription limits

The annual subscription limit is £10,680 per tax year , of which £5,340 may go into the cash component.

An individual can invest in either:

(a) Cash ISA maximum £5,340 p.a.

(b) Stocks and shares ISA maximum £10,680 p.a.

(c) Both stocks and shares and cash with the maximum cash £5,340 p.a., the balance up to £5,340 p.a. in stocks & shares

These limits will be given in the Tax Rates and Allowances section of the exam paper

7 National savings

These offer a variety of products some of which are tax free, namely:

National Savings Certificates

However, some National Savings Products are taxable, namely:

- NSB Easy Access account
- NSB Investments accounts

The income is paid without deduction of tax at source, ie GROSS

The nature of the investments are historically risk free.

Chapter 4

TAX ADJUSTED TRADING PROFIT – INDIVIDUALS

Question 1, 2, 4 or 5

1 Badges of trade

The following tests are used to establish if a series of transactions should be treated as a trade and taxed under tax adjusted trading profit.

1.1 Subject matter

Whether a person is trading or not may sometimes be decided by looking at the subject matter of the transaction.

1.2 Frequency of transactions

Transactions of a capital nature will be interpreted as trading transactions where their frequency indicates the carrying on of a trade.

1.3 Length of ownership

Where items purchased are sold soon afterwards, the transactions are likely to be treated as a trade.

1.4 Profit motive

The presence of a profit motive will be a strong indication that a person is trading.

1.5 Supplementary work and marketing

When work is done to make an item more marketable, or attempts are made to find purchasers, the transactions are more likely to be treated as a trade.

1.6 Manner in which assets were acquired

If acquired unintentionally (e.g. by inheritance) and then sold, it is unlikely that trading has taken place.

2 Adjusting the accounting profit

2.1 Introduction

(a) Tax adjusted trading profits are not the same as the profits shown in the individuals business Income Statement. Accounting profits before tax are adjusted to arrive at tax adjusted trading profit

(b)

		£
Net profit per accounts		X
ADD BACK: Expenditure not deductible for tax		X
		X
Deduct items not assessed under tax adjusted trading profit		
- Income assessable elsewhere	X	
- Non-taxable income	X	
		(X)
Adjusted profits		X
LESS: Capital allowances		(X)
Tax adjusted trading profit		X

Note:

When preparing this calculation, be careful to start with the NET profit per accounts.

2.2 Typical expenditure by a business

(a) Capital expenditure including depreciation is not allowable

Note:

» repair to an asset is revenue expenditure and is allowable

» improvement to an asset is capital expenditure and is not allowable

(b) Reliefs, such as qualifying loan interest payments are not allowable as they are dealt with as a deduction from total income

(c) Patent royalties payable are an allowable deduction for adjusted trading profit.

(d) Irrecoverable Debts (Trade debt write offs & allowances)

» These are allowable; the tax treatment follows the accounting treatment

» However non trade write offs are not allowable and so the expense is added back.

(e) Entertaining and gifts

» entertaining is disallowed, unless entertaining employees

» gifts to employees are allowable

» gifts to customers are only allowable if

- they cost less than £50 per person per year, and
- the gift is not food, drink, tobacco or vouchers exchangeable for goods and services
- the gift carries a conspicuous advertisement for the business.

(f) Subscriptions and donations

» trade or professional association subscriptions are allowable

» charitable donation (Not made under Gift Aid)

- if it is wholly and exclusively for trading purposes (e.g promoting business' name), and it is to a local charity then it is allowable
- National charity donations are not allowable

» charitable donations (made under Gift Aid) these are not allowable.

» Political donations - these are not allowable

(g) Legal and professional charges

» allowable if connected with the trade and are not related to capital items

» specifically **allowed** by statute:

- costs of obtaining loan finance
- costs of renewing a short lease (50 years or less)

(h) Interest payable

» interest paid on borrowings for **trading purposes** is allowable on an accruals basis therefore no adjustment is needed.

(i) Lease rentals on cars with CO_2 emissions exceeding 160g/km

» the disallowed amount is 15% of the leasing charges p.a..

(j) Premium paid for the grant of a lease.

» the premium itself is disallowed as is any amortisation of the premium

» the allowable amount is:

$$\frac{\frac{51-n}{50} \times \text{Premium}}{n}$$

where n is the number of years of the lease.

(k) Fines and penalties - Disallowed unless the fine is paid on behalf of an employee and incurred whilst on business

(l) The accounting profit must be adjusted for the private expenditure of the business owner. If the owner uses a car in the business and 20% of his mileages private, then only 80% of motor expenses are allowable.

However if the owner provides an employee with a car, and 20% of the mileage is for private use by the employee, then the full amount of motor expenses is allowable. (The employee is taxed on the private use under Employment Income).

(m) Any deduction described as the owner's salary, or drawings or interest on capital invested in the business is disallowed.

(n) Interest paid on overdue tax is not deductible and interest received on overpaid tax is not taxable

(o) Any salary paid to the family of the owner of the business must not be excessive.

Only salary at the commercial rate for the work done is allowable.

(p) If an owner removes goods from the business for his own use he must add back the item as a sale at market value, unless the owner accounts for the cost of the goods in the business accounts then they need only add back the lost profit on the item.

(q) Pre-trading expenditure – allowable if it is expenditure incurred in the seven years before a business commences to trade then it is treated as an expense incurred on the day the business starts trading and follows the above rules.

(r) The general rule is that expenditure not wholly and exclusively for the purpose of the trade is not allowable

Example 1

On 1 June 2011 Jeremy commenced in self-employment running a retail shop. Jeremy's Income Statement for the year ended 31 May 2012 is as follows:

	£	£
Gross Profit		140,880
Expenses:		
Depreciation	4,760	
Light and heat (Note 1)	1,525	
Motor expenses (Note 2)	4,720	
Professional fees (Note 3)	2,300	
Rent and rates (Note 1)	3,900	
Repairs and renewals (Note 4)	5,660	
Sundry expenses (Note 5)	2,990	
Wages and salaries (Note 6)	84,825	
		110,680
Net profit		30,200

Notes

Note 1: Private accommodation

Jeremy and his wife live in a flat that is situated above the clothing shop. Of the expenditure included in the Income Statement for light, heat, rent and rates, 40% relates to the flat.

Note 2: Motor expenses

During the year ended 31 May 2012, Jeremy drove a total of 12.000 miles, of which 9,000 were for private journeys.

Note 3: Professional fees

Professional fees are as follows:

	£
Accountancy	700
Legal fees in connection with the purchase of the clothing shop	1,200
Debt collection	400
	2,300

Included in the figure for accountancy is £250 in respect of a capital gains tax computation.

Note 4: Repairs and renewals

The figure of £5,660 for repairs and renewals includes £2,200 for decorating the clothing shop during July 2011, and £1,050 for decorating the private flat during August 2011. The building was in a usable state when it was purchased.

Note 5: Sundry expenses

The figure of £2,990 for sundry expenses, includes £640 for gifts to customers of food hampers costing £40 each, £320 for gifts to customers of pens carrying an advertisement for the clothing shop costing £1.60 each, £100 for a donation to a national charity, and £40 for a donation to a local charity's fete. The fete's programme carried a free advertisement for the clothing shop.

Note 6: Wages and salaries

The figure of £84,825 for wages and salaries includes the annual salary of £15,500 paid to Jeremy's wife. She works in the clothing shop as a sales assistant. The other sales assistants doing the same job are paid an annual salary of £11 ,000.

Note 7: Goods for own use

During the year ended 31 May 2012, Jeremy took clothes out of the shop for his personal use without paying or accounting for them. The cost of these clothes was £460, and they had a selling price of £650.

Note 8: Plant and machinery

The capital allowances available for the year ended 31 May 2012 are £13,060.
(In the actual examination you will be required to do a capital allowances computation and work out this figure.)

Calculate Jeremy's tax adjusted trading profit for the year ended 31 May 2012.

Chapter 5

CAPITAL ALLOWANCES

Questions 1, 2, 4 or 5

1 Capital allowances

(a) Capital allowances are available for expenditure on plant and machinery

(b) Plant and machinery is something with which a trade is carried on. It includes not only the obvious items of plant and machinery, but also such items as movable partitions, office furniture and carpets, heating systems, motor vehicles, computers, lifts and any expenditure incurred to enable the proper functioning of the item such as reinforced floors or air-conditioning systems for computers.

(c) Capital allowances are deducted in arriving at the tax adjusted trading profit

2 Calculating the Allowances

2.1 The pool of expenditure

(a) The cost of most plant and machinery purchased by a business becomes part of a general pool of expenditure on which capital allowances may be claimed. An addition increases the general pool; a disposal reduces the pool.

(b) The following items are not included in the pool:

» motor cars costing more than £12,000 (acquired pre 6 April 2009)

» expenditure on short-life assets where an election to de-pool is made

» expenditure on items included in the 'special rate pool'

» assets with private use by the owner of the business

2.2 Writing down allowances (WDA)

(a) A WDA of 20% per annum is given on the reducing balance basis.

(b) Proforma calculation

Year ended 31 March 2012	*Pool*
	£
WDV b/f at 1 April 2011	X
Additions	X
less: disposals	(X)
	X
WDA – 20%	(X)
WDV c/f at 31 March 2012	X

The written down value brought forward (WDV b/f) is the unrelieved expenditure in the pool brought forward at the beginning of the accounting period.

(c) If the accounting period is less or more than 12 months long, the WDA is scaled down or up proportionately.

2.3 Length of ownership in the accounting period

The WDA is never restricted by reference to the length of ownership of an asset in the accounting period. If a business's accounting period is for example, the year ended 31 March 2012 the same WDA is given if an asset is purchased on 1 April 2011 or on 31 March 2012.

2.4 Sale of plant and machinery

(a) Where plant and machinery is sold during the accounting period, the sale proceeds are deducted from the balance of unrelieved expenditure in the pool.

(b) The proceeds deducted must never exceed the original cost of the asset that has been sold. On the disposal of an asset always deduct the lower of the sale proceeds and the original cost from the pool.

EXAMPLE 1

Mike prepares accounts to 31 March.
In the year to 31 March 2012 the following transactions took place:
3 April 2011 plant is sold (originally purchased for £2,000) for £2,400

The WDV on the pool at 1 April 2011 was £6,000

Calculate the capital allowances for the year ended 31 March 2012

2.5 Annual Investment Allowance (AIA)

- This is available to all businesses and allows 100% relief for the first £100,000 p.a. of expenditure on plant and machinery with the exception of cars.
- The £100,000 limit is prorated where a period of account is shorter or longer than 12 months.
- If a business spends more than £100,000 p.a. on assets qualifying for the AIA then expenditure above £100,000 will qualify for a WDA of 20% on general pool expenditure or 10% on special rate pool expenditure.

EXAMPLE 2

Jeremy prepares accounts to 31 March
In the year ended 31 March 2012 the following transactions took place
1 May 2011 Purchased plant for £70,000
1 October 2011 Purchased plant for £46,200
9 February 2012 Sold plant for £4,000 (original cost £10,000)

The WDV on the pool as at 1 April 2011 was £16,000.

Calculate the capital allowances for the year ended 31 March 2012.

Example 3

James prepares accounts for the 9 months to 31 December 2011.

The following transactions occurred:

5 July 2011	Purchased machinery for £80,000
10 September 2011	Sold machinery for £6,000 (original cost £10,000)

The WDV on the pool as at 1 April 2011 was £12,000

Calculate James' capital allowances for the 9 months to 31 December 2011

2.6 Motor cars

Motor cars are not eligible for AIA

- The rate of allowance for a motor car depends on its CO_2 emissions:
  (1) Motor cars with CO_2 emissions of 110g/km or below qualify for a First Year Allowance **(FYA) of 100%**
  (2) Motor cars with CO_2 emissions of between 111 –160g/km qualify for a **WDA of 20%**
  (3) Motor cars with CO_2 emissions of above 160g/km qualify for a **WDA of 10%**
- Unless there is private use by the owner of an unincorporated business, motor cars qualifying for a WDA of 20% are included in the general pool and motor cars qualifying for a WDA of 10% are included in the special rate pool.
- Motor cars with private use by the owner of an unincorporated business are kept separately so a private use adjustment can be made (see below)
- Motor cars purchased pre 6/4/09 with an amount brought forward at start of Accounting Period are to remain as per the pre 6/4/09 rules. Motor cars costing more than £12,000 were kept separately from other items and qualified for a WDA of 20% restricted to a maximum of £3,000 p.a.. This was regardless of a motor cars CO_2 emissions.
- **Note:** Motorcycles and vans are not classed as motor cars and do **not** follow the above rules, they are treated as any other plant and machinery and will therefore rank for AIA
- The FYA for motor cars with CO_2 emissions of 110g/km or below is never time apportioned

Example 4

Steven prepares accounts to 31 March.
The WDV of the general pool at 1 April 2011 is £22,700 and on an expensive car £15,600. The following transactions took place during the year ended 31 March 2012:

4 May 2011	Purchased plant for £24,800
30 November 2011	Purchased a motor car for £11,200 CO_2 of 130g/km
6 January 2012	Purchased a motor car for £14,100 CO_2 of 170g/km
15 February 2012	Purchased a motor car for £14,400 CO_2 of 105g/km

Calculate the capital allowances for the year ended 31 March 2012.

2.7 Balancing allowances and charges

(a) The intention of capital allowances is to give relief for the fall in value of an asset during the period of ownership.

(b) On disposal of an expensive car (purchased pre 6 April 2009) owned at start of Accounting Period a balancing allowance or charge may occur which assures the correct allowances have been claimed over the life of the asset. A balancing allowance arises where the asset is sold for less than its tax wdv and this is added into the capital allowances of the period. If the asset is sold for more than its tax wdv a balancing charge will arise and this will reduce the capital allowances available for the period.

EXAMPLE 5

Adam prepares accounts to 31 March.
The following transactions took place during the year ended 31 March 2012.
1 August 2011 an expensive car was sold for £8,000. It had originally cost £19,000 and the WDV on 1 April 2011 was £13,000

Calculate the balancing adjustment on sale

EXAMPLE 6

Rework the above example assuming the car was sold for £20,000

(c) A Balancing charge can arise at any time on the general pool or special rate pool if disposal proceeds exceed the balance on the pool.

Example 7

Peter prepares accounts to 31 March. In the year ended 31 March 2012 the following transactions took place:

1 April 2011	Plant sold (originally purchased for £10,200) for £8,600
1 October 2011	Second hand motor car (emissions 135g/km) purchased for £2,000

The WDV on the pool as at 1 April 2011 was £4,000.

Calculate the balancing adjustment for the year ended 31 March 2012

(d) A Balancing allowance can only occur on the general pool and special rate pool on cessation of the trade

(e) No AIA, WDA or FYA are available in the final accounting period of the business

Example 8

Kris prepares accounts to 31 March.
Kris ceased to trade on 31 March 2012 on which date all plant and machinery was sold for £5,000.
The WDV on the pool as at 1 April 2011 was £12,000.
Machinery was purchased on 1 June 2011 for £4,000

Calculate the balancing allowance for the year ended 31 March 2012

2.8 Short-life assets

(a) An election can be made to omit short life assets from the pool and include them in their own individual column. This is known as a 'depooling election'

(b) This allows the acceleration of capital allowances on short-life plant and machinery where they are sold or scrapped within 8 years following the end of the accounting period in which it was acquired.

(c) Any plant and machinery, **except cars**, can be treated as a short-life asset.

(d) Capital allowances on each short-life asset are calculated separately

(e) On disposal within 8 years of the end of the accounting period in which the acquisition took place a balancing allowance or charge arises, which would not occur if the item was pooled.

(f) If no disposal takes place within 8 years of the end of the accounting period in which the acquisition took place the unrelieved balance is transferred to the pool.

The transfer is immediately after the 8th anniversary of the end of the accounting period in which it was acquired.

(g) The AIA is available against expenditure on short life assets. If expenditure is outside this limit then expenditure on general pool items will qualify for a WDA of 20%.

(h) The AIA could be matched with short life assets. However if total expenditure on plant and machinery is above £100,000 the AIA would be allocated to the general pool additions first, as no balancing allowance occurs on sale. If the AIA is allocated to general pool items first then a short life asset election could be made on the excess, with balancing allowances hopefully crystalising on disposal.

Example 9

John prepares accounts to 31 March.
At 1 April 2011 the WDV of the general pool was £16,000.
On 1 July 2011 John purchased machinery for £120,000
On 1 September 2011 John purchased a photocopier for £4,000 and made a short life asset election.
On 1 July 2012 the photocopier was sold for £1,500.

Calculate the capital allowances for years ended 31 March 2012 and 31 March 2013

3 Private use assets

3.1 Private use of an asset by the owner of the business

Where an asset is used by the owner of the business (this can be either a sole trader or a partner in a partnership) partly for business and partly for private purposes (typically a motor car), only the business proportion of the available capital allowances is given. This proportion is computed by reference to the percentage of business use to total use. The following rules must be followed when computing capital allowances:

(a) The cost is not brought into the general or special rate pool, but must be the subject of a separate computation

(b) The WDA (or AIA or FYA) of the asset is based on its full cost but only the business proportion of any allowance is actually given.

(c) On disposal of the asset, a balancing adjustment is computed by comparing sale proceeds with the WDV (there is a balancing charge if there is a profit, and a balancing allowance if there is a loss). Having computed the balancing adjustment, the amount assessed or allowed is then reduced to the business proportion.

(d) Where the asset concerned is an expensive motor car (brought forward at 6 April 2009) WDAs are first restricted to the £3,000 limit (for WDVs over £15,000) and then the business proportion of the WDA is actually given as an allowance.

(e) Private use by an employee of an asset owned by the business has effect on the business's entitlement to capital allowances. This is why the private use of an asset is irrelevant for companies, as directors are treated as employees for this purpose. Instead, there will normally be a benefit charge on the employee or director.

(f) It is unlikely the AIA would be matched against private use assets as only the business proportion could be claimed, it would be more beneficial to allocate AIA against other assets where there is no restriction.

Example 10

Jane prepares accounts to 5 April. At 6 April 2011 the WDVs brought forward are as follows:

	£
General Pool	21,200
Expensive motor car (used 30% for private purposes by Jane)	13,600

The following transactions took place during the year ended 5 April 2012:

10 May 2011	Purchased plant for £6,600
25 June 2011	Purchased a motor car for £10,600 CO_2 emissions of 140g/km
15 February 2012	Sold the expensive motor car for £9,400
16 February 2012	Purchased a motor car for £16,000 CO_2 emissions of 180g/km (used 30% for private purposes by Jane)

Calculate Jane's capital allowances for the year ended 5 April 2012.

4 Special rate pool

This is a pool for expenditure on the following types of assets:

- long life assets
- integral features of a building or structure
- thermal insulation of a building
- motor cars with CO_2 emissions exceeding 160g/km

Expenditure in the special rate pool qualifies for a WDA of 10% per annum on a reducing balance basis

The AIA is available on the expenditure classed as 'special rate' (except motor cars) and it would be more beneficial to allocate the AIA on expenditure of this nature in priority to general pool items as assets are only eligible for 10% WDA not 20% WDA as is the case with general pool items.

4.1 Long-life assets

(a) Long-life assets are items of plant and machinery with a working life of 25 years or more.

(b) All long-life assets are included in the special rate pool.

(c) If the company spends less then £100,000 p.a. on long-life assets, then the reduced rate of 10% WDA does not apply, and the asset qualifies as a general pool item.

4.2 'Integral features' of a building or structure

- electrical and general lighting systems
- cold water systems
- space or water heating systems
- powered systems of ventilation, cooling or air purification
- lifts and escalators

4.3 Thermal insulation of a building

This is for all business buildings (except residential buildings in a property business)

4.4 Motor cars with CO_2 emissions exceeding 160g/km

These are special rate pool assets. (Note if there is private use of the car the asset would be depooled).

Example 11

Kenny prepares accounts to 31 March. As at 1 April 2011 the WDV brought forward on the general pool was £22,000.
The following transactions occurred in the year ended 31 March 2012.

July 2011	Purchased machinery	£45,000
November 2011	Purchased a long life asset	£160,000
February 2012	Purchased a motor car CO_2 emissions of 145g/km	£8,000

Calculate Kenny's capital allowances for year ended 31 March 2012

5 The Small pools WDA

- Where the tax wdv of either the general pool or special rate pool prior to calculating the WDA is less than £1,000, the entire balance may be taken as a WDA in that period. The £1,000 is prorated if the accounting period is other than 12 months.

Example 12

Beth prepares accounts to 31 March. The WDV as at 1 April 2011 of her general pool is £750. She purchases machinery for £10,000 in the year.

Calculate her capital allowances for the year ended 31 March 2012

5.1 Layout

		General pool	*Special Rate Pool*	*Expensive car (1)*	*Short life asset (1)*	*(Business %) Private use Asset*	*Allowances*
	£	*£*	*£*	*£*	*£*	*£*	*£*
WDV b/f		X		X	X	X	
Additions qualifying for AIA							
- long life assets	X						
- integral features of a building	X						
- thermal insulation	X						
AIA (Note a)	(X)						X
Additions qualifying for AIA			X				
- machinery	X						
- plant	X						
AIA (Note a)	(X)						X
		X					
Other Additions							
Motor cars							
emissions 111-160g/km		X					
emissions >160 g/km			X				
Disposals		(X)			(X)		
		X	X	X	X	X	
WDA × 20%		(X)					X
WDA × 20%/10%						(X)	X
						× Business use	
WDA × 10%			(X)				X
WDA - restricted				(3,000)			3,000
Balancing allowance					(X)		X
Additions qualifying for FYA							
Motor car emissions ≤ 110g/km	X						
FYA @ 100%	(X)						X
							X
WDV c/fwd		X	X	X	–	X	

Notes

(a) The AIA is allocated to assets included in the special rate pool in priority to those included in the general pool,

(b) If the balance on the general pool +/or special rate pool is ≤ £1,000 for a 12 month accounting period, the small pool WDA could be claimed

Example 13 (Comprehensive)

Ling prepares accounts to 31 March. The WDV of the general pool at 1 April 2011 was £22,700, and on an expensive car £14,000. The car was used by Ling 20% for private use. The following transactions took place during the year ended 31 March 2012.

5 April 2011	Purchased a motor car (emissions 105g/km)	£17,000
10 April 2011	Purchased a computer	£6,000
25 June 2011	Purchased a machine	£84,700
7 September 2011	Purchased plant	£10,000
10 November 2011	Purchased a motor car (emissions 155g/km)	£11,200
30 December 2011	Purchased thermal insulation for the business building	£18,800
9 January 2012	Disposed of the expensive car	£8,000

Calculate the capital allowances for year ended 31 March 2012. No short life asset election has been made in respect to the computer.

Chapter 6

TRADING PROFIT – BASIS PERIODS

Questions 1, 4 or 5

1 Basis periods

Having adjusted the trading profit of the accounting period and computed and deducted the capital allowances for this period the profit must now be included in the Income Tax Computation for the relevant Tax Year of assessment.

Traders are assessed on their trading profit using a current year basis, this is the accounting period ending in the year of assessment. (i.e. the tax year)

If a trader makes accounts to 31 October each year, his 2011/12 assessment will be based on the trading profit for the accounting period ending 31 October 2011.

EXAMPLE 1

(a) Andrew has been trading for many years preparing accounts to 31 March

Which tax year will the trading profits for the year ended 31 March 2011 be assessed in?

(b) Eric has been trading for many years preparing accounts to 31 August.

Which tax year will the trading profits for the year ended 31 August 2011 be assessed in?

(c) Cathy has been trading for many years preparing accounts to 30 April.

Which tax year will the trading profits for the year ended 30 April 2011 be assessed in?

1.1 Opening year rules

(a) There are special rules for the first three tax years of trading as a CYB assessment will not be available from the first tax year:

(b) For a new business:

Tax year — Basis of assessment

Year 1 — Actual profits from commencement of trade to the following 5 April

Year 2 — Is there a set of Accounts which end in tax year 2?

- no: Assesses the actual profits in tax year 2 i.e 6 April to 5 April
- yes: How long is this set of Accounts?
  - < 12 months long: Assess profits for the first 12 months of trading
  - ≥ 12 months long: Assess profits for the 12 months to the set of Accounts ending in year 2

Year 3 — Assess profits for the 12 months to the set of Accounts ending in year 3

(c) Some profits may fall into more than one basis period in the opening years and are known as overlap profits. Where there has been an 'overlap', relief will be available on cessation, or sometimes, on change of accounting date. (See later notes)

Example 2

Andrew started to trade on 1 January 2010 and makes up his first accounts to 30 June 2010 and then 30 June annually thereafter. His trading profits are as follows:

6 months	to 30 June 2010	£30,000
Year	to 30 June 2011	£70,000
Year	to 30 June 2012	£82,000

What are the assessments for 2009/10 to 2012/13?

How much overlap relief is available?

Example 3

Chris started to trade on 1 May 2011 and makes up his first accounts to 31 October 2012 and then 31 October annually thereafter.

He made £36,000 trading profits in the 18 months to 31 October 2012 and £30,000 in the year ended 31 October 2013.

What are the assessments for 2011/12 to 2013/14?

How much overlap relief is available?

1.2 Closing year rules

The basis of assessment for the final tax year of a business is as follows:

(a) Closing year: the actual trading profits from the end of the basis period for the previous year of assessment until the date of cessation (anything not yet taxed). The previous tax year should be assessed on a CYB

(b) Any unrelieved overlap profits can be deducted in deriving the assessment for the final tax year.

Example 4

Boris, who has been trading for many years making up his accounts to 31 January, ceases to trade on 31 May 2012 with trading profits as follows:

	Trading Profit
	£
Year to 31 January 2012	47,000
4 months to 31 May 2012	8,000

The overlap profits from the opening years of his trade were £6,000.

What are the assessments for 2011/12 and 2012/13?

2 Change of accounting date

2.1 Conditions

(a) Provided certain conditions are met, an unincorporated business is allowed to change its accounting date. There may be tax advantages in doing so, or the change may be made for commercial reasons. For example, it may be easier to perform a stocktake at certain times of the year.

(b) Conditions to be met

A change in accounting date will only be valid if the following conditions are met

» The change of accounting date must be notified to the HMRC on or before 31 January following the tax year in which the change is to be made.

» The first accounts to the new accounting date must not exceed 18 months in length,

» If the period between the old accounting date and the proposed new accounting date is longer than 18 months, then two sets of accounts will have to be prepared.

» There must not have been another change of accounting date during the previous five tax years. (This condition may be ignored if the HMRC accept that the present change is made for genuine commercial reasons. Not surprisingly, obtaining a tax advantage is not accepted as a genuine commercial reason.)

(c) Failure to meet the conditions

If the conditions are not met, the old accounting date will continue to apply. If accounts are made up to the new accounting date, then the figures will have to be apportioned accordingly.

2.2 Procedure

Situations

A change of accounting date will always be achieved by having a period of account of less than or more than 12 months. This will result in any of four possible situations:

(1) A short period of account ending in a tax year
(2) A long period of account ending in a tax year
(3) Two periods of account ending in a tax year
(4) No period of account ending in a tax year

The absence of the normal CYB assessment is then dealt with as follows:

(1) A short period of account ending in tax year

- assess the 12 months to the new accounting date

This will create additional overlap profits that may be relieved at cessation of the business or possibly a further change of accounting date.

Example 5

Amy has been trading for several years. She has prepared accounts which showed trading profit figures as follows:

	Trading Profit
y/e 31 August 2010	£10,000
y/e 31 August 2011	£12,000
9 months to 31 May 2012	£11,000
y/e 31 May 2013	£16,000

What are her basis periods for 2010/11 to 2013/14?

(2) One long period of account ending in tax year - assess the long period to the new accounting date.

This will result in more than 12 months profit being assessed in a tax year so therefore the relevant number of months of overlap profit from the opening years will be deducted to bring it down to a 12 month assessment.

Example 6

Jane has been trading for several years. She has prepared accounts which showed trading profit figures as follows:

	Trading Profit
y/e 30 November 2010	£8,000
y/e 30 November 2011	£9,000
14 months to 31 January 2013	£15,000
y/e 31 January 2014	£12,000

Overlap profit was £8,000 representing 4m of profit.

What are her basis periods for 2010/11 to 2013/14?

(3) Two periods of account ending in tax year - assess both periods and being more than 12 months reduce assessment to 12 months by deducting relevant number of overlap months from opening years

Example 7

Emma has been trading for several years. She has prepared accounts which showed trading profit as follows:

	Trading Profit
y/e 30 April 2010	£15,000
y/e 30 April 2011	£18,000
9 months to 31 January 2012	£16,000
y/e 31 January 2013	£17,000
y/e 31 January 2014	£20,000

Overlap profit on commencement was £11,000 representing 11 months of overlap.

What are her basis periods for 2010/11 to 2013/14?

(4) No period of account ending in tax year - this will require two basis periods to be determined:

(i) for the tax year in which no period of account ends take the 12 months to the new chosen date one year before actually used - this will create overlap profits

(ii) for the following tax year in which the long period of account ends take the 12 months to the new accounting date

Example 8

Stella has been trading for several years. She has prepared accounts which showed trading profit figures as follows:

	Trading Profit
y/e 31 January 2011	£6,000
y/e 31 January 2012	£7,000
17 months to 30 June 2013	£11,000
y/e 30 June 2014	£8,000

What are her assessments for 2010/11 to 2014/15?

3 Basis periods for capital allowances

Capital allowances are calculated for a period of account. They are then treated as an expense, and deducted from profits. This adjusted profit figure is then what is used to determine assessment for relevant Tax Year.

3.1 Opening years

Capital allowances are deducted from profits before the opening year rules are applied. For an accounting period longer or shorter than 12 months the AIA and WDAs are scaled up or down as appropriate. The FYA at 100% on cars with emissions of ≤ 110g/km, is never time apportioned.

Example 9

Until 31 December 2011 Wendy was employed as a management consultant. Her gross salary for the period 6 April to 31 December 2011 totalled £36,090.

On 1 January 2012 Wendy commenced in self-employment running a music-recording studio. The following information relates to the period of self-employment from 1 January to 5 April 2012:

1 The Adjusted profit for the period 1 January to 5 April 2012 is £39,000. This figure is before taking account of capital allowances.
2 Wendy purchased the following assets:

		£
1 January 2012	Recording equipment	30,000
15 January 2012	Motor car (CO_2 emissions are 170 g/km) used by Wendy - 60% business use	14,800
20 February 2012	Motor car (CO_2 emissions are 140 g/km) used privately by employee - 20% private use)	10,400
4 March 2012	Computer	2,600

The computer purchased on 4 March 2012 for £2,600 is to be treated as a short-life asset.

Calculate Wendy's income tax liability for 2011/12.

3.2 Cessation of trade

(a) No allowances (WDA, AIA or FYA) are available in the final period of trading.

(b) If there are additions in the final period, these are added to the relevant pool, then disposal proceeds (limited to cost) are deducted to find a balance.

(c) If proceeds are less than this balance a balancing allowance is given, if greater, a balancing charge arises.

Chapter 7

TAX ADJUSTED TRADING LOSSES – INDIVIDUALS

Question 1, 4 or 5

1 Trading losses

1.1 Trading Profit assessment

(a) If the basis period has a trading loss, the trading profit assessment to include in the income tax computation is **nil**.

(b) The trading profit figure in an income tax computation can never be negative

1.2 Relieving the loss

The loss may be relieved according to the following rules. A repayment of income tax may result in some circumstances.

2 The reliefs available

The main reliefs available for a trading loss, are as follows:

(a) Carry forward against future trading profits

(b) Relief against total income of current and/or preceding tax year.

(c) Opening year loss relief against total income of preceding 3 tax years

(d) Terminal loss relief against previous 3 years trading profits

3 Carry forward of trading losses

(a) A trading loss may be carried forward and set against the first trading profits arising from the same trade.

(b) The trading loss must be set off if this option is chosen.

(c) Any loss remaining is carried forward until further profits arise.

(d) The loss may be carried forward indefinitely

Example 1

Albert has had the following recent trading results as adjusted for tax:

		£
Year to 31 December 2009	Loss	(5,000)
Year to 31 December 2010	Profit	3,000
Year to 31 December 2011	Profit	10,000

Assume that Albert wishes to carry forward the loss.

Calculate his assessable amounts for 2009/10 to 2011/12 inclusive.

4 Loss relief against total income

(a) A trading loss may be relieved against total income (after any qualifying loan interest payments) of the tax year of the loss and/or the previous tax year.

» the loss is calculated on an accounting period basis.

» a loss for the year ended 30 November 2011 maybe relieved against total income of 2011/12 and/or 2010/11

(b) If relief against total income is taken,

» the loss must be set off to the maximum possible extent

» personal allowances may be lost.

» a claim against total income may be made for either the tax year of the loss of the previous year or both. The two years are treated separately and thus a claim is required for each year.

Example 2

Charles has the following trading profit/ (loss) results:

	£
Year ended 31 December 2008	23,000
Year ended 31 December 2009	32,000
Year ended 31 December 2010	25,000
Year ended 31 December 2011	(84,000)

Charles also has property income in each year of £6,000.

Calculate Charles' taxable income, assuming that the trading loss is used in the most beneficial way and trading losses will continue for the next few years. Assume the personal allowance for 2011/12 applies in all tax years.

Example 3

David makes up accounts annually to 31 December. His recent trading results as adjusted for tax have been:

		£
Year ended 31 December 2010	Profit	40,000
Year ended 31 December 2011	Loss	(48,000)
Year ended 31 December 2012	Profit	60,000

For 2010/11 David has other income of £5,000 and pays qualifying interest of £2,800.
In 2011/12 the figures are £6,000 and £2,500 respectively.

Show how relief for the loss would be given, assuming that David makes all claims to the extent that they are beneficial. Assume the PA for 2011/12 applies in all tax years.

4.1 In the first tax year of the trade the assessable profit (or loss) is measured from the day trade commences to 5 April.

Unless the trader prepares accounts to 5 April, this requires the profit (or loss) to be apportioned.

- A loss may only be relieved once. If, in the opening years, a loss has been taken into account in one year, it is treated as nil when calculating the next assessment.

Example 4

Matthew starts trading on 1 August 2010. His trading results, as adjusted for tax purposes are:

		£
10 months to 31 May 2011	Loss	(20,000)
Year ended 31 May 2012	Profit	48,000

Calculate Matthew's trading profit assessable amounts for 2010/11 and 2011/12.

5 Relief of trading losses against capital gains

(a) This relief is an extension to current year and carryback against total income and may only be claimed after a claim has been made against the total income of the tax year in question.

(b) A trading loss may be relieved against capital gains, but only if any Net Income of the year in question has been reduced to zero by the trading loss under a normal claim, and an unrelieved loss remains.

(c) The remaining unrelieved trading loss may be set off as a deemed capital loss against the taxpayer's gains for the year; after setting off current year capital losses against current year capital gains. It takes precedence over both the annual exemption and any capital losses brought forward.

Example 5

For 2011/12 Kathy has a capital gain of £44,000. She has trading loss relief available of £24,000 after a claim against the total income of the tax year to offset against the gains.

Calculate Kathy's chargeable gain for 2011/12, assuming that Kathy makes the election.

6 Relief for trading losses incurred in the early years of the trade (Opening year loss relief)

(a) The relief is available for losses in the first four tax years of trade.

(b) Relief is available against total income of the three tax years preceding the tax year of the loss.

There is no need for the trade to have been carried on in these preceding tax years

(c) The relief operates automatically for all three years (FIFO)

(d) The loss available for this relief is computed in the same way as profits.

(e) In the early years of the trade it is possible to claim the following reliefs:

- » Opening year loss relief
- » Relief against total income of the current and previous tax year, including against gains
- » Carry forward against trading profit

Example 6

Fiona started trading on 1 July 2010. Her results, as adjusted for tax purposes, for the first two years are as follows:

		£
Year ended 30 June 2011	Loss	(12,000)
Year ended 30 June 2012	Profit	2,500

Fiona had previously been employed.

Her remuneration from this employment, which ceased on 30 September 2009, for recent years was:

	£
2009/10	5,868
2008/09	11,050
2007/08	12,800

Fiona has other income of £4,500 (gross) p.a.

Calculate the taxable income for all years after claiming relief under opening year loss relief.

Assume the allowances for 2011/12 apply throughout.

7 Terminal loss relief

(a) The terminal loss is set against trading profit for the tax year of cessation (if any) and then the previous three tax years (LIFO)

(b) The terminal loss is loss of the final 12 months of trading, calculated as follows:

(i) The actual trade loss for the tax year of cessation (from 6 April to the date of cessation) including any overlap relief.

(ii) The actual trade loss for the period 12 months before cessation until the end of the penultimate tax year

If the result in i) or ii) is a profit it is treated as zero for purposes of the terminal loss computation.

Example 7

David has the following trading results before ceasing to trade on 30 April 2011

		£
Year ended	31 July 2009	12,000
Year ended	31 July 2010	10,000
9 months	30 April 2011	(20,000)

Show the loss available for relief under terminal loss relief, assuming overlap profits on commencement were £500

8 Business transferred to a company

(a) Relief is available for trading losses when a business is sold to a company controlled by the former owner of the business ie the incorporation of an unincorporated trade.

(b) The trading losses are carried forward by the individual and set against the first available income derived from the company eg salary, dividends or interest.

(c) Losses are set off firstly against earned income and then unearned income

(d) Conditions

(i) At least 80% of the consideration for the business given by the company must be in the form of shares

(ii) The owner must continue to own the shares in the year that he relieves the loss.

Chapter 8

PARTNERSHIPS

Examined in question 1, 4 or 5

1 Introduction

A partnership is a single trading entity. Each individual partner is effectively treated as trading in his own right and is assessed on his/her share of the adjusted trading profit of the partnership.

2 Trading income

(a) The partnership's tax adjusted profits or loss for an accounting period is computed in the same way as for a sole trader

(b) Partners' salaries and interest on capital are not deductible: these are an allocation of profit.

3 Allocation of the trading profit or trading loss

(a) The trading income or trading loss is divided between the partners according to their profit sharing arrangements for the accounting period.

(b) Partners may be entitled to salaries and interest on capital. The balance will be allocated in the profit sharing ratio.

4 A change in the profit sharing agreement

If the profit sharing agreement is changed during a period of account, the profit must be time apportioned before allocation.

Example 1

Doug and Rob are in partnership. The trading income for the year ended 30 September 2011 was £18,000

Up to 30 June 2011 profits were shared between Doug and Rob 3:2, after paying salaries of £3,000 and £2,000 per annum.

From 1 July 2011 profits were shared 2:1 after paying salaries of £6,000 and £4,000 per annum.

Show the allocation of trading profits for the Accounting Period ended 30 September 2011.

5 Partnership capital allowances

(a) Capital allowances are deducted as an expense in calculating trading profit.

(b) If assets are used privately, the business proportion is included in the partnership's capital allowances computation.

6 Commencement and cessation

(a) The rules for commencement and cessation are the same as for a sole trader.

(b) The profit is allocated between the partners for accounting periods and then the assessment rules are applied.

(c) Each partner is effectively taxed as a sole trader

(d) When a partner joins a partnership, he is treated as commencing

(e) When a partner leaves a partnership he is treated as ceasing

(f) Each partner has his own overlap profit available for relief.

7 A change in the membership of a partnership

(a) As long as there is at least one partner common to the business before and after the change, the partnership continues.

(b) The commencement or cessation rules apply to the individual joining or leaving the partnership.

Example 2

Ann and Beryl have been in partnership since 1 July 2009 making up their accounts to 30 June each year. On 1 July 2011 Clair joins the partnership.
The partnership's trading profit is as follows:

	£
Year ended 30 June 2010	12,000
Year ended 30 June 2011	14,000
Year ended 30 June 2012	24,000

Profits are shared equally.

Show the amounts assessed on the individual partners for 2009/10 to 2012/13

8 Partnership losses

(a) Losses are allocated between partners in the same way as profits.

(b) Loss relief claims available are the same as for sole traders.

(c) A partner joining the partnership may claim under opening year loss relief, for losses in the first four years of his membership of the partnership.

This relief is not available to existing partners.

(d) A partner leaving a partnership may claim under terminal loss relief.

This relief is not available to partners remaining in the partnership.

Example 3

John, James and Paul are in partnership making up their accounts to 5 April. During 2011/12 Paul left the partnership and George joined in his place.

For the year ended 5 April 2012 the partnership made a trading loss of £40,000.

State the loss relief claims that will be available to the partners.

9 Limited liability partnerships

(a) The amount that each partner is required to contribute towards partnership losses, debts and liabilities is limited by an agreement.

(b) The partnership is taxed in the same way as other partnerships.

(c) Normal loss reliefs are available.

(d) The amount of a loss that may be set against income not arising from the partnership is limited to the amount of capital that the partner has contributed to the partnership.

Chapter 9

EMPLOYMENT INCOME

Examined in question 1, 4 or 5

1 The scope of employment income

An employee is taxable under Employment Income

A self employed person is taxable under trading income

2 Employment or self-employment?

2.1 The following principles should be taken into account in deciding if a person is employed or self employed.

The main test of an employment as opposed to self-employment is the existence of a contract of service **(employee)** compared with a contract for services (**self employed**).

2.2 If there is no contract of service, the following suggest employment.

- An obligation by the employer to offer work and an obligation by the employee to undertake the work offered. An employee would not normally be in a position to decline work when offered.
- The employer controls the manner and method of the work.
- The employee is entitled to benefits normally provided to employees such as sick pay and holiday pay.
- The employee is committed to work a specified number of hours at certain fixed times, and is paid by the hour, week or month.
- The engagement is for a long period of time.
- The employee does not provide his own equipment.
- The employee is obliged to work personally and exclusively for the employer, and cannot hire his own helpers.
- The work performed by the employee is an integral part of the business of the employer and not merely an accessory to it.
- The economic reality of self-employment is missing - namely the financial risk arising from not being paid an agreed, regular, remuneration.
- The employee cannot profit from sound management.

3 Assessable emoluments

3.1 Individuals are assessed on the amount of emoluments received in the tax year.

3.2 **Emoluments includes:**

(a) wages
(b) salary
(c) bonus
(d) commission
(e) benefits

4 Deductibility of expenses from employment income

4.1 The following expenditure is deductible:

- Contributions to approved occupational pension schemes (within certain limits see chapter 10)
- Fees and subscriptions to professional bodies
- Payments to charity made under a payroll deduction scheme
- Travel expenses incurred necessarily in the performance of the duties of employment
- Expenses incurred wholly, exclusively and necessarily in the performance of the duties of employment
- Capital allowances are available for plant and machinery provided by an employee for use in his duties

5 Approved mileage allowances

(a) For 2011/12 the approved mileage allowance is 45p per mile for the first 10,000 business miles, and then 25p per mile thereafter.

(b) Employees who use their **own motor car** for business mileage must use the approved mileage allowances in order to calculate any taxable benefit arising from mileage allowances received from their employer.

(c) Employees who use their motor cars for business mileage without being reimbursed by their employer (or where the reimbursement is less than the approved mileage allowances), can use the approved mileage allowances as a basis for an allowable deduction.

Example 1

Kerry uses her own 1800cc motor car for business travel. During 2011/12 she drove 12,000 miles in the performance of her duties. Her employer pays her 30p per mile.

Compute the allowable deduction that the Kerry can claim against her employment income.

6 Exempt benefits

(a) Canteen available to all staff.

(b) Luncheon vouchers up to 15p per day.

(c) Qualifying removal expenses up to £8,000.

(d) Car parking spaces near place of work.

(e) Workplace nurseries (crèches).

(f) Childcare voucher up to £55 per week for basic rate taxpayers, £28 per week for higher rate and £22 per week for additional rate taxpayers. and any related administration costs

(g) Contributions by an employer to an approved pension scheme.

(h) Workplace parking for bicycles plus a tax free cycling allowance of 20p per business mile.

(i) Provision of a mobile telephone for private use (one per employee)

(j) Christmas parties etc for staff (up to £150 per person per year)

(k) Sport and recreational facilities available generally for the staff.

(l) Outplacement counselling services to employees made redundant. The services can include counselling to help adjust to the loss of the job and to help in finding other work, ie retraining courses up to 2 years

(m) Contributions towards additional household costs (such as light and heat) incurred by an employee who works at home up to £156 per tax year or if higher evidence must be provided by the employee to justify the expense.

(n) Long service awards up to £50 per each year of service (maximum 20 years)

(o) Use of Employer bicycles if used by employees to and from work.

(p) Provision of eye care tests and/or corrective glasses for employees using VDU's (if paid directly, by reimbursement to the employee or by providing vouchers)

(q) Incidental overnight expenses provide by the employer for overnight stays from home. Up to £5 per night (UK) and up to £10 per night (overseas)

7 Taxable benefits

7.1 Benefits assessable on all employees

(a) Vouchers exchangeable for goods and services unless specifically exempt.

(b) Living accommodation

(i) There is no taxable benefit if the accommodation is job-related
- where it is necessary for the proper performance of the employee's duties (e.g. a caretaker); or
- for better performance of the employee's duties and (for that type of employment) it is customary for employers to provide living accommodation (e.g. hotel-worker); or
- where there is a special threat to the employee's security and he resides in the accommodation as part of special security arrangements.

(ii) If the accommodation is not job related then the benefit is the higher of
- the accommodation's annual value, and
- the rent actually paid for it by the employer (if the property is rented)
- The benefit is reduced by any rent or contribution paid by the employee

(iii) There is an additional benefit where the cost of providing the accommodation is greater than £75,000;
- (cost of providing accommodation – £75,000) × the official rate of interest)
- The cost of providing the accommodation is the purchase price of the property plus expenditure on improvements incurred before the start of the tax year.

(iv) If the employer bought the accommodation more than six years before first providing it to the employee, the property's market value when first occupied by the employee is used in the calculation instead of purchase price.

Example 2

Jones, a sales manager, occupies a flat owned by his employer. Its annual value is £4,000 and Jones pays his employer £500 p.a. for use of the flat. The flat was purchased in 2007 for £120,000.

Calculate the total benefit assessable on Jones for 2011/12 assuming an official rate of interest of 4.00%

7.2 Benefits assessable on employees earning £8,500 or more and directors

(a) Principles

The amount assessed is generally the cost of providing the benefit.

Where in-house benefits are provided (free air travel for employees of a airline company) the amount assessed is the marginal cost incurred by the employer

(b) Expenses connected with living accommodation

(i) Expenses such as lighting and heating are taxable on the employee if they are paid by the employer.

(ii) When the accommodation is job related, the taxable limit is 10% of other employment income. In addition the payment of council tax by the employer is an exempt benefit if the accommodation is job related.

(c) Use of assets

Amount assessed is the higher of

» 20% × market value of the asset when first provided

» rental paid by employer (if asset is rented)

(d) Gifts of assets

(i) If an employee is gifted a new asset, he is taxed on the cost of the asset.

(ii) If an employee is gifted an asset that has previously been used he is taxed on the higher of:

» the market value of the asset when given to him

» the market value of the asset when first made available to the employee less the benefit assessed on the employee during the time he had the use of it.

(iii) The above rule does not apply to the gift of a motor car or van, where the benefit is simply the market value of the asset when gifted.

Example 3

Gerald's employer purchased a dishwasher for Geralds' use on 1 June 2010, costing £900. On 6 April 2011 Gerald was given the dishwasher by his employer (its market value then being £150).

Calculate the benefit assessable on Gerald on the basis of:

(a) if Gerald made no payment for the dishwasher

(b) if Gerald paid his employer £150 for the dishwasher

(e) **Motor cars**

(i) If there is no private use of the car there is no taxable benefit

(ii) The benefit is a percentage of the car's list price

» the list price includes the list price of any accessories fitted to the motor car.

» the list price is reduced by any capital contribution from the employee subject to a maximum of £5,000.

(iii) Percentage

CO_2 emissions	*Percentage*	
	Petrol	*Diesel*
≤ 75 g/km	5%	8%
76 - 120 g/km	10%	13%
120 - 125 g/km	15%	18%
> 125 g/km	Add an additional 1% for every complete 5g/km above 125 g/km	
Maximum percentage	35%	35%

(iv) Reductions
The car benefit is proportionately reduced if

» a motor car is unavailable for periods of at least 30 days of the tax year, and

» where the employee makes a contribution to the employer for the use of the motor car.

(v) Second motor cars
Where more than one motor car is made available to an employee, the benefit of each motor car is simply based on its list price and CO_2 emissions.

(vi) Pool cars
The use of a pool car does not result in a company car benefit.

Example 4

During 2011/12 Fabulous plc provided the following employees with company motor cars:

Agnes was provided with a new diesel powered company car on 6 August 2011. The motor car has a list price of £13,500 and an official CO_2 emission rate of 122 grams per kilometre.

Billy was provided with a new petrol powered company car throughout 2011/12. The motor car has a list price of £16,400 and an official CO_2 emission rate of 187 grams per kilometre.

Carla was provided with a new petrol powered company car throughout 2011/12. The motor car has a list price of £22,600 and an official CO_2 emission rate of 249 grams per kilometre. Carla paid Fabulous plc £1,200 during 2011/12 for the use of the motor car.

Dennis was provided with a new petrol powered company car throughout 2011/12. The motor car had a list price of £16,000 and an efficient CO_2 emission rate of 110 grams per kilometre.

Eileen was provided with a new diesel car throughout 2011/12. The motor car had a list price of £11,000 and an official CO_2 emission rate of 60 grams per kilomtre.

Calculate the taxable benefit for 2011/12 for Agnes, Billy, Carla, Dennis and Eileen.

(f) Fuel provided for private use

(i) The car benefit does not take account of fuel provided for private use.

(ii) The amount of fuel benefit is equal to £18,800 multiplied by the percentage used for calculating the car benefit. The fuel scale charge is reduced proportionately where private use fuel is withdrawn (and not reintroduced during the year) or the car is only given part way through the tax year.

(iii) No reduction is made if the employee contributes towards the cost of petrol for private use. If he pays for all fuel used for private motoring the charge is cancelled.

Example 5

Using example 4 – calculate the fuel benefit for Agnes, Billy, Carla, Dennis and Eileen assuming also that Carla pays Fabulous plc £600 during 2011/12 towards the cost of private fuel, although the actual cost of this fuel was £1,000.

(g) **Vans and heavier commercial vehicles**

(i) Where an employee uses an employers van for journeys between home and work and other private use is insignificant there is no benefit.

(ii) Where private use is not insignificant the tax charge is £3,000 p.a.

(iii) An additional charge is made for fuel provided for unrestricted private use equal to £550p.a.

(iv) Both benefits are time apportioned if the van is unavailable to the employee for 30 days or more during any part of the tax year.

(h) **Beneficial loans**

(i) A beneficial loan is one made to an employee below the official rate of interest (assumed to be 4.00% for 2011/12)

(ii) The benefit is the interest on the loan at the official rate, less any interest actually paid by the employee.

(iii) There is no benefit if the loans do not exceed £5,000 in total at any time in the tax year

(iv) The benefit is calculated using the ***average method*** or the ***accurate method***

Average method.

This uses the loan outstanding at the beginning and the end of the tax year.

If the loan is taken out or paid back during the tax year, that date is used instead of the beginning or end the tax year.

Accurate method

This calculates benefit day by day on the balance actually outstanding.

Either the taxpayer or HMRC can decide to use the accurate method.

Example 6

Jack was given a loan of £35,000 by his employer on 31 March 2011. Interest is payable on the loan at 3% p.a. On 1 June 2011 Jack repaid £5,000 and on 1 December 2011 further £15,000. The remaining £15,000 was still outstanding on 5 April 2012. Jack earns £30,000 p.a.

Calculate the taxable benefit for 2011/12 under

(a) the averaging method and

(b) the accurate method

You should assume that the official rate of interest is 4% p.a.

8 PAYE system

8.1 Pay As You Earn

The purpose of the PAYE system is to deduct the correct amount of income tax and National Insurance Contributions over the year.

8.2 Employers' duties

The employer has a duty to:

(a) deduct income tax from the pay of his employees

(b) calculate the amount of NIC that should be deducted

(c) keep a record of each employee's pay and deductions

(d) pay the tax/NIC over on the due date – by the 19th of the month. But employers whose payments are, (on average), less than £1,500 per month are allowed to make payments quarterly rather than monthly. Note that employers with 250 or more employees must make their monthly PAYE payments electronically on the 22nd of the month.

(e) send the appropriate returns to the HMRC when required.

8.3 Application of PAYE

The following count as pay:

(a) salaries, wages, overtime, bonuses

(b) pensions

8.4 PAYE codes

(a) An employee's PAYE code indicates the amount of tax free pay he is entitled to.

(b) The PAYE code will include the employee's personal allowance and any allowable deductions and be restricted by various taxable amounts.

It is calculated as follows:

	£	£
Allowances:		
Personal allowances	X	
Personal pension contributions - higher rate relief	X	
Expense deductions	X	
		X
Less Deductions,		
Benefits	X	
Untaxed income	X	
Tax under payments b/f (grossed up) $\times \frac{100}{20} \times \frac{100}{40} \times \frac{100}{50}$	X	
		(X)
Allowance to set against pay		X

(c) To obtain the code number the last figure is removed and replaced with a letter

L - code for PA
K - increases taxable pay instead of reducing it (benefits exceed allowances) with no tax free allowances
BR - tax will be deducted at the basic rate
NT - no tax is to be deducted

Example 7

Annabel earns £20,000 and is single, She has benefits of £480 and her unpaid employment income tax for 2010/11 was £132.
Annabel pays income tax at the marginal rate of 20%

Calculate Annabel's tax code for 2011/12.

8.5 Changes to coding

An employer must use the last code notified to him for existing employees until new written instructions are sent from HMRC.

8.6 Year end returns

The employer must send to HMRC the following:

By 19 May:

» PI 4 End of year return for each employee (includes form P60)

» P35 Summary of tax and NIC deducted

By 6 July:

» P11D Benefits for directors and employees earning in excess of £8,500 for the year

» P9D Benefits of other employees.

The employer must give to the employee

By 31 May:

» P60 Permanent record of pay and tax deducted as well as NIC's made in the tax year.

By 6 July:

» P11D Benefits for directors and employees earning in excess of £8,500 for the year

» P9D Benefits of other employees.

8.7 Employees leaving or joining

(a) Employees leaving

The employer should complete form P45 and send part 1 to Tax Office and give parts 2, 3 and 4 to the employee.

(b) Employees joining

(i) When an employee joins and has a P45 the employer can operate PAYE

(ii) The employer uses the tax code on the P45 if it relates to the current year; otherwise he uses the emergency code.

(iii) If the employee does not have a P45, the new employee must complete form P46.

Chapter 10

PENSION SCHEMES

Questions 1, 4 or 5

1 Types of Pension Scheme

Employees may join an occupational scheme set up by their employers and/or a personal pension scheme arranged by the individual directly with a pension provider. Self employed individuals may simply join a personal pension scheme. To encourage individuals to join a pension scheme generous tax reliefs have been provided by HMRC.

Occupational schemes will always have contributions made into them by employers and may also have contributions made by the employee. There are no limits on the amount of contribution that may be made by the employer but they will count towards the employee's annual allowance and the value of the fund for the lifetime allowance (see later notes). These contributions will be tax deductible for the employer attracting tax relief in the accounting period in which they are paid.

Contributions made by the employer are exempt benefits for the employee and are not subject to any NIC payments (see chapter 11).

Contributions made each tax year by an individual into a pension scheme that will attract tax relief are limited to the higher of:

- the relevant earnings of the taxpayer, being mainly employment income and/or trading profits plus any profits from furnished holiday lettings, and
- £3,600 of gross contribution

This amount will also contribute towards the annual allowance permitted each year.

When an employee makes a contribution into an occupational scheme tax relief is given at source under the "net pay arrangement". The employer will deduct the gross contribution from the individual's employment income before computing the tax to be deducted under PAYE.

Illustration 1

If an employee has a gross annual salary of £25,000 and wants to contribute £1,000 into his pension scheme, the employer over the tax year will pay £1,000 into the pension scheme and put a salary of £24,000 through PAYE.

This would be presented on the Income Tax Computation as a salary of £25,000 less a pension contribution of £1,000.

When an individual contributes into a personal pension scheme no such deductions are made from income on the computation, instead tax relief is given as follows:

- basic rate tax relief is given at source – this means that if the taxpayer pays £800 into his pension fund, this is deemed to be net of basic rate tax at 20%. HMRC will then pay the pension provider an amount equivalent to the basic rate deduction (20/80 x £800 = £200). Thus the individual's pension fund is increased by £1,000 in total.
- Higher rate and additional rate taxpayers achieve higher and additional rate relief by extending the basic and higher rate bands by the gross amount of the personal pension contribution. Hence in this example the higher rate and additional rate tax bands will increase by £1,000 so that higher and additional rate tax will only arise above taxable income figures of £36,000 and £151,000 respectively.

2 Annual Allowance (AA)

From 6 April, 2011 the AA determining the total pension input allowed each year is limited to £50,000. If the AA for a year is not fully utilised and the taxpayer was a member of a pension scheme in that year it is now possible to carry forward any unused amount for 3 years. Although these rules only apply from 2011/12 onwards a notional £50,000 AA is used for the preceding 3 tax years.

If the AA is exceeded for a year, from 2011/12 there will be an AA charge (see note below)

Example 1

Aston made the following gross amount of contributions into his pension scheme:

08/09	£62,000
09/10	£30,000
10/11	£25,000

Aston has an annual salary of £120,000.

Compute the total pension input allowed for Aston for the 2011/12 tax year.

3 Annual Allowance Charge

If the total pension input for the year exceeds the maximum gross contribution, the excess is subject to an AA Charge by treating it as additional non-savings income of the year.

Illustration 2

Villa has a trading profit assessment for the 2011/12 tax year of £250,000 and made his first contribution into a personal pension scheme during this year of £80,000 (gross).

Compute the annual allowance charge that will arise in 2011/12 and prepare an Income tax computation for Villa showing his Income Tax liability for the tax year

Villa has relevant earnings of £250,000 so the gross contribution of £80,000 will all attract tax relief. However as Villa was not previously a member of a pension scheme he will have no unused AA brought forward and therefore an AA charge of £30,000 will arise (80,000 – 50,000).

His higher and additional rate bands will be increased by the gross contribution of £80,000 to £115,000 and £230,000 respectively. As personal pension scheme contributions are made net of basic rate tax relief, Villa will actually have made a payment of £64,000 (80,000 x 80%) into the pension scheme.

Villa's Income Tax computation for 2011/12 will therefore be as follows:

			£	
Trading Profit			250,000	
AA Charge			30,000	
Net Income			280,000	
Less: PA (note 1)			(NIL)	
Taxable Income			280,000	
Basic rate	115,000 @ 20%	=	23,000	
Higher rate	115,000 @40%	=	46,000	
Additional rate	50,000 @50%	=	25,000	
Income Tax Liability				94,000

Note 1 Villa's Adjusted Net Income for purposes of computing his personal allowance is £200,000 (280,000 – 80,000). As this exceeds £114,950 his personal allowance will be reduced to zero.

4 Lifetime Allowance

In addition to the AA limiting the tax relief available on yearly contributions a Lifetime Allowance of £1.8M applies to the value of the pension fund built up at the date the taxpayer takes their pension. If the fund value exceeds this limit an Income Tax charge will arise on the excess dependent upon how the excess is used. This may be in the form of either a higher annuity or lump sum. These calculations however are not within the syllabus!

Chapter 11

NATIONAL INSURANCE CONTRIBUTIONS (NIC)

National insurance contributions may be examined for a few marks in questions 1, 2 4 and 5

1 Employed earners

1.1 Class 1 contributions

(a) Class 1 NIC is paid by employees and employers

(b) Employees

The contributions begin when the employee is aged 16 or over. For 2011/12 the rate of employee Class 1 NIC is at 12%. It is paid where **cash** earnings exceed a threshold of £7,225 per annum, but only up to an upper limit of £42,475 per annum, however for earnings above £42,475 per annum there is a rate of 2% payable with no limit. The contributions cease when the employee reaches 60 (women) and 65 (men).

(c) Employers

The rate of employer Class 1 NIC is 13.8%. It is paid on **cash** earnings that exceed a threshold of £7,072 per annum. These are payable from the employees 16th birthday - but there is no upper age limit.

1.2 Class 1A Contributions

The rate of Class 1A NIC is payable by employers on taxable benefits provided to employees. The rate is 13.8% multiplied by the value of the benefits.

Example 1

Riga Ltd has one employee who is paid £50,000 per annum, and was provided with the following taxable benefits during 2011/12:

	£
Company motor car	6,400
Fuel	4,320
Living accommodation	1,800

Calculate the Class 1 and Class 1A NIC liability.

2 Self-employed earners

2.1 Class 2 contribution

(a) Self-employed earners pay a flat rate contribution of £2.50 per week from their 16th birthday until they reach 60 (women) or 65 (men).

2.2 Class 4 contribution

(a) The self employed also pay Class 4 contributions which are based on trading profit.

(b) The rate of Class 4 is 9% and is payable on trading income between £7,226 and £42,475.

(c) For trading income in excess of £42,475, a rate of 2% is payable

(d) Contributions begin if the employee is 16 at the start of the relevant tax year but contributions cease, when the tax payer is older than 60 (women) or 65 (men) at the start of the relevant tax year

Example 2

Jerome, a trader, has trading profit of £50,000 for 2011/12.

Calculate his Class 4 NIC and Class 2 NIC for 2011/12

Chapter 12

CORPORATION TAX

Question 2, 4 or 5

1 Introduction

1.1 Scope of corporation tax

Companies resident in the UK are chargeable to corporation tax on worldwide income and gains.

A company is UK resident if it is either,

(1) Incorporated in UK eg A Ltd or V plc, or
(2) Centrally managed and controlled from UK eg A Inc., which is incorporated overseas, but the majority of its directors are resident in UK and board meetings are held in UK.

1.2 Definitions

- A **period of account** is the period for which a company prepares its accounts. Usually a company will prepare accounts for a period of 12 months, but a period of account may be for a shorter or longer period than this. This may occur when a company either commences or ceases trading, or whenever it changes its accounting date.
- Corporation tax is charged in respect of **chargeable accounting periods**. Normally a company's chargeable accounting period (CAP) will be the same as its period of account but it cannot exceed 12 months. This is the period for which the Corporation Tax computation is prepared.
- The tax rates to be used however, are set for **Financial Years**. (FY)

  FY 2011 = 1 April 2011 to 31 March 2012.

1.3 Accounting periods

- A CAP will normally start immediately after the end of the preceding CAP.
- A CAP will also start when a company commences to trade, or when its profits otherwise become liable to corporation tax.
- A CAP will normally finish twelve months after the beginning of the period or at the end of a company's period of account.
- A CAP will also finish when a company ceases to trade, or when its profits otherwise cease being liable to corporation tax.

2 Taxable Total Profits

A company's corporation tax liability for an accounting period is calculated by computing profits (income + gains) from all sources and deducting gift aid payments. This figure is known as Taxable Total Profits and is then charged to tax at the relevant rate(s) of corporation tax for the company.

Pro forma corporation tax computation

Corporation Tax Computation for the year ended 31 March 2012

	£	£
Trading income		
Adjusted profit	X	
Less: Capital allowances	(X)	
Tax Adjusted Trading Profit		X
Other income & gains		
Interest receivable		X
Property Income		X
Net chargeable gains		X
Total Profits		X
Less: Donations to charity (corporate gift aid)		(X)
Taxable Total Profits		X

2.1 Notes

(a) Dividends received from other UK and overseas companies are not taxable, dividends paid are not deductible.

(b) Companies pay corporation tax (not capital gains tax) on chargeable gains.

(c) Overseas income will be included according to its type as adjusted trading profit for the profits of an overseas branch or as, overseas property income or overseas interest. The figure to include in the corporation tax computation is gross of any overseas taxes suffered. See Chapter 20 for details.

3 Royalties payable

Relief for royalties payable is given in line with the accounting treatment, and therefore royalties payable are allowed as a deduction when calculating the adjusted trading profit. No adjustment is therefore required.

4 Royalties receivable

The taxation of royalties receivable will follow the accounting treatment on an accruals basis. Royalties receivable will therefore be included in the adjusted trading profit, with no adjustment being required.

5 Tax Adjusted Trading Profit

5.1 This calculation is similar to unincorporated business:

Adjusted profit	X
less Capital Allowances	(X)
Tax adjusted trading profit	X

5.2 Adjusted profit

The rules discussed in chapter 4 for unincorporated business are similar for incorporated businesses but with some notable exceptions:

(a) No private element of expenses added back

(b) Drawings (cash or goods) is not relevant for companies. Any distributions are out of post tax profit

(c) Family salaries are not relevant for companies

(d) Legal fees regarding the issue of share capital are an expense only for companies and as they are of a capital nature, the expense is disallowed and added back in the adjustment of trading profit

(e) Legal fees with regard to registering patents and trademarks are allowable by statute

(f) Interest payable on a non-trading loans are added back, but the expense is deductible instead against interest income

(g) Interest payable to HMRC is treated as non-trading so is also tax relievable against interest income (interest receivable from HMRC is taxable as interest income)

5.3 Capital allowances

As per unincorporated business, (see chapter 5) but, there is no private use asset column and note only one AIA is allowable to a group of companies.

5.4 Basis periods

The rules are not relevant for companies. Tax adjusted trading profit is calculated for a CAP and included with other income and gains to arrive at Taxable Total Profits. The tax is then calculated for the CAP.

6 Property Income

6.1 As per individuals (see chapter 3) with some notable exceptions

(a) The property income is calculated on an accruals basis for the CAP

(b) Interest payable on a loan to buy a rental property is deductible against interest income not property income

(c) There is no rent a room relief for companies

(d) If a company makes a property loss on its properties

it must be offset against total profits before gift aid of the current period and any excess is carried forward against total profits before gift aid of future periods.

7 Interest income

(a) All interest receivable is assessed as interest income on an accruals basis

(b) Companies receive all interest GROSS

(c) Interest payable is deductible against tax adjusted trading profit if loan used for trading purposes eg to acquire property or plant & machinery to use in the trade, or to increase working capital. If the loan is used for non trading purposes then it is deductible against interest income. It is relievable on an accruals basis. The main examples of non trading loans are those taken out to acquire a rental / investment property, as stated above, or to acquire shares

8 Gift Aid

For companies to ensure tax relief is achieved on their charitable donations they should make such payments under the corporate gift aid system. The payment is GROSS and deductible on a paid basis. Thus in the adjustment of trading profit any gift aid payments should be added back and instead included as a separate gift aid deduction on the Corporation Tax computation

9 Dividends

Dividends received from **UK and overseas companies** are never included as part of Taxable Total Profits.

Example 1

Westmorland Ltd has the following income and outgoings for the year ending 31 March 2012.

	£
Tax-adjusted trading profit	1,456,500
Property Income	25,000
Interest receivable	10,000
Chargeable gains	37,500
Capital losses	(2,500)
Dividends from UK companies	14,400
Gift Aid donation	(10,000)

Compute the Taxable Total Profits for the year ending 31 March 2012.

Chapter 13

CALCULATION OF CORPORATION TAX LIABILITY

Question 2, 4 or 5

1 Calculation

1.1 Corporation tax payable

(a) Corporation tax payable is calculated as:
Taxable Total Profits × corporation tax rate for the financial year(s)

(b) The rate of corporation tax depends on the level of Augmented profits
Augmented profits = Taxable Total Profits + Franked Investment Income (FII)

(c) Franked investment income is dividends received from UK and overseas companies plus the associated 10% tax credit
UK and overseas dividends received × 100/90 (from non associated (non subsidiary) companies)

1.2 Corporation tax rates

The corporation tax rates for the Financial Year (FY) 2010 are as follows:

Small profits rate	21%
Main rate	28%

For FY 2011

Small profits rate	20%
Main rate	26%

1.3 Main Rate

If Augmented profits are equal to or above the upper limit of £1,500,000, then Taxable Total Profits are taxed at the main rate.

Small profits rate

If Augmented profits are equal to or below the lower limit of £300,000, then Taxable Total Profits are taxed at the small profits rate.

If Augmented profits fall between £300,000 and £1,500,000 the company is marginal and is taxed as follows:

Taxable Total Profits × Main Rate	=	x
Less Marginal Relief	=	(x)
		x

See note 1.4 below for detail

1.4 Changes in the rates

(a) When a company's accounting period falls into two financial years in which the rates have changed, the tax must be calculated for each financial year separately.

(b) The rates and marginal relief fractions for FY 2009, FY 2010 and FY 2011 are as follows:

Financial year	*2009*	*2010*	*2011*
Small profits rate	21%	21%	20%
Main rate	28%	28%	26%
Lower limit	300,000	300,000	300,000
Upper limit	1,500,000	1,500,000	1,500,000
Marginal relief fraction	7/400	7/400	3/200

(c) If a company's accounting period falls into FY 2010 and FY 2011, then as the rates have changed there is a need to apportion the results in to respective financial years - this is only necessary if the tax rates change from one financial year to another.

Example 1

A Ltd had the following results for the year ended 31 March 2012

	£
Taxable Total Profits	1,800,000
Dividend from UK company (amount received)	9,000

Calculate the corporation tax payable for the year ended 31 March 2012 and then show a revised computation of corporation tax payable if the accounting year had ended 31 December 2011.

Example 2

A Ltd had the following results for the year ended 31 March 2012

	£
Taxable Total Profits	60,000
Dividend from an overseas company (amount received)	1,800

Calculate the corporation tax payable for the year ended 31 March 2012 and then show a revised computation of corporation tax payable if the accounting year had ended 31 December 2011.

1.5 Marginal companies

(a) If the company's Augmented profits lie between the lower and upper limits for the financial year then marginal relief applies.

(b) Corporation tax payable is calculated as follows:

Taxable Total Profits × Main rate	X
Less: FRACTION × (UPPER LIMIT – AUGMENTED PROFITS) × $\frac{\text{TAXABLE TOTAL PROFITS}}{\text{AUGMENTED PROFITS}}$	(X)
Corporation Tax Payable	X

(c) The fraction for FY 2010 is 7/400 and for FY 2011 is 3/200

(d) The upper limit will be £1,500,000 (scaled down if there are associated companies and/or if accounting period is less than 12 months). The marginal relief fractions and lower and upper limits are given on the tax rates and allowances page within the exam paper.

Example 3

A Ltd had the following results for the year ended 31 March 2012

	£
Taxable Total Profits	430,000
Dividend from UK company (amount received)	18,000

Calculate the corporation tax payable for the year ended 31 March 2012 and then show a revised computation of corporation tax payable if the accounting year had ended 31 December 2011.

1.6 Short chargeable accounting periods

(a) the upper and lower limits are limits for a 12 month period.

(b) if the accounting period is less than 12 months then the limits need restricting

Example 4

A Ltd had the following results for the 4 months ended 31 March 2012:

	£
Taxable Total Profits	300,000
Dividend from an overseas company (amount received)	9,000

Calculate the corporation tax payable for the 4 months ended 31 March 2012

1.7 **Associated companies**

(a) The Upper and Lower limits are restricted when there are associated companies. [> 50% held UK and overseas subsidiaries]

(b) Associated companies are dealt with in chapter 19.

Chapter 14

LONG PERIOD OF ACCOUNT

Question 2, 4 or 5

1 Apportioning income and expenditure

(a) No period of account exceeding 12 months can be charged to corporation tax.

(b) If a company has a period of account longer than 12 months it must be split into two Chargeable Accounting Periods (CAP)

» the first 12 months

» the remaining months

(c) The income and expenditure is divided between the CAP's as follows:

Adjusted profit	Time apportioned	
Property Income	Accruals basis	
Interest receivable	Accruals basis	
Gift aid payments Chargeable gains	Date of receipt/payment	
Capital allowances	Two calculations	(WDA and AIA will be restricted in the second short period, but note that FYAs on motor cars with emissions ≤ 110 g/km are never restricted for short accounting periods)

Example 1

A plc prepared accounts for a 16 month period to 31 March 2012. The results for the period are as follows:

	£
Adjusted profit	4,800,000
Chargeable gain (sale of asset on 6 January 2012)	80,000
Corporate gift aid (paid annually on 31 July)	20,000

The tax written down value of plant and machinery qualifying for capital allowances at 1 December 2010 was £30,000. The only capital transaction during the 16 month period was the purchase of new vans for £68,000 on 12 January 2012.

Calculate the corporation tax liabilities for both accounting periods

Chapter 15

TAX ADJUSTED TRADING LOSSES – COMPANIES

Tax adjusted trading losses may appear in question 2, 4 or 5

1 Trading losses

1.1 Trading profit assessment

If a company makes a trading loss, its trading income assessment for that period is nil. The loss may then be relieved in the current period followed by carry back to an earlier period(s) and / or by carry forward to relieve in future periods

1.2 Current period relief

The loss may be relieved against total profits before gift aid in the period that the loss arose.

EXAMPLE 1

A Ltd had the following results for the year ended 31 March 2012

	£
Trading loss	(45,000)
Interest receivable	20,000
Chargeable gain	50,000
Gift Aid payment	15,000

Show how current year relief would be obtained in the year ended 31 March 2012

1.3 Carryback relief

(a) Having first relieved the trading loss in the accounting period of loss, only then may any remaining trading losses be carried back against total profits before gift aid of the preceding 12 months. The loss must be applied fully against the available profits. Partial claims, for example to leave sufficient profit to cover the gift aid payment, are not allowed. These claims may therefore result in no tax relief being achieved for gift aid payments.

Example 2

A Ltd has produced the following results over recent years.

	Year ended 31 March		
	2010	*2011*	*2012*
	£	*£*	*£*
Trading profit / (loss)	30,000	60,000	(90,000)
Interest receivable	10,000	10,000	10,000

Show how loss relief would be claimed assuming that relief is taken as soon as possible.

Example 3

A Ltd has the following results:

	y/e 31/3/10 £	y/e 31/3/11 £	y/e 31/3/12 £
Trading profit / (loss)	25,000	20,000	(40,000)
Bank interest	2,000	1,000	1,000
Chargeable gains	–	5,000	–
Gift Aid payments	(500)	(500)	(500)

Show the Taxable Total Profits for all accounting periods, assuming loss relief is taken as soon as possible.

1.4 Losses in the final twelve months of trading

The carryback period is extended to 36 months for losses incurred in the twelve months prior to the cessation of trading. Losses can be carried back against total profits before gift aid of the 36 months preceding the loss making period on a LIFO basis.

Example 4

A Ltd ceased trading on 31 March 2012. It had the following results for the five accounting periods to 31 March 2012.

	y/e 30/9/08	*6 months to 31/3/09*	*y/e 31/3/10*	*y/e 31/3/11*	*y/e 31/3/12*
	£	*£*	*£*	*£*	*£*
Trading profit / (loss)	10,000	16,000	20,000	32,000	(97,000)
Bank interest	2,000	-	2,000	2,000	2,000
Chargeable gains	-	-	6,000	-	8,000
Gift Aid payments	500	-	500	500	-

Show the Taxable Total Profits for all accounting periods.

1.5 Carry forward relief

(a) If any loss remains unrelieved after current year and carryback claims have been made or no such claims were made, then the loss is automatically carried forward.

(b) Under carry forward relief any remaining losses are carried forward for relief against the first available trading profit from the same trade. There is no time limit on the carry forward period, but losses must be relieved as soon as possible.

Example 5

A plc had the following results since it started trading on 1 April 2008

	y/e 31/3/09	*y/e 31/3/10*	*y/e 31/3/11*	*y/e 31/3/12*
	£	*£*	*£*	*£*
Trading profit / (loss)	40,000	20,000	(43,000)	20,000
Property Income	3,000	3,000	3,000	3,000
Interest receivable	4,000	3,000	5,000	3,000
Gift Aid payments	(1,000)	(1,000)	(1,000)	(1,000)

Show how losses will be relieved on the assumption that any relief is to be taken as soon as possible.

2 Non-trading losses

2.1 Capital losses

Capital losses are relieved against:

(a) Current year capital gains, then

(b) Capital gains in future accounting periods.

2.2 Property Business losses

Property Business losses are relieved by

(a) Setting them off against total profits before gift aid of the current period, then

(b) By carrying them forward against total profits before gift aid of future periods.

Chapter 16

CHARGEABLE GAINS – COMPANIES

Question 2, 3, 4 or 5

1 General

Companies pay corporation tax on their chargeable gains.

1.1 Exempt assets

Motor vehicles

Certain chattels

1.2 Calculation of gains and losses for companies

	£
Disposal proceeds (or market value)	X
Less incidental costs of disposal	(X)
Net proceeds	X
Less allowable costs	(X)
Unindexed gain	X
Less indexation allowance	(X)
Chargeable gain	X

1.3 The indexation allowance

(a) The increase in value of an asset due to inflation is not taxable - this increase is removed from the gain by way of indexation allowance.

(b) Companies are entitled to an indexation allowance from the month of acquisition until the month of disposal of an asset.

(c) It is calculated as:

$$\frac{\text{RPI for month of disposal - RPI for month of acquisition}}{\text{RPI for month of acquisition}} \times \text{cost of the asset}$$

(d) RPI is the Retail Price Index

(e) The increase in the RPI is expressed as a decimal and is rounded to three decimal places.

(f) The indexation allowance cannot increase or create a loss.

(g) If the RPI has fallen from the month of acquisition to the month of the disposal, the indexation allowance will be nil.

Example 1

A company bought an asset on 6 June 1986 (RPI = 97.85) at a cost of £20,000.
Enhancement expenditure of £6,000 is incurred on 16 August 1990 (RPI = 128.1).
The asset is sold for £100,000 on 2 October 2011 (RPI = 216.0).
Incidental costs of sale are £1,000.

Calculate the chargeable gain arising on the disposal of the asset

2 Gains and losses

(a) Capital gains are chargeable to corporation tax.

(b) Capital losses only arise when proceeds are less than original cost.

(c) If capital gains and losses arise in the same accounting period, they are netted off.

If the resultant figure is a gain, it is charged to corporation tax.

If the resultant figure is a loss, it is carried forward and set against future capital gains, and does not go into the Corporation Tax Computation.

(d) Capital losses brought forward may only be relieved against capital gains, not any other type of income.

(e) The terms capital gains and chargeable gains are interchangeable.

3 Share matching rules for companies

Disposal of shares gives rise to a chargeable gain. However as it is difficult to identify which shares are being sold, and therefore establish the cost, we need to identify the shares sold by using matching rules as follows:

- same day
- previous 9 days
- 1/4/82 to the previous 10 days - Construct a share pool. Essentially we find a weighted average cost.

The share pool records the number and cost of shares for each acquisition and whenever shares are purchased or sold a reindexation of the indexed cost of the shares in the pool is added to the indexed cost total of the share pool. Follow the answer to example 2 below to see how the share pool is constructed.

Example 2

A Ltd bought the following shares in B Ltd:
20 August 1989 (RPI 115.8) 1,000 shares at a cost of £5,000
16 November 1996 (RPI 153.9) 2,000 shares at a cost of £12,000
7 October 2011 (RPI 216.0) 500 shares at a cost of £3,000

A Ltd sold 3,000 shares on 10 October 2011 (RPI 216.0) for £30,000
The company has a 31 March year end.

Calculate the gain to include in the Corporation Tax Computation for year ended 31 March 2012.

4 Bonus issues

(a) A bonus issue increases the number of shares held with no corresponding increase in cost.

(b) The bonus shares are added to the pool.

(c) It is not necessary to index the cost of the original shares to the date of the bonus.

5 Rights issues

(a) A rights issue increases the number of shares held, but this time there is a cost associated with the shares.

(b) The pool is indexed to the date of the rights issue. The rights shares and cost are then added to the pool.

Example 3

Y Ltd acquired 3,000 shares in X Ltd on 20 July 1993 for £10,000. In February 1995 X Ltd made a 1:3 bonus issue. Y Ltd sold 2,000 shares in December 2011 for £12,000.

Calculate the gain on the disposal of the shares in December 2011

RPI are as follows:

December 2011	229.2
February 1995	146.9
July 1993	140.7

6 Takeovers

(a) Where a takeover is a paper for paper transaction shareholders of the company taken over acquire shares in the acquiring company. This normally does not constitute a chargeable disposal.

(b) The new shares are deemed to have been acquired at the same time and for the same cost as the original shares.

(c) A takeover may involve attributing the cost of the original holding to the different component parts of the new holding, if a mix of consideration is received e.g. a combination of ordinary and preference shares. This is done by allocating the cost of the original holding to the new shares according to their market value at the time of the takeover.

(d) If at takeover, cash is received, a chargeable gain needs to be calculated at takeover for the cash element received.

Example 4

Z Ltd acquired 10,000 A Ltd shares in July 1989 for £10,000. In July 2011 B plc takes over A Ltd and for each share in A Ltd, Z Ltd receives:

2 B plc ordinary shares valued at £1.50 each and, 1 B plc preference shares valued at £1 each.

The preference shares are sold in October 2011 for £15,000 and the indexed rise from July 1989 to October 2011 is 0.842

Calculate the Gain arising as a result of the takeover in July 2011, and the sale of the B plc preference shares in October 2011

Example 5

Using example 4 what difference would it make if Z Ltd receives at takeover

2 B plc ordinary shares valued at £1.50 each and £1 cash for each share in A Ltd.
The indexed rise between July 1989 and July 2011 is 0.836.

Chapter 17

CHARGEABLE GAINS – COMPANIES – FURTHER ASPECTS

Question 2, 3, 4 or 5

1 Part Disposals

(a) A chargeable asset partly disposed of will give rise to chargeable gain

(b) The cost of the whole asset is apportioned using the formula:

$$\frac{A}{A + B}$$

where:

A – Gross proceeds of part disposed

B – Market value of the remainder of the asset

Example 1

ST Ltd owned 10 acres of land which originally cost £26,000 in March 2009 (RPI 212.1). ST Ltd sold 2 acres of the land in December 2011 (RPI 229.2) for £16,000.
The remaining 8 acres where valued at £34,000 in December 2011.

Calculate the chargeable gain on the disposal of the 2 acres of land in December 2011

2 Chattels

(a) A chattel is a tangible moveable asset

(b) A wasting chattel is one with an estimated remaining life of 50 years or less. These are exempt from chargeable gains & losses. Examples include racehorses and greyhounds.

(c) There is an exception for plant & machinery on which capital allowances have been claimed, these assets are treated as non wasting chattels

(d) A non wasting chattel is one with an estimated remaining life of more than 50 years. Examples include antiques and paintings. There are special rules to determine the chargeable gain or capital loss.

Cost	Proceeds	Treatment
≤ £6,000	≤ £6,000	Exempt
≤ £6,000	> £6,000	Normal calculation but the gain is restricted to 5/3 [Gross proceeds – 6,000]
> £6,000	≤ £6,000	Deemed Gross Proceeds = £6,000
> £6,000	> £6,000	Normal calculation

Example 2

JM Ltd sold the following assets in December 2011

(a) an antique table which had cost £3,000 in February 2007 and sold for £5,000

(b) a painting which had cost £2,000 in January 2009 and sold for £10,000

(c) an antique vase which had cost £8,000 in August 2002 and sold for £3,000

(d) a vintage car which had cost £7,000 in July 1999 and sold for £9,000

RPI is:

Feb 2007	194.2
January 2009	209.8
August 2002	176.4
July 1999	165.1
December 2011	229.2

Calculate the net chargeable gains or losses arising in JM Ltd in December 2011

3 Other wasting assets (that are not chattels)

An example of a wasting asset which are not chattels are copyrights.

The allowable expenditure is deemed to waste away over the life of the asset.

When a disposal is made, the allowable expenditure is restricted to take account of the assets natural fall in value. This fall in value is deemed to occur on a straight line basis over its predictable useful life.

The allowable cost is therefore restricted by

$$\frac{P}{L} \times (C - S)$$

where

P = Disposers period of ownership

L = Assets predictable life

C = Cost of the asset

S = Scrap value at the end of the assets predictable life

Example 3

On 1 February 2000 Z Ltd bought a wasting asset at a cost of £25,000. It had an estimated useful life of 30 years, and an estimated scrap value of £1,000.
Z Ltd sold the asset for £38,000 on 1 February 2012.
The indexed rise between 1 February 2000 and 1 February 2012 is 0.378

Calculate the chargeable gain arising on the sale of the wasting asset in February 2012.

4 Assets damaged, lost or destroyed

4.1 Damaged assets

(a) If an asset is damaged and compensation or insurance money is received as a result, then this will normally be treated as a part disposal of the asset. The cost is calculated using the normal part disposal formula:

$$\frac{A}{A + B}$$

where

A = value of part disposal

B = market value (MV) of the remainder at the time of part disposal

(b) If insurance money is received then:

(i) if the insurance money is not used in restoring the asset a normal part disposal arises, with the MV of the part retained equating to the value of the asset in its damaged condition.

(ii) if the insurance money is fully used in restoring the asset the tax payer can elect to have the proceeds deducted from the cost of the asset for a future calculation thereby deferring any gain when the insurance is received.

EXAMPLE 4

MI Ltd bought a painting on 1 April 2000 for £10,000. The painting was damaged on 1 May 2011 when it was worth £50,000. After the damage it was only worth £25,000. On 1 July 2011 insurance proceeds of £30,000 were received and were not used to restore the painting. The indexed rise from April 2000 to July 2011 = 0.324.

Calculate the chargeable arising on the receipt of the insurance proceeds

Example 5

Daisy Ltd purchased a painting on 1 April 2000 for £10,000. The painting was damaged on 1 May 2011 when it was worth £50,000. After the damage it was worth £40,000.

On 1 July 2011 insurance proceeds of £8,000 were received. All of the insurance proceeds were used to restore the painting.

Assuming Daisy Ltd elects for the proceeds to be rolled over against the cost of the painting, calculate the base cost of the painting on a future disposal.

4.2 Destroyed or lost assets

(a) If an asset is destroyed or lost and no compensation or insurance money is received there is a disposal which will result in a capital loss.

If there is any compensation or insurance monies received this will normally be brought into an ordinary gains computation as proceeds.

(b) The date of disposal is the date the insurance money is received. If the insurance money is used to buy a replacement asset within 12 months, the gain can be deferred until the new asset is sold.

(c) If only part or the insurance money is used to buy a replacement asset then some of the gain will be taxed immediately and some of the gain will be deferred.

Example 6

SC Ltd bought an asset for £23,000 in June 2007, It was destroyed in March 2011. Insurance proceeds of £34,000 were received in September 2011. SC Ltd spent £30,000 on a replacement asset.

Calculate the chargeable gain and the base cost of the new asset.

RPI is	September 2011	226.8
	June 2007	198.5

Chapter 18

CHARGEABLE GAINS – COMPANIES – RELIEFS

Question 2, 3, 4 or 5

1 Replacement of business assets (Rollover Relief)

1.1 Definition

A gain may be 'rolled over' (deferred) where it arises on the disposal of a business asset whose sale proceeds are reinvested in another qualifying business asset.

1.2 Qualifying assets

Both the old and new assets must fall into one of the following categories:

(a) Land and buildings

(b) Fixed plant and fixed machinery

Both the old and new assets must be used in the business.

1.3 The relief

(a) The gain is not taxed immediately but is postponed until the company makes a disposal of the replacement asset without further replacement.

(b) The postponement is achieved by deducting the gain made on the old asset from the cost of the new one.

(c) Where the disposal proceeds of the old asset are not fully reinvested, the surplus retained reduces the amount of capital gain that can be rolled over.

(d) The replacement asset must be bought in the period 12 months before to 36 months after the disposal of the old asset.

(e) A claim must be made within 4 years from the end of the accounting period in which the disposal occurred.

Example 1

JM Ltd bought a building for use in the business in October 1994 RPI (145.2) for £150,000. The building was sold in September 2011 RPI (226.8) for £400,000. In December 2011 JM Ltd bought some land for use in the business for £500,000. (JM Ltd has a 31 December year end)

Calculate the chargeable gain and the base cost of the new asset.

Example 2

A Ltd bought land for use in the business in May 1993 (RPI 141.1) for £200,000. The land was sold in September 2011 (RPI 226.8) for £350,000.

In October 2011 A Ltd bought a factory for use in the business for £335,000 (A Ltd has a 31 December year end)

Calculate the chargeable gain and the base cost of the new asset.

2 Depreciating assets

2.1 Definition

(a) An asset with an expected life of a maximum 60 years or

(b) Fixed plant and machinery

Note: You will only be examined on fixed plant and machinery and leases with a life of 60 years or less.

2.2 Effect

If the new asset is a depreciating asset.

(a) The gain deferred is not deducted from the cost of the new asset

(b) Instead it is postponed until the earliest of:
- (i) disposal of the new asset
- (ii) the date the new asset ceases to be used in the trade
- (iii) 10 years after the new asset was acquired

Example 3

YR Ltd bought land for use in the business in April 1997 (RPI 156.3) for £200,000. The land was sold for £350,000 in May 2008 (RPI 206.2).
In March 2009 YR Ltd bought fixed plant for use in the business, costing £390,000.
YR Ltd sold the plant in February 2012. (YR Ltd has a 31 March year end)

Calculate the chargeable gains for y/e 31/3/09 and y/e 31/3/12

(c) When the replacement asset is a depreciating asset, the gain is deferred as in (b) above. However, if a non-depreciating asset is purchased before the deferred gain crystallises, the original gain may be rolled over against the cost of the new, non-depreciating asset and will only crystallise on sale of the non-depreciating asset..

Chapter 19

CORPORATION TAX – GROUPS

Examined in question 2 or 5

1 Introduction

A group exists for taxation purposes where one company is a subsidiary of another. The various reliefs are only available to members of certain group structures.

There are two types of group structure, based on the level of share ownership that are relevant for tax purposes, 51% groups and 75% groups

(1) 51% groups issues

- associated companies
- transfer pricing (see Chapter 20)
- Group VAT registration (see Chapter 25)
- Availability of AIA

(2) 75% groups issues

- group relief of losses
- gains group membership

2 Associated companies

2.1 Definition

Companies are associated with each other if:

(a) One controls the other or

(b) Both are under control of another person

2.2 Control

Control is established by holding:

(a) Over 50% of the share capital, or

(b) Over 50% of the voting rights, or

(c) Being entitled to over 50% of the distributable profits or net assets on a winding up

2.3 The tax implications

(a) The upper and lower limits to determine the size of the company are divided by the number of associated companies in the group.

» overseas companies are included

» companies associated for only part of an accounting period are included

» dormant companies are excluded

(b) In calculating augmented profits dividends received from associated companies are excluded.

Example 1

A Ltd prepares accounts for the year ended 31 March 2012. The company acquired a subsidiary on 1 April 2011 that is resident overseas, and a further subsidiary on 1 July 2011 that is resident in the UK.

A Ltd has Taxable Total Profits of £140,000 for the year ended 31 March 2012, and also received franked investment income from non associated companies of £10,000 during the year.

Calculate A Ltd's corporation tax payable for the year ended 31March 2012

3 The Annual Investment (AIA)

Only one AIA is available to a group of companies and the group members can allocate the AIA in any way across the group.

- A group for AIA purposes is where a parent company holds more than 50% in another **UK** company or UK companies **at the end** of the accounting period

EXAMPLE 2

Using example 1

Advise on which companies in the A Ltd group would be eligible to claim AIA and how it may best be allocated between them.

4 Group relief

4.1 Introduction

The relief allows companies in a 75% group to transfer any part of current year trading losses to set off against any part of a claimant company's taxable total profit of a corresponding accounting period.

4.2 Definition of a 75% group

(a) One company is the 75% subsidiary of another, or

(b) Both companies are 75% subsidiaries of a third company.

The holding company must :

(c) own at least 75% of share capital, and

(d) be entitled to at least 75% of the subsidiary's assets on winding up, and

(e) be entitled to at least 75% of the subsidiary's income on a distribution.

4.3 Sub-subsidiaries

The holding company must have an effective interest in the sub-subsidiary of at least 75%

EXAMPLE 3

Z plc is the holding company for a group of companies. The group structure is as follows:

Z plc
|
100%
|
A Ltd
|
80%
|
B Ltd
|
80%
|
C Ltd

For the year ended 31 March 2012 Z plc has a trading loss.

State the companies Z plc may surrender its trading loss to in y/e 31/3/12.

4.4 Group loss relief

(a) Trading losses may be surrendered to other companies in the group, which may then relieve the losses against their own taxable total profits.

(b) Any member company may surrender its loss to any other member of the group:

» a holding company may surrender a loss to its subsidiary company

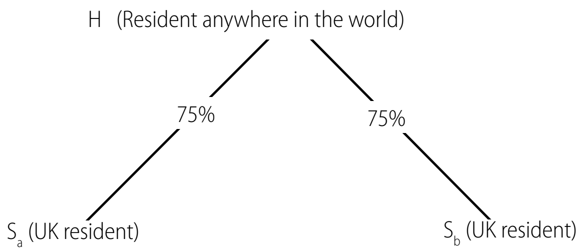
» a subsidiary company may surrender a loss to its holding company

» a subsidiary company may surrender a loss to a fellow subsidiary company.

(c) The surrendering company is the company that surrenders its loss.

(d) The claimant company is the company to which the loss is surrendered.

(e) The group relief rules allow groups to be created through companies resident anywhere in the world. This means that the following group structure qualifies for group relief.



Despite the holding company not being resident in the UK and therefore not itself eligible for group relief, the two UK subsidiaries can claim and surrender group relief between each other. Trading income and losses of a UK branch of H can also participate in a group relief claim.

4.5 The surrendering company

(a) The surrendering company may surrender as much of the loss as it wants to

(b) It is not necessary to relieve the loss against its own income and gains first.

(c) The losses which may be surrendered are:

» trade losses

» unrelieved Gift Aid

» unrelieved Property Business losses

Note that capital losses are not eligible for group relief but are dealt with separately under gains group membership.

4.6 The claimant company

The relief is taken against Taxable Total Profits of the same period as the surrendering company's loss making period

4.7 Group relief

(a) There are two important points to remember as regards group relief:

» Losses can be group relieved against 100% of a 75% subsidiary's Taxable Total Profits, or conversely 100% of a 75% subsidiary's loss can be group relieved.

» The relief is not restricted to the percentage shareholding.

» Only current year losses can be group relieved. No relief is available for trading losses brought forward from previous years or trading losses carried back.

(b) Where the accounting periods of two group companies are different, then group relief may be restricted.

Example 4

Continuing with Example 3 suppose that B Ltd had commenced trading on 1 October 2011 preparing accounts for the six-month period to 31 March 2012

Discuss the group relief available in respect of Z plc trading loss for y/e 31/3/12 if it were to consider surrendering the trading loss to B Ltd.

Example 5

Beyonce Ltd prepares its accounts to 31 March in each year and has two wholly owned subsidiaries J Ltd and Z Ltd. J Ltd has been owned for several years but prepares its accounts to 30 June, while Z Ltd started trading on 1 January 2012 and made a trading profit of £50,000 in its 3 month period to 31 March 2012. Beyonce made a trading loss of £240,000 in its year ended 31 March 2012 while J Ltd has Taxable Total Profits of £160,000 for the year ended 30 June 2011 and £280,000 for the year ended 30 June 2012.

Compute the maximum group relief claims available to J Ltd and Z Ltd in respect of Beyonce's loss of £240,000.

4.8 Marginal rates of tax

(a) The most important factor to be taken into account when considering group relief claims is the rate of corporation tax payable by the claimant companies. Group relief should be surrendered as follows:

- » Initially to companies subject to corporation tax in the higher marginal relief band (effective rate of 27.5%% for FY 2011) to bring augmented profits down to the small profits rate limit (£300,000 divided by the number of associated companies).
- » Surrender should then be to those companies subject to the main rate of corporation tax of 26% (FY 2011), (again to bring their augmented profits down to the small profits rate limit)
- » Finally surrender to those companies subject to the small profits rate of 20% (FY 2011)

Example 6

S Ltd has two 100% subsidiaries, E Ltd and F Ltd. The results of each company for the year ended 31 March 2012 are as follows:

	S Ltd	*E Ltd*	*F Ltd*
	£	*£*	*£*
Trading profit/(loss)	(125,000)	650,000	130,000
Property Income	120,000	–	–

As at 31 March 2011 S Ltd had unused trading losses of £7,500.

Calculate the corporation tax payable of each of the group companies, assuming that the loss is relieved in the most beneficial way.

4.9 Payment for group relief

The claimant company may make payments to the surrendering company for group relief. Any payment up to the amount of the loss surrendered is ignored for corporation tax purposes.

5 Groups – Chargeable gains

5.1 Definition of a 75 % group

(a) A group consists of a parent company and its 75% subsidiaries, and also the 75% subsidiaries of the first subsidiaries.

(b) The parent company must have an effective interest of over 50% in all group companies.

(c) Groups may be established through companies resident anywhere in the world.

5.2 The Tax Implications

(a) Group companies will transfer assets between themselves without incurring a chargeable gain or allowable loss. This will be a no gain / no loss transfer and will be deemed to take place at a value equal to the cost of the asset to the transferor company plus the available Indexation Allowance.

(b) Group companies can make an election such that any part of a capital gain or loss incurred by one company may be treated as arising in another company.

(c) Members of a 75% group are treated as one for the purposes of roll over relief.

Where:

- one company sells qualifying asset, and
- another company buys a qualifying asset within the rollover relief qualifying time period.
- the gain can be rolled over

5.3 Advantages

(a) The group's capital losses can be better utilised

(b) Gains can be taxed at the lowest available tax rate in the group

(c) Rollover relief is available on a group wide basis

5.4 Capital losses

(a) An asset does not have to be moved between group companies in order to match capital losses and gains.

(b) Companies in a capital gains group can make an election to deem any part of a gain or loss made by one group member to have been made by any other gains group member..

(c) The election has to be made within two years of the end of the accounting period in which the asset is disposed of outside the group.

(d) The advantages of the election

- The two-year time limit for making an election means that tax planning regarding the set-off of capital losses and gains can be done retrospectively.
- The two-year time limit also means that it is possible for capital gains to be treated as being made by the company in the group with the lowest rate of corporation tax.
- By not having to actually transfer assets within a group means a saving in legal and administrative costs
- The election can be made in respect of just part of a capital gain or capital loss.

Example 7

During the year ended 31 March 2012 Large Ltd disposed of an asset that resulted in a capital loss of £75,000. Small Ltd, the 100% subsidiary of Large Ltd, disposed of an asset that resulted in a capital gain of £100,000.
Large Ltd has Taxable Total Profits of £1M and Small Ltd has Taxable Total Profits of £100,000 excluding the chargeable gain. Large Ltd holds no other shareholdings.

Discuss the elections available to minimize the groups corporation tax liability.

Chapter 20

OVERSEAS ASPECTS – COMPANIES

Examined in question 2 or 5

1 Residence

1.1 Definition

(a) A company incorporated in the UK will be deemed resident in the UK for tax purposes

(b) A company incorporated overseas will be deemed resident in the UK only if its central management and control are exercised in the UK. Key tests for central management and control will be where the directors are based and board meetings are held.

1.2 Liability to UK corporation tax

Companies resident in the UK are chargeable to corporation tax on worldwide income and chargeable gains.

2 Comparison of an overseas branch to an overseas subsidiary

2.1 Branch

(a) An overseas branch of a UK company is effectively an extension of the UK trade, and 100% of the branch profits will be assessed to UK corporation tax. Whether or not profits are remitted to the UK is irrelevant

(b) UK capital allowances are available on plant and machinery purchased.

(c) As profits will also be subjected to overseas tax within the country in which it trades, double taxation will therefore occur. Double Taxation Relief (DTR) will be given for the overseas tax suffered reducing the UK Tax liability within the UK Company's Corporation Tax computation (see later note).

(d) Trading losses of an overseas branch are available for set off, since they are losses of the UK company

(e) Trading losses of an overseas branch may be group relieved to other UK companies

2.2 Overseas subsidiary

(a) Profits will be subject to overseas Corporate Tax but are not charged to UK corporation tax

(b) Dividends remitted are exempt from UK corporation tax

(c) UK capital allowances are not available

(d) Intra-group transactions between overseas subsidiary and a UK resident group member will be subject to the Transfer Pricing rules (see note 5)

(e) No group relief is available for trading losses of an overseas subsidiary

(f) Will be classed as an associated company (reduces the limits) if ownership is > 50%

(g) If the dividend is received from an overseas company in which the UK parent owns more than 50% of the voting power it will be ignored in computing the figure of FII used to determine Augmented Profits. If a UK company receives a dividend from a non-subsidiary overseas company this will be grossed up as for a UK dividend by 100/90 and included within the FII figure in the normal way..

Example 1

U Ltd is a UK company that is planning to set up an overseas operation. It is unsure whether to operate overseas through a branch or a subsidiary. A subsidiary would remit 50% of its distributable profits to the UK as dividends.

Discuss the tax implications of each option.

EXAMPLE 2

Pod limited received an overseas dividend of £87,500 (net) in year ended 31 March 2012. Withholding tax of 15% was withheld from the dividend.

Discuss how the overseas dividend will be treated for UK corporation tax purposes in Pod Ltd if:

(a) Pod Ltd owns 35% of the voting power of the overseas company

(b) Pod Ltd owns 70% of the voting power of the overseas company.

3 Overseas Income

(a) A UK resident company may operate an overseas branch.
The overseas income is included before deduction of any overseas tax suffered.

(b) A UK resident company may instead own an overseas property or receive interest from an overseas bank account. This income may therefore be received net of overseas tax; the gross income is included in the UK corporation tax computation.

4 Double Tax Relief

4.1 Introduction

UK resident companies are subject to UK corporation tax on worldwide income and gains. Overseas income may therefore be subject to both overseas tax and UK corporation tax.

(a) Relief is given for this double taxation

(b) Relief is given by means of a tax credit to the UK resident company.

(c) The tax credit will reduce the UK corporation tax liability. The relief cannot exceed the equivalent UK tax charge.

4.2 Withholding tax (WHT)

Withholding tax (WHT) is the term used for any overseas tax deducted from the overseas income. The term refers to any direct tax imposed at source by the overseas country, and so it also covers all overseas tax deducted from overseas income paid to a UK resident company.

4.3 Computation of double taxation relief

(a) Overseas income is included in the corporation tax computation under Trading Income (overseas branch trading profit) or Property Income if the income is overseas rental income or Interest Income if overseas bank interest. Any withholding tax deducted at source is added back to amounts received so that the gross figure is included.

(b) The amount of DTR is limited to the lower of:

- the amount of overseas tax on the overseas income
- the UK corporation tax payable on that overseas income.

(c) If the company has made gift aid payments during the accounting period, these for purposes of DTR are deemed to be deducted firstly from UK profits and then the source of overseas income suffering the lowest rate of overseas tax. This will maximise the available DTR for the company.

Example 3

A Ltd is a UK company with an overseas branch. The results of A Ltd for the year ended 31 March 2012 are as follows:

	Total	*UK*	*Branch*
	£	£	£
Trading income	180,000	50,000	130,000

In addition it receives overseas property income of £9,000. This is net of 10% overseas tax.
The overseas branch is subject to tax overseas at the rate of 15%.

Calculate the corporation tax payable of A Ltd for the year ended 31 March 2012.

Example 4

A Ltd is a UK company with an overseas branch. The results of A Ltd for the year ended 31 March 2012 are as follows:

	Total	*UK*	*Branch*
	£	£	£
Trading income	180,000	50,000	130,000

In addition it receives overseas property income of £9,000. This is net of 25% overseas tax.
The overseas branch is subject to tax overseas at the rate of 15%.

Calculate the corporation tax payable of A Ltd for the year ended 31 March 2012.

Example 5

A Ltd is a UK company with an overseas branch. The results of A Ltd for the year ended 31 March 2012 are as follows:

	Total	*UK*	*Branch*
	£	£	£
Trading income	180,000	50,000	130,000

In addition it receives overseas property income of £9,000. This is net of 25% overseas tax.
The overseas branch is subject to tax overseas at the rate of 15%.
A Ltd had also made a gift aid payment during the accounting period of £10,000

Calculate the corporation tax payable of A Ltd for the year ended 31 March 2012.

5 Transfer pricing

The transfer pricing rules prevent UK companies from reducing their Taxable Total Profits subject to UK corporation tax by, for example, making sales at below market price to an overseas subsidiary, or purchasing goods at above market price from an overseas holding company.

Illustration 1
A Ltd, a UK company, is to export goods to its overseas subsidiary company at 30% less than their normal trade selling price.

(a) The export of goods at 30% less than their normal trade selling price will reduce A Ltd's trading income, and hence UK corporation tax.

(b) The sales are at an under valuation to an overseas subsidiary company, and so a market price must be substituted for the transfer price.

(c) The market price will be an arms' length one that would be charged if the parties to the transaction were independent of each other.

(d) A Ltd will be required to make the adjustment on its self-assessment tax return.

Chapter 21

CAPITAL GAINS TAX – INDIVIDUALS

Examined in question 1 and 3

1 Companies versus individuals

Company capital gains form part of the Taxable Total Profits and are chargeable to Corporation Tax..

An individuals capital gains are subject to a separate tax – Capital Gains Tax (CGT)

1.1 Overview

CGT is charged on gains arising on chargeable disposals of chargeable assets by chargeable persons.

1.2 Chargeable Disposal

A chargeable disposal will usually occur by the sale of an asset but will also arise when an asset is gifted, lost or destroyed (see chapter 17). There is no chargeable disposal upon the death of the taxpayer, however, and assets will pass free of CGT to the beneficiaries at their market (probate) value. Sadly, although no CGT arises upon death, a chargeability to Inheritance Tax (IHT) may arise (see chapter 24).

1.3 Chargeable Assets

All assets are chargeable unless specifically exempted.

Exempt assets include:

- Motor vehicles suitable for private use
- National Savings & Investment certificates
- Foreign currency for private use
- Decorations awarded for bravery
- Damages for personal injury
- Life insurance policies
- Works of art given for national use
- Gilt edged securities
- Qualifying Corporate Bonds
- Certain Chattels (tangible moveable property) (see chapter 17)
- Investments held in an ISA

1.4 Chargeable Person

An individual who is either resident or ordinarily resident in the UK is a Chargeable Person and is therefore liable on their worldwide assets.

1.5 CGT computation

(a) Capital gains are aggregated for each tax year.

(b) Basic capital gains computation

Capital Gains in tax year	X
Less: Capital losses in tax year	(X)
Net Capital Gains in tax year	X
Less: Capital losses brought forward	(X)
Net Capital Gains	X
Less Annual exemption	(10,600)
Taxable Gains	X
CGT × 10%, 18% or 28%	X
Due (2011/12)	31/1/13

To calculate a Capital Gain or capital loss we use:

Disposal proceeds	X
Less: Incidental cost of disposal	(X)
Net proceeds	X
Less: Costs	(X)
Capital Gain / (Capital loss)	X / (X)

Individuals do not get indexation allowance on disposals as companies do, but they do benefit from an Annual Exemption which is not available to companies.

1.6 Annual exemption

(a) Every individual has an exempt amount for each tax year. For 2011/12 it is £10,600

(b) If the annual exemption is not used it is wasted.

1.7 Payment of CGT

CGT is due in one amount on 31 January following the tax year (2011/12 by 31 January 2013)

No payments on account of the CGT liability are required.

1.8 Rates of CGT

(a) The capital gains tax rates are determined by either the taxable level of a persons income or the availability of entrepreneurs relief. If entrepreneurs relief is available (see later notes), then on those gains qualifying a CGT rate of 10% is applied.

(b) After considering a persons taxable income from their Income Tax Computation a CGT rate of 18% is applied on those taxable gains that fall into any remaining basic rate band of £35,000 (or extended basic rate band if the person makes gift aid donations or pays personal pension contributions).

(c) After considering a persons taxable income, a CGT rate of 28% is then applied on those gains in excess of the basic rate band (or extended).

Example 1

Tina sold a painting on 1 July 2011 for £500,000. She purchased the painting in February 1997 for £350,000.
She also disposed of an investment property for £310,000 on 1 December 2011 and incurred agency fees of £15,000 on the disposal. She had purchased the property in August 1998 for £200,000.
In addition she sold an antique vase for £10,000 in January 2012 which had cost her £15,000 in September 2009.
Tina had capital losses brought forward from previous tax years of £12,000. Tina's taxable income for 2011/12 is £50,000.

Calculate Tina's Capital Gains Tax for 2011/12

Example 2

Matthew has trading profit of £20,000 in 2011/12 and sold an antique vase giving rise to a capital gain of £18,000.

Calculate Matthew's capital gains tax for 2011/12

Example 3

Katie has trading profit of £40,000 in 2011/12. In addition she sold an investment property giving rise to a capital gain of £30,000.

Calculate Katie's capital gains tax for 2011/12

Example 4

Elliot has trading profit of £45,000 in 2011/12. In addition he sold a painting giving rise to a capital gain of £26,000. He made a gift aid payment of £2,400 in 2011/12.

Calculate Elliot's capital gains tax for 2011/12

1.9 Disposal proceeds

Actual consideration is used when the bargain is made at arm's length.

Market value is used in other cases for example when the disposal is a gift

When quoted shares are gifted the value may not be given in the exam and needs to be calculated using the **lower of**

(a) the quarter up rule, [lowest price + ¼ (highest price – lowest price)] or

(b) mid bargain price [Average of highest and lowest marked bargains]

Example 5

Jenny gifted 1,000 shares in M plc when they were quoted at 400 - 408p and the bargain prices were 399, 400, 403, 407, 408

Calculate the value to be used for capital gains disposal proceeds

1.10 Incidental costs would include:

(a) legal fees
(b) advertising fees
(c) auctioneers fees
(d) agency fees

1.11 Costs

Costs include:

(a) the cost of acquisition and any incidental costs of acquisition
(b) expenditure on enhancing the value of the asset (improvement expenditure)

The exception is when an individual acquires an asset where the previous owner had to use the asset's market value for his disposal proceeds, then the current owner must use the same market value as his cost of acquisition.

2 Losses

(a) Where capital losses arise they are set against capital gains in the same tax year.
(b) The set off is made to the maximum possible extent – it cannot be restricted to avoid wasting the annual exemption
(c) If there are insufficient gains to set off the capital losses in the year they arise, the unrelieved capital losses may be carried forward.
(d) Current year capital losses are deducted in priority to capital losses brought forward. The capital losses brought forward only reduce capital gains to the level of the annual exemption.
(e) Any unrelieved capital losses brought forward are carried forward to the next tax year.

Example 6

Fiona and Jane made capital gains and capital losses for the years 2010/11 and 2011/12 as set out below:

	Fiona	*Jane*
2010/11		
Capital gains	15,000	7,000
Capital losses	10,000	10,000
2011/12		
Capital gains	16,000	12,700
Capital losses	5,200	2,000

Calculate the taxable gains for Fiona and Jane for both 2010/11 and 2011/12 and the amount of any losses carried forward at the end of 2011/12

3 Transfer of assets between a husband and wife or between civil partners

The transfer of assets is at Nil gain/ Nil loss. Essentially the transferee acquires the asset at the original cost and date of acquisition of the transferor.

The Nil gain / Nil loss transfer rules will be useful in order to utilize both parties annual exemptions, and to take advantage of capital losses and lower capital gains tax rates.

Example 7

Mike bought a ring in July 1993 for £12,000. He transferred it to his wife Barbara in December 2011. Barbara sold the ring in January 2012 for £20,000.

Calculate Barbara's capital gain in 2011/12

3.1 Chattels, part disposals, lost, destroyed and damaged assets

Same rules as companies (see chapter 17) with the exception that no indexation allowance calculation is necessary.

Chapter 22

CAPITAL GAINS TAX – INDIVIDUALS – SHARES

Question 3, 4 or 5

1 Shares and securities

1.1 Gift edged securities and Qualifying Corporate Bonds

Disposal of these investments by an individual are exempt.

1.2 Disposal of shares

Where shares are sold, they are matched against acquisitions in the following order:

- Shares acquired on the same day (as the sale)
- Shares acquired within the 30 days following the sale
- Shares from the share pool

Note: The matching rules for individuals are different from those that apply to companies

1.3 The share pool

This keeps a record of the following details of all shares acquired

(a) number of shares

(b) actual cost

(c) the number of shares will include all acquisitions including bonus issue and rights issues

(d) the shares disposed of from the share pool will be disposed of at their average costs.

The share pool is easier to produce for individuals as no indexation applies the only information recorded is number of shares and cost of shares

Example 1

Jane owns shares in ABC Ltd. She acquired 1,500 shares in the company on 31 May 2011 for £20,000, and 500 shares on 30 June 2011 for £10,000. On 7 March 2012 Jane bought a further 200 shares in ABC Ltd for £4,000.
Jane sold 1,000 shares in ABC Ltd on 28 February 2012 for £25,000. She is not an employee of ABC Ltd.

Calculate Jane's capital gain on the disposal of the shares in February 2012.

2 Bonus issues

(a) Bonus shares increase the number of shares held with no corresponding increase in cost

EXAMPLE 2

Graham had the following transactions in the Alderholt Ltd shares:

February 2011	Purchased 7,000 shares for £15,000
June 2011	Purchased 1,000 shares for £4,000
July 2011	Bonus issue of one for five
October 2011	Sold 5,000 shares for £20,000

Calculate the capital gain arising on the disposal in October 2011.

3 Rights issue

The share pool is increased by the number and cost of the shares acquired via the rights

Example 3

Mark in an employee of Romsey Ltd. He had the following transactions in the company shares:

February 2011	Purchased 6,000 shares for £15,000
June 2011	Purchased 900 shares for £2,700
July 2011	Took up 1 for 3 rights issue for £3.00 per share
September 2011	Sold 6,000 shares for £24,000

Calculate the capital gain on the disposal in September 2011.

4 Takeovers

(a) Where a takeover is a share for share exchange, known as a paper for paper transaction, shareholders of the company taken over acquire shares in the acquiring company. This normally does not constitute a disposal for CGT purposes.

(b) The new shares are deemed to have been acquired at the same time and at the same cost as the original shares.

(c) The cost of the original holding is attributed to the different components of the new holding on a basis of the market values of the new holding.

(d) This treatment is automatic however, the shareholders can elect for the event to be treated as a disposal for CGT purposes such that the entrepreneurs' relief tax rate of 10% (see later note) may be available on the gain.

(e) If at takeover, some cash is also received, a capital gain needs to be calculated at takeover for the cash element received.

Example 4

Mark owned shares in Silver Ltd. In May 2011 he purchased 4,000 ordinary shares in the company for £10,000. In June 2011 Silver Ltd was taken over by Gold Ltd and Mark received 2 ordinary shares and 1 preference share in Gold Ltd for each ordinary share in Silver Ltd.

Immediately after the takeover the ordinary shares in Gold Ltd were valued at £5 and the preference shares in Gold Ltd were valued at £2.

In January 2012 Mark sold all his holding ordinary shares in Gold Ltd for £20,000.
Mark was not an employee of Silver Ltd or Gold Ltd.

Calculate the capital gain arising on the disposal in January 2012.

Example 5

Using example 4 what difference would it make if Mark received at takeover

2 Gold Ltd ordinary shares valued at £5.00 each and £2 cash for each share in Silver Ltd

Calculate the capital gain arising in June 2011

Chapter 23

CAPITAL GAINS TAX – INDIVIDUALS – RELIEFS

Question 3, 4 or 5

1 Entrepreneurs' relief

1.1 Introduction

- This relief is available for individuals disposing of a business or part of a business.
- The relief covers the first £10m of qualifying gains that an individual makes during **their lifetime.** This gain qualifying is taxed at a lower capital gains tax rate of 10% regardless of a persons taxable income.

1.2 Conditions

(a) The assets must have been owned for one year prior to the date of disposal

(b) The relief is available on:

» A disposal of the whole or part of a business run as an unincorporated business (sole trader or partnership). However the assets must be used for the purpose of the business, so the relief is not available on investments.

» Assets of the individuals' or partnerships' trading business that has now ceased. Note the disposal of assets must take place within three years of the cessation of trade.

» The disposal of shares in a trading company where the individual has at least a 5% a shareholding in the company AND is also an employee (part time or full time) of the company. There is no restriction of the relief if the company own investments. The company is either a trading company or it is not, there is no apportionment of the gain eligible for relief.

1.3 Time limit for claim

The relief must be claimed within 12 months of the 31 January following the end of the tax year in which the disposal is made for 2011/12 by 31 January 2014

Example 1

Daisy disposed of the following assets in 2011/12
On 30 September 2011 Daisy sold a business that she ran as a sole trader since February 2006. The sale resulted in the following capital gains and capital losses

Goodwill	250,000
Factory	320,000
Warehouse	(90,000)

In December 2011 Daisy also sold a 20% shareholding in Bed Ltd, an unquoted company. Daisy had been an employee of Bed Ltd from the date she acquired the shares in July 2007. The gain arising was £370,000

Calculate Daisy's Capital Gains Tax in 2011/12

1.4 Further points

- The gains qualifying for entrepreneurs' relief must be taken into account when establishing which rate applies to other capital gains, in that they are deemed to firstly use any amount of unused basic rate band.
- The annual exemption and any capital losses should however be deducted from gains that do not qualify for entrepreneurs' relief as they are taxed at a higher capital tax gains rate (18% and/or 28%)
- The easiest approach in dealing with questions that include gains qualifying for entrepreneur's relief and gains that do not qualify is to keep the gains separate

Example 2

Anne sold her shareholding in Annie limited for £5,000,000 in 2011/12. The shares had cost her £500,000 in July 1991. She owned 100% of the shares in Annie Limited and had been a full time director since the date of acquisition. She has not made any disposals qualifying for entrepreneurs' relief in the past.
In addition she sold an antique painting realising a capital gain of £100,000.
Anne had capital losses brought forward of £25,000 from 2010/11 and her taxable income for 2011/12 was £18,000.

Calculate Anne's capital gains tax for 2011/12 and state the due date for payment.

2 Rollover relief and reinvestment in depreciating assets

2.1 Rollover relief

(a) Rollover relief for unincorporated businesses is practically the same as for companies except for the impact of entrepreneurs' relief.

(b) Rollover relief is available on the sale of an individual asset so entrepreneurs' relief would not normally be available.

However, if the whole business is sold and rollover relief is claimed on part of the gains - any remaining gains could be eligible for entrepreneurs' relief.

(c) A claim for rollover relief must be made within 4 years from the end of the tax year in which the disposal occurred. For disposals in 2011/12 by 5 April 2016

Example 3

Jones purchased an asset qualifying for rollover relief in March 1990 for £250,000. In August 2011 he sold the asset for £300,000 and spent £320,000 in November 2011 on a new qualifying asset.

Calculate the gain to be deferred and the base cost of new asset.

Example 4

Jerome bought a factory in June 1991 for £680,000. In August 2011 wishing to move to a more convenient location, he sold the factory for £800,000. He moved into a rented factory until January 2012 when he purchased and moved to a new factory.

Calculate the base cost of the new factory if it was purchased for

(a) £750,000

(b) £600,000

2.2 Non-business use

(a) Full rollover relief is only available where the asset being replaced (the old asset) was used entirely for business purposes throughout the trader's period of ownership

(b) Where this condition is not met rollover relief is scaled down in proportion to the non-business use.

(c) The asset is treated as two separate assets, one that qualifies for relief (the part wholly used in the trade) and another that does not.

Example 5

Jake purchased factory in May 1991 for £540,000. He let out 15% of the factory. In July 2011 he sold the factory for £600,000 and bought another factory in August 2011 for £650,000 claiming rollover relief.

(a) **what is the chargeable gain arising on the disposal in July 2011?**

(b) **what is the base cost of a new factory?**

2.3 Reinvestment in depreciating asset

(a) The rules are practically the same as for companies except for the impact of entrepreneurs' relief.

(b) Entrepreneurs' relief is only available if any remaining gains after the relief are in relation to the disposal of the whole business.

Example 6

Charles purchased a freehold factory in May 1991 for £300,000. In June 2010 he sold it for £500,000 and in July 2010 bought fixed plant and machinery for £600,000. In February 2012 Charles sold the fixed plant and machinery.

Calculate the chargeable gains arising in 2011/12 assuming Charles claims to defer gains where possible.

2.4 Acquisition of a new non-depreciating asset

(a) If a new non-depreciating asset is acquired before the deferred gain becomes taxable, rollover relief can be claimed instead.

(b) The capital gain on the original asset is then rolled over into the new non-depreciating asset and the depreciating asset is, effectively, ignored.

3 Relief for the gift of business assets

3.1 Nature of relief

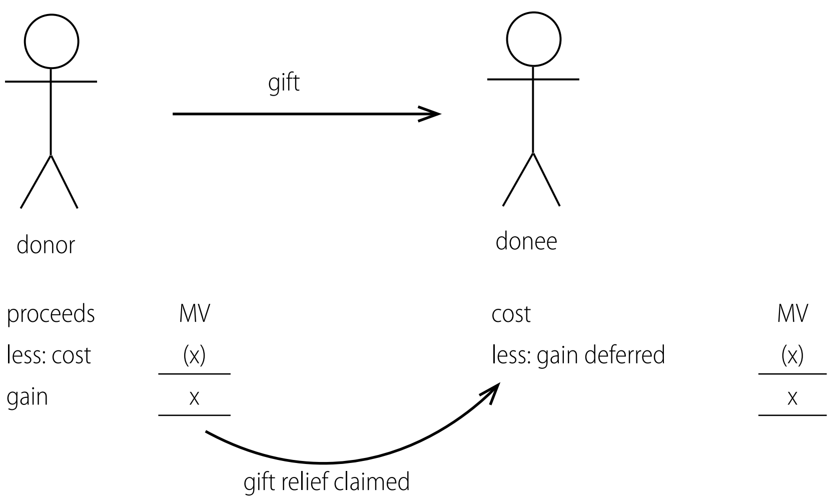
(a) A gift is subject to capital gains tax

(b) The donor (the person making the gift) is treated as making a disposal at market value.

The donee (the person receiving the gift) is treated as if he had acquired a gift at market value.

(c) When gift relief is claimed, the donor has no gain. The gain is deducted from the donee's cost (market value)

This can be illustrated as follows:



Example 7

David bought an asset for £60,000 in June 2010. In September 2011 he gifted it to Tommy, when its market value was £100,000. The asset qualified for gift relief.

Calculate David's capital gains tax on the gift to Tommy and calculate Tommy's Base cost.

3.2 Entrepreneurs' relief

(a) When a claim for gift relief is made, the donor may lose entitlement to entrepreneurs' relief

(b) If the asset qualifies, gift relief if claimed is applied before entrepreneurs' relief.

3.3 Availability of the relief

(a) The relief is only available to individuals not companies

(b) The claim must be made by both the donor and donee and must be made 4 years from the end of the tax year in which the disposal occurred. For a gift made in 2011/12 the claim must be made by 5 April 2016.

3.4 Qualifying assets

Gift relief may be claimed on the gift of the following assets:

(a) Assets used in the trade of:

- » the donor (i.e. where he is a sole trader)
- » the donor's personal company (this extends the relief to assets owned by the individual but not used by him directly for trading purposes).

(b) Shares and securities of trading companies provided that one of the following conditions apply:

- » the shares or securities are not quoted on a recognised stock exchange or
- » the shares or securities gifted are those of the individual's personal company

A company qualifies as an individual's personal company if at least 5% of the voting rights are owned by the individual

3.5 Sale at undervalue

(a) Gift relief is also available for sales made below market value, where there is an element of gift.

(b) Any proceeds received over and above the original cost are chargeable to CGT immediately.

(c) The gain deferred is reduced by this amount

Example 8

Richard acquired a 25% holding in an unquoted trading company in March 1991 for £60,000. He immediately became an employee of the company.

In March 2012 he sold the shares to his son for £85,000 when their value was £200,000. Richard and his son claimed relief for a gift of a business assets.

(a) What is the chargeable gain, if any, incurred by Richard?

(b) What is the base cost for Richard's son?

3.6 Assets not wholly used for trading purposes

(a) Where only part of an asset is used for trading purposes, or where an asset has been used for only part of the donor's period of ownership, then gift relief is restricted.

(b) Where the gift is shares and the individual owns at least 5% of the voting rights, then the capital gain on the shares eligible for relief is restricted by the following fraction:

$$\frac{\text{Market value of company's chargeable business assets (CBA)}}{\text{Market value of company's chargeable assets CA)}}$$

Note that this treatment is completely different to that which applies for entrepreneurs' relief. Remember that for entrepreneurs' relief purposes there is no question of apportionment. A company is either a trading company (and therefore qualifies for the entrepreneurs' relief) or it is not.

3.7 Chargeable assets (CA) and chargeable business assets (CBA)

(a) An asset cannot be a chargeable asset where a capital gain that might arise on its disposal would not be a chargeable gain. This provision rules out exempt assets such as motor cars, but not those that could produce a gain on disposal but currently stand at a loss.

(b) Chargeable business assets are those used for the purposes of a company's trade (including goodwill purchased before 1/4/02, but excluding shares, securities and other assets held as investments).

Example 9

John owns 100% of the shares in John Ltd of which he is the managing director. On 1 December 2011 he made a gift of the shares to his son, when the market value of the shares was £800,000. The shares cost £200,000 in February 2006. At the time of the gift John Ltd owned the following assets.

	£
Freehold trading premises	500,000
Goodwill (pre 1/4/02)	200,000
Investments	100,000
Stock and work in progress	150,000
Debtors	80,000
Cash	170,000
	1,200,000

Calculate John's Capital Gains Tax on disposal of the shares in John Ltd and base cost of the shares for his son.

4 Transfer of a business to a limited company

4.1 Incorporation relief

(a) When an individual incorporates his business chargeable gains will arise because the transfer of the individual business assets to the Limited Company are deemed to be at market value, irrespective of the actual consideration

(b) There is incorporation relief when a business is transferred to a company, and consideration is at least in part in the form of shares. Gains on business assets are deferred by deducting them from the base cost of the company shares acquired.

(c) The relief is automatic without any claim being made so long as the transfer complies with the qualifying conditions (see note 4.2 below)

(d) It is possible to make an election so that the relief does not apply. The election must be made 2 years from 31 January following the end of the tax year in which the business is transferred. For transfers in 2011/12 by 31 January 2015.

This may be beneficial in order to allow entrepreneurs' relief to apply to the gains arising

The use of incorporation relief means the delay of any entitlement to entrepreneurs' relief on gains deferred and the possibility that on a subsequent disposal of the shares the conditions for entrepreneurs' relief do not apply, such that the gain would be taxed at 18%/28% instead of 10%

4.2 Conditions for the relief

(a) All the assets of the business (other than cash) must be transferred

(b) The transfer must be of a business as a going concern

(c) The consideration must be wholly or partly in shares

To the extent that the consideration is not in the form of shares, the potential relief is scaled down.

4.3 Operation of the relief

(a) The capital gains on the individual business assets transferred to the company are deferred and deducted from the allowable cost of the shares that are acquired from the company

(b) Where some of the consideration given by the company for the assets is not shares (for example loan stock or cash) the capital gain eligible for incorporation relief is calculated by the formula:

$$\text{Capital Gain} \times \frac{\text{Value of shares issued}}{\text{Total consideration}}$$

4.4 Entrepreneurs' relief

Any gains remaining after incorporation relief could be eligible for entrepreneurs' relief as the whole of the business is being disposed of. (Subject to the conditions being satisfied). Any gains deferred, under incorporation relief will result in the possible loss of entrepreneurs' relief if the conditions are not satisfied when the shares are eventually sold.

Example 10

Mark started a retail business in 1990. On 1 September 2011 he transferred his business to a company, Mark Ltd. The assets transferred are set out below. In exchange he received 1,000 £1 ordinary shares, valued at £160,000 and £40,000 cash.

Assets transferred	*Market value at 1/9/11*	*Gain*
	£	*£*
Freehold premises	75,000	45,000
Furniture and fittings	15,000	-
Plant and machinery	25,000	-
Stock	40,000	-
Goodwill	45,000	45,000
	200,000	90,000

On 1 March 2012 Mark sold his entire holding in Mark Ltd for £350,000.

Calculate Mark's capital gains tax for 2011/12 assuming his taxable income is £90,000.

5 Principal Private Residence Relief

5.1 The sale of an individuals only or main private residence is covered by Principal Private Residence Relief (PPR). The relief also covers grounds up to half a hectare.

The relief is available in full if the taxpayer occupied the property throughout the entire period of ownership. Where occupation has been for only part of the period , a proportion of the gain is covered by the relief

$$\text{Gain} \times \frac{\text{Period of occupation}}{\text{Period of ownership}}$$

5.2 There are however periods of absence which are deemed to be full occupation

(a) Last 36 months - if the property was the individuals main residence at some point in time

(b) Any periods during which the individual was required by his employment to live abroad

(c) Any period up to four years during which the individual is required to live elsewhere in the UK due to employment

(d) Up to three years for any reason.

Points (b – d) must be preceded and followed by periods of actual occupation, but for points (b – c) if the individual could not reoccupy due to the terms of employment requiring them to work elsewhere, by concession, the condition of actual occupation following the period of absence is not applied.

Example 11

David bought a house on 1 April 1985 for £10,000. he lived in it until 30 June 1985. He worked abroad for 2 years and then moved back into the house on his return on 1 July 1987. He lived in the house until 31 December 2001 before leaving to live and work in Liverpool. The house was sold on 31 December 2011 for £150,000.

Calculate the chargeable gain arising.

5.3 Business use

Where part of a residence is used exclusively for business purposes throughout the period of ownership, the gain in relation to that part is not covered by relief.

The last 36 months rule does not apply to that part unless the business part was at some time used as part of the only or main residence.

5.4 Letting relief

Letting relief is available to cover any gain not covered by PPR if:

(a) owner is absent (not covered by deemed occupation rules) and the property is rented out.

(b) part of the property is rented out, the remaining part being occupied by the taxpayer

Letting relief is the lower of:

- » PPR relief given
- » £40,000
- » gain attributable to letting

Example 12

Ken bought a house on 1 April 1985 for £30,000 and occupied as follows:

1/4/85 – 31/3/87	lived in it
1/4/87 – 30/9/92	travels the world and lets the house
1/10/92 – 31/3/01	lived in it
1/4/01 – 31/3/12	Moved out of the house to live with his girlfriend and the property was empty.

Ken sold the house on 31 March 2012 for £250,000.

Calculate the chargeable gain arising.

Chapter 24

INHERITANCE TAX

Examined in question 4 or 5

1 Introduction

The majority of UK taxpayers will only experience chargeability to Inheritance Tax (IHT) on one occasion – when they die! If their Chargeable Estate exceeds the nil rate band, currently £325,000, the excess will be taxed at 40%.

If only the assets still owned at the time of death were to be taxable, "deathbed gifting", giving assets away just prior to death, would effectively avoid this tax. This means that certain lifetime gifts, those made within 7 years of death, will also become chargeable on the death of the taxpayer. In addition there are also some transfers made in lifetime, transfers into trusts that will generate immediate chargeability to IHT as well as chargeability on death.

2 Transfer of Value

IHT is a cumulative donor based tax and for it to arise an individual must make a transfer of value i.e. a gift, computed as the loss to the estate of the donor. This is calculated as the difference in estate value before and after the gift of the asset.

The amount of tax that may be payable on a transfer of value is based on the cumulative amount of transfers made by the donor over a 7 year period.

For most assets the transfer of value will be the same as the open market value of the asset e.g. gifting a property worth £250,000 or cash of £100,000, but for some assets, notably shares in unquoted companies the transfer of value may be considerably higher than the market value of the asset being gifted.

Illustration 1

A owns 60% of the shares in A Ltd. A Ltd has 100,000 £1 ordinary shares in issue.

Share valuations have been agreed as follows:

20%	£10 per share
40%	£15 per share
60%	£25 per share
80%	£40 per share

Compute the transfer of value if A were to die leaving his shares to his daughter, or alternatively if he were to make a lifetime gift of 20,000 shares to his daughter.

If A died owning his 60,000 shares, a 60% shareholding, they would be valued at £25 per share i.e. 60,000 @ £25 = £1,500,000.

If, however, he were to give 20,000 shares in lifetime the transfer of value would not be based on the value of a 20% interest i.e. £10 per share, but would be computed as the difference between the value of his estate before and after the transfer:

Before	60,000 shares (60%) @ £25 =	1,500,000
After	40,000 shares (40%) @ £15 =	600,000
Transfer of Value		900,000

A transfer of value will arise by the gift of an asset either in lifetime and / or on death. For most taxpayers, as stated above, their only transfers of value will arise as a result of their death.

3 The Death Estate

On death the assets owned by the deceased are valued and included in the death estate. If the deceased was UK domiciled, all assets owned are included in the death estate. If non UK domiciled, only assets situated in the UK are included.

If a property held in the estate is mortgaged, the mortgage will reduce the property value if it is a repayment or interest only mortgage. Endowment mortgages are not deducted as they are repaid on death by the life assurance part of that mortgage. The estate should also include the proceeds of any separate life assurance policy on the deceased's life, not the market value of the policy at the date of death.

The value of the estate will be reduced by any legally enforceable debts due at that date e.g. credit card bills, plus funeral expenses and by exempt bequests.

Bequests are exempt IHT if made to:

- Spouse / Civil Partner
- Charity
- Qualifying political party

The "available" nil rate band is deducted from the value of the chargeable estate. The nil rate band is £325,000 in 2011/12.

The "available" nil rate band is the £325,000 reduced by the value of any lifetime chargeable transfers made by the deceased in the 7 years before death. The balance of the estate is then taxed at 40%.

This IHT liability has to be paid by the Personal Representatives before they get letters of probate allowing the estate to be distributed, but is anyway due 6 months after the end of the month in which the taxpayer died. The IHT is suffered by the beneficiaries, usually the residuary legatee of the estate – the person receiving the balance of the estate after any specific legacies have been paid out.

Illustration 2

Dee Parted, a spinster, died on 1st February, 2012 leaving an estate valued at £1M. She had made no chargeable transfers of value in her lifetime and now bequeathed £250,000 to charity and the remainder to be split equally between her nieces and nephews.

Compute the IHT liability arising as a result of Dee's death and state the date by which the liability should be paid.

Dee Parted

Chargeable Estate at Death – February 1, 2012	*£'000*
Net Assets	1,000
Less: Exemptions	
Bequest to Charity	(250)
Chargeable Estate	750

IHT

325,000 @ Nil	= Nil
425,000 @ 40%	= 170,000
750,000	

The Personal Representatives will be required to pay the IHT liability of £170,000 by 31 August 2012. The tax will come out of the estate and hence is borne by the nieces and nephews.

Illustration 3

As in Illustration 2 but Dee had made a chargeable transfer of value of £200,000 in June 2008.

Compute the IHT liability arising as a result of Dee's death

As the chargeable transfer made in lifetime falls within the 7 years before the date of death it will become chargeable as a result of Dee's death. It will however fall within the nil rate band of £325,000 in force at the date of death so no IHT will be payable thereon. This will however mean that only £125,000 of nil rate band will now be available in taxing the estate at death. The IHT payable on the Chargeable Estate at Death will now be computed as follows:

IHT

125,000 @ Nil	= Nil
625,000 @ 40%	= 250,000
750,000	

Illustration 4
If in the above Illustration 2, Dee was a widow and had received all of her husband's estate on his earlier death the husband would have made no chargeable transfers as transfers between spouses are exempt. This would mean that 100% of his nil rate band would have been unused. As Dee has then died post 8 October, 2007, a claim may be made for the unused proportion (100%) of the husband's nil rate band to transfer to Dee. Thus Dee's nil rate band will now be:

£325,000 + (100% x £325,000) = £650,000

This will therefore allow tax of £130,000 (40% x £325,000) to be saved.

Lifetime transfers are either Exempt Transfers (as noted above), Potentially Exempt Transfers (PET) or Chargeable Lifetime Transfers (CLT).

4 Potentially Exempt Transfers (PET)

A PET is defined as a lifetime gift by an individual to an individual.

With a PET, the original assumption is that the gift will be exempt IHT. There is therefore no tax liability at the date of the gift.

If the donor survives more than 7 years from making the gift, the PET becomes fully exempt and is ignored for IHT purposes (though it may still use up annual exemptions (see later note)).

If the donor dies within 7 years of making the gift, it becomes chargeable on the death of the donor. IHT is then payable at 40% on the value of the gift (less any available nil rate band). If the taxpayer did survive for at least 3 years however, any IHT charge is reduced by the available taper relief (see note 5 below). Any IHT payable on the PET is paid by the donee.

Where more than one PET has occurred within the 7 years before death the nil rate band is applied strictly on a chronological basis – the earlier transfers benefit first from the nil rate band!

Illustration 5
As in Illustration 3 but Dee had made 2 chargeable transfers in lifetime of £200,000 each, the first in June 2008 and the second in August 2010.

Compute the IHT liabilities arising as a result of Dee's death.

As Dee has made PET's within 7 years of the date of death these now become chargeable along with the Chargeable Estate and the IHT may be computed as follows:

Lifetime Transfers Chargeable on Death

		Gross Transfers	*IHT*
June 2008	PET	200,000	nil
August 2010	PET	200,000	30,000
125,000 @ Nil	= Nil	400,000	
75,000 @ 40%	= 30,000		
200,000			

The £30,000 liability will be paid by the donee of the gift.

As the Nil rate band has been fully used on the lifetime transfers the entire chargeable estate of £750,000 will be taxed at 40% giving a further liability of £300,000 to be paid by the Personal Representatives.

It can be seen therefore that if the taxpayer survives for more than 7 years from the date of the PET it will be both exempt in its own right and in addition will have no effect on the chargeability of either those lifetime transfers falling within the 7 years before death or on the chargeable estate itself.

Illustration 6
If in Illustration 3 and 5 there had been an earlier PET of £200,000 8 years before the date of death, this would be exempt and would have no effect on the amount of IHT payable.

5 Taper Relief

If a taxpayer does not survive for 7 years following the PET but does survive for at least 3 years any IHT payable on the transfer is reduced by taper relief. The relief is applied to the tax charge as follows:

Time from transfer to date of death	Relief
3 – 4 years	20%
4 – 5 years	40%
5 – 6 years	60%
6 – 7 years	80%

(This table is provided in the examination)

Illustration 7
As in Illustration 5 but the 2 lifetime transfers of £200,000 occurred in January 2007 and June 2008 respectively.

Compute the amount of IHT payable as a result of Dee's death.

Lifetime Transfers Chargeable on Death

			Gross Transfers	*IHT*
January 2007		PET	200,000	nil
June 2008		PET	200,000	30,000
125,000	@ Nil	= Nil	400,000	
75,000	@ 40%	= 30,000		

As the PET falls between 3-4 years from the date of death
The tax charge may be reduced by taper relief of 20%

Less; Taper Relief (20%)	(6,000)
	24,000

As in Illustration 5 the nil rate band has been fully utilised on the lifetime transfers made in the 7 years before death so the entire chargeable estate of £750,000 is taxed at 40% giving an IHT liability of £300,000.

It can now be seen that the amount of tax that arises on either transfers made in lifetime or on death cannot be computed in isolation and is nothing to do with the circumstances of the donee. IHT is a cumulative donor based tax.

6 Chargeable Lifetime Transfers (CLT)

A CLT is a transfer into a trust.

With a CLT, IHT is chargeable at the date of the gift using the nil rate band in force at that date. If IHT is payable it should be paid 6 months after the end of the month in which the transfer was made, but earliest the 30th April following the end of the tax year in which the transfer took place.

The gross rate of IHT above the nil rate band is 20% if the tax is being paid by the donee (i.e. the trustees of the trust).

If the tax is paid by the donor, the gift has to be "grossed up" as the IHT payable becomes part of the gift. The simple solution to this problem is to apply an IHT rate of 25% to any part of the net gift in excess of the available nil rate band at that date.

Illustration 8

Kay Babb has decided to make a chargeable transfer into a trust of £400,000 in June 2012. She has made no previous lifetime transfers. Assume the nil rate band remains at £325,000.

Compute the amount of IHT payable, assuming firstly the trustees will pay any IHT due, and then that Kay will pay any IHT due.

Lifetime Transfers Chargeable When Made

		£	*Gross Transfers*	*IHT*
CLT		400,000	400,000	15,000
325,000 @ Nil	= Nil			
75,000 @ 20%	= 15,000			

If Kay pays the tax the first £325,000 is still within the nil rate band but the excess £75,000 is now taxed at 25%. This tax is then added to the £400,000 to establish the gross amount of the gift:

	£	Gross Transfers	IHT
CLT	400,000	418,750	18,750

As a CLT is immediately chargeable to IHT, it goes into the donor's IHT cumulation, using up his nil band for the next 7 years.

If the donor dies within 7 years of a CLT, additional death tax may be due to top up the lifetime tax paid. The IHT liability is calculated in the same way as the tax on a PET, with credit then given for any lifetime tax paid.

Illustration 9

Having made the chargeable transfer of £400,000 into the trust in June 2012, Kay then died in December 2016 leaving a chargeable estate of £1M.

Compute the IHT payable as a result of Kay's death. Assume that the trustees paid the tax payable in lifetime as shown in Illustration 8 and that the nil rate band at the date of death had risen to £340,000

Lifetime Transfers Chargeable on Death

		Gross Transfers	*IHT*
June 2012	CLT	400,000	24,000
340,000 @ Nil	= Nil		
60,000 @ 40%	= 24,000		

(The tax charge is now reduced by any available taper relief as with PET's but also by any lifetime tax that was paid)

Less:	Taper Relief (40%) (4-5 years)	(9,600)
		14,400
Less:	Lifetime Tax Paid	(15,000)
Additional Tax Due on Death		Nil

As the lifetime tax paid exceeds the amount of tax payable on death no additional tax is payable but no lifetime tax is repayable either!

7 Lifetime Exemptions

The following exemptions are available against lifetime gifts

- Annual exemption (AE). The first £3,000 of gift each tax year is exempt. Any unused AE is carried forward a maximum of one tax year for use after that year's own AE The exemption is allocated on a strict chronological basis within the tax year.
- Marriage exemption. A gift in consideration of marriage / civil partnership is exempt up to certain limits. For each of the parents of the bride or groom, the first £5,000 is exempt. For remoter ancestors (e.g. grandparents) and for the parties to the marriage themselves the exemption is £2,500. For others, the exemption is £1,000.

These exemptions, firstly marriage, if available and then annual exemption(s) are deducted from the transfer of value to compute the amount of chargeable transfer.

- Small gifts. Gifts of up to £250 per donee per tax year are exempt. However, if this limit is exceeded, the exemption is lost.
- Gifts for family maintenance. Any gifts made to maintain family members are fully exempt.
- Regular gifts out of income. For this exemption, the donor must show a regular pattern of giving. Also the donor must have enough income left to retain their normal standard of living.

Illustration 10
Compute the Chargeable transfer figure for each of the following lifetime transfers:

1)	7 June 2010	a gift to her daughter of £2,000
2)	12 August 2010	a wedding present to her son of £5,500
3)	19 September 2010	a gift to her husband of £20,000
4)	9 July 2011	a gift to her nephew as a wedding gift of £8,000
5)	25 December 2011	gifts of £200 each to two friends as a Christmas gift
6)	25 March 2012	a gift to a trust of a valuable painting worth £100,000

The gift on 19 September 2010 is exempt as a transfer between spouses and the gifts on 25 December 2011 are exempt as they are covered by the small gifts exemption.

The chargeable transfer figures are then computed as follows:

	7/6/10	*12/8/10*	*9/7/11*	*25/3/12*
	PET	PET	PET	CLT
Transfer of value	2,000	5,500	8,000	100,000
Less: Exemptions				
AE 10/11	(2,000)			
Marriage		(5,000)		
AE 10/11		(500)		
Marriage			(1,000)	
AE 11/12			(3,000)	
AE 10/11 (b/f balance unused)			(500)	
Chargeable Transfer	nil	nil	3,500	100,000

Note: although the 09/10 AE is unused and would be brought forward into the 10/11 tax year, it may only be used after the 10/11 AE has itself been fully utilised. The 10/11 AE is not however fully used and a balance of £500 is carried forward into 11/12 for use after that year's own AE, while the 09/10 AE is lost.

8 Approach to Exam Questions

In an examination question the following approach should be adopted:

(1) Compute the chargeable transfer for each lifetime gift (as per illustration 10)

(2) If any CLT's have been made the computation for Lifetime Transfers Chargeable When Made must be prepared (as per illustration 8). To compute any tax payable it must be ascertained who paid the tax, donor or donees to determine the tax rate to apply above the nil rate band

(3) Any lifetime transfers, CLT's or PET's within the 7 years of death are now included in the computation for Lifetime Transfers Chargeable On Death (as per illustrations 7 and 9).

(4) The Chargeable Estate is now established and the tax thereon computed.

In short exam questions not all of the above steps may be necessary and hence the steps should be applied as applicable to the question set.

It may also be required to state by whom and by when the IHT should be paid.

Example 1

Joe Kerr died on April 1 2012, leaving £250,000 to his wife and the remainder of his estate to his son.

At the date of his death Joe owned the following assets:

(1) His principal private residence valued at £300,000 upon which the outstanding repayment mortgage at the date of death was £80,000

(2) A holiday home valued at £140,000

(3) Bank and Building Society Deposits amounting to £230,000

(4) ISA's with a market value of £50,000

(5) 12,000 Shares in Joe Ltd valued at £20 per share

(6) A life assurance policy with an open market value at April 1 2012 of £125,000 from which proceeds of £140,000 were received following Joe's death.

Joe had outstanding credit card bills of £6,000 and an unpaid gambling debt of £1,000 when he died. Funeral expenses amounted to £6,000.

During his lifetime he had made the following lifetime transfers:

(1) On 20 November 2007 a cash gift of £40,000 to his son on the occasion of his wedding.

(2) On 15 July 2008 he transferred £405,000 into a trust and paid the IHT due thereon

(3) On 8 December 2010 he gave 4,000 shares in Joe Ltd to his son. Prior to the gift Joe owned 16,000 of the 20,000 shares in Joe Ltd. Share valuations agreed with HMRC at this date were as follows:

20% shareholding	-	£8 per share
40% "	-	£12 "
60% "	-	£18 "
80% "	-	£25 "

The nil rate band for 08/09 was £312,000

Compute the amount of IHT payable during Joe's lifetime and upon his death.

9 The 7 year cumulation period

In the illustrations so far, apart from illustration 6, all the lifetime transfers, both PET's and CLT's have taken place within the 7 years prior to death and have all therefore been chargeable to IHT on the death of the taxpayer. The earliest / oldest transfers within this period are first to use the nil rate band with the later transfers and / or the chargeable estate at death then being taxed at 40%.

If PET's have been made more than 7 years before the date of death they were neither chargeable when made nor chargeable on death (illustration 6) – they are exempt IHT and are ignored when looking at the 7 year cumulation period used to compute the IHT on transfers that do fall within the 7 years of death and which are therefore chargeable.

The most difficult concept to grasp, however, is how to deal with a CLT made more than 7 years before death. These transfers were chargeable when made using the nil rate band in force at that date but are not chargeable on death as the taxpayer has survived for the required 7 years.

The 7 year cumulation period, however means that when computing the IHT on either a PET or CLT made within the 7 years of death it is necessary to take account of any CLT made within the 7 years prior to it so as to determine how much nil rate band, if any, remains to use against that transfer.

e.g. If an individual dies in January 2012 having made a CLT in June 2003, this CLT will not be taxable on the death as he survived for more than 7 years. If he had also made a PET in August 2008 this will be taxable. In computing the nil rate band available to go against the PET, however, the £325,000 will be reduced by the amount of the June 2003 CLT as it had been made within the 7 years prior to the PET.

Example 2

Dee Ceased died on 1 March 2012 with a Chargeable Estate of £500,000 having made the following lifetime gifts:

1 October 2001	£100,000 cash to son
1 June 2002	£265,000 cash into a trust
1 September 2008	£296,000 cash to daughter

Required:

(a) Calculate the IHT payable on the lifetime gifts when they were made assuming that Dee paid any lifetime tax due

(b) Calculate the IHT payable as a result of Dee's death.

Nil rate bands are as follows:

02/03	£250,000
08/09	£312,000

10 IHT Planning

As the Chargeable Estate of the taxpayer is charged at 40% above the nil rate band, making lifetime transfers is the easiest way an individual may reduce the IHT liability that would otherwise arise upon his death. This of course assumes that the individual has both the capacity and willingness to make such gifts.

If an individual makes regular lifetime gifts to others out of his income these transfers will be exempt as normal expenditure out of income.

Other gifts to individuals will be PET's:

- these will only become chargeable if the donor dies within 7 years of having made them
- if the individual dies within 7 years the value of the transfer is "frozen" at the time of the transfer. It is therefore beneficial to gift in lifetime those assets that are likely to increase in value over time
- if the donor survives for at least 3 years then any IHT payable thereon is reduced by taper relief

Chapter 25

VALUE ADDED TAX – VAT

Questions 1, 2, 4 or 5

1 VAT registration

1.1 Compulsory registration – historical turnover

(a) Trader

Supplies (i.e. sales) may be

- Standard rated – 20%
- Zero rated – 0%
- Exempt

Taxable supplies are those that are either standard rated or zero rated

(b) A trader making taxable supplies must register for VAT if during the previous 12 months the value of taxable supplies exceeded £73,000. However, VAT registration is not required if taxable supplies in the following 12 months will not exceed £71,000. These figures are exclusive of VAT.

(c) HMRC must be notified within 30 days after the end of the period when taxable supplies exceeded £73,000.

(d) The trader will be registered from the beginning of the month following the date for notification, or from an earlier agreed date.

Example 1

Orchid Ltd commenced trading on 1 June 2011. Its sales are as follows:

		£			£
2011	June	3,900	2012	January	4,800
	July	3,800		February	6,000
	August	4,300		March	6,100
	September	5,100		April	5,900
	October	4,700		May	6,200
	November	4,700		June	9,800
	December	4,900		July	11,500

The company's sales are all standard rated.

State

(a) When Orchid Ltd will become liable to compulsory VAT registration

(b) The date by which Orchid Ltd must notify HMRC

(c) The date Orchid Ltd will be registered from

1.2 Compulsory registration – future turnover

(a) A company must also register for VAT if taxable supplies will exceed £73,000 during the following 30 days. This is regardless of any taxable supplies preceding this 30 day period. Again the figure is exclusive of VAT.

(b) HMRC must be notified by the end of the 30 day period

(c) The trader will be registered from the beginning of the 30 day period.

EXAMPLE 2

Tulip Ltd commenced trading on 1 April 2012, and its forecast income is £75,000 per month. The company's sales are all standard rated.

State the date that Tulip Ltd must notify HMRC by and the date from which the company will be registered.

1.3 Voluntary VAT Registration

(a) A trader may decide to voluntarily register for VAT where taxable supplies are below the £73,000 registration limit. This will be beneficial when:

» The company makes zero-rated supplies. Input VAT will be reclaimed, but no VAT will be charged on the zero-rated outputs.

» The company makes supplies to VAT registered customers. Input VAT will be reclaimed, and it should be possible to charge output VAT on top of the pre-registration selling price. This is because the output VAT will be recoverable by the customers.

(b) It will probably not be beneficial to voluntarily register for VAT where customers are members of the general public, as such customers cannot recover the output VAT charged. If selling prices cannot be increased, the output VAT will become an additional cost.

Whether or not output VAT can be passed on to customers will also be an important factor when deciding whether to remain below the VAT registration limit, or whether it is beneficial to accept additional work that results in the limit being exceeded.

Example 3

Vine Ltd has been in business for a number of years. All of its sales are standard rated and are to the general public. The company is not registered for VAT. At present, Vine Ltd's annual income is £70,000.

The company is planning to put up its prices, and this will increase annual income to £75,000. There is no further scope for any price increases. Vine Ltd's standard rated expenses are £4,800 p.a. (inclusive of VAT).

Determine if it is beneficial for Vine Ltd to put up its prices.

1.4 Pre-registration Input VAT

(a) Input VAT incurred prior to registration can be recovered in certain circumstances.

(b) The circumstances in which a trader will be allowed to recover input VAT incurred on goods purchased and services incurred prior to the date of VAT registration are as follows:

- » Inventory & non-current assets must be acquired for business purposes, and not be sold or consumed prior to registration.
- » The goods were not acquired more than four years prior to registration.
- » Services must be supplied for business purposes.
- » The services were not supplied more than six months prior to registration.

1.5 VAT Deregistration

(a) A company stops being liable to VAT registration when it ceases to make taxable supplies. The company must notify HMRC within 30 days, and will then be deregistered from the date of cessation or from an agreed later date.

(b) A company can also request voluntarily VAT deregistration if taxable supplies in next 12 months are less than £71,000

Illustration 1

Iris Ltd has been registered for VAT since 1990, and its sales are all standard rated. The company has recently seen a downturn in its business activities, and sales for the years ended 30 June 2012 and 2013 are forecast to be £60,000 and £49,500 respectively.

- Iris Ltd can request that HMRC cancel its VAT registration because its taxable supplies during the following 12-month period will not exceed £71,000.
- This is provided the fall in the value of taxable supplies is not due to the temporary or permanent cessation of taxable supplies.
- The company's VAT registration will be cancelled from the date on which the request is made or from an agreed later date.

(c) There is a deemed supply of business assets such as plant, equipment and trading inventory when a company ceases to be registered for VAT, unless VAT due is ≤ £1,000

Illustration 2

Daisy is a self-employed builder. She is registered for VAT. The business has been quite successful, and Daisy therefore incorporated her trade into a new limited company on 30 April 2012. All of the business assets were transferred to the new company in return for ordinary share capital.

- No output VAT will have to be charged on the value of inventory and other assets on which VAT has been claimed, since the business is transferred as a going concern.
- The company must be or will be VAT registered
- The company will be able to take over Daisy's VAT registration number.

2 The Tax Point

(a) It is very important to correctly identify the time of supply or tax point, as this determines when output VAT will be due.

(b) The VAT rules that determine the tax point in respect of a supply of goods are as follows:

» The basic tax point is the date goods are made available to the customer or service completed.

» If an invoice is issued or payment received before the basic tax point, then this becomes the actual tax point.

» If an invoice is issued within 14 days of the basic tax point, the invoice date will usually replace that in (a).

3 Output VAT and Input VAT

3.1 Major points

There are several important points regarding output VAT and input VAT as follows:

(a) VAT is only chargeable on the net amount where a discount is offered for prompt payment.

(b) Relief for irrecoverable debts is only available if the debt is over six months old as measured from the time that payment was due.

(c) Input VAT cannot be recovered in respect of business entertainment of UK customers or on motor cars (unless they are used 100% for business purposes).

Example 4

Rose Ltd is registered for VAT, and its sales are all standard rated. The following information relates to the company's VAT return for the quarter ended 31 March 2012:

(1) Standard rated sales amounted to £120,000. Rose Ltd offers its customers a 5% discount for prompt payment.
(2) Standard rated purchases and expenses amounted to £35,640. This figure includes £480 for entertaining UK customers.
(3) On 15 March 2012 the company wrote off irrecoverable debts of £2,000 and £840 in respect of invoices due for payment on 10 May and 5 December 2011 respectively.
(4) On 31 March 2012 the company purchased a motor car at a cost of £16,450 for the use of a salesperson, and machinery at a cost of £21,150. Both these figures are inclusive of VAT. The motor car is used for both business and private mileage.
(5) Unless stated otherwise, all of the above figures are exclusive of VAT.

Calculate the VAT payable for the quarter ended 31 March 2012.

3.2 The refund of VAT

The refund of VAT that has been overpaid is subject to a three-year time limit.

4 Motor Expenses

(a) Input VAT can be recovered where fuel is used for private mileage (either by a sole trader or an employee), but output VAT must be accounted for. Output VAT is calculated according to the cars carbon dioxide emissions rating.

Note: The scale charge, which is VAT inclusive, will be given to you in the examination.

(b) Provided there is some business use, input VAT can be fully recovered in respect of repairs to a motor car.

Example 5

Poppy Plc is to provide one of its directors with a company motor car which will be used for both business and private mileage.
The company will pay for all the running costs of the motor car, including petrol and repairs. The relevant quarterly scale charge is £445 for quarter to 31 March 2012 based on the cars CO_2 emission rating.

State the VAT treatment of the cost of petrol and repairs for the quarter to 31 March 2012.

5 VAT Returns

(a) VAT returns are normally completed on a quarterly basis. Each return shows the total output VAT and total input VAT for the quarter to which it relates. A VAT return must be submitted to HMRC within one month of the end of the relevant quarter. Any VAT payable is due at the same time. All newly registered businesses now have to file their VAT returns on line and pay any VAT due automatically. The deadline for this is extended by seven days.

Illustration 3

For the quarter ended 31 March 2012 Buttercup Ltd had output VAT of £12,400 and input VAT of £7,100.

Buttercup Ltd's VAT return for the quarter ended 31 March 2012 should be submitted by 30 April 2012. VAT of £5,300 (£12,400 - £7,100) is payable, and this is due on 30 April 2012 when the VAT return is submitted. If Buttercup Ltd is a newly registered business they will have until 7 May 2012 to file an online VAT return and pay any VAT that is due.

(b) Because VAT is a self-assessed tax, HMRC make control visits to VAT registered companies. The purpose of a control visit is to provide an opportunity for HMRC to check the accuracy of VAT returns.

(c) If a trader's VAT liability exceeds £2,000,000 over a 12 month period; they must make monthly payments on account of the VAT liability.

6 VAT Invoices

A VAT registered company making a supply to another taxable person must issue a VAT invoice within 30 days of the relevant tax point. A VAT invoice must contain certain information.

Illustration 4

Daffodil Ltd only sells goods, and at present issues sales invoices that show (1) the invoice date and invoice number, (2) the type of supply, (3) the quantity and a description of the goods supplied, (4) Daffodil Ltd's name and address, and (5) the name and address of the customer. The company does not offer any discount for prompt payment.

Daffodil Ltd wants to know the additional information that it will have to show on its sales invoices in order that these are valid for VAT purposes.

The following information is required:

» the VAT registration number;

» the tax point;

» the rate of VAT for each supply;

» the VAT-exclusive amount for each supply;

» the total VAT-exclusive amount;

» the amount of VAT payable.

7 The Default Surcharge

(a) A default occurs if a VAT return is not submitted on time or a payment of VAT is made late.

(b) On the first default, HMRC serve a surcharge liability notice on the trader. The notice specifies a surcharge period, starting on the date of the notice and ending on the twelve-month anniversary of the VAT period to which the default relates.

(c) If the trader has a further default during the surcharge period there are two consequences:

» the surcharge period is extended to the twelve-month anniversary of the VAT period to which the new default relates

» if the default involves the late payment of VAT, then the trader will be subject to a surcharge penalty.

(d) There is therefore no surcharge penalty where a late VAT return involves the repayment of VAT.

(e) The rate of surcharge penalty depends on the number of defaults in the surcharge period:

Default in the surcharge period	*Surcharge as a percentage of the VAT unpaid at the due date*
First	2%
Second	5%
Third	10%
Fourth or more	15%

Surcharge penalties at the rates of 2% and 5% are not made for amounts less than £400.

Where the rate of surcharge is 10% or 15%, a surcharge penalty is the higher of £30 or the actual amount of the calculated surcharge.

(f) In order to escape from the surcharge liability period, a trader must submit four consecutive quarterly VAT returns on time and also pay any VAT due on time.

Example 6

Bluebell Ltd has submitted its VAT returns as follows:

Quarter ended	*VAT paid (£)*	*Date submitted*
30 September 2010	3,100	5 December 2010
31 December 2010	21,300	2 March 2011
31 March 2011	4,300	25 April 2011
30 June 2011	7,600	24 July 2011
30 September 2011	1,900	25 October 2011
31 December 2011	3,200	27 January 2012
31 March 2012	6,900	16 May 2012

Bluebell Ltd paid the VAT due on the same date that the VAT returns were submitted.

State the consequences for Bluebell Ltd of the late submission of the VAT returns.

8 Penalties and Interest

8.1 Failure to notify liability for registration or change in the nature of supplies by persons exempted from registration

- There will be a standard penalty based on a percentage of the VAT lost during the period from when the notification should have been made until it is actually made.
- The actual penalty payable is linked to the taxpayers behaviour.

(a) There will be no penalty where the taxpayer has a reasonable excuse for the failure to notify

(b) There will be a penalty of 30% of the tax unpaid where there is non-deliberate failure to notify

(c) There will be a penalty of 70% of the tax unpaid where there is deliberate failure to notify

(d) There will be a penalty of 100% of the tax unpaid where there is deliberate failure to notify with concealment

However a penalty will be substantially reduced where a taxpayer make a disclosure, especially when this is unprompted by HMRC.

8.2 Errors in a VAT return

A trader that makes an error in a VAT return that results in the underpayment of VAT can be subject to a standard penalty for submission of an incorrect return and penalty interest. There are three different situations:

(a) Net errors of less than a de-minimis can be voluntarily disclosed by a trader. Correction is made by simply entering the errors on the next VAT return. There maybe a penalty for submission of an incorrect return, but no interest charged.

(b) Net errors of more than the de-minimis can be voluntarily disclosed by a trader. In this case the trader must disclose the errors separately to HMRC. Penalty interest will be charged, and there may be a penalty for submission of an incorrect return.

(c) Errors may be discovered as a result of a control visit. Both a penalty for submission of an incorrect return and penalty interest can be charged.

(d) The de-minimus level is the greater of

» £10,000 and

» 1% × turnover (subject to on upper limit of £50,000)

8.3 Submission of an incorrect return leading to:

- an understatement of VAT liability
- a failure of inflated claim for repayment of tax

The amount of penalty is based on the amount of tax understated, but the actual penalty is linked to the taxpayer behaviour, as follows:

(a) there will be no penalty where a taxpayer simply makes a mistake.

(b) there will be a moderate penalty (up to 30% of the understated tax) where a tax payer fails to take reasonable care.

(c) there will be a higher penalty (up to 70% of the understated tax) if the error is deliberate.

(d) there will be an even higher penalty (up to 100% of the understated tax) where there is also concealment of the error.

A penalty will be substantially reduced where the taxpayer makes disclosure, especially unprompted disclosure to HMRC.

Example 7

Blanche Ltd has made an error relating to understated output VAT of £8,500 on the VAT return, for quarter to 31 December 2011. Blanche Ltd has turnover for the quarter of £700,000.

How should this error be disclosed to HMRC and what penalties and interest will be charged by HMRC?

9 The Cash Accounting and Annual Accounting Schemes

(a) The cash accounting and annual accounting schemes are both available to small businesses.

(b) The cash accounting scheme enables a trader to account for output VAT on a cash basis. The scheme will normally be beneficial where a period of credit is given to customers, and it also results in automatic bad debt relief. The disadvantage is that input VAT will only be recovered on a cash basis.

Illustration 5

Violet Ltd gives its customers a 30-day credit period, but pays for most of its expenses in cash. Violet wants to know what conditions must be satisfied before it will be permitted to use the cash accounting scheme, and the implications of using the scheme.

1. Violet Ltd will be able to operate the cash accounting scheme provided its expected taxable turnover for the next 12 months does not exceed £1,350,000.
2. In addition, the company must be up-to-date with its VAT returns and VAT payments.
3. The scheme will result in the company's tax point becoming the date that payment is received from customers.
4. This will delay the payment of output tax, and also provides for automatic bad debt relief should a customer not pay.
5. Since Violet Ltd pays in cash for its expenses, the company's recovery of input VAT will not be affected
6. Stay in scheme until annual taxable turnover reaches £1,600,000

(c) The advantage of the annual accounting scheme is mainly administrative, since a trader only has to make one VAT return each year. Payments on account of the annual VAT liability are normally required.

Illustration 6

Crocus Ltd wants to know the advantages of the annual accounting scheme, and when it will be permitted to join. The company's annual turnover is £450,000.

1. Crocus Ltd can apply to use the annual accounting scheme provided its expected taxable turnover for the next 12 months does not exceed £1,350,000.
2. In addition the company must be up-to-date with its VAT returns.
3. However, Crocus Ltd will only be able to use the annual accounting scheme if it has been VAT registered for 12 months. (Businesses with a turnover of less than £150,000 can join the annual accounting scheme as soon as they register for VAT)
4. Under the scheme only one VAT return is submitted each year. This is due within two months of the end of the year.
5. Nine monthly payments are made on account, with any balancing payment being made with the VAT return or they can choose to pay quarterly instead representing 25% of the estimated liability
6. Stay in scheme until annual taxable turnover reaches £1,600,000

10 Flat rate scheme

(a) The flat rate scheme is optional. It simplifies the way in which small businesses calculate their VAT liability.

(b) The scheme can be used if the expected taxable turnover for the next 12 months does not exceed £150,000. The business can stay in the scheme if turnover is ≤ £230,000. Turnover is determined by the method used to determine the VAT whilst in the scheme, that is cash basis or invoice basis.

(c) Under the flat rate scheme, a business calculates its VAT liability by simply applying a flat rate percentage to total income. This removes the need to calculate and record output VAT and input VAT.

(d) The flat rate percentage is applied to the gross total income figure, with no input VAT being recovered. The percentage varies according to the type of trade that the business is involved in, and will be given to you in the examination.

(e) VAT at the rate of 20% is still treated as being charged where a supply is made to another VAT registered business, and in this case a VAT invoice must still be issued.

Illustration 7

a. Snowdrop Ltd has annual sales of £84,000, all of which are standard rated and are to the general public. The company's standard rated expenses are £4,800 p.a. These figures are inclusive of VAT. The relevant flat rate percentage for Snowdrop Ltd's trade is 15%. Using the normal basis of calculating its VAT liability, Snowdrop Ltd will have to pay VAT as follows:

	£
Output VAT (84,000 × 20/120)	14,000
Input VAT 4,800 × 20/120)	(800)
VAT payable	13,200

If Snowdrop Ltd uses the flat rate scheme then it will pay VAT of £12,600 (84,000 × 15%). There is a VAT saving of £600 (13,200 – 12,600) in addition to the simplified administration. As none of Snowdrop Ltd's customers are VAT registered, there will be no need to issue VAT invoices.

b. Primrose Ltd has annual sales of £80,000, of which 50% are standard rated and 50% are zero-rated. All of the company's sales are to VAT registered businesses. The company's standard rated expenses are £28,200 p.a. These figures are inclusive of VAT. The relevant flat rate percentage for Primrose Ltd's trade is 11%. Using the normal basis of calculating its VAT liability, Primrose Ltd will have to pay VAT as follows:

	£
Output VAT (80,000 x 50% x 20/120)	6,667
Input VAT (28,200 x 20/120)	(4,700)
VAT payable	1,967

If Primrose Ltd uses the flat rate scheme then it will pay VAT of £8,800 (80,000 × 11%). Although the flat rate scheme will result in simplified administration, it is not beneficial as additional VAT of £6,833 (8,800 – 1,967) is payable. Primrose Ltd will still have to issue VAT invoices as its customers are registered for VAT.

11 Group VAT Registration

(a) Two or more companies can register as a group for VAT purposes. They must be under common control of a third company and resident in the UK

(b) The group is treated for VAT purposes as if it were a single company registered for VAT on its own.

(c) A representative member of the group is appointed and this company is responsible for completing and submitting a single VAT return and paying the VAT on behalf of the group.

(d) All companies in the VAT group are jointly and severally liable for any VAT liabilities of the group.

(e) The advantages of group VAT registration are:

» No VAT is accounted for on transactions between group members within the VAT group

» Only one VAT return is submitted for the group; therefore an administrative advantage.

» The group can choose which companies to include or exclude (beneficial to exclude a zero rated company)

(f) The disadvantages of group VAT registration are:

» The limits for Cash and Annual Accounting schemes will apply to the group as a whole and not on an individual company basis.

» Joint and several liability of each company in the group

» Possible administration issues collecting information to be passed on to the representative member.

12 UK companies trading within and outside the European Union.

(a) UK companies frequently trade with companies/individuals within other European Union and non European Union countries. The VAT treatment of exports and imports must be appreciated on these transactions.

(b) Trading with **non European** countries

» Exports

- The supply of goods is zero rated
- The supply of services is outside the scope of UK VAT

» Imports

- The importation of goods involves UK VAT being paid directly to HMRC at point of entry into the UK.
- This is treated as normal input VAT
- Regular importers can defer this payment of VAT under the duty deferment scheme if the UK business provides HMRC with a bank guarantee. The VAT on the import is accounted for on a monthly basis.
- The supply of services from non-European countries generally is treated as above. BUT input VAT is not paid to HMRC at point of entry into the UK (Not goods), the UK customer will account for UK VAT when the service is performed.

(c) Trading with European countries

(i) Exports (Dispatches)

- When a UK VAT registered business supplies goods to another VAT registered business within the EU the supply is zero rated.
- If the customer does not have a VAT registration the UK supplier will charge UK VAT at the rate in force at the time of the supply.
- The same treatment generally applies to the supply of services from a UK VAT registered business to a EU customer.

(ii) Imports (Acquisitions)

- The VAT registered EU supplier will zero rate the transaction and the UK VAT registered business will "self supply" for the VAT on its VAT return.
- 'Self supply' effectively means the UK VAT registered business will calculate UK VAT on the acquisition and declare it as output VAT on the VAT return.
- This VAT can then be reclaimed as input VAT, that is the VAT contras out and there is no VAT cost.
- The only time there will be a VAT cost is if the business makes some exempt supplies as the exempt part of the business cannot reclaim input VAT.
- When a UK VAT registered business acquires goods from another business in the EU, the VAT is accounted for according to the date of acquisition which is the earlier of:
  - the VAT invoice is issued or
  - 15th day of the month following the months in which the goods came into the UK
- If the UK customer is non VAT registered - the EU supplier will charge local country VAT to the UK customer
- The same treatment as above generally applies where a UK customer is supplied with services from an EU supplier.

Example 8

BW Ltd a UK VAT registered UK business acquires £12,000 of goods from its suppliers in the United States of America (Non EU) and £20,000 of goods from its supplier in Germany (EU) in the quarter to 31 March 2012.

In the same VAT quarter BW Ltd exported £50,000 to a VAT registered customer in France (EU) and £10,000 of goods to a non VAT registered individual in Latvia (EU).

Discuss the VAT implications of the above transactions. (All transactions are stated exclusive of VAT)

13 VAT administration

13.1 General

The administration of VAT is dealt with by HMRC. Local offices are responsible for the local administration of VAT and providing advice to registered businesses.

Completed VAT returns are sent to VAT Central Unit at Southend

Businesses may be visited by staff from the local VAT office for a control visit

13.2 Assessments

HMRC may issue assessments of VAT if they believe a trader has failed to make returns or the returns are incorrect or incomplete.

The time limit for issuing an assessment is 4 years after the end of a VAT period (this is extended to 20 years in cases of deliberate failure to make returns or deliberate incorrect or incomplete returns)

13.3 Appeals

The Revenue and Customs Prosecution Office (RCPO) provides a method of dealing with disputes. Provided the returns and payments shown thereon have been made, appeals can be heard.

An appeal must be lodged within 30 days of any decision by HMRC

A new tribunal system has been introduced for all taxes, including VAT.

Before an appeal is heard by a tribunal, there is the option for the taxpayer to request a review of the decision by a HMRC review officer. The decision by the review officer can still be appealed.

If there appeal goes to tribunal then the case will be allocated to one of four tracks. This will depend on the issues and the amount of tax at stake.

(a) the "paper" track - will hear the simplest appeals, such as an appeal against a fixed penalty and the case will be normally decided by the tribunal without a hearing

(b) The "basic" track will involve a hearing but the exchange of documents beforehand will be minimum.

(c) The "standard" track will involve cases that are more detailed in case management and formality.

(d) The "complex" track will be for long or complex cases or those that involve a large tax sum or important principle.

The new tribunal system consists of two tribunals.

» First-tier tribunal - deals with all but the most complex of cases

» Upper tribunal - deals with the more complex cases and hears appeals against the decisions of the first tier-tribunal.

13.4 Information and Inspection powers

A single regime of HMRC information & inspection powers covers income tax, corporation tax, capital gains tax, PAYE and VAT

HMRC can request information from taxpayers by making a written information notice. Requests to third parties for information must normally either be agreed by the tax payer or approved by the first-tier tribunal.

HMRC have powers to enter and inspect a taxpayer business premises so they can inspect business records and assets.

Chapter 26

SELF ASSESSMENT AND PAYMENT OF TAX FOR COMPANIES

Question 2, 4 or 5

1 Corporation tax – payment dates

1.1 Notification of chargeability

A company falling within the scope of corporation tax for the first time must notify HMRC when its first accounting period begins, within 3 months of the start of the accounting period. Failure to notify chargeability to tax within 12 months of the end of the accounting period will lead to a standard penalty based on a percentage of the tax unpaid 12 months after the end of the accounting period. The standard penalty is discussed in chapter 25, (VAT) 8.1.

1.2 Payment of tax

(a) Companies pay tax by self assessment

(b) Estimated tax is payable 9 months and one day after the end of each accounting period (due date), with provisions for quarterly instalment payments for 'large' companies.

(c) Interest due to the HMRC on tax paid late will run from the due date to the date of payment at a rate of 3.0% per annum.

(d) Interest on overpayments of tax will run from the later of the due date or the date tax was actually paid at a rate of 0.5% per annum.

(e) Under self assessment interest on tax paid late will be deductible against interest receivable.

Interest received on overpaid corporation tax will be taxable as Interest receivable.

1.3 Quarterly Instalments

(a) Quarterly instalments apply to large companies.

(b) A large company is one paying the main rate of corporation tax.

(c) The instalments are based on the estimated current year's liability.

(d) The four quarterly instalments will be made in months 7, 10, 13 and 16 following the start of the accounting period. The instalments are due on the 14th of the month.

(e) Transitional relief is available for companies becoming large in an accounting period. Quarterly payments are not required if

» current profits do not exceed £10 million

and

» the company was not large in previous year.

Example 1

Photo plc has Taxable Total Profits for the year ended 31 December 2011 of £2M, its lowest profit figure for several years.

Show how the liability for the year ended 31 December 2011 will be settled.

2 Corporation tax return

(a) Companies that do not receive a tax return are required to notify HMRC if they have income or chargeable gains on which tax is due. This must be done within 12 months from the end of the accounting period in which the liability arises, otherwise the standard penalty for late notification will arise (as above 1.1).

(b) Complete accounts and computations are due 12 months after the end of the Statement of Financial Position date (this is called the filing date). If the accounts and computations are filed late there is a fixed penalty of £100. (This becomes £500 if it is the third consecutive time the return is late).

The return must include a self assessment of the amount of corporation tax payable for that period.

With effect from 1 April 2011 returns filed for accounting periods ended after 31 March 2010 must now be made online and any corporation tax paid electronically.

The HMRC software if used will now compute the amount of corporation tax payable.

The tax computation and accounts must be submitted online using inline eXtensible Business Reporting Language (iXBRL). This is the global standard for reporting business information in electronic format using tags that can be read by a computer.

Small companies with straightforward accounts and tax computations may use the HMRC software but other companies must use:

- commercial software that automatically inserts tags

- a tagging service

- conversion software that allows tags to be added to accounts and computations

(c) Returns may be subject to a random or specific enquiry by the HMRC. Written notice of the Inland Revenue's intention to make an enquiry is given within 12 months from the date the return is received by HMRC.

(d) The penalty increases to £200 if the self-assessment tax return is more than three months late. (This becomes £1,000 if it is the third consecutive time the return is late).

(e) There will be an additional corporation tax related penalty of 10% of the tax unpaid 6 months after the return is due, if the self-assessment tax return is more than six months late, or 20% of the tax unpaid 6 months after the return is due, if more than 12 months late.

(f) HMRC may amend a return to correct obvious error within nine months of the day the return is filed. A company may amend a return within 12 months of the filing date.

3 Claims

(a) Wherever possible claims must be made on a tax return or on an amendment to it and must be quantified at the time the return is made.

(b) If a company believes it has made an error in a return, an error or mistake claim may be made within four years from the end of the accounting period.

(c) Other claims must be made within four years of the end of the accounting period unless a different time limit specified.

4 Records

(a) Companies must keep records until the latest of
- » six years from the end of the accounting period
- » the date any enquiries are completed
- » the date after which enquiries may not be commenced

(b) All businesses records and accounts including contracts and receipts must be kept

(c) Failure to keep records can lead to a penalty or up to £3,000 for each accounting period affected

5 Enquiries

(a) HMRC may enquire into a corporation tax return provided that they first give written notice that they are going to enquire.

(b) The notice must be given within a year after the later of:
- » 12 months following the date the return is actually received by HMRC
- » If the return is late, 12 months following the relevant quarter days ie 31/1, 30/4, 31/7, 31/10

(c) An enquiry may be made due to:
- » A suspicion income is understated
- » Deductions being incorrectly claimed
- » Other information in HMRC's possession
- » Being part of a random review process

6 Determinations and Discovery assessments

(a) If a return is not delivered by the filing date, HMRC may issue a determination of the tax payable within 3 years of the filing date. There is no appeal against it.

(b) If HMRC believe that not enough tax has been assessed for an accounting period they can make a discovery assessment to collect the tax.

(c) A discovery assessment can only be made if:

HMRC could not reasonably be expected to have been aware of a loss of tax and are supplied with information to draw their attention to a contentious matter such as the use of a valuation or estimate. HMRC can raise an assessment within 4 years from the end of the accounting period; this is extended to 6 years if there is a careless error or 20 years if there is a deliberate error or failure to notify a chargeability to tax.

7 Appeals and Disputes

(a) The company can appeal against amendments to the corporation tax return.

(b) The appeal must be normally be made within 30 days of the amendment and must state the grounds for appeal.

(c) The appeals procedure is as per VAT - see chapter 25.

8 Penalties for incorrect returns

The amount of penalty is based on the amount of tax understated, but the actual penalty payable is linked to the taxpayer's behaviour, as follows:

(i) there will be no penalty where a taxpayer simply makes a mistake.

(ii) there will be a moderate penalty (up to 30% of the understated tax) where a tax payer fails to take reasonable care.

(iii) there will be a higher penalty (up to 70% of the understated tax) if error is deliberate.

(iv) there will be an even higher penalty (up to 100% of the understated tax) where there is also concealment of the error.

A penalty will be substantially reduced where the taxpayer makes disclosure, especially unprompted disclosure to HMRC.

9 Information and Inspection powers

These are as per VAT - see chapter 25.

Chapter 27

SELF-ASSESSMENT AND PAYMENT OF TAX FOR INDIVIDUALS

Question 1, 4 or 5

1 Due dates for payment

Type of income		*Dates for 2011/12 assessment*
Trading income Property Business profit	due	31/1/12 Payment on account (50% of 11/12 income tax payable by self assessment) 31/7/12 Payment on account (50% of 11/12 income tax payable by self assessment) 31/1/13 Balancing payment
Employment Income	due	14 days after the end of the tax month (PAYE)
Savings income Dividend	due	31/1/13 if higher rate liability

No payments on account are due if the previous years tax payable by self assessment was ≤ £1,000 **or** if more than 80% of the tax liability for the previous year was deducted at source.

Class 4 NIC is payable at the same time as the income tax on trading income.

Note, the tax payer can claim to reduce payments on account at any time before 31 January following the tax year. This would be done if they expected actual income tax and class 4 NIC is expected to be less than the previous year. If the claim is incorrect, penalties and interest will be charged.

The maximum penalty is the difference between the amounts actually paid on account and the amounts that should have been paid on account.

Example 1

Janice is self employed, her tax liability for 2010/11 was as follows:

Total Income tax liability	12,000
Less tax deducted at source	(1,000)
Income tax payable by self assessment	11,000
Class 4 NIC	2,000
	13,000

For 2011/12 her total income tax liability was £14,000 with £2,000 being deducted at source. She had a class 4 NIC liability of £2,500 and a capital gains tax liability of £1,700

Show how her 2011/12 liability will be settled and determine the first payment on account for 2012/13

2 Interest on tax

2.1 Late payments

(a) Interest is charged on late payment of tax at a rate of 3.0%.

For 2011/12

Payment on account:	Interest runs from 31/1/12 or 31/7/12
Other payments:	Interest runs from 31/1/13

(b) Interest charged is not tax deductible for individuals

(c) In addition late payments of tax will attract a penalty as follows:

» If tax is paid more than one month late there will be a penalty of 5% of the amount due.

» Further penalties of 5% will be charged where tax is unpaid after six months and again twelve months.

Note:

The penalties only apply to the balancing payment, and not payments on account. They therefore cover income tax, Class 4 NIC and capital gains tax paid late.

2.2 Repayment

If tax is repaid, HMRC pay interest at a rate of 0.5% p.a. from 31 January, or if later, the date of original payment.

Interest received is not taxable for an individual.

2.3 Capital gains tax

(a) Capital gains tax is payable on 31 January after tax year – 31 January 2013 for 2011/12.

(b) There are no payments on account for capital gains tax.

(c) Under self assessment, gains must be reported to the HMRC within 6 months of the end of the tax year in which the asset is sold. (ie by 5 October)

3 Notification of chargeability

An individual who receives a source of income subject to income tax or capital gains tax must notify HMRC by 5th October following the end of the tax year the source arose.

Failure to notify HMRC will result in a standard penalty based on a percentage of tax unpaid on 31 January following the end of the tax year - see chapter 25 (VAT).

4 Self assessment tax return

(a) Individuals complete their own tax return. The first part details income and capital gains for the tax year, the second part shows the calculation of the income tax liability.

(b) The tax payer has the choice of filing a paper return or filing electronically online. The dates by which a return must be filed depends on the method used.

(c) All completed and signed paper returns must be normally filed by 31 October following the end of the tax year

(d) All online electronic returns must be filed by 31 January following the end of the tax year.

(e) The relevant dates for a 2011/12 return are therefore 31 October 2012 (paper returns) and 31 January 2013 (electronic returns)

(f) The 31 October date will also be the deadline for a taxpayer to complete a paper return if they wish HMRC to prepare a self assessment on their behalf. For tax returns filed online a self assessment is automatically provided as part of the online filing service.

(g) The 31 January following the end of the tax year is known as the "filing date" regardless of whether the return is filed on paper or electronically. This must be distinguished from the date on which the return is filed. (Known as the "actual filing date")

(h) HMRC can amend a tax payer self assessment to correct obvious errors or mistakes within nine months of receiving the return.

(i) The tax payer can give notice to an officer to amend his tax return within 12 months of the "filing date" regardless of whether the return is paper based or filed electronically.

5 Late filing of returns

- There will be an initial penalty of £100 if the return is filed after the 'filing date'
- If a return is more than three months late then there will be a daily penalty of £10 per day (for a maximum of 90 days)
- If a return is more than six months late a penalty of 5% of the tax due on the return will be charged (subject to a minimum of £300).
- If a return is more than twelve months late a further penalty of 5% of the tax due can be charged, although a higher percentage will be charged if the failure to submit is deliberate.

6 Records

(a) Records must be retained until five years after the filing date, which is 31 January 2018 for the year 2011/12 if the tax payer is a business or has properties to let. However records must be retained for only one year after the filing date, which is 31 January 2014 for the year 2011/12 if not in business.

(b) Retaining copies of original documents except originals of documents showing tax deducted at source must be kept

(c) A failure to retain records can result in a penalty of up to £3,000.

The maximum penalty will only be charged in serious cases

7 Claims

(a) All claims and elections which can be made in a tax return must be made in this manner if a return has been issued.

(b) The time limit for making a claim is 4 years from the end of the tax year, unless a different limit is specifically set.

8 Error or mistake claim

The time limit is 4 years from the end of the tax year to correct errors in a tax return when the tax would otherwise be overcharged, for 2011/12 this will be 5 April 2016.

9 Enquiries into returns

HMRC can enquire into a taxpayer return by written notice by the later of:

(a) 12 months following the date the return is actually filed.

(b) If the return is late (ie after the "filing date"), 12 months following the relevant quarter days ie 31/1, 30/4, 31/7, 31/10

(c) An enquiry may be made due to:

» A suspicion that income is understated
» Deductions being incorrectly claimed
» Other information in HMRC's possession
» Being part of a random review process

10 Determinations and discovery assessments

(a) If a return is not delivered by the filing date, HMRC may issue a determination of the tax payable within three years of the filing date. There is no appeal against it.

(b) If HMRC believe that not enough tax has been assessed for an accounting period they can make a discovery assessment to collect the tax.

(c) A discovery assessment can only be made if:

HMRC could not reasonably be expected to have been aware of a loss of tax and are supplied with information to draw their attention to a contentious matter such as the use of a valuation or estimate. HMRC can raise an assessment within 4 years from end of the tax year if there is no careless or deliberate behaviour by the taxpayer. This increases to 6 years from the end of the tax year if there is careless behaviour, and 20 years from the end of the tax year if there is deliberate error or failure to notify a chargeability to tax.

11 Appeals & Disputes

The individual can appeal against amendments to the income tax return.

The appeal must normally be made within 30 days of the amendment.

The appeal must state the grounds of appeal.

The process of the appeals procedure is as per VAT chapter 25.

12 Penalties for incorrect returns

The amount of penalty is based on the amount of tax understated, but the actual penalty payable is linked to the taxpayer's behaviour, as follows:

(i) there will be no penalty where a taxpayer simply makes a mistake.
(ii) there will be a moderate penalty (up to 30% of the understated tax) where a tax payer fails to take reasonable care.
(iii) there will be a higher penalty (up to 70% of the understated tax) if error is deliberate.
(iv) there will be an even higher penalty (up to 100% of the understated tax) where there is also concealment of the error.

A penalty will be substantially reduced where the taxpayer makes disclosure, especially unprompted disclosure to HMRC.

13 Income Tax Fraud

There is a statutory offence of evading income tax. The penalty may be up to seven years in prison or an unlimited fine or both

14 Information and Inspection powers

This is as per chapter 25 (VAT).

Paper F6

ANSWERS TO EXAMPLES

Chapter 1

Answer to Example 1

(a) Income Tax and NIC - both direct taxes
(b) Corporation tax on profits and NIC in respect of employees - both direct taxes. Employees pay income tax and NIC on salary
(c) Capital gains tax - direct tax
(d) The business is charged VAT – indirect tax
(e) Corporation tax - direct tax
(f) Inheritance tax - direct tax

Chapter 2

Answer to Example 1

Mr Smith Income tax computation 2011/12

	Non-savings	*Total*
	£	*£*
Employment Income	50,000	50,000
Total income	50,000	50,000
Less: Personal Allowance	(7,475)	(7,475)
Taxable income	42,525	42,525
Tax calculation:		
35,000 × 20%	7,000	7,000
7,525 × 40%	3,010	3,010
42,525		
Tax liability	10,010	10,010
Less: tax suffered at source (PAYE)	(10,010)	(10,010)
Tax payable	–	–

Answer to Example 2

Billy Income Tax Computation 2011/12

	Non-savings income	*Savings income*	*Total*
	£	*£*	*£*
Trading income	25,000		25,000
Bank Deposit interest 8,000 × 100/80		10,000	10,000
Total Income	25,000	10,000	35,000
Less: Personal Allowance	(7,475)		(7,475)
Taxable Income	17,525	10,000	27,525
Tax calculation:			
Non Savings			
17,525 @ 20% =			3,505
Savings			
10,000 @ 20%			2,000
Tax liability			5,505
Less tax deducted @ source:			
Bank deposit interest 10,000 @ 20%			(2,000)
Tax payable			3,505

Note: The starting rate for savings income is not applicable as non savings income exceeds £2,560

Answer to Example 3

Billy Income Tax Computation 2011/12

	Non-savings income	Savings income	Total
	£	£	£
Trading income	25,000		25,000
Bank Deposit interest 16,000 × 100/80		20,000	20,000
Total Income	25,000	20,000	45,000
Less: Personal Allowance	(7,475)		(7,475)
Taxable income	17,525	20,000	37,525

Tax calculation:	
Non Savings	
17,525 @ 20% =	3,505
Savings	
17,475 @ 20% =	3,495
2,525 @ 40% =	1,010
20,000	
Tax liability	8,010
Less tax deducted @ source:	
Bank deposit interest 20,000 @ 20%	(4,000)
Tax payable	4,010

Note: The starting rate for savings income is not applicable as non savings income exceeds £2,560

Answer to Example 4

Molly Income Tax Computation 2011/12

	Savings	Total
	£	£
Bank interest 16,000 × 100/80	20,000	20,000
Total Income	20,000	20,000
Less: Personal Allowance	(7,475)	(7,475)
Taxable income	12,525	12,525

Tax calculation:	
Savings	
2,560 @ 10% =	256
9,965 @ 20%	1,993
12,525	
Income Tax liability	2,249
Less tax deducted @ source:	
Bank Deposit interest £20,000 @ 20%	(4,000)
Income Tax repayable	(1,751)

Answer to Example 5

Molly Income Tax Computation 2011/12

	Non-savings income	Savings income	Total
	£	£	£
Trading income	8,000		8,000
Bank interest 16,000 × 100/80		20,000	20,000
Total Income	8,000	20,000	28,000
Less: Personal Allowances	(7,475)		(7,475)
Taxable income	525	20,000	20,525

Tax calculation	
Non Savings	
525 @ 20% =	105
Savings	
(2,560 – 525 = 2,035)	
2,035 @ 10% =	203
17,965 @ 20% =	3,593
20,000	
Income tax liability	3,901
Less tax deducted at source	
Bank deposit interest 20,000 @ 20%	(4,000)
Income Tax Repayable	99

Answer to Example 6

Daisy Income Tax Computation 2011/12

	Non-savings income	*Savings income*	*Dividends*	*Total*
	£	£	£	£
Employment Income	15,000			15,000
Bank deposit interest 8,000 × 100/80		10,000		10,000
Dividends 1,800 × 100/90			2,000	2,000
Total Income	15,000	10,000	2,000	27,000
Less: Personal Allowance	(7,475)			(7,475)
Taxable income	7,525	10,000	2,000	19,525

Tax calculation:	
Non Savings	
7,525 @ 20% =	1,505
Savings	
10,000 @ 20% =	2,000
Dividends	
2,000 @ 10% =	200
Income Tax liability	3,705
Less tax deducted @ source	
Dividends 2,000 @10%	(200)
Bank Deposit Interest 10,000 @ 20%	(2,000)
PAYE	(1,505)
Income Tax payable	–

Note: The starting rate for savings income is not applicable as non savings income exceeds £2,560

Answer to Example 7

Daisy Income Tax Computation 2011/12

	Non-savings income	*Savings income*	*Dividends*	*Total*
	£	£	£	£
Employment Income	35,000			35,000
Bank interest 9,600 × 100/80		12,000		12,000
Dividends 1,800 × 100/90			2,000	2,000
Total Income	35,000	12,000	2,000	49,000
Less: Personal Allowance	(7,475)			(7,475)
Taxable income	27,525	12,000	2,000	41,525

Tax calculation:

		£
Non savings		
27,525 × 20%		5,505
Savings		
7,475 × 20%		1,495
4,525 × 40%		1,810
12,000		
Dividends:		
2,000 × 32.5%		650
Income Tax liability		9,460
Less: Tax suffered at source		
Dividend income (2,000 × 10%)		(200)
Bank deposit interest (£12,000 × 20%)		(2,400)
PAYE		(5,705)
Income Tax Payable		1,155

Note: The starting rate for savings income is not applicable as non savings income exceeds £2,560

Answer to Example 8

Mike Income Tax Computation 2011/12

	Non-savings	*Total*
	£	£
Employment income	108,000	108,000
Total income	108,000	108,000
Less: Personal Allowance (W1)	(3,475)	(3,475)
Taxable Income	104,525	104,525

Income Tax calculation:	
Non Savings	
35,000 @ 20% =	7,000
69,525 @ 40% =	27,810
104,525	
Income Tax Liability	34,810
Less: Tax deducted at source	
PAYE	(33,130)
Income tax Payable	1,680

(W1) Standard personal allowance	7,475
Less ½ [108,000 – 100,000]	(4,000)
Revised Personal Allowance	3,475

Answer to Example 9

Ken Income Tax Computation 2011/12

	Non-savings	*Savings*	*Dividends*	*Total*
	£	£	£	£
Trading income	130,000			130,000
Bank interest 32,000 × 100/80		40,000		40,000
Dividends 32,400 × 100/90			36,000	36,000
Total Income	130,000	40,000	36,000	206,000
Less: Personal allowance (W1)	(–)			(–)
Taxable Income	130,000	40,000	36,000	206,000

Income Tax calculation:	
Non Savings	
35,000 @ 20% =	7,000
95,000 @ 40% =	38,000
130,000	
Savings	
20,000 @ 40% =	8,000
20,000 @ 50% =	10,000
40,000	
Dividends	
£36,000 × 42.5%	15,300
Income Tax Liability	78,300
Less: Tax deducted at source	
Dividends 36,000 × 10%	(3,600)
Bank Interest 40,000 × 20%	(8,000)
Income tax Payable	66,700

(W1)	Standard personal allowance	7,475
	Less ½ [206,000 – 100,000]	(53,000)
	Restricted to	Nil

[Alternatively as adjusted net income > £114,950 the personal allowance is reduced to Nil]

Answer to Example 10

Personal Age Allowance	9,940
Less	
½ [25,000 – 24,000]	(500)
Revised Age Allowance	9,440

Answer to Example 11

Personal Age Allowance	9,940
Less ½ [30,000 – 24,000]	(3000)
Revised Age Allowance	6,940

However the age allowance cannot fall below £7,475 (standard) so his allowance is **£7,475**

Answer to Example 12

James Income Tax Computation 2011/12

	Non-savings	*Savings*	*Total*
	£	*£*	*£*
Trading income	102,000		102,000
Bank interest 3,200 × 100/80		4,000	4,000
Total Income	102,000	4,000	106,000
Less: Personal allowance (W1)	(4,475)		(4,475)
Taxable income	97,525	4,000	101,525

Income Tax calculation:	
Non Savings	
35,000 @ 20% =	7,000
62,525 @ 40% =	25,010
97,525	
Savings (4,000 × 40%)	1,600
Income Tax Liability	33,610
Less: Tax deducted at source	
Bank Interest 4,000 × 20%	(800)
Income tax Payable	32,810

(W1)	Personal age allowance	9,940
	Less ½ [106,000 – 24,000]	(41,000)
	Revised to standard personal allowance	7,475

As adjusted net income exceeds £100,000, the standard personal allowance is restricted

Standard personal allowance	7,475
Less ½ [106,000 – 100,000]	(3,000)
Revised personal allowance	4,475

Answer to Example 13

Kathy Income Tax Computation 2011/12

	Non-savings	*Total*
	£	*£*
Trading income	50,000	50,000
Total income	50,000	50,000
Less reliefs – Qualifying interest	(1,000)	(1,000)
Net Income	49,000	49,000
Less: Personal Allowances	(7,475)	(7,475)
Taxable Income	41,525	41,525

Tax calculation:	
Non Savings	
35,000 @ 20% =	7,000
6,525 @ 40% =	2,610
41,525	
Income Tax Liability	9,610

Answer to Example 14

Elliot Income Tax Computation 2011/12

	Non-savings	*Total*
	£	*£*
Trading income	48,000	48,000
Total Income	48,000	48,000
Less: Personal Allowance	(7,475)	(7,475)
Taxable income	40,525	40,525

Tax calculation	
Non Savings	
37,000 (W1) @ 20% =	7,400
3,525 @ 40% =	1,410
40,525	
Income Tax Liability	8,810

(W1) 35,000 + (1,600 × $^{100}/_{80}$) = 37,000

Answer to Example 15

Thomas Income Tax Computation 2011/12

	Non-savings	*Total*
	£	*£*
Trading income	160,000	160,000
Total Income	160,000	160,000
Less: Personal Allowance (W1)	(–)	(–)
Taxable income	160,000	160,000

Income Tax Non savings

	Non Savings	
(W3)	43,000 @ 20% =	8,600
(W4)	115,000 @ 40% =	46,000
	2,000 @ 50% =	1,000
	160,000	
	Income Tax Liability	55,600

(W1)	Standard personal allowance	7,475
	less	
	½ [(W2)152,000 – 100,000]	(26,000)
	Revised Personal Allowance	Nil

(W2)	Net Income	160,000
	Less Gross gift aid payment (6,400 × 100/80)	(8,000)
	Adjusted Net income	152,000

(W3) 35,000 + (6,400 × 100/80) = 43,000
150,000 + (6,400 × 100/80) = 158,000
(W4) 158,000 – 43,000 = 115,000

Answer to Example 16

Kerry Income Tax Computation 2011/12

	Non-savings	*Savings*	*Dividends*	*Total*
	£	*£*	*£*	*£*
Trading income	102,000			102,000
Bank interest 3,200 × 100/80		4,000		4,000
Dividends 2,700 × 100/90			3,000	3,000
Total Income	102,000	4,000	3,000	109,000
Less reliefs:				
Qualifying interest	(3,000)			(3,000)
Net Income	99,000	4,000	3,000	106,000
Less: Personal allowances (W1)	(7,475)			(7,475)
Taxable income	91,525	4,000	3,000	98,525

Income Tax	
Non Savings	
(W3) 41,000 @ 20% =	8,200
50,525 @ 40% =	20,210
91,525	
Savings	
4,000 × 40% =	1,600
Dividends	
3,000 × 32.5%	975
Income Tax Liability	30,985
Less: Tax deducted at source	
Dividends	
3,000 × 10%	(300)
Bank Interest	
4,000 × 20%	(800)
Income tax payable	29,885

(W1)	Standard personal allowance	7,475
	Less ½ [(W2)100,000 – 100,000]	(–)
	Revised Personal Allowance	7,475
(W2)	Net Income	106,000
	Less Gross gift aid payment (4,800 × $\frac{100}{80}$)	(6,000)
	Adjusted Net income	100,000

(W3) 35,000 + (4,800 × $\frac{100}{80}$) = 41,000
150,000 + (4,800 × $\frac{100}{80}$) = 156,000

Answer to Example 17

If Elton transfers a 5% (say) holding in his property to David, they will automatically be treated as jointly owning the property for tax purposes and each will be taxed on 50% of the income. Elton's tax liability will be reduced by £4,000 and David's liability will increase to:

	£
	10,000
Less: Personal Allowance	(7,475)
	2,525
2,525 @ 20%	505
Tax liability	505

This will save the couple £3,495 (4,000 - 505)

Chapter 3

Answer to Example 1

The rent assessable in each case is the rent due for the period 1 July 2011 to 5 April 2012
Expenses relating to the same period are deductible.

	£	£
Rent due $\frac{9}{12}$ × 6,000		4,500
Expenses:		
Redecoration	300	
Repairs	500	
		800
Property Income for 2011/12		3,700

Answer to Example 2

	£	£
Rent due £300 × 12		3,600
Expenses		
Bad debt – June 2011 rent	300	
Insurance ($\frac{3}{12}$× £420) + ($\frac{9}{12}$ × £480)	465	
Drain clearance	380	
Redecoration	750	
Wear and tear (10% × £3,300)	330	
		(2,225)
Property Income for 2011/12		1,375

The garage is an improvement, not a repair, and is therefore not deductible.

Answer to Example 3

(a) Ordinary calculation

Gross rent (85 × 52)	4,420
Less: expenses	(120)
Wear & tear (10% × 4,420)	(442)
Property Income	3,858

(b) Alternative calculation

Gross rent (85 × 52)	4,420
Less: Rent a Room Relief	(4,250)
Property Income	170

Barbara should elect for the alternative treatment in 2011/12 by 31 January 2014

Answer to Example 4

	£
Premium $\frac{51 - 20}{50} \times 60{,}000$	37,200
Rent ($\frac{9}{12} \times 5{,}000$)	3,750
Property Income	40,950

Answer to Example 5

Relief available = $\frac{£37{,}200}{20}$ = **£1,860 p.a.**

Chapter 4

Answer to Example 1

Tax adjusted trading profit for the year ended 31 May 2012

	£	£
Net profit as per accounts		30,200
Add: Items debited in P&L – not allowed for tax purposes		
Depreciation	4,760	
Light and heat (40% × £1,525)	610	
Motor expenses (9,000/12,000 × £4,720)	3,540	
Personal tax work	250	
Purchase of new shop	1,200	
Rent and rates (40% × £3,900)	1,560	
Decorating private flat	1,050	
Gift of food hampers	640	
Donation to national charity	100	
Excessive remuneration to Jeremy's wife		
(£15,500 – £11,000)	4,500	
Own consumption	650	
		18,860
Adjusted trading profit		49,060
Less: Capital allowances (given)		(13,060)
Tax adjusted trading profit		36,000

Chapter 5

Answer to Example 1

Accounting period to 31 March 2012	*General Pool*	*Allowances*
	£	£
WDV b/f	6,000	
Less Disposal – 3/4/10 (limited to cost)	(2,000)	
	4,000	
WDA – 20%	(800)	800
WDV c/f	3,200	800

Answer to Example 2

Accounting period to 31 March 2012

		General Pool	Allowances
	£	£	£
WDV b/f		16,000	
Additions qualifying for AIA			
Plant	116,200		
AIA (Maximum)	(100,000)		100,000
		16,200	
		32,200	
Disposal		(4,000)	
		28,200	
WDA @ 20%		(5,640)	5,640
			105,640
WDV c/f		22,560	

Answer to Example 3

Accounting period 9m to 31 December 2011

		General Pool	Allowances
	£	£	£
TWDV b/f		12,000	
Additions qualifying for AIA			
Machinery	80,000		
AIA (Maximum 100,000 × 9/12)	(75,000)		75,000
Balance qualifying for WDA		5,000	
Disposal		(6,000)	
		11,000	
WDA @ 20% × 9/12		(1,650)	1,650
			76,650
WDV c/f		9,350	

Answer to Example 4

Accounting period to 31 March 2012

		General Pool	Expensive car	Special Rate Pool	Allowances
		£	£	£	£
WDV b/f		22,700	15,600		
Additions qualifying for AIA					
Plant	24,800				
AIA	(24,800)				24,800
Other additions					
Motor car (130g/km)		11,200			
Motor car (170 g/km)				14,100	
		33,900	15,600	14,100	
WDA @ 20%		(6,780)			6,780
WDA restricted (max)			(3,000)		3,000
WDA @ 10%				(1,410)	1,410
Additions qualifying for 100% FYA					
Motor car (105g/km)	14,400				
FYA @ 100%	(14,400)				14,400
					50,390
WDV c/f		27,120	12,600	12,690	

Answer to Example 5

	Expensive car	Allowances
	£	£
WDV b/f	13,000	
Disposal	(8,000)	
	5,000	
Balancing allowance	(5,000)	5,000
	–	

Answer to Example 6

	Expensive car	Allowances
	£	£
WDV b/f	13,000	
Disposal (restricted to cost)	(19,000)	
	(6,000)	
Balancing charge	6,000	(6,000)
	–	

A net balancing charge from the capital allowance computation would be added to the adjusted trading profit of the accounting period.

Answer to Example 7

Year ended 31 March 2012

	General Pool	Allowances
	£	£
WDV b/f	4,000	
Addition – 1/10/11	2,000	
	6,000	
Less Disposal 1/04/11	(8,600)	
	(2,600)	
Balancing charge	2,600	(2,600)

Answer to Example 8

Year ended 31 March 2012

	General Pool	Allowances
	£	£
WDV b/f	12,000	
Addition – 1/6/11	4,000	
	16,000	
Less Disposals – 31/3/12	(5,000)	
	11,000	
Balancing allowance	(11,000)	11,000
	–	

Answer to Example 9

Accounting period to 31 March 2012

	£	*General Pool* £	*Short life Asset* £	*Allowances* £
WDV b/f		16,000		
Additions qualifying for AIA				
Machinery	120,000			
Photocopier	4,000			
	124,000			
AIA (Maximum)	(100,000)			100,000
		20,000	4,000	
		36,000	4,000	
WDA @ 20%		(7,200)		7,200
WDA @ 20%			(800)	800
WDV c/f				108,000
		28,800	3,200	

Accounting period to 31 March 2013

	General Pool £	*Short life Asset* £	*Allowances* £
WDV b/f	28,800	3,200	
Disposal		(1,500)	
	28,800	1,700	
WDA @ 20%	(5,760)		5,760
Balancing allowance		(1,700)	1,700
			7,460
WDV c/f	23,040	–	

Answer to Example 10

Year ended 5 April 2012

	£	*General Pool* £	*70% Expensive car (1)* £	*70% Private use Asset (2)* £	*Allowances* £
WDV b/f		21,200	13,600		
Additions Qualifying for AIA					
Plant	6,600				
AIA	(6,600)				6,600
Other additions					
Motor car (CO_2 140g/km)		10,600			
Motor car (CO_2 180g/km)				16,000	
Disposal			(9,400)		
		31,800	4,200	16,000	
WDA @ 20%		(6,360)			6,360
Balancing allowance			(4,200) × 70%		2,940
WDA @ 10%				(1,600) × 70%	1,120
					17,020
WDV c/f		25,440	–	14,400	

ANSWERS TO EXAMPLES

ANSWER TO EXAMPLE 11

Accounting period to 31 March 2012

		General Pool	Special Rate Pool	Allowances
	£	£	£	£
WDV b/f		22,000		
Additions qualifying for AIA				
Long life asset	160,000			
AIA (Maximum)	(100,000)			100,000
			60,000	
Additions qualifying for AIA				
Machinery	45,000			
AIA	(–)			
		45,000		
Other additions				
Motor car (emissions 145g/km)		8,000		
		75,000	60,000	
WDA @ 20%		(15,000)		15,000
WDA @ 10%			(6,000)	6,000
				121,000
WDV c/f		60,000	54,000	

ANSWER TO EXAMPLE 12

		General Pool	Allowances
	£	£	£
WDV b/f		750	
Additions Qualifying for AIA	10,000		
AIA	(10,000)	–	10,000
Small pool WDA		(750)	750
WDV c/f		–	10,750

Answer to Example 13

Accounting period to 31 March 2012

	£	*General Pool* £	*Special rate pool* £	*80% Expensive car* £	*Allowances* £
WDV b/f		22,700		14,000	
Additions Qualifying for AIA					
Thermal insulation for business building	18,800				
AIA	(18,800)				18,800
			–		
Additions Qualifying for AIA					
Computer	6,000				
Machine	84,700				
Plant	10,000				
	100,700				
AIA (100,000 – 18,800)	(81,200)				81,200
		19,500			
Other additions					
Motor car (111-160g/km)		11,200			
Disposals				(8,000)	
		53,400		6,000	
WDA @ 20%		(10,680)			10,680
Balancing allowance				(6,000) × 80%	4,800
Additions Qualifying for FYA					
Motor car (≤ 110g/km)	17,000				
FYA @ 100%	(17,000)				17,000
					132,480
WDV c/f		42,720	–	–	

Chapter 6

Answer to Example 1

(a) 2010/11

(b) 2011/12

(c) 2011/12

Answer to Example 2

				£
2009/10	Actual (1/1/10 – 5/4/10)	3/6 × 30,000		15,000
2010/11	First 12 months (1/1/10 – 31/12/10)			
	1/1/10 – 30/6/10		30,000	
	1/7/10 – 31/12/10	6/12 × 70,000	35,000	65,000
2011/12	CYB (year to 30/6/11)			70,000
2012/13	CYB (year to 30/6/12)			82,000
Overlap profits:	1/1/10 – 5/4/10		15,000	
	1/7/10 – 31/12/10		35,000	50,000

Answer to Example 3

			£
2011/12	Actual (1/5/11 – 5/4/12)	11/18 × 36,000	22,000
2012/13	12 months to 31/10/12	12/18 × 36,000	24,000
2013/14	CYB (y/e 31/10/13)		30,000
Overlap profits	1/11/11 – 5/4/12	5/18 × 36,000	10,000

ANSWERS TO EXAMPLES

Answer to Example 4

		£
2011/12	CYB (y/e 31/1/12)	47,000
2012/13	4 months: 1/2/12 – 31/5/12	8,000
	Less: 'overlap' relief	(6,000)
		2,000

Answer to Example 5

			Trading income
2010/11	y/e 31 August 2010		£10,000
2011/12	y/e 31 August 2011		£12,000
2012/13	12 months to 31 May 2012	($3/12 \times$ £12,000 + £11,000)	£14,000
2013/14	y/e 31 May 2013		£16,000

Creates 'overlap profits' from 1 June 2011 – 31 August 2011 (3/12 x 12,000 = 3,000).

Answer to Example 6

			Trading income
2010/11	y/e 30 November 2010		£8,000
2011/12	y/e 30 November 2011		£9,000
2012/13	14 months to 31 January 2013	(£15,000 – $2/4 \times$ £8,000)	£11,000
2013/14	y/e 31 January 2014		£12,000

Relief available for 2 months of overlap profits.

Answer to Example 7

			Trading income
2010/11	y/e 30 April 2010		£15,000
2011/12	y/e 30 April 2011 + 9 months to 31 January 2012	(£18,000 + £16,000 – $9/11 \times$ £11,000)	£25,000
2012/13	y/e 31 January 2013		£17,000
2013/14	y/e 31 January 2014		£20,000

Relief available for 9 months of overlap profits. ie £9,000

Answer to Example 8

			Trading income
2010/11	y/e 31 January 2011		£6,000
2011/12	y/e 31 January 2012		£7,000
2012/13	12 months to 30 June 2012	($7/12 \times$ £7,000 + $5/17 \times$ £11,000)	£7,318
2013/14	12 months to 30 June 2013	($12/17 \times$ £11,000)	£7,765
2014/15	12 months to 30 June 2014		£8,000

Creates overlap profits from 1 July 2011 – 31 January 2012. ie £4,083 (7/12 x 7,000)

Answer to Example 9

Income tax computation 2011/12

	Non savings
Employment Income	36,090
Trading Profit (W1)	12,878
Total Income	48,968
Personal allowance	(7,475)
Taxable income	41,493
Tax calculation:	
35,000 @ 20%	7,000
6,493 @ 40 %	2,597
41,493	
Income Tax Liability	9,597

(W1)	Adjusted profit	39,000
	Less capital allowance (W2)	(26,122)
	Trading income	12,878

(W2)

		General Pool	60% Private use asset (1)	Short-life asset (1)	Allowances
	£	£	£	£	£
Accounting Period to 5 April 2012		–			
Additions qualifying for AIA					
Recording equipment	30,000				
AIA (Max (3/12 × £100,000)	(25,000)				25,000
		5,000			
Computer	2,600				
AIA (none remaining)	(–)				
				2,600	
Other Additions					
Motor car (111-160g/km)		10,400			
Motor car (>160g/km)			14,800		
		15,400	14,800	2,600	
WDA × 20% × 3/12		(770)			770
WDA × 10% × 3/12			(370) × 60%		222
WDA x 20% x 3/12				(130)	130
					26,122
WDV c/f		14,630	14,430	2,470	

Chapter 7

Answer to Example 1

	2009/10	2010/11	2011/12
	£	£	£
Trading income	nil	3,000	10,000
Less: carryfoward relief	nil	(3,000)	(2,000)
Revised trading income	nil	nil	8,000

Working — loss memorandum	£
Trading loss	5,000
Less: carryfoward relief in 2010/11	(3,000)
	2,000
Less: carryfoward relief in 2011/12	(2,000)
Loss carried forward to 2012/13	nil

Note

The loss is set off against the first trading profits to arise, to the maximum extent possible. Thus £3,000 of the loss is set off in 2010/11 and the remainder carried forward to 2011/12.

Answer to Example 2

Trading profit assessments:	£
2008/09	
Year ended 31 December 2008	23,000
2009/10	
Year ended 31 December 2009	32,000
2010/11	
Year ended 31 December 2010	25,000
2011/12	
Year ended 31 December 2011	NIL

Income tax computations

	2008/09	2009/10	2010/11	2011/12
	£	£	£	£
Trading profit	23,000	32,000	25,000	Nil
Property income	6,000	6,000	6,000	6,000
Total income	29,000	38,000	31,000	6,000
Less relief's				
Loss relief against total income			(31,000)	(–)
Net income	29,000	38,000	–	6,000
PA	(7,475)	(7,475)	(7,475)	(7,475)
Taxable income	21,525	30,525	–	–

- A claim against total income in 2011/12 would waste the personal allowance for 2011/12 and save no income tax. The claim in 2010/11 will also waste the PA but will generate a repayment of tax of 20% on a taxable income of £23,525.
- The balance of the trading loss £53,000 (£84,000 - £31,000) can be carried forward against the first available future trading profits that arise from the same trade.

Answer to Example 3

			£
(1)	Assessments		
	2010/11	y/e 31/12/10	40,000
	2011/12	y/e 31/12/11	–
	2012/13	y/e 31/12/12	60,000

(2) Income Tax computations

	2010/11	2011/12	2012/13
	£	£	£
Trading profit	40,000	–	60,000
Carryforward			(5,800)
Other income	5,000	6,000	
Total income	45,000	6,000	54,200
Less reliefs			
Qualifying interest	(2,800)	(2,500)	(–)
	42,200	3,500	54,200
Loss reliefs			
Current Year		(–)	
Carryback	(42,200)		
Net income	–	3,500	54,200
Personal Allowance	(7,475)	(7,475)	(7,475)
Taxable income	–	–	46,275

(3) Loss options

Trading loss arising 2011/12 £48,000

Option (1)

(I) Current Year against total income of 2011/12 £3,500 - save tax at 0%, waste Personal allowance

and (II) carryforward £44,500 to 2012/13 save tax at

£17,525 @ 40%	£7,010
£26,975 @ 20%	£5,395
Total tax saving	12,405
Repayment	NIL

Option 2

(I) Carryback against total income £42,200 - save tax at

£34,725 @ 20% = £ 6,945

waste £7,475 of personal allowance but repayment of tax of £6,945

and (II) carryforward £5,800 to 2012/13 save tax at

£5,800 @ 40%	£2,320
Total tax saving	£9,265
Repayment	£6,945

Option 3

(I) carryforward £48,000 against trading profit of 2012/13 save tax at

£17,525 @ 40%	£7,010
£30,475 @ 20%	£6,095
Total tax saving	£13,105
Repayment	Nil

Conclusion

If David is experiencing cashflow problems then it may be advisable to choose option (2) as this will result in a repayment of tax of £6,945. The Income Tax computations shown above represent this outcome.

If David wishes to maximise his tax saving then he should choose option (3) as this result in the higher tax saving BUT there is no repayment of tax. This however will be the most tax efficient claim.

Answer to Example 4

Trading income assessable amounts:

2010/11 (Actual basis)

1/8/10 – 5/4/11 (8/10 × (20,000)) = (£16,000)	Nil
2011/12 (First 12 months)	
1/8/10 – 31/7/11	
Loss	(20,000)
Less: Taken into account in 2010/11	16,000
	(4,000)
Profits 2/12 × 48,000	8,000
	4,000
2012/13 (CYB)	
A/C year ended 31/5/12	48,000

When calculating the amount assessable for 2011/12, the loss already taken into account in 2010/11 must be deducted. The loss of £4,000 allocated to 2011/12 is then used in aggregation against the profit of £8,000 creating a net assessment of £4,000. No further relief is therefore available for this part of the loss. The taxpayer would then need to choose his preferred use of the £16,000 loss in respect of 2010/11.

Answer to Example 5

Provided an election is made, the whole of the trading loss available can be offset against the capital gain as follows:

	£
Capital gain	44,000
Loss relief	(24,000)
	20,000
Annual Exemption	(10,600)
Taxable gain	9,400

Answer to Example 6

Taxable income computations

	2007/08	*2008/09*	*2009/10*	*2010/11*	*2011/12*	*2012/13*
	£	*£*	*£*	*£*	*£*	*£*
Employment Income	12,800	11,050	5,868	Nil		
Trading profit (W1)					Nil	2,500
Other income	4,500	4,500	4,500	4,500	4,500	4,500
Total income	17,300	15,550	10,368	4,500	4,500	7,000
Less: Opening year relief	(9,000)	(3,000)	–	–	–	–
Net Income	8,300	12,550	10,368	4,500	4,500	7,000
Less: Personal Allowances	(7,475)	(7,475)	(7,475)	(7,475)	(7,475)	(7,475)
Taxable income	825	5,075	2,893	Nil	Nil	Nil

Under opening year loss relief the loss of 2010/11 (£9,000) is set initially against Total Income of 2007/08. Any loss remaining would then be set automatically against Total Income of 2008/09 and finally against Total Income of 2009/10. Similarly the loss of 2011/12 (£3,000) is set initially against Total Income of 2008/09 before relieving 2009/10 and 2010/11 (had any loss remained).

Workings

(W1) New business – assessments

		Assessment	*Loss*
2010/11 (Actual)	1/7/10 – 5/4/11	Nil	
	9/12 × (12,000)		(9,000)
2011/12 (CYB)	y/e 30/6/11	Nil	(12,000)
	Less allocated to 10/11		9,000
			(3,000)
2012/13	(y/e 30/6/12)	2,500	
Loss available for relief			
2010/11		(9,000)	
2011/12		(3,000)	

Answer to Example 7

Trading loss arising in final 12m of trading available for terminal loss relief is calculated as

2011/12		
6/4/11 –30/4/11		
1/9 × (20,000)		(2,222)
Overlap Relief		(500)
2010/11		
1/5/10 – 5/4/11		
3/12 × 10,000	2,500	
+ 8/9 × (20,000)	(17,778)	(15,278)
Trading Loss available under terminal loss relief		(18,000)

Chapter 8

Answer to Example 1

	Total	Doug	Rob
	£	£	£
A/C Year Ended 30/9/11	18,000		
1/10/10 to 30/6/11			
(Profits £18,000 × 9/12 = 13,500)			
Salaries (9/12)	3,750	2,250	1,500
Balance (3:2)	9,750	5,850	3,900
	13,500	8,100	5,400
1/7/11 to 30/9/11			
(Profits £18,000 × 3/12 = 4,500			
Salaries (3/12)	2,500	1,500	1,000
Balance (2:1)	2,000	1,333	667
	4,500	2,833	1,667
Total allocation	18,000	10,933	7,067

Each partner will be assessed on their share of the profit in 2011/12 using the normal CYB assessment

Answer to Example 2

Allocate the trading income for accounting periods between the partners.

Profits will be allocated between the partners as follows:

	Total	Ann	Beryl	Clair
		£	£	£
y/e 30/6/10	12,000	6,000	6,000	–
y/e 30/6/11	14,000	7,000	7,000	–
y/e 30/6/12	24,000	8,000	8,000	8,000

Compute each partner's trading income as though they were a sole trader.

Ann and Beryl will both be assessed as follows, based upon a commencement on 1 July 2009:

		£
2009/10 (Actual)	1 July 2009 to 5 April 2010 £6,000 × 9/12	4,500
2010/11 (CYB)	Year ended 30 June 2010	6,000
2011/12 (CYB)	Year ended 30 June 2011	7,000
2012/13 (CYB)	Year ended 30 June 2012	8,000

They will both carry forward overlap profits of £4,500.

Clair will be treated as commencing on 1 July 2011, and will be assessed on her share of the partnership profits as follow:

2011/12 (Actual)	1 July 2011 to 5 April 2012 £8,000 × 9/12	6,000
2012/13 (CYB)	Year ended 30 June 2012	8,000

She will carry forward overlap profits of £6,000

Answer to Example 3

Paul will be entitled to terminal loss relief since he has actually ceased trading.

George will be entitled to claim opening years relief since he has actually commenced trading.

John and James will not be entitled to either of the above reliefs.

All the partners will be entitled to relief against total income of the current or previous tax year and against gains.

All the partners except Paul will be entitled to carryforward relief.

Chapter 9

Answer to Example 1

The mileage allowance of £3,600 (12,000 at 30p) received is tax free. Kerry can make an expense claim of £1,400 as follows:

	£
10,000 miles at 45p	4,500
2,000 miles at 25p	500
	5,000
Mileage allowance from employer (12,000 × 30p)	(3,600)
Allowable deduction	1,400

Answer to Example 2

	£
Accommodation benefit - Annual Value	4,000
Less: Employee contribution for personal use	(500)
	3,500
Additional accommodation benefit (120,000 – 75,000) × 4.00%	1,800
Total assessable benefit	5,300

Answer to Example 3

(a) Gift of dishwasher

	£
Market value when first made available to Gerald	900
Less: Benefit already assessed 2010/11: 900 × 20% × 10/12	(150)
Taxable benefit on gift: 2011/12	750

The benefit is £750 since this is greater than the dishwasher's market value when given to Gerald (£150)

(b) Sale of dishwasher to Gerald for £150

	£
Benefit calculated in (a) above	750
Less: Price paid	(150)
Taxable benefit on gift: 2011/12	600

Notes :

1. Where the benefit for use is provided for only part of tax year the benefit is reduced proportionately.
2. Gerald would also have been taxed on the benefit of using the dishwasher.

Taxed in 2010/11 – use £150

Taxed in 2011/12 – Gift 750 (a) or £600 (b)

Answer to Example 4

Agnes

The CO_2 emissions are between 120 - 125 grams per kilometre, so the relevant percentage is 18% (15% plus a 3% charge for a diesel car). The motor car was only available for eight months of 2011/12, so the benefit is £1,620 (13,500 × 18% × 8/12).

Billy

The CO_2 emissions are above the base level figure of 125 grams per kilometre. The CO_2 emissions figure of 187 is rounded down to 185 so that it is divisible by five. The minimum percentage of 15% is increased in 1% steps for each five grams per kilometre above the base level, so the relevant percentage is 27% (15% + 12% (185 – 125 = 60/5)). The motor car was available throughout 2011/12 so the benefit is £4,428 (16,400 × 27%).

Carla

The CO_2 emissions are above the base level figure of 130 grams per kilometre. The relevant percentage is 39% (15% + 24% (245 – 125 = 120/5)), but this is restricted to the maximum of 35%. The motor car was available throughout 2011/12 so the benefit is £6,710 (22,600 × 35% = 7,910 - 1,200). The contribution by Carla towards the use of the motor car can reduce the benefit.

Dennis

The CO_2 emissions are between 76 grams per kilometre and 120 grams per kilometre so the relevant percentage is 10%. The benefit is

£16,000 × 10% = £1,600 for 2011/12.

Eileen

The CO_2 emissions are below 75 grams per kilometre and the relevant percentage is 8% (diesel car). The benefit is £11,000 × 8% = £880 for 2011/12.

Answer to Example 5

Agnes

£18,800 × 18% × 8/12 = £2,256

The fuel was not available for first 4 months

Billy

£18,800 × 26% = £5,076

Carla

£18,800 × 35% = £6,580

There is no reduction for the contribution made by Carla since the cost of private fuel was not fully reimbursed.

Dennis

£18,800 × 10% = £1,888

Eileen

£18,800 × 8% = £1,504

Answer to Example 6

(a) Average method

		£
$\frac{35,000 + 15,000}{2} \times 4.00\%$		1,000
Less: interest paid (as below)		(775)
		225
6/4/11 – 31/5/11	£35,000 × 3% × 2/12	175
1/6/11 – 30/11/11	£30,000 × 3% × 6/12	450
1/12/11 – 5/4/12	£15,000 × 3% × 4/12	150
		775

(b) Accurate method

		£
6/4/11 – 31/5/11	£35,000 × 4.00% × 2/12	233
1/6/11 – 30/11/11	£30,000 × 4.00% × 6/12	600
1/12/11 – 5/4/12	£15,000 × 4.00% × 4/12	200
		1,033
Less: Interest paid (as above)		(775)
		258

HMRC would be entitled to opt for the accurate basis as this gives a higher assessment.

Answer to Example 7

	£
Personal Allowances	7,475
Benefits	(480)
Tax underpaid: 132 × 100/20	(660)
	6,335
Tax code	633L

Chapter 10

Answer to Example 1

The total pension input allowed is made up as follows:

AA for 2011/12	50,000	
Unused AA b/f		
- 08/09 fully used		–
- 09/10 (50,000 – 30,000)		20,000
- 10/11 (50,000 – 25,000)		25,000
Maximum gross contribution	95,000	

It can be seen from the above working that the current year's AA is used first and then unused AA brought forward is used on a FIFO basis.

If therefore in 2011/12 Aston made a gross contribution of £65,000, this would utilise all of the 2011/12 AA of £50,000 and £15,000 of the £20,000 unused AA brought forward from 09/10.

The remaining £5,000 would be carried forward for one more year to 2012/13. If a £40,000 payment were then made this would be within the AA for 2012/13 so no unused AA brought forward would be utilised.

The £5,000 unused AA from 09/10 would now lapse so that in 2013/14 after that year's AA is used there would be unused AA brought forward for use as follows:

-10/11		£25,000
-11/12		£NIL
-12/13	(50,000 – 40,000)	£10,000

Chapter 11

Answer to Example 1

The Class 1 and Class 1A NIC liability is as follows:

Class 1		£
Employee	. ≤ £7,225 @ 0%	Nil
	. [£42,475 – £7,225] × 12%	4,230
	. [£50,000 – £42,475] × 2%	150
		4,380
Employer	. ≤ £7,072 @ 0%	Nil
	. [£50,000 – £7,072] × 13.8%	5,924
		5,924

Class 1A

Employer 6,400 + 4,320 + 1,800 = 12,520 @ 13.8% = £1,728

Answer to Example 2

Class 4	£
(£42,475 – £7,225) × 9%	3,172
(50,000 – 42,475) × 2%	150
	3,322
Class 2	
£2.50 × 52 weeks	£130

Chapter 12

Answer to Example 1

Corporation tax computation for the chargeable accounting period of 12 months ended 31 March 2012

Tax adjusted trading profits		1,456,500
Property income		25,000
Interest receivable		10,000
Chargeable gains	37,500	

Less: Capital losses	(2,500)	35,000
		1,526,500
Less: Gift Aid donation		(10,000)
Taxable Total Profits		1,516,500

Note: Dividends from other companies (UK or overseas) are ignored when calculating Taxable Total Profits

Chapter 13

Answer to Example 1

Augmented profits = Taxable Total Profits + FII

= £1,800,000 + £9,000 × $^{100}/_{90}$ = £1,810,000

Therefore the main rate of 26% applies

Corporation tax payable = £1,800,000 × 26% = £468,000

If the company had prepared accounts to 31 December 2011 the computation would now span 2 Financial Years (FY 2010 and FY 2011) where the tax rates had changed and therefore the corporation tax must now be computed as follows:

FY 2010 3/12 × 1,800,000 × 28%	= 126,000
FY 2011 9/12 × 1,800,000 × 26%	= 351,000
CT payable	= £477,000

Answer to Example 2

Small profits rate

Augmented profits = 60,000 + 1800 × $^{100}/_{90}$

= 62,000 < £300,000

∴ Small profits rate applies, 20%

Corporation Tax payable = 60,000 × 20% = £12,000

If the company had prepared accounts to 31 December 2011 thus spanning 2 Financial Years, the tax would be computed as follows:

FY 2010 3/12 x 60,000 x 21%	= 3,150
FY 2011 9/12 x 60,000 x 20%	= 9,000
CT Payable	= £12,150

Answer to Example 3

Marginal relief

Augmented profits = 430,000 + 20,000

= 450,000

∴ marginal relief applies

Corporation Tax payable

		£
430,000 × 26%		111,800
Less:	$^{3}/_{200}$ (1,500,000 – 450,0000) × $^{430,000}/_{450,000}$	(15,050)
		96,750

If the company had prepared accounts to 31 December 2011 thus spanning 2 Financial Years, the tax would be computed as follows:

FY 2010	3/12 x 430,000 x 28%	= 30,100
Less Marginal Relief	7/400 × (1500 - 450) × 430/450 × 3/12	= (4,390)
		25,710
FY2011	9/12 x 430,000 x 26%	= 83,850
Less Marginal Relief	3/200 x (1500 - 450) x 430/450 x 9/12	= (11,287)
		72,563
CT Payable		98,273

Answer to Example 4

Augmented profits = 300,000 + (9,000 × $^{100}/_{90}$) = 310,000

Accounting period is less than 12 months therefore pro–rate upper and lower limits.

1,500,000 × $^{4}/_{12}$ = 500,000

300,000 × $^{4}/_{12}$ = 100,000

300,000 @ 26%	78,000
less	
$^{3}/_{200}$ × (500,000 – 310,000) × $^{300,000}/_{310,000}$	(2,758)
Corporation Tax payable	75,242

Chapter 14

Answer to Example 1

	12 months to 30/11/11 £	4 months to 31/3/12 £
Adjusted profit (12 : 4)	3,600,000	1,200,000
Less: CA (W1)	(6,000)	(37,244)
Tax adjusted trading profit	3,594,000	1,162,756
Chargeable Gain (6/1/12)	–	80,000
Corporate gift aid (31/7/11)	(20,000)	–
Taxable Total Profits	3,574,000	1,242,756
Corporation Tax (W2)	£953,066	£323,117

(W1)

12 months to 30/11/11		*General pool*	*Allowances*
WDV b/f		30,000	
WDA @ 20%		(6,000)	6,000
WDV c/f		24,000	
4 months to 31/3/12			
WDV b/f		24,000	
Additions qualifying for AIA			
Vans	68,000		
AIA - (Maximum 100,000 × 4/12)	(33,333)		33,333
		34,667	
		58,667	
WDA × 20% × 4/12		(3,911)	3,911
			37,244
WDV c/f		54,756	

(W2) *12 months to 30/11/11*

	£
Augmented profits	= 3,574,000
FY 2010 and FY 2011	
Limits	300,000
	1,500,000

As the augmented profit exceeds £1.5M the company is large and its Taxable Total Profits will be taxed at the main rate(s). The Chargeable Accounting Period spans FY 2010 and FY 2011 where the tax rates have changed meaning the Taxable Total Profits must be time apportioned between the two FY's and taxed at the respective rates of 28% and 26%.

Main rate	
Corporation tax	£
FY 2010	
4/12 x £3,574,000 x 28% =	333,573
FY 2011	
8/12 x £3,574,000 x 26% =	619,493
	953,066

4 months to 31/3/12

Augmented profits	= £1,242,756
FY 2011	
limits × 4/12	100,000
	500,000

As Augmented Profit exceeds the upper limit of £500,000 the company is large.

Main rate	
Corporation tax	
£1,242,756 × 26% =	£323,117

Chapter 15

Answer to Example 1

Current year relief

	y/e 31/3/12
	£
Trading profit	–
Interest receivable	20,000
Chargeable gain	50,000
	70,000
Current year relief	(45,000)
	25,000
Gift Aid	(15,000)
Taxable Total Profits	10,000

Answer to Example 2

	y/e 31/3/10	y/e 31/3/11	y/e 31/3/12
	£	£	£
Trading profit	30,000	60,000	–
Interest receivable	10,000	10,000	10,000
	40,000	70,000	10,000
Current year relief			(10,000) (i)
Carryback relief		(70,000) (ii)	
Taxable Total Profits	40,000	–	–

Loss memorandum

Loss arising		
y/e 31/3/12		90,000
Current year relief	y/e 31/3/12	(10,000) (i)
Carry back relief	y/e 31/3/11	(70,000) (ii)
Available to carryforward		10,000

Answer to Example 3

	y/e 31/3/10	y/e 31/3/11	y/e 31/3/12
	£	£	£
Trading profit	25,000	20,000	–
Interest Income	2,000	1,000	1,000
Chargeable Gain	–	5,000	–
Total profit before gift aid	27,000	26,000	1,000
Current year relief			(1,000) (i)
Carryback relief		(26,000) (ii)	
	27,000	–	–
Less Gift Aid	(500)	(500) (a)	(500) (a)
Taxable Total Profits	26,500	–	–

Note (a) Gift Aid is unrelieved

Loss memorandum

Trading loss	
y/e 31/3/12	40,000
Current year 31/3/12	(1,000)
	39,000
Carry back y/e 31/3/11	(26,000)
Available to carryforward	13,000

Answer to Example 4

	y/e 30/9/08	6 months 31/3/09	y/e 31/3/10	y/e 31/3/11	y/e 31/3/12
	£	£	£	£	£
Trading profit	10,000	16,000	20,000	32,000	–
Interest income	2,000	–	2,000	2,000	2,000
Chargeable Gain	–	–	6,000	–	8,000
	12,000	16,000	28,000	34,000	10,000
Current year relief					(10,000)
Carry back relief	(6,000)	(16,000)	(28,000)	(34,000)	–
Gift Aid	(500)	–	–	–	–
Taxable Total Profits	5,500	–	–	–	–
Gift Aid unrelieved			500	500	–

Loss memorandum		£
Loss arising y/e 31/3/12		97,000
Current year relief	y/e 31/3/12	(10,000)
Carry back relief	y/e 31/3/11	(34,000)
Carry back relief	y/e 31/3/10	(28,000)
Carry back relief	6m to 31/3/09	(16,000)
Carry back relief	y/e 30/9/08 £12,000 × 6⁄12 = £6,000 maximum set off	(6,000)
Loss unrelieved		3,000

Answer to Example 5

	y/e 31/3/09		y/e 31/03/10		y/e 31/3/11		y/e 31/3/12
	£		£		£		£
Trading income	40,000		20,000		–		20,000
Carry forward relief						(iii)	(9,000)
Property Income	3,000		3,000		3,000		3,000
Interest receivable	4,000		3,000		5,000		3,000
	47,000		26,000		8,000		17,000
Current year relief				(i)	(8,000)		
Carryback relief		(ii)	(26,000)				
	47,000		–		–		17,000
Less Gift Aid	(1,000)		–		–		(1,000)
Taxable Total Profits	46,000		–		–		16,000
Unrelieved Gift Aid			1,000		1,000		

Loss memo			£
Loss arising y/e 31/3/11			43,000
Current year relief	31/3/11	(i)	(8,000)
			35,000
Carry back relief	31/3/10	(ii)	(26,000)
			9,000
Carry forward y/e 31/3/12		(iii)	(9,000)
			–

Chapter 16

Answer to Example 1

		£	£
Sale proceeds		100,000	
Less: Incidental costs of sale		(1,000)	
			99,000
Less: Cost		20,000	
Enhancement expenditure		6,000	
			(26,000)
Unindexed gain			73,000
Less: Indexation allowance on cost	$20{,}000 \times \dfrac{216.0 - 97.85}{97.85}$ (1.207)	24,140	
On enhancement	$6{,}000 \times \dfrac{216.0 - 128.1}{128.1}$ (0.686)	4,116	
			(28,256)
Chargeable gain			44,744

Answer to Example 2

1) Same day X
2) Previous 9 days 500 shares

	£
Proceeds $\dfrac{500}{3{,}000} \times 30{,}000$	5,000
Less cost	(3,000)
Chargeable gain	2,000

3) 1/4/82 to previous 10 days

FA 85 Pool	*Number*	*Cost*	*Indexed cost*
	£	£	£
20th August 1989	1,000	5,000	5,000
Index up to November 1996 $\dfrac{153.9 - 115.8}{115.8} \times 5{,}000$			1,645
	1,000	5,000	6,645
Addition 16th November 1996	2,000	12,000	12,000
	3,000	17,000	18,645
Index up to October 2011 $\dfrac{216.0 - 153.9}{153.9} \times 18{,}645$			7,523
	3,000	17,000	26,168
Disposal 10th October 2011	(2,500)	(14,167)	(21,807)
	500	2,833	4,361

Note: when reindexing the share pool we do not round the indexation factor to 3 decimal places.

Calculate the gain on the 2,500 shares

	£
Proceeds $\dfrac{2{,}500}{3{,}000} \times 30{,}000$	25,000
Cost	(14,167)
Unindexed gain	10,833
I.A (21,807 – 14,167)	(7,640)
Chargeable gain	3,193

Total Gains	*Gains*
Previous 9 days	2,000
Pool	3,193
Chargeable Gains to include in the corporation tax computation	5,193

Answer to Example 3

Matching rules
Same day ×
Previous 9 days ×
1/4/82 previous 10 days ✓

Pool	Number	Cost	Indexed cost
	£	£	£
July 1993	3,000	10,000	10,000
February 1995 Bonus 1:3	1,000	–	–
	4,000	10,000	10,000
Index up to December 2011 from July 1993 $\frac{229.2-140.7}{140.7}\times 10,000$			6,290
	4,000	10,000	16,290
Sale	(2,000)	(5,000)	(8,145)
	2,000	5,000	8,145

Calculate the Gain

	£
Proceeds	12,000
Less Cost	(5,000)
Unindexed Gain	7,000
Less Indexation allowance (8,145 – 5,000)	(3,145)
Chargeable gain	3,855

Answer to Example 4

	Market value	*Cost*
B plc ordinary shares 10,000 × 2 × £1.50	30,000	7,500
B plc preference shares 10,000 × 1 × £1.00	10,000	2,500
	40,000	10,000

Calculate Gain on sale of preference shares in October 2011:

	£
Proceeds	15,000
Cost	(2,500)
Less: indexation allowance 0.842 × 2,500	(2,105)
Chargeable gain	10,395

The cost of B plc ordinary shares when they are sold will be £7,500

Answer to Example 5

Z Ltd receives at takeover:

	Market value	*Cost*
20,000 B plc ordinary shares	£30,000	£7,500
Cash	£10,000	£2,500
Total	£40,000	£10,000

Chargeable gain in July 2011:

	£
Proceeds	10,000
Less Cost	(2,500)
Indexation allowance (0.836 × £2,500)	(2,090)
Chargeable gain	5,410

Chapter 17

Answer to Example 1

	£
Proceeds	16,000
Less Acquisition cost $26{,}000 \times \frac{16{,}000}{16{,}000 + 34{,}000}$	(8,320)
	7,680
Unindexed gain	
Less I.A $\frac{229.2 - 212.1}{212.1} = 0.081 \times 8{,}320$	(674)
Chargeable gain	7,006

Answer to Example 2

(a) Antique table – this is an exempt asset as cost and proceeds are both ≤ £6,000 and it is a non wasting chattel.

(b) Painting – non wasting chattel

Normal calculation

	£
Disposal proceeds	10,000
Cost	(2,000)
	8,000
Less: Indexation allowance $\frac{229.2 - 209.8}{209.8} = 0.092 \times 2{,}000$	(184)
Gain	7,816

Restricted to ⁵⁄₃ [10,000 – 6,000] = **£6,667**

(c) Antique vase – non wasting chattel

	£
Disposal (deemed)	6,000
Less cost	(8,000)
Capital loss	(2,000)

(d) The vintage car is exempt

	£
Asset (1)	–
Asset (2)	6,667
Asset (3)	(2,000)
Asset (4)	–
Net chargeable Gain	4,667

Answer to Example 3

	£	£
Proceeds		38,000
Less Acquisition cost		
Purchase	25,000	
Less 11/30 × [25,000 – 1,000]	(8,800)	
		(16,200)
Unindexed gain		21,800
Less indexation allowance 0.378 × 16,200		(6,124)
Chargeable gain		15,676

ANSWERS TO EXAMPLES

Answer to Example 4

	£
Proceeds (July 2011)	30,000
Less Acquisition cost $10{,}000\times\dfrac{30{,}000}{30{,}000+25{,}000}$	(5,455)
Unindexed gain	24,545
Less indexation allowance $0.324 \times 5{,}455$	(1,767)
Chargeable gain	22,778

Answer to Example 5

On 1 July 2011 there is no chargeable gain as the company has elected to rollover the proceeds against the cost of the painting. When the painting is eventually sold its cost will be:

	£
Original cost	10,000
Less insurance proceeds	(8,000)
Base cost of painting	2,000

In addition the restoration costs themselves of £8,000 can be deducted on a future disposal.

Answer to Example 6

	£
Proceeds	34,000
Less cost	(23,000)
Unindexed gain	11,000
Less indexation allowance $\dfrac{226.8-198.5}{198.5}=0.143 \times 23{,}000$	(3,289)
Chargeable gain	7,711
Less gain rolled over	(3,711)
Revised chargeable gain	4,000

Proceeds have been used to buy a replacement asset but only partially used, therefore £4,000 (£34,000 – £30,000) of the gain is chargeable immediately and £3,711 (£7,711 – £4,000) can be deferred.

Base cost of the replacement asset	
Cost	30,000
Less Gain Deferred	(3,711)
Base cost	26,289

Chapter 18

Answer to Example 1

	£
Proceeds	400,000
Less Cost	(150,000)
Unindexed Gain	250,000
Less I.A $\dfrac{226.8-145.2}{145.2}=0.562\times150{,}000$	(84,300)
Chargeable gain	165,700

Proceeds are fully reinvested into a qualifying asset within the specified time period, so the entire gain of £165,700 can be deferred until the sale of the land.

Base cost of the land	
Cost	500,000
Less Gain deferred	(165,700)
Base cost	334,300

Answer to Example 2

		£
Proceeds		350,000
Cost		(200,000)
		150,000
Less: I.A	$\frac{226.8 - 141.1}{141.1} = 0.607 \times 200{,}000$	(121,400)
Chargeable gain		28,600

Proceeds not reinvested = 350,000 – 335,000 = £15,000
.£15,000 will be taxed in y/e 31/12/11
The remaining gain £13,600 (28,600 – 15,000) can be deferred

Base cost of new asset:

Cost	335,000
Gain deferred	(13,600)
	321,400

Answer to Example 3

		£
Proceeds		350,000
Cost		(200,000)
		150,000
I.A	$\frac{206.2 - 156.3}{156.3} = 0.319 \times 200{,}000$	(63,800)
		86,200

The gain is deferred due to the purchase of the fixed plant and will be chargeable in year ended 31 March 2012, when the depreciating asset is sold/ceases to be used in the trade (Feb 2012). This is earlier than 10 years from its date of acquisition (March 2018).

Chapter 19

Answer to Example 1

As companies are associated if they have been associated for any part of the Chargeable Accounting Period, A Ltd is treated as having two associated companies, so the lower and upper limits must be divided by three (A Ltd plus two associated companies). The lower limit is therefore £100,000 (£300,000/3) and the upper limit is £500,000 (£1,500,000/3). As A Ltd has Augmented Profits of £150,000 it is a marginal company. The company's corporation tax liability is therefore computed as follows:

		£
Taxable Total Profits		140,000
Franked investment income		10,000
Augmented profits		150,000
Corporation tax liability £140,000 at 26%		36,400
Less: Marginal relief $\frac{3}{400}$ (£500,000 – 150,000) ×	$\frac{140{,}000}{150{,}000}$	(4,900)
		31,500

The Augmented profits of £150,000 lie between £100,000 and £500,000, so marginal relief applies

Answer to Example 2

The AIA may be split in anyway the group chooses between A Ltd and its UK resident subsidiary acquired during the accounting period. As previously seen it is better to allocate AIA to special rate pool expenditure ahead of main pool expenditure, but within a group a more important issue is the marginal tax rate applicable in each company. A Ltd is a marginal company and therefore on augmented profit above £100,000 its Taxable Total Profits are being taxed at the highest corporate tax rate, the marginal rate of 27.5%. If the UK subsidiary acquired is for example a small company the tax rate on its profits would be only 20%. It would therefore be better to use the available AIA in A Ltd to save paying tax at 27.5% rather than in the subsidiary where tax is payable at only 20%.

Answer to Example 3

Group relief

(1) Z plc will be able to group relieve its trading loss to effective 75% subsidiaries. The shareholding can be held directly or indirectly.
(2) Z plc will therefore be able to group relieve its trading loss to A Ltd and B Ltd.
(3) Z plc does not have the required 75% shareholding in C Ltd (100% × 80% × 80% = 64%).

C Ltd may however separately group relieve with B Ltd its 80% parent. It is therefore possible where sub - subsidiaries (indirect) exist that more than one group will exist for purposes of group relief.

Answer to Example 4

(1) Group relief will be restricted to 6/12ths of Z plc's trading loss for the year ended 31 March 2012.
(2) The set–off will be against B Ltd's Taxable Total Profits for the six–month period to 31 March 2012.

Answer to Example 5

Both Beyonce Ltd and Z Ltd prepare accounts to 31 March but as Z Ltd only commenced trading on 1 January, 2012 only £60,000 (3/12 x 240,000) of Beyonce's loss period corresponds with Z Ltd's profit period. This, however will not be a problem as Z Ltd's profit is only £50,000 and will therefore represent the maximum group relief available. J Ltd's accounting period is not coterminous and therefore both its profits and Beyonce's loss must be time apportioned between the corresponding periods:
3 months of Beyonce's loss corresponds with 3 months of J's profit for the year ended 30 June 2011, hence maximum group relief is lower of:
3/12 × (240,000) = (60,000)
3/12 × 160,000 = 40,000
Maximum group relief £40,000.

9 months of Beyonce's loss corresponds with 9 months of J's profit for the year ended 30 June 2012, hence group relief restricted to lower of:
9/12 × (240,000) = 180,000
9/12 × 280,000 = 210,000
Maximum group relief £180,000

Answer to Example 6

The corporation tax liability of each of the group companies for the year ended 31 March 2012 is as follows:

	Year ended 31 March 2012		
	S Ltd	*E Ltd*	*F Ltd*
	£	*£*	*£*
Trading profit	–	650,000	130,000
Property Income	120,000		
Current year relief	(20,000)		
Taxable Total Profits	100,000	650,000	130,000
Group relief		(75,000)	(30,000)
Revised Taxable Total Profits	100,000	575,000	100,000
Corporation tax at 20%	20,000		20,000
Corporation tax at 26%		149,500	

(1) There are three associated companies in the group, so the relevant lower and upper limits for corporation tax purposes are £100,000 (300,000/3) and £500,000 (1,500,000/3) respectively. E Ltd is a large company paying tax at 26% whereas both S Ltd and F Ltd are marginal companies paying tax at 27.5% on those profits above the lower limit of £100,000.
(2) S Ltd's trading loss has been relieved so as to reduce both its own and F Ltd's 'augmented profits' down to the lower limit. The remaining loss of £75,000 is used to reduce the main rate profits in E Ltd. To achieve this optimal outcome the group relief claims must be made first so as to leave S Ltd with only £20,000 loss remaining which is then relieved with a normal current period claim. This is because partial claims are not allowed in current period relief but are in group relief!
(3) S Ltd's brought forward trading losses of £7,500 are carried forward in S Ltd only and are not available for group relief.

Answer to Example 7

(1) The two companies can make an election to transfer the capital loss from Large Ltd to Small Ltd.
(2) Alternatively, the capital gain or any part thereof can be transferred from Small Ltd to Large Ltd.
(3) In either case, the capital loss will be set against the capital gain, leaving £25,000 (100,000 – 75,000) chargeable to corporation tax.
(4) There is no need for either asset to be actually transferred between the companies simply an election needs to be made for the capital gain or loss to be transferred.
(5) The election must be made by 31 March 2014.
(6) It is therefore possible to choose the alternative that results in the £25,000 being chargeable in the company with the lowest rate of corporation tax. Large is paying tax at the main rate of 26% as its profits exceed the revised upper profit limit of £750,000 (£1.5M / 2). Small will pay tax at 20% on the taxable net gain of £25,000 as its other profits of £100,000 leave it £50,000 below the revised

lower profit limit of £150,000.

(7) An election should therefore be made to deem the capital loss made by Large to have been made by Small. This will net off the loss against Small's gain and ensure that the remaining taxable gain is taxed at the lowest available rate within the group.

Chapter 20

Answer to Example 1

(1) Relief will be available for trading losses if incurred by an overseas branch. No relief is available in respect of a trading loss incurred by an overseas subsidiary.

(2) Capital allowances will be available in respect of plant and machinery purchased by an overseas branch.

(3) An overseas subsidiary will be an associated company, and so the corporation tax limits will be halved.

(4) The full profits of an overseas branch are liable to UK corporation tax in the year that they are earned regardless of whether they are remitted to the UK. If the overseas operation is established as an overseas subsidiary - any profits remitted to U Ltd, in the form of a dividend are exempt from UK Corporation tax. However, if they are from a non associated overseas company the dividend (× 100/90) will be included as Franked Investment Income in the determination of 'augmented profits'.

Answer to Example 2

(a) If Pod Ltd owns 35% of the voting power of the overseas company (≤50%), then the overseas dividend will be exempt from UK corporation tax but included as Franked Investment Income (FII). The amount of FII will be £97,222 (87,500 × $^{100}/_{90}$)

(b) If Pod Ltd owns 70% of the voting power of the overseas company (>50%) then the dividend will be exempt from UK corporation tax and not included as FII. This is because the dividend received is from an associated company.

Answer to Example 3

The corporation tax liability of A Ltd for the year ended 31 March 2012 is as follows:

	Total	*UK Income*	*Overseas branch*	*Overseas property*
Trading profit	180,000	50,000	130,000	
Overseas Property Income (9,000 × 100/90)	10,000			10,000
Taxable Total Profits	190,000	50,000	130,000	10,000
Corporation Tax @ 20%	38,000	10,000	26,000	2,000
Less DTR (W1) / (W2)	(21,500)		(19,500)	(1,000)
UK Corporation Tax payable	16,500	10,000	6,500	1,000

(W1) Overseas branch

Lower of	£
1) overseas tax 130,000 × 15%	= **19,500**
2) UK tax	= 26,000

Overseas property

Lower of	
1) overseas tax 10,000 × 10%	= **1,000**
2) UK tax	= 2,000

Answer to Example 4

	Total	*UK*	*Overseas branch*	*Overseas Property*
Trading profit	180,000	50,000	130,000	
Overseas Property Income (9,000 × 100/75)	12,000			12,000
Taxable Total Profits	192,000	50,000	130,000	12,000
Corporation Tax @ 20%	38,400	10,000	26,000	2,400
Less DTR (W1) / (W2)	(21,900)		(19,500)	(2,400)
CT Liability	16,500	10,000	6,500	Nil

(W1) Overseas branch

Lower of	£
Overseas tax 130,000 × 15%	19,500
UK tax (130,000 @ 20%)	26,000
DTR	**19,500**

(W2) Overseas property Income

Lower of	
Overseas tax	3,000
UK tax (12,000 @ 20%)	2,400
DTR	**2,400**

Answer to Example 5

	Total	*UK*	*Overseas branch*	*Overseas Property*
Trading profit	180,000	50,000	130,000	
Overseas Property Income (9,000 × 100/75)	12,000			12,000
Total Profits	192,000	50,000	130,000	12,000
Less: Gift Aid	(10,000)	(10,000)		
Taxable Total Profits	182,000	40,000	130,000	12,000
CT @ 20%	36,400	8,000	26,000	2,400
Less DTR (W1) / (W2)	(21,900)		(19,500)	(2,400)
CT Liability	14,500	8,000	6,500	Nil

W1 & W2 As per Example 4

In order to maximise the DTR gift aid payments are deemed for this purpose to have firstly reduced UK profits. If gift aid payments exceeded the UK profits the excess would then be deemed to reduce the overseas income with the lowest rate of overseas tax i.e. branch profits

Chapter 21

Answer to Example 1

Tina – Capital Gains tax computation as 2011/12

	£	£
Painting		
Disposal proceeds	500,000	
Less Cost	(350,000)	
Capital Gain		150,000
Investment property		
Disposal proceeds	310,000	
Less incidental costs of disposal	(15,000)	
Net proceeds	295,000	
Less cost	(200,000)	
Capital Gain		95,000
Antique vase		
Disposal proceeds	10,000	
Less cost	(15,000)	
Capital loss		(5,000)
Net capital gains in 2011/12		240,000
Less capital losses b/f		(12,000)
Net Capital Gains		228,000
Less Annual Exemption		(10,600)
Taxable Gains		217,400

CGT × 28% (Note)	£60,872
Due	31/1/13

Note: Tina's taxable income of £50,000 exceeds the basic rate band of £35,000 so all of the taxable gain is taxed at 28%

Answer to Example 2

	£
Capital Gain	18,000
Less Annual Exemption	(10,600)
Taxable Gain	7,400
Capital Gains Tax (W1)	
7,400 × 18%	£1,332
Due	31/1/13

Income Tax Computation

Trading profit	20,000
Less Personal allowance	(7,475)
Taxable income	12,525

Basic rate band remaining.
35,000 – 12,525 = £22,475. The gains fall wholly into the remaining basic rate band so the CGT rate is 18%

Answer to Example 3

	£
Capital Gain	30,000
Less Annual Exemption	(10,600)
Taxable Gain	19,400
Capital Gains Tax (W1)	
2,475 × 18%	445
16,925 × 28%	4,739
19,400	£5,184
CGT Due	31/1/13

Income Tax Computation

Trading profit	40,000
Less Personal allowance	(7,475)
Taxable income	32,525

Basic rate band remaining.
35,000 – 32,525 = £2,475.
Part of the taxable gain falls within the remaining basic rate band so will be taxed at 18%, but (£19,400 – £2,475) £16,925 exceeds the basic rate band so will be taxed at 28%.

Answer to Example 4

	£
Capital Gain	26,000
Less Annual Exemption	(10,600)
Taxable Gain	15,400
Capital Gains Tax (W1)	
475 × 18%	85
14,925 × 28%	4,179
15,400	£4,264
CGT Due	31/1/13

W1 Income Tax Computation

Trading profit	45,000
Less Personal allowance	(7,475)
Taxable income	37,525

Basic rate band remaining £38,000 – £37,525 = £475
Part of the taxable gain falls into the remaining basic rate band so will be taxed at 18%, but (£15,400 – £475) £14,925 exceeds the basic rate band so will be taxed at 28%.
The basic rate band is extended by the gross gift aid payment: (£35,000 + 2,400 × $^{100}/_{80}$) = 38,000

Answer to Example 5

Lower of
400 + ¼ (408 – 400) = 402p
or

$$\frac{408+399}{2} = 403.5\text{p}$$

The lower figure is 402p
Value 1,000 × 402p = £4,020

Answer to Example 6

Fiona

	£
2010/11	
Capital gains in the tax year	15,000
Capital losses in the tax year	(10,000)
Net Capital gains in the tax year	5,000

Net Capital gains are covered by the Annual Exemption. No losses to carry forward to 2011/12.

2011/12	
Capital gains in the tax year	16,000
Capital losses in the tax year	(5,200)
Net Capital gains in the tax year	10,800
Annual Exemption	(10,600)
Taxable gains	200

Fiona is taxed on taxable gains of £200 in 2011/12. No losses to carry forward.

Jane

2010/11	
Capital gains in the tax year	7,000
Capital losses in the tax year	(10,000)
Net Capital Gains in the tax year	Nil

Jane is unable to use her 2010/11 Annual Exemption since her gains are covered by current year losses. She has losses of £3,000 (10,000 - 7,000) to carry forward to 2011/12.

2011/12	
Capital gains in the tax year	12,700
Capital losses in the tax year	(2,000)
Net Capital Gains in the tax year	10,700
Less capital loss b/f (restrict)	(100)
Net Capital Gains	10,600
Less Annual Exemption	(10,600)
Taxble Gain	–

Capital loss to carry forward 3,000 – 100 = £2,900

Answer to Example 7

Mike transfers the Ring at Nil Gain/Nil Loss in December 2011
Barbara sells the ring

	£
Disposal Proceeds	20,000
Less Cost	(12,000)
Capital gain	8,000

Barbara simply takes on the original cost of the asset from Mike as if she acquired it herself in July 1993

Chapter 22

Answer to Example 1

(a) Match with acquisitions on same day as sale X

(b) Match with acquisitions in next 30 days

7 March 2012		200 shares
	£	
Disposal proceeds ($^{200}/_{1,000} \times$ £25,000)	5,000	
Less: cost	(4,000)	
Capital gain		1,000

(c) Match with share pool

	Number	*Cost*
31/5/11	1,500	20,000
30/6/11	500	10,000
	2,000	30,000
Disposal	(800)	(12,000)
	1,200	18,000

Calculate Gain	£	
Disposal proceeds ($^{800}/_{1,000} \times$ £25,000)	20,000	
Less: cost	(12,000)	
Capital gain		8,000
Capital Gains 2011/12		9,000

Answer to Example 2

(a) Match with acquisitions on same day X
(b) Match with acquisitions in next 30 days X
(c) Match with share pool

	Number	*Cost*
Feb 2011	7,000	15,000
June 2011	1,000	4,000
	8,000	19,000
July 2011 Bonus 1:5	1,600	–
	9,600	19,000
October 2011 Disposal	(5,000)	(9,896)
	4,600	9,104

Calculate Gain

	£
Disposal proceeds	20,000
Less: cost	(9,896)
Capital gain	10,104

ANSWERS TO EXAMPLES

Answer to Example 3

(a) Match with acquisitions on same day X

(b) Match with acquisitions in next 30 days X

(c) Match with share pool

	Number	Cost
Feb 2011	6,000	15,000
June 2011	900	2,700
	6,900	17,700
July 2011 Rights 1: 3 @ £3.00	2,300	6,900
	9,200	24,600
September 2011 Disposal	(6,000)	(16,043)
	3,200	8,557

Calculate Gain

	£
Disposal proceeds	24,000
Less: cost	(16,043)
Capital gain	7,957

Answer to Example 4

Disposal proceeds	20,000
Less Cost (W)	(8,333)
Capital gain	11,667

Working: Cost of ordinary shares in Gold Ltd

Mark received:

8,000 ordinary shares, valued at 8,000 × £5 = £40,000

4,000 preference shares, valued at 4,000 × £2 = £8,000

The cost attributable to the ordinary shares is therefore: $£10,000 \times \frac{40,000}{48,000} = £8,333$

Answer to Example 5

Mark receives at takeover:

	Market value	Cost
8,000 Gold Ltd ordinary shares	£40,000	£8,333
Cash	£8,000	£1,667
Total	£48,000	£10,000

Capital gain in June 2011:

	£
Proceeds	8,000
Less Cost	(1,667)
Capital gain	6,333

Chapter 23

Answer to Example 1
Daisy
Sale of business

	£
Goodwill	250,000
Factory	320,000
Warehouse	(90,000)
	480,000
Sale of shares	
Gain on shares	370,000
Net chargeable gains	850,000
Less Annual Exemption	(10,600)
Taxable gain	839,400
Capital Gains Tax £839,400 × 10%	£83,940
Due	31/1/13

Daisy has utilised £850,000 (£480,000 + £370,000) of entrepreneurs' relief in 2011/12 so has (£10,000,000 – £850,000) = £9,150,000 to utilise over the rest of her lifetime.

Answer to Example 2
Anne
Capital Gains Calculation

	£	£
Capital gains qualifying for entrepreneur's relief		
Sale of shares		
Proceeds	5,000,000	
Cost	(500,000)	
Capital gains / taxable gain	4,500,000	
Capital gains not qualifying for entrepreneur's relief		
Sale of painting		100,000
Less capital loss brought forward		(25,000)
		75,000
Less Annual Exemption		(10,600)
Taxable gain		64,400
Capital Gains Tax (W1)	£450,000	£18,032
Due date	31/1/13	31/1/13

(W1)	£
£4,500,000 × 10%	450,000
£64,400 × 28% (Note)	18,032
Capital Gains Tax	468,032

Note: £17,000 (£35,000 – £18,000) of Anne's basic rate band is unused, but this is utilised by the gains qualifying for entrepreneur's relief (even though this does not affect the 10% tax rate)
There is a lifetime allowance of £5,500,000 (£10000,000 – £4,500,000) remaining to utilise on future gains qualifying for entrepreneur's relief.

ANSWERS TO EXAMPLES

Answer to Example 3

	£
Cost of new asset	320,000
Less: Capital gain on old asset (£300,000 - £250,000)	(50,000)
Deemed cost of new asset	270,000

Entrepreneurs' relief would not be available as this is the disposal of an individual asset used in the business, not the whole business.

Answer to Example 4

(a) New factory purchased for £750,000

	£	£
Purchase cost of new factory		750,000
Capital gain on old factory (£800,000 - £680,000)	120,000	
Restriction on rollover (£800,000 - £750,000)	(50,000)	
Gain rolled over		(70,000)
Base cost of new factory		680,000

Entrepreneurs' relief is not available in respect of the gain of £50,000 that is immediately chargeable as it is not the disposal of the whole business.

(b) New factory purchased for £600,000

In this case the amount of proceeds not reinvested of £200,000 (800,000 - 600,000) exceeds the gain made on the old factory. Thus none of the gain is eligible to be rolled over and so there is no adjustment to the base cost of the new factory. It remains at the purchase price of £600,000. Entrepreneurs' relief would not be available against the gain of £120,000 in 2011/12 as it is not the disposal of the whole of the business.

Answer to Example 5

(a) The non-qualifying part of the gain is:

£9,000 (£600,000 - £540,000 = £60,000 × 15%).

This is taxable immediately, as it does not qualify for rollover relief. Entrepreneurs' relief will not be available as the whole of the business has not been sold.

(b) The base cost of the new factory is reduced by the amount of the gain rolled over. It is therefore:

	£
Purchase cost	650,000
Capital gain rolled over (£60,000 × 85%)	(51,000)
	599,000

Answer to Example 6

As Charles reinvested all of the proceeds from the sale of the freehold factory in fixed plant and machinery, a depreciating asset, the entire gain may be held over. The held over gain on the sale of the factory in June 2010 becomes chargeable in 2011/12, this is because the depreciating asset has been sold. The capital gain is £200,000 (£500,000 - £300,000). Entrepreneurs' relief is not available as the whole business was not disposed of.

Answer to Example 7

David has made a disposal in September 2011 as follows:

	£
Market value of asset	100,000
Less: Cost	(60,000)
	40,000
Less: Gift relief	(40,000)
Revised gain	Nil

Tommy has a Base cost to set against a future disposal, calculated as follows.

	£
Market value of asset acquired	100,000
Less: gained deferred	(40,000)
	60,000

ANSWER TO EXAMPLE 8

(a) Richard – Chargeable gain on shares sold in March 2012

	£	£
Market value of shares in March 2012		200,000
Less cost		(60,000)
Capital Gain		140,000
Less: Gain deferred		
Capital gain	140,000	
Less: Proceeds received – actual cost (85,000 – 60,000)	(25,000)	
		(115,000)
Revised gain eligible for entrepreneurs' relief		25,000
Less Annual Exemption		(10,600)
Taxable gain		14,400
CGT @ 10%		£1,440

(b) Richard's son – Base cost

	£
Market value of shares in March 2012	200,000
Less: Gain deferred	(115,000)
Base cost	85,000

ANSWER TO EXAMPLE 9

	£
John's Proceeds (market value)	800,000
Less: cost	(200,000)
Capital Gain	600,000
Less gift relief (W1)	(525,000)
Revised gain eligible for entrepreneur's relief	75,000
Less Annual Exemption	(10,600)
Taxable gain	64,400
CGT @ 10%	£6,440

John's son Base cost of shares	
Cost (Market value)	800,000
Less: Gain deferred	(525,000)
Base cost	275,000

(W1) Gain eligible for Gift relief

$$600{,}000 \times \frac{700{,}000}{800{,}000} = 525{,}500$$

ANSWER TO EXAMPLE 10

Capital gain on incorporation – September 2011

		£
Total gains		90,000
Less: Gain rolled over	$\frac{160{,}000}{160{,}000 + 40{,}000} \times 90{,}000$	(72,000)
Revised gain qualifying for entrepreneur's relief		18,000
CGT @ 10%		1,800

ANSWERS TO EXAMPLES

Capital Gain on sale of shares - 1 March 2012

	£	£
Disposal proceeds		350,000
Less: Cost	160,000	
Less: gain deferred	(72,000)	
		(88,000)
Capital gain		262,000
Less: Annual Exemption		(10,600)
Chargeable gain		251,400
CGT @ 28%		70,392
Total CGT £1,800 + £70,392 =		**£72,192**

Note (1) The Annual Exemption is allocated to the 1/3/12 disposal as it does not qualify for entrepreneur's relief.
(2) Entrepreneurs' relief would not be available on the share disposal as the shares have not been owned for one year.

Answer to Example 11

	£
Disposal proceeds	150,000
less cost	(10,000)
Capital gain	140,000
less PPR relief (W1)	(124,299)
Chargeble Gain	15,701

(W1)

		Actual & Deemed Occupation (months)	*Absent (months)*
1/4/85 – 30/6/85	(actual)	3	
1/7/85 – 1/7/87	(working overseas)	24	
1/7/87 –31/12/01	(actual)	174	
31/12/01 –31/12/11	(4 years work in UK/last 3 years)	84	36
		285	36

PPR relief $\frac{285}{321} \times 140{,}000 = 124{,}299$

Answer to Example 12

	£
Disposal proceeds	250,000
Less cost	(30,000)
Capital Gain	220,000
Less PPR relief (W1)	(134,444)
	85,556
Less Letting relief (W2)	(20,370)
Chargeable Gain	65,186

(W1)

	Actual & Deemed (months)	*Absent (months)*	
1/4/85 – 31/3/87 (actual)	24		
1/4/87 – 30/9/92 (Any reason)	36	30	
1/10/92 –31/3/01 (actual)	102		
1/4/01 –31/3/12 (last 36 months)	36	96	
	198	126	324

PPR relief $\frac{198}{324} \times 220{,}000 = 134{,}444$

(W2) (i) £134,444
(ii) £40,000
(iii) $\frac{30}{324} \times 220{,}000 = 20{,}370$

Chapter 24

Answer to Example 1

Chargeable Transfers	20/11/07	15/7/08	8/12/10
	PET	*CLT*	*PET*
Transfer of value	40,000	405,000	184,000 (W1)
Less: Exemptions			
Marriage	(5,000)		
AE 07/08	(3,000)		
AE 06/07	(3,000)		
AE 08/09		(3,000)	
AE 10/11			(3,000)
AE 09/10			(3,000)
	29,000	402,000	178,000

W1 Transfer of value

Before transfer (16,000 @ £25) =	400,000
After transfer (12,000 @ £18) =	(216,000)
	184,000

Lifetime Transfers Chargeable When Made

		£	*Gross Transfers*	*IHT*
15/7/08	CLT	402,000	424,500	22,500
	312,000 @ nil = nil			
	90,000 @ 25% = 22,500			
	402,000			

Lifetime Transfers Chargeable on Death – April 1, 2012

	Gross Transfers	*IHT*
20/11/07 PET	29,000	nil
15/7/08 CLT	424,500	51,400
Available nil rate band (325,000 - 29,000) = 296,000		
296,000 @ nil = nil	453,500	
128,500 @ 40% = 51,400		
424,500		
Less: Taper Relief (20%) (3-4 years)		(10,280)
		41,120
Less: Lifetime tax paid		(22,500)
Additional tax due on death		18,620

Chargeable Estate at Death – April 1, 2012.

	£	£
Principal Private Residence	300,000	
Less: Repayment Mortgage	(80,000)	220,000
Holiday Home		140,000
Bank & Building Society Deposits		230,000
ISA's		50,000
Shares (12,000 @ £20)		240,000
Life Assurance		140,000
		1,020,000
Less: Debts	6,000	
Funeral Expenses	6,000	(12,000)
		1,008,000
Less: Exempt bequest to spouse		(250,000)
Chargeable Estate		758,000
Gross Chargeable Transfers in 7 years before death		453,500
Nil Rate Band fully used therefore entire estate taxed @ 40%		
£758,000 @ 40%		£303,200

Answer to Example 2

The gift on 1 October 2001 to her son is a PET. This was not chargeable when made nor will it be chargeable on death as Dee survived for the required 7 years. The transfer is therefore exempt but will be deemed to have used the Annual Exemptions for 01/02 and 00/01.

The gift on 1 June 2002 is a CLT and was chargeable when made but not on death as again Dee survived for 7 years.

The gift on 1 September 2008 is a PET and will be chargeable on death as Dee died within the next 7 years.

Step 1 Compute the Chargeable Transfers

	1/6/02	*1/9/08*
	CLT	*PET*
Transfer of value	265,000	296,000
Less: Exemptions		
AE 02/03	(3,000)	
AE 08/09		(3,000)
AE 07/08		(3,000)
Chargeable Transfer	262,000	290,000

AE 01/02 will have been applied to the 1 October 2001 PET despite it never becoming chargeable.

Step 2 Lifetime Transfers Chargeable When Made

	£	*Gross Transfers*	*IHT*
1/6/02 CLT	262,000	265,000	3,000
250,000 @ nil = nil			
12,000 @ 25% = 3,000			

As the donor, Dee, paid the IHT the transfer is a net transfer and therefore the excess over the nil rate band is taxed at 25%

Step 3 Lifetime Transfers Chargeable on Death

This is the hardest part of the question and requires us to firstly determine the earliest transfer within the 7 years before death as the starting point. In this example there is only one such transfer the PET on 1/9/08. However in computing any IHT payable we must take account of what nil rate band is available after firstly deducting from it any CLT's made within the 7 years of this transfer:

			Gross Transfers	*IHT*
CLT 7 years < 1/9/08			265,000	
1/9/08	PET		290,000	92,000
Available nil rate band = 325,000 – 265,000			555,000	
= 60,000	@ nil	= nil	453,500	
230,000	@ 40%	= 92,000		
290,000				
Less:	Taper Relief (20%)			(18,400)
				73,600

Although the CLT of 1 June 2002 has drastically affected the tax payable on the PET of 1 September 2008 it will only be relevant for transfers within the following 7 years hence any transfer after that date, 1 June 2009, or as here the Chargeable Estate will not take account of this earlier CLT in computing any IHT payable.

The 7 year cumulation period at the date of death will only therefore consider the PET of 1/9/08 in determining any available nil rate band.

Step 4 Chargeable Estate at Death – 1 March 2012

Chargeable Estate			500,000
Available nil rate band = 325,000 – 290,000 = 35,000			
IHT on Estate			
35,000	@ nil	= nil	
465,000	@ 40%	= 186,000	
500,000			

Chapter 25

Answer to Example 1

(a) Orchid Ltd will become liable to compulsory VAT registration when its taxable supplies during any 12-month period exceed £73,000.

This will happen on 31 July 2012 when taxable supplies will amount to £74,000 (4,300 + 5,100 + 4,700 + 4,700 + 4,900 + 4,800 + 6,000 + 6,100 + 5,900 + 6,200 + 9,800 + 11,500).

(b) Orchid Ltd will have to notify HMRC by 30 August 2012, being 30 days after the end of the period.

(c) The company will be registered from 1 September 2012 or from an agreed earlier date.

Answer to Example 2

A company must register for VAT if there are reasonable grounds for believing that taxable supplies will exceed £73,000 in the following 30 days.

Forecast income is £75,000 per month, and so taxable supplies for the 30-day period to 30 April 2012 will exceed £73,000.

Tulip Ltd will have to notify HMRC by 30 April 2012, being the end of the 30-day period, and will be registered from 1 April 2012.

Answer to Example 3

Prior to putting up its prices, Vine Ltd's net profit is £65,200 (£70,000 - £4,800).

If Vine Ltd puts up its prices, then it will exceed the VAT registration limit of £73,000, and the company will have to register for VAT.

Output VAT will have to be absorbed by Vine Ltd, as sales are to the general public and there is no further scope for price increases.

The revised annual net profit will be:

	£
Income (75,000 × 100/120)	62,500
Expenses (4,800 × 100/120)	(4,000)
Net profit	58,500

This is a decrease in net profit of £6,700 (65,200 – 58,500), and so it is not beneficial for Vine Ltd to put up its prices.

ANSWERS TO EXAMPLES

Answer to Example 4

VAT Return - Quarter ended 31 March 2012

	£	£
Output VAT		
Sales (120,000 × 95% (100% - 5%) × 20%)		22,800
Input VAT		
Purchases and expenses (35,640 - 480 = 35,160 × 20%)	7,032	
Irrecoverable debt (2,000 × 20%)	400	
Machinery (21,150 × 20/120)	3,525	
		10,957
VAT payable		11,843
Due date		30/4/12

Notes:

(1) The calculation of output VAT must take into account the discount for prompt payment, even if customers do not take it.

(2) Input VAT on UK business entertaining cannot be reclaimed If they had been overseas customers the input tax would now be recoverable..

(3) Relief for a irrecoverable debt is not given until six months from the time that payment is due.

(4) Input VAT on motor cars not used wholly for business purposes cannot be reclaimed.

Answer to Example 5

Input VAT can be reclaimed in respect of the cost of petrol and repairs.

Because fuel is being provided for private use to the director, Poppy plc will have to account for output VAT based on the scale charge. The quarterly cost is £74 (445 × 20/120)

Answer to Example 6

The late submission of the VAT return for the quarter ended 30 September 2010 will have resulted in HMRC issuing a surcharge liability notice specifying a surcharge period running to 30 September 2011.

The late payment of VAT for the quarter ended 31 December 2010 will result in a surcharge of £426 (£21,300 × 2%).

The surcharge period will have been extended to 31 December 2011.

Bluebell Ltd then submitted four VAT returns on time.

The late submission of the VAT return for the quarter ended 31 March 2012 will therefore only result in a surcharge liability notice (specifying a surcharge period running to 31 March 2013).

Answer to Example 7

Greater of

- £10,000 ✓
- 1% × 700,000 = £7,000

The de minimis level is therefore £10,000. As the error is less than the de minimis level, it can be disclosed on the next VAT return, that is the VAT return for the quarter to 31 March 2012. No interest will be charged by HMRC but a penalty for submission of an incorrect return could be imposed, unless Blanche Ltd simply made a mistake. But if HMRC believes Blanche Ltd failed to take reasonable care, the penalty may be 30% × £8,500 = £2,550.

Answer to Example 8

(1) The export of £50,000 of goods to the VAT registered customer in France will be zero rated.

(2) The export of £10,000 of goods to the non VAT registered individual in Latvia will need to have VAT equal to (20% × £10,000) £2,000 accounted for by BW Ltd on its VAT return as output VAT.

(3) The import of £12,000 of goods from the Non EU supplier will necessitate VAT of £12,000 × 20% = £2,400 being paid to HMRC at the point of entry (assuming the duty deferment scheme is not in place). This can then be recovered as input VAT

(4) The import of £20,000 of goods from the EU supplier will involve a "self supply" of output VAT of £20,000 × 20% = £4,000 being accounted for by BW Ltd on its VAT return for quarter to 31 March 2012. However assuming BW Ltd makes wholly taxable supplies the same amount of £4,000 can be recovered as input VAT.

Extract from BW Ltd VAT return for quarter to 31 March 2012

	£
Output VAT	
1) On supplies to Non VAT registered EU customer	2,000
2) On self supply of acquisition from EU supplier	4,000
Input VAT	
1) On import from non EU supplier	(2,400)
2) On self supply of acquisition from EU supplier	(4,000)

Chapter 26

ANSWER TO EXAMPLE 1

Photo Plc
Corporation tax liability

FY 2010 (3/12 × £2M) × 28% =	140,000
FY 2011 (9/12 × £2M) × 26% =	390,000
	530,000

All payable by instalments
This will be paid as follows:

£132,500	on	14 July 2011
£132,500	on	14 October 2011
£132,500	on	14 January 2012
£132,500	on	14 April 2012

Chapter 27

ANSWER TO EXAMPLE 1

The payments on account for 2011/12 will be based on the tax payable by self assessment and the class 4 (NIC) liability in 2010/11
Due dates:

31/1/12	13,000/2	= £6,500
31/7/12	13,000/2	= £6,500

The Balancing payment for 2011/12 is made up as follows

	£
Total income tax liability	14,000
Less tax deducted at source	(2,000)
Income tax payable by self assessment	12,000
Class 4 NIC liability	2,500
Capital Gains tax	1,700
less Payments on Account	(13,000)
Balancing Payment due 31/1/13	3,200

The payments on Account for 2012/13 will be based on the tax payable by self assessment and class 4 NIC liability in 2011/12

31/1/13	(12,000 + 2,500)/2	= 7,250
31/7/13		= 7,250

Total payment to be made on 31 January 2013 is 10,450 (3,200 + 7,250)

Paper F6

PRACTICE QUESTIONS

1 UK Tax System

Jackie received property income of £5,000 but accidently entered the figure on her tax return as £500.
Michelle receives property income of £7,000 p.a. and deliberately declares £5,000 on her tax return.

Which of the above represents tax avoidance or tax evasion?

2 Kate

Kate has the following income and outgoings for 2011/12:

	£
Trading profit	36,535
Employment Income	9,000
Bank Deposit Interest (amount received)	2,800
Dividend income (amount received)	1,800
Qualifying interest (amount paid)	1,000
Gift aid (amount paid)	2,000

PAYE of £505 was deducted from the Employment Income.

Calculate the amount of income tax payable by Kate for 2011/12.

3 Jessica

Jessica had the following income and outgoings for 2011/12

Trading profit	£90,000
Bank interested received	£16,000
Gift Aid (amount paid)	£1,600

Calculate the amount of income tax payable by Jessica for 2011/12

4 Karl

Karl has the following income and outgoings for 2011/12

	£
Employment income	140,000
Dividends received	27,000
Qualifying interest (amount paid)	3,000
Gift aid (amount paid)	3,200

PAYE of £48,520 was deducted from the Employment income

Calculate the amount of income tax payable by Karl for 2011/12

5 Mr & Mrs Elderely

Mr Elderely is 68 years old and receives Property Income of £45,000 in the tax year 2011/12
His wife Mrs Elderely is 73 years old and earns no income in 2011/12.

Calculate Mr Elderley's income tax liability and recommend what course of action you would advice the couple to take to reduce this liability.

6 Michael

Michael is 69 years old and received Property income of £110,000 in 2011/12.

Calculate his income tax liability

7 Peter

Peter acquired two properties on 1 June 2011 that were first let on 1 July 2011.
Property A is let unfurnished for an annual rental of £4,000 payable quarterly in advance. Peter incurred the following expenditure in respect of this property during the period to 5 April 2012.

		£
20 June 2011	Repairs to roof following a violent storm on 15 June 2011	1,600
29 June 2011	Insurance for y/e 31/5/12	420
01 February 2012	Repainting exterior	810

Property B is let furnished for an annual rental of £5,000, payable quarterly in arrears. The tenants were late in paying the amount due on 5 April 2012, and this was not received until 15 April 2012. Peter incurred the following expenditure in respect of this property during the period to 5 April 2012.

		£
4 June 2011	Letting expenses paid to agent	40
29 June 2011	Insurance for y/e 31/5/12	585

You are required to calculate Peter's Property Income for the tax year 2011/12.

8 Matthew

Matthew owns three cottages that are let out. For the tax year 2011/12 the rent and allowable deductions for each cottage are as follows:

	Rent	*Deductions*
	£	£
Cottage 1	5,000	7,500
Cottage 2	4,000	2,000
Cottage 3	1,500	4,500

All the cottages are let unfurnished.

Calculate Matthew's Property loss for the tax year 2011/12 and discuss the options for its use.

9 Charlie

Charlie lets out a room in his residence to a lodger. The lodger pays rent of £120 per week throughout 2011/12, and the total allowable expenses are £5,100 (including a wear and tear allowance)
Charlie had elected for rent a room relief to apply for 2010/11.

Advice Charlie whether or not he should withdraw the election

10 John

For the past five years John has run a business importing electrical goods from the Far East which he then sells to wholesalers in the UK. His income statement for the year ended 31 December 2011 is as follows:

	£	£
Sales		325,000
Cost of sales		(172,500)
Gross profit		152,500
Rent received (Note 1)		9,500
		162,000
Wages and salaries	50,200	
Rent and rates (Note 1)	12,900	
Light and heat (Note 1)	5,250	
Depreciation of fixtures and fittings	1,500	
Insurance	3,550	
Travelling and entertaining (Note 2)	10,750	
Irrecoverable debts (Note 3)	6,750	
Depreciation of vehicles	7,500	
Motor car expenses (Note 4)	4,500	
Sundry expenses (Note 5)	750	
Legal and professional charges (Note 6)	4,750	
Interest on bank overdraft	1,500	
Van expenses	9,300	
Telephone	3,350	
Repairs and renewals (Note 7)	3,500	
		126,050
Net profit		35,950

Notes

(1) Rent received is in respect of a flat above John's business premises that is rented out. John estimates that a tenth of the rent and rates, and a seventh of the light and heat is in respect of this flat.

(2) Travelling and entertaining expenses:

John's business travelling expenses	5,175
Christmas presents for staff	250
Entertaining UK customers	5,050
Gifts to customers that carry the business name:	
Boxes of chocolate costing £5.00 each	125
Calendars costing £1.50 each	150
	10,750

(3) Irrecoverable Debts

Trading debts written off	5,250
Increase in allowance against specific debtors	1,750
Non trading loan written off	200
A trade debt recovered which had been written off the previous year	(450)
	6,750

(4) Motor car expenses

John's motor car expenses	3,300
Salesman's motor car expenses	1,200
	4,500

John's total mileage for the year was 12,000 miles. During the year he drove 2,000 miles on a touring holiday and estimates that the balance of his mileage is 20% private and 80% business.

(5) Sundry expenses

Donation to national charity	50
Donation to local political party	100
Subscription to chamber of commerce	25

A gift to a member of staff upon marriage	45
John's squash club subscription	250
Advertising in trade press	280
	750

John often uses his squash club as a place to take customers since several of them are keen squash players.

(6) Legal and professional charges

The cost of renewing a 21 year lease in respect of the business premises	250
Accountancy	3,050
Debt collection	300
Legal fees in connection with an action by an employee for unfair dismissal	1,150
	4,750

Included in John's accountancy fee is £950 for taxation services. Of this, £200 is for the normal taxation work involved in submitting accounts to the HMRC. The balance is in respect of calculating John's capital gains tax liability following the disposal of some shares that he had owned.

(7) Repairs and renewals

Repairs to the office photocopier	175
A new printer for the office computer	650
The installation of new central heating for the office	2,200
Decorating the office	475
	3,500

During the year ended 31 December 2011 John took various electrical goods out of stock for his own and his family's use without paying for them. These goods cost £450 and would have normally been sold at a mark up of 30%.

John has a room in his private house that he uses as an office as he often works at home. The allowable amount for the use of the office is £250 and appears to be a fair estimate. Also, John makes business calls from his private telephone and he estimates the business use as two fifths. The total of his private telephone calls for the year was £450.

Calculate John's adjusted profit (before capital allowances) for the year ended 31 December 2011.

11 Carl

Carl prepares accounts to 31 March.
The written down value on the general pool as at 1 April 2011 was £23,500.
In the two years ended 31 March 2013 the following transactions took place.

Year ended 31 March 2012

1 Nov 2011	Purchased machinery costing £106,000.
10 Nov 2011	Sold two lorries (purchased for £8,450 each) for £2,500 each. Purchased two replacement lorries for £15,250 each.
1 Dec 2011	Purchased a motor car with CO_2 emissions of 170 g/km for £16,600.

Year ended 31 March 2013

1 July 2012	Purchased thermal insulation for a business building of £120,000
1 Nov 2012	Purchased a motor car with CO_2 emissions of 140 g/km for £7,500.
1 Dec 2012	Sold the motor car purchased on 1 December 2011 for £12,000.

Calculate the capital allowances available to Carl for the years ended 31 March 2012 and 31 March 2013.

12 Jason

Jason commenced trading on 1 July 2010 drawing up accounts to 31 May each year.
Trading profit for each accounting period is as follows:

	£
1 July 2010 to 31 May 2011	33,000
Year ended 31 May 2012	24,000
Year ended 31 May 2013	36,000

Calculate the trading profit assessments for the relevant tax years and any overlap profits arising.

13 Stephen

Stephen started to trade on 1 February 2007 and decided to retire on 31 October 2012. His accounts shows the following trading income.

	£
P/e 30 April 2008	30,000
Y/e 30 April 2009	10,000
Y/e 30 April 2010	12,000
Y/e 30 April 2011	15,000
Y/e 30 April 2012	18,000
P/e 31 October 2012	7,000

Calculate the trading profit assessments for all relevant tax years.

14 Grace

Grace starts a trade on 1 March 2011, and has the following results (before capital allowances).

Period of account	*Profit*
	£
1 March 2011 – 31 July 2012	192,111
1 August 2012 – 31 July 2013	91,218
1 August 2013 – 31 July 2014	71,671

Plant is bought as follows:

Date	*Cost*
	£
1 May 2011	163,000
1 Dec 2011	18,000
1 Oct 2012	40,000
1 Feb 2014	20,000

On 1 May 2014, plant which had cost £25,000 is sold for £22,000.

Calculate the trading profit assessments for the first five tax years assuming maximum capital allowances are claimed.

15 David

David had been trading for many years preparing accounts to 31 December when he decided to cease trading, results (before capital allowances) have been as follows:

Year ended	£
31 December 2010	25,000
31 December 2011	27,000
Six months to 30 June 2012	14,000

Expenditure on plant had been as follows:

	£
Date	*Cost*
1 June 2010	2,800
1 October 2011	4,600

All items of plant were sold on 30 June 2012 for £4,000 (no item was sold for more than cost).
The written down value of the general pool as at 1 January 2010 was £14,800.
Overlap profit from commencement was £2,000

Calculate the trading profit assessments for the last three tax years of assessments.

16 Max

Max began trading on 1 January 2011. He prepares accounts to 31 December annually, with results as follows:

	Trading profit
	£
Year ended 31 December 2011 Loss	(12,000)
Year ended 31 December 2012 Loss (estimated)	(4,000)
Year ended 31 December 2013 Profit (estimated)	8,000
Year ended 31 December 2014 Profit (estimated)	11,500

Prior to commencing self-employment, Max had the following income from employment:

2007/08	9,200
2008/09	13,800
2009/10	10,100
2010/11	1,400

Max wishes to obtain relief for his initial trading losses as soon as possible.

(a) **Calculate the trading profit assessments for relevant tax years assuming loss relief is carried forward.**

(b) **Show how the losses incurred in the first years of trading can be relieved under special opening year loss relief, by showing the net income of each year affected by the loss relief.**

17 Elliot

Elliot has been in business many years producing accounts to 31 December.
His recent trading profit results are as follows:

y/e 31 Dec 2008	£60,000
y/e 31 Dec 2009	£30,000
y/e 31 Dec 2010	£40,000
y/e 31 Dec 2011	(£60,000)

Elliot's only other income is property income of £6,000 in each relevant tax year.

Assuming Elliot wants to claim relief for the trading loss as soon as possible calculate the taxable income for each relevant tax year.

18 Anne and Betty

(a) Briefly explain the basis by which partners are assessed in respect of their share of a partnership's trading profit.

(b) Anne and Betty have been in partnership since 1 January 1997 sharing profits equally. On 30 June 2011 Betty resigned as a partner, and was replaced on 1 July 2011 by Chloe. Profits continued to be shared equally. The partnership's trading profit is as follows:

	£
Year ended 31 December 2011	60,000
Year ended 31 December 2012	72,000

As at 6 April 2011 Anne and Betty each have unrelieved overlap profits of £3,000.

Calculate the trading profit assessments of Anne, Betty and Chloe for 2011/12 and 2012/13.

(c) Daniel and Elvis have been in partnership since 6 April 1995, making up accounts to 5 April. On 31 December 2011 Elvis resigned as a partner, and was replaced on 1 January 2012 by Frank. For 2011/12 the partnership made a trading loss of £40,000, and this has been allocated between the partners as follows:

	£
Daniel	20,000
Elvis	15,000
Frank	5,000

Each of the partners has investment income. None of them have any capital gains.

State the possible ways in which Daniel, Elvis and Frank can relieve their Trading losses for 2011/12.

19 Renner

Renner is employed by C Ltd, a small family company, in which he holds 20,000 £1 ordinary shares; the remaining 80% are held by the other senior employees.

The company accounts show the following information:

Year to 30 November	*2011*	*2012*
	£	*£*
Salary to Renner (paid at the end of each month)	28,500	33,000
Bonus to Renner (paid in the following February)	4,200	2,700

The following information is provided in respect of 2011/12.

(1) The senior employees have been able to use the company yacht moored on the south coast for two weeks each year since its purchase. Renner spent his fortnight on the boat along with his family. The yacht cost the company £42,000 in 2007 (current value £33,000) and running and maintenance expenses amounted to £6,000 during the year.

(2) Renner belongs to a private medical scheme and the company paid the required premium of £270 (including £50 for his family),

(3) Renner took meals in the fully-subsidised executive canteen; the cost for the year being £135. Another subsidised canteen was available for the other staff.

(4) When at the company premises Renner has use of a 3,500 cc Rolls Royce car owned by the company which emits 268 g/km of CO_2 . It had a list price of £62,000 when new in 2007 and costs £4,800 a year to run. It is garaged at the company's head office and is also used by all the directors.

Renner is also provided with a three year old 2 litre Rover (list price £15,348) with CO_2 emissions of 149 g/km. Renner is provided with private fuel. Both cars run on petrol, and the list price includes delivery and number plates.

(5) He pays 3% of his basic salary into the company's occupational pension scheme. The company contributes 7% of his salary.

(6) Renner is provided with a 3% loan from his employer of £20,000 which was granted three years ago to assist with the purchase of his daughter's residence. He has no other loans and has paid interest only on a monthly basis.

(7) The company also loaned Renner one of its personal computers, with a printer, for use at home so that he could improve his IT skills. The equipment had cost the company £2,800 (including £350 for the printer) in June 2009. The market value of the equipment when it was first provided to Renner on the 6 April 2011 was £2,010.

(8) From 6 June 2011 he lived in Southampton in a house owned by the company which cost £80,000 in 1995. Its market value on 6 June 2011 was £138,000. The annual value for the period from 6 June 2011 to 5 April 2012 can be taken as £900. The company paid the following expenses in connection with the house during his period of residence in 2011/12.

	£
Council tax	550
Electricity	260
Telephone	110
Cleaning	130

The furniture in the house is estimated to have cost £7,200.

(9) Renner received a dividend of 20p per share in May 2011.

Compute Renner's income tax liability for 2011/12

Assume the official rate of interest for 2011/12 is 4.00%.

20 George

(a) George is employed by Exchequer plc earning an annual salary of £100,000 and has made the following gross personal pension contributions since first joining a scheme in June 2009:

2009/10	£28,000
2010/11	£33,000

During 2011/12 he made cash payments of £60,000 into the pension scheme and wishes to know whether tax relief will be available in full on this amount and what will be the maximum contribution he will be able to make in 2012/13.

(b) Osbourne is an employee of Chancellor plc with an annual salary of £200,000pa. He has made regular annual gross personal pension contributions of £60,000pa other than in 2009/10 when his gross contributions were only £30,000. In 2011/12 Osbourne has made gross pension contributions of £90,000.

Compute Osbourne's Income Tax liability for 2011/12.

21 Tony

Tony is in business as a baker, and prepares accounts to 31 March each year. He has given you the following information:

(1) His trading income for the year ended 31 March 2012 was £18,479.
(2) Tony employed Jack and Jill during 2011/12. Their gross wages were £8,200 and £12,480 respectively.

Jack's and Jill's wages and employer's NIC are already accounted in the profit figure which Tony has given you.

You are required to calculate the following:

(c) The total Class 1 NICs payable for 2011/12.

(d) The Class 2 and Class 4 NICs payable by Tony for 2011/12.

22 Chorley Ltd

You are presented with the accounts of Chorley Ltd for the year to 31 December 2011 (see below). Chorley Ltd runs a small printing business and the managing director wishes to know the amount of the companies' Adjusted profit for the year ended 31 December 2011.

	£	£
Gross profit from trading		25,620
Profit on sale of business premises (1)		1,750
		27,370
Advertising	642	
Irrecoverable Debts	75	
Depreciation	2,381	
Light and heat	372	
Miscellaneous expenses (2)	347	
Motor car expenses (3)	555	
Rates	1,057	
Repairs and renewals (4)	2,598	
Staff wages (5)	12,124	
Telephone	351	
		20,502
Profit before tax		6,868

Notes

(1) The profit on the sale of premises relates to the sale of a small freehold industrial unit in which the company stored paper before building the extension.

(2) Miscellaneous expenses included:

	£
Subscription to Printers' Association	45
Contribution to local Enterprise Agency	50
Gifts to customers	
Calendars costing £7.50 each	75
Two food hampers	95

(3) A director uses the motor car 75% for business purposes and 25% for private purposes.

(4) Repairs and renewals comprises the following expenditure:

	£
Refurbishing second hand press before it could be used in the business	522
Redecorating administration offices	429
Building extension to enlarge paper store	1,647
	2,598

(5) Staff wages includes an amount of £182 for a staff Christmas lunch.

Calculate Chorley Ltd's Adjusted profit for year ended 31 December 2011.

23 Sail Ltd

Sail Ltd has the following results for the year ended 31 March 2012. It has one associated company.

	£
Trading profit	380,000
Interest receivable	9,000
Property Income	12,000
Chargeable gains	21,000
Dividends received from UK companies (non associated)	45,000
Gift Aid	22,000

Calculate the amount of corporation tax payable by Sail Ltd for the year ended 31 March 2012.

24 Swish Ltd

Swish Ltd has the following results for the year ended 31 March 2012

	£
Net loss per Accounts (Note (1))	(116,500)
Interest receivable	3,500
Chargeable gain	44,500

Notes

(1) Net loss is after charging:

	£
Depreciation	10,800
Entertaining customers	1,200

(2) All other expenses are allowable for corporation tax.

(3) The written down value of plant and machinery on the general pool at 1 April 2011 was £20,000. There were no purchases or sales during the year ended 31 March 2012.

(4) Swish Ltd has the following results for the previous year:

	31/3/11
Trading profit	40,000
Interest receivable	2,000
Chargeable gain	–
	42,000

(a) To compute the trading loss for the year ended 31 March 2012.

(b) To show how the trading loss is relieved assuming relief is taken as soon as possible.

25 Trunk Limited

Trunk Limited acquired 1,000 shares in Branch Limited on 17th July 1994 costing £10,000. A further 500 shares in this company were acquired on 20th February 1996 costing £6,000. In September 1998 there was a 1 for 2 Bonus issue and in October 1998 a 1 for 3 Rights issue at £9 per share by Branch Limited.

On 15th December 2011 Trunk Limited acquired a further 1,000 shares in Branch Limited costing £15,000 and on 20th December 2011 sold 2,500 shares in Branch Limited for £40,000

Calculate the chargeable gain arriving on the sale of the Branch Limited shares

RPI's to be used are

July 1994	144.0
February 1996	150.9
September 1998	164.4
October 1998	164.5
December 2011	229.2

26 Granger Limited

Granger Limited bought a piece of land in January 1991 for £5,000. In March 2012 the company sold part of the land for £4,500. In March 2012 the remaining part was valued at £20,500.
In addition the company sold some antique furniture for £5,000 in January 2012. It had originally purchased the furniture in August 1996 for £8,000.
It also sold a painting for £6,600 in February 2012. It was purchased in July 1996 for £2,000.

Calculate the net chargeable gain arising on the above transactions

RPI's to be used

January 1991	130.2
July 1996	152.4
August 1996	153.1
January 2012	217.9
February 2012	219.2
March 2012	220.7

27 Westcroft Limited

Westcroft Ltd purchased a painting in June 2007 for £100,000. In September 2011 it was stolen and never recovered. In December 2011 the company received insurance proceeds of £500,000 and immediately acquired a replacement painting for £450,000.

Calculate the chargeable gain arising in December 2011 and the base cost of the replacement painting.

RPI's to be used

June 2007	197.7
September 2011	226.8
December 2011	229.2

28 Mighty Ltd

Mighty Ltd has been offered £160,000 for a freehold factory that it owns, and is now considering disposing of the factory. The company acquired the factory on 15 March 1984 and it now has an indexed cost of £120,000. The factory has always been used by Mighty Ltd for business purposes.

Explain the chargeable gains implications of each of the following alternative courses of action that Mighty Ltd is considering taking to replace the factory if sold:

(a) Acquiring a larger freehold factory for £170,000.

(b) Acquiring a smaller freehold factory for £155,000 and using the remainder of the proceeds as working capital.

(c) Using the proceeds to pay a premium of £180,000 for a 40-year lease of a new factory (it is possible that a freehold warehouse will also be bought in the next two or three years for an estimated cost of £200,000).

29 Claude

For 2011/12 Claude has made the following gains and capital losses:

- a gain of £31,000
- a gain of £24,000
- a capital loss of £7,000
- a capital loss brought forward of £10,000

All three assets were purchased during May 2009 and were sold during September 2011.

Calculate the CGT in 2011/12 assuming his taxable income is £50,000

30 Cheryl

Cheryl disposed of various assets in 2011/12 resulting in chargeable gains of £40,000. Her taxable income was £32,000 and she made a gift aid payment of £1,600 in the tax year.

Calculate Cheryl's capital gains tax for 2011/12 and state the due date for payment

31 Shamus

Shamus acquired a property in October 2011 for £124,000. This was damaged by flooding in December 2011. In January 2012 the insurance company made a payment of £50,000. In February 2012 Shamus spent £60,000 restoring the property. The property was worth £160,000 prior to the restoration. He made an election to deduct the proceeds from the cost of the property on a future disposal.

Calculate the capital gain arising on the receipt of the insurance proceeds in January 2012 and the base cost of the property on a future disposal.

32 Zoe

Zoe acquired 1,500 shares in XYZ Ltd on 30 April 2011 for £18,000, and 500 shares on 31 May 2011 for £7,000.
On 10 February 2012 Zoe bought a further 200 shares in the company for £3,600.

Zoe sold 1,000 shares in XYZ Ltd on 31 January 2012 for £20,000.
Zoe owned less than 5% of the shares in the company.

Calculate Zoe's capital gain on the disposal of the shares

33 Michael

Michael is an employee of Rubber Ltd but owned less than 5% of the company shares. He had the following transactions in the company's shares:

January 2011	Purchased 2,700 shares for £5,400
May 2011	Purchased 600 shares for £1,500
June 2011	Took up 1 for 3 rights issue at £2.30 per share
August 2011	Sold 4,000 shares for £14,000

Calculate the capital gain on the disposal in August 2011.

34 Jenny

Jenny disposed of her entire business in October 2011 giving rise to the following gains and losses.

	Gain	*Loss*
Goodwill	100,000	
Factory used in the business	250,000	
Investment Asset	80,000	
Warehouse		(50,000)

She had owned the business for five years. In addition she disposed of her entire shareholding in Max Limited giving rise to a gain of £145,000.
She owned 15% of the shares in Max Limited for two years and had worked for Max Ltd as an employee for the entire period of ownership.
Jenny has capital losses brought forward at 6 April 2011 of £15,000 and her taxable income was £30,000.

Calculate Jenny's Capital Gains Tax for 2011/12 and state the due date for payment.

35 Beth

Beth bought a factory in September 1988 for £635,000. In December 2011, wishing to move to a more convenient location, she sold the factory for £750,000. She moved into a rented factory until March 2012 when she purchased and moved into a new factory.

What is the base cost of the new factory if it was purchased for

(a) **£700,000,**

or

(b) **£550,000?**

36 Wendy

Wendy purchased shares in an unquoted trading company of which she owned a 1% holding (and worked part time) in November 1989 for £40,000. In January 2012 she sold them to her grandson for £70,000 when their value was £165,000. Wendy and her grandson claimed relief for a gift of business assets.

Required

(a) **What is the chargeable gain, if any, incurred by Wendy?**

(b) **What is the Base cost for Wendy's grandson?**

37 Smithers

Smithers started a retail business in 1985. On 1 May 2011 he transferred his business to a company, Smithers Ltd. The assets transferred are set out below. In exchange he received 4,000 £1 ordinary shares, valued at £80,000 and £20,000 cash.

Assets transferred	*Market value at 1/5/11*	*Gain*
	£	*£*
Freehold premises	35,000	25,000
Furniture and fittings	8,000	-
Plant and machinery	14,000	-
Stock	25,000	-
Goodwill	18,000	18,000
	100,000	43,000

On 1 February 2012 Smithers' sold his entire holding in Smithers Ltd for £150,000

What is Smithers' chargeable gain for 2011/12?

38 Amy

Amy bought a house on 1 April 1985 and occupied as follows:

1/4/85	–	1/4/86	lived in it
1/4/86	–	30/9/90	travels the world and lets the house
1/10/90	–	1/4/94	lived in it
1/4/94	–	1/5/11	house empty

Amy sold the house in May 2011 for £400,000. It cost £190,270 on 1 April 1985

Calculate the chargeable gain on the sale of the house after considering all reliefs

39 Nathan

(a) Nathan made the following lifetime gifts:

(1) 23 October 2002 – A gift of £356,000 into a trust
(2) 17 September 2007 – A gift of £47,000 to his nephew on the occasion of his marriage
(3) 14 February 2009 – A gift to his civil partner of £100,000
(4) 26 August 2010 – A gift of £276,000 to a trust.

Calculate the IHT payable assuming that Nathan pays any IHT due on the first trust and the donees pay IHT due on the second trust. Clearly state who is responsible for paying the tax and the due date for payment.

The nil rate bands are as follows

2002/03	242,000
2007/08	285,000
2008/09	300,000
2010/11	325,000

(b) Nathan dies on 30 November 2011 leaving an estate comprising of a Property valued at £500,000. There was an interest only mortgage of £150,000 outstanding on this property

In addition he owned

Quoted shares in various companies valued at	£120,000
Paintings valued at	£205,000
Motor cars valued at	£50,000
Building society accounts of	£36,000

Nathan had a life assurance policy on his own life. The surrender value at 30 November 2011 was £120,000 and proceeds were received on 30 December 2011 of £105,000

Nathan had credit card debts of £2,500, he had also verbally promised to pay the £1,000 legal fees of a friend. Funeral expenses amounted to £5,000.

Under the terms of his will he left £100,000 to his civil partner Norris, £20,000 to his niece and the residue of the estate to his nephew.

Using the information from the part (a), calculate the IHT as a result of death on the lifetime gifts made by Nathan and the IHT on the death estate.

Clearly state who is responsible for paying the tax, who suffers it and the due date for payment

40 VAT

(a) Kite Ltd started trading on 1 December 2011, and its forecast turnover is as follows:

	£
One month ended 31 December 2011	36,000
Quarter ended 31 March 2012	57,000
Quarter ended 30 June 2012	48,000
Quarter ended 30 September 2012	51,000

Assume that the amounts accrue evenly.

Advise Kite Ltd when it should register for VAT, and if so, when HMRC should be notified.

(b) Cart Ltd is registered for VAT, and its sales are all standard rated. The following information relates to the company's VAT return for the quarter ended 31 December 2011:

(1) Standard rated sales amounted to £240,000. Cart Ltd offers its customers a 5% discount for prompt payment, and this discount is taken by half of the customers.
(2) Standard rated purchases and expenses amounted to £71,280. This figure includes £960 for entertaining UK customers.
(3) On 15 December 2011 the company wrote off irrecoverable debts of £4,000 and £1,680 in respect of invoices due for payment on 10 May and 5 August 2011 respectively.
(4) On 30 December 2011 the company purchased a motor car at a cost of £32,900 for the use of a director, and machinery at a cost of £42,300. Both these figures are inclusive of VAT. The motor car is used for both business and private mileage.

Unless stated otherwise, all of the above figures are exclusive of VAT.

Calculate the amount of VAT payable by Cart Ltd for the quarter ended 31 December 2011.

41 Geewizz Ltd

Geewizz Ltd commenced trading as a manufacturer of children's toys on 1 April 2011, and the company is in the process of completing its VAT return for the quarter ended 31 March 2012.

All of Geewizz Ltd's sales are standard rated. It has recently been suffering a number of irrecoverable debts where customers have not paid. At present, the company does not use the cash accounting scheme.

Geewizz Ltd's first three VAT returns were submitted on 20 August 2011, 26 October 2011 and 25 January 2012 respectively. The VAT payable in respect of the second and third returns was not paid until 11 November 2011 and 5 March 2012 respectively.

(a) Explain the implications if the VAT return and the VAT payable for the quarter ended 31 March 2012 are not submitted to HMRC until 20 May 2012.

(b) State the conditions that Geewizz Ltd needs to satisfy before it will be permitted to use the cash accounting scheme or the annual accounting scheme.

(c) Explain the advantages of using either scheme.

42 Factor Limited

Factor Limited manufactures music CD's. Its customers are mainly overseas.

Discuss the VAT implications of selling the music CD's to non European Union (EU) customers and alternatively EU customers.

Further what are the VAT implications of buying the raw materials to manufacture the music CD's from non EU suppliers and alternatively from EU suppliers.

43 Group Relief

A Ltd controls four companies (all subsidiaries being 100% owned). Each company had the following results for the year ended 31 March 2012.

	Trading profit/(loss)
	£
A Ltd	(100,000)
B Ltd	20,000
C Ltd	83,000
D Ltd	96,000
E Ltd	375,000

Calculate the corporation tax payable.

(a) If no election for group relief is made; and

(b) If an election for group relief is made, on the assumption that A Ltd's loss is allocated in such a manner as to save the maximum amount of tax.

(c) Discuss which companies could form part of a VAT group and why. What are the advantages and disadvantages of a forming of a VAT group?

44 Mn Plc

MN plc, a UK company, has a 100% owned overseas subsidiary, AB Inc and received a dividend of £247,500 net of 10% withholding tax. For the year ended 31 March 2012 MN plc made a UK trading profit of £2,000,000. It also received foreign rental income of £302,250 (net). Overseas tax of £97,750 had been paid in respect of this income.

Compute the UK corporation tax payable for the year ended 31 March 2012.

45 Jim

Jim is required to make payments on account. His income tax payable by self assessment for 2010/11 was £5,100. His income tax payable by self assessment in 2011/12 is £7,629, and he has a capital gains tax liability of £1,000.

State the due dates for payments for tax year 2011/12 and the amount of payment due on each due date.

46 Enquiries

HMRC must give written notice before starting an enquiry into a self assessment personal tax return.

(a) **State the date by which the written notice must normally be given**

(b) **State the circumstances under which HMRC can extend the above deadline and the time limits for this extension.**

(c) **State the three main reasons for the commencement of an enquiry.**

(d) **Explain the choices available to a taxpayer who is notified of an additional liability as a result of an enquiry.**

47 Cannock Limited

Cannock limited is a large company and has Taxable Total Profits in y/e 31 January 2012 of £2,400,000.

Calculate the corporation tax liability of Cannock Limited for the accounting period ended 31 January 2012 and state when this liability is due for payment and the filing date for the corporation tax return.

Paper F6

PRACTICE ANSWERS

1 UK Tax System

Jackie made a mistake on her tax return so this is neither tax avoidance or evasion. She could amend her tax return within 12 months of the filing date. It is unlikely a penalty will be imposed for an incorrect return as this was a genuine mistake.
Michelle deliberately understated the income received. This is tax evasion.
A penalty is likely to be imposed for an incorrect return up to 70% of the tax revenue lost as the behaviour of the tax payer was a deliberate understatement. (The penalty will be 100% if the error was concealed).

2 Kate

Kate Income tax computation 2011/12

	Non savings	*Savings*	*Dividends*	*Total*
	£	*£*	*£*	*£*
Trading profit	36,535			36,535
Employment Income	9,000			9,000
Interest 2,800 × $^{100}/_{80}$		3,500		3,500
Dividends 1,800 × $^{100}/_{90}$			2,000	2,000
Total Income	45,535	3,500	2,000	51,035
Less: Reliefs - Qualifying Interest	(1,000)			(1,000)
Net Income	44,535	3,500	2,000	50,035
Less: Personal Allowance	(7,475)			(7,475)
Taxable income	37,060	3,500	2,000	42,560

Tax calculation	
Non Savings:	
(W1) 37,060 × 20%	7,412
Savings [37,500 - 37,060 = 440]	
440 @ 20%	88
<u>3,060</u> @ 40%	1,224
3,500	
Dividends 2,000 @ 32.5 %	650
Income Tax liability	9,374
Less: tax deducted at source	
Dividends (2,000 × 10%)	(200)
Savings (3,500 × 20%)	(700)
PAYE	(505)
Tax payable	7,969

(W1) 35,000 + (2,000 × $^{100}/_{80}$) = 37,500

Note: The starting rate for savings income is not available as non savings income exceeds £2,560

3 Jessica

Jessica Income tax computation 2011/12

	Non savings	Savings	Total
	£	£	£
Trading profit	90,000		90,000
Bank interest 16,000 × 100/80		20,000	20,000
Total income	90,000	20,000	110,000
Less Personal allowance (W1)	(3,475)		(3,475)
Taxable income	86,525	20,000	106,525

Tax calculation	
Non savings	
(W2) 37,000 × 20% =	7,400
49,525 × 40% =	19,810
86,525	
Savings	
20,000 × 40% =	8,000
Income tax liability	35,210
Less tax deducted at source	
Bank interest 20,000 × 20%	(4,000)
Income tax payable	31,210

(W1) Total income = Net Income	110,000
Less Gift and payment 1,600 × 100/80	(2,000)
Adjusted net income	108,000
Personal allowance	7,475
Less	
½ × (108,000 – 100,000)	(4,000)
Revised personal allowance	3,475

(W2) 35,000 + 2,000 = 37,000
150,000 + 2,000 = 152,000
Note: The starting rate for savings income is not available as non savings income exceeds £2,560.

4 Karl

Karl Income tax computation 2011/12

	Non savings	Dividends	Total
	£	£	£
Employment income	140,000		140,000
Dividend Income 27,000 × 100/90		30,000	30,000
Total income	140,000	30,000	170,000
Less reliefs			
Qualifying interest	(3,000)		(3,000)
Net income	137,000	30,000	167,000
Less personal allowance (W1)	(–)		(–)
Taxable income	137,000	30,000	167,000

Tax calculation	
Non savings (W2)	£
39,000 × 20% =	7,800
98,000 × 40% =	39,200
137,000	

Dividends

(154,000 – 137,000 = 17,000)

17,000 × 32½% =	5,525
13,000 × 42½ % =	5,525
30,000	
Income tax liability	58,050
Less tax deducted of source	
Dividends 30,000 × 10%	(3,000)
PAYE	(48,520)
Income tax payable	6,530

(W1) Adjusted Net income:

Net income	167,000
Less Gift aid 3,200 × 100/80	(4,000)
Adjusted net income	163,000

As Adjusted Net Income exceeds £114,950 the personal allowance is reduced to nil.

(W2) Base rate band £35,000 + £4,000 = £39,000
Additional rate band £150,000 + £4,000 = £154,000

5 Mr & Mrs Elderely

	Non savings	*Total*
	£	*£*
Property Income	45,000	45,000
Total Income	45,000	45,000
Less: Personal Allowance (W1)	(7,475)	(7,475)
Taxable income	37,525	37,525

Tax calculation	
35,000 @ 20%	7,000
2,525 @ 40%	1,010
Tax liability	£8,010

(W1) As Mr Elderely is 68, he is entitled to the age allowance of £9,940, however this is abated to £7,475

PAA	9,940	
less ½ (45,000 – 24,000)	(10,500)	Restriction too high
	7,475	

Mr Elderely is paying tax at 40% on part of his income and is wasting the personal age allowance, and Mrs Elderely is not using her allowance. It would be better to transfer part of the property to his wife such that she would receive some of the income.

Mr Elderely should transfer any share of the property, the income should would then be split 50:50, such that each has income of £22,500 which is below the income threshold for abatement.

Revised calculations

	Mr Elderely		*Mrs Elderely*
Property Income	22,500		22,500
Total Income	22,500		22,500
Less: Personal Allowance	(9,940)		(9,940)
Taxable income	12,560		12,560
Tax calculation			
12,560 @ 20%	2,512	12,560 @ 20%	2,512
Tax liability	2,512		2,512

Combined liability	£5,024
Original liability	£8,010
Tax Saving	£2,986

6 Michael

Michael Income tax computation 2011/12

	Non savings
Property income	110,000
Total income	110,000
Less personal allowance (W1)	(2,475)
Taxable income	107,525

Tax calculation	£
Non savings	
35,000 × 20%	7,000
72,525 × 40%	29,010
107,525	
Income tax liability	36,010

(W1) Michael is 69 years old so is entitled to the personal age allowance.

This will be restricted as net income > £24,000 and the standard personal allowance will be restricted further as adjusted net income > £100,000

Personal age allowance	9,940	
Less ½ × (110,000 – 24,000)	(43,000)	restriction too high
Standard personal allowance	7,475	
Less ½ × (110,000 – 100,000)	(5,000)	
Revised Personal allowance	2,475	

7 Peter

	£	£
Rental income		
Property A - 9/12 × £4,000		3,000
Property B - 9/12 × £5,000		3,750
		6,750
Expenses		
Property A		
Insurance 10/12 × £420	350	
Repainting exterior	810	
Roof repairs (pre-trading expenditure)	1,600	
Property B		
Insurance 10/12 × £585	487	
Letting expenses	40	
Wear and tear allowance 10% × 3,750	375	
		(3,662)
Property Income for the tax year 2011/12		3,088

8 Matthew

The Property loss for the tax year 2011/12 will be £3,500 calculated as follows:

	£
Rental income (5,000 + 4,000 + 1,500)	10,500
Expenses (7,500 + 2,000 + 4,500)	14,000
Property loss	(3,500)

This is carried forward against future property income only.

9 Charlie

Gross rents exceed £4,250
(52 × 120 = £6,240) so two treatments

(1) Normal calculation

	£
Rental income	6,240
less expenses	(5,100)
Property Income	1,140

(2) Alternative calculation

	£
Gross rents	6,240
less rent a room relief	(4,250)
Property Income	1,990

Charlie should withdraw the election so he is assessed on £1,140 in 2011/12

10 John

The adjusted profit should be £48,120 calculated as follows:

	£	£
Net profit per accounts		35,950
Deduct		
Rent received	9,500	
Business use of office at private home	250	
Business use of private telephone: (£450 × ⅖)	180	
		(9,930)
		26,020
Add back:		
Wages and salaries	–	
Rent and rates: £12,900 × 1/10	1,290	
Light and heat: £5,250 × 1/7	750	
Depreciation of fixtures and fittings	1,500	
Insurance	–	
John's business travel	–	
Christmas presents for staff	–	
Entertaining UK customers	5,050	
Gifts of chocolate to customers	125	
Gifts of calendars	–	
Trading debt written off	–	
Increase in allowance	–	
Non trading loan written off	200	
Trade debt recovered (Taxable)	–	
Depreciation of vehicles	7,500	
Private motor expenses: £3,300 × 4,000/12,000 (W1)	1,100	

Salesman's motor car expenses	–	
Donation to national charity	50	
Donation to local charity	–	
Political donation	100	
Subscription to chamber of commerce	–	
Squash club subscription	250	
Advertising in trade press	–	
Cost of renewing 21 year lease	–	
Accountancy:		
Taxation services re capital gains tax	750	
Balance	–	
Interest on bank overdraft	–	
Van expenses	–	
Telephone	–	
Repairs to office photocopier	–	
New printer	650	
Central heating	2,200	
Decorating the office	–	
Goods for own consumption: £450 × 130/100	585	
		22,100
Adjusted profit		48,120

(W1)	Total mileage	12,000
	Private (touring)	(2,000)
		10,000
	Private 20% × 10,000	2,000
	Business 80% × 10,000	8,000

Total private use 4,000/12,000

11 Carl

Year ended 31 March 2012		*General Pool*	*Special Rate Pool*	*Allowances*
	£	£	£	£
WDV b/f		23,500		
Additions Qualifying for AIA				
Machinery	106,000			
Lorries	30,500			
	136,500			
AIA(Maximum)	(100,000)			100,000
		36,500		
Other additions				
Motor car > 160 g/km			16,600	
Disposals		(5,000)		
		55,000	16,600	
WDA @ 20%		(11,000)		11,000
WDA @ 10%			(1,660)	1,660
				112,660
WDV c/f		44,000	14,940	

Year ended 31 March 2013

WDV b/f		44,000	14,940	
Additions Qualifying for AIA				
Thermal insulation for business building	120,000			
AIA - (Maximum)	(100,000)			100,000
			20,000	
Other Additions				
Motor car (111 - 160g/km)		7,500		
Disposals			(12,000)	
		51,500	22,940	
WDA @ 20%		(10,300)		10,300
WDA @ 10%			(2,294)	2,294
				112,594
WDV c/f		41,200	20,646	

12 Jason

		£
2010/11: Actual		
1 July 2010 - 5 April 2011	($\frac{9}{11}$ × 33,000)	27,000
2011/12: 1st 12 months (no CYB)		
1 July 2010 - 30 June 2011	33,000 + ($\frac{1}{12}$ × 24,000)	35,000
2012/13		
Year ended 31 May 2012		24,000
2013/14: (CYB)		
Year ended 31 May 2013		36,000

			£
Overlap period is	1 July 2010 - 5 April 2011		27,000
	1 June 2011 - 30 June 2011	($\frac{1}{12}$× 24,000)	2,000
			29,000

13 Stephen

			£
2006/07 Actual	1/2/07 – 5/4/07	(30,000 × $\frac{2}{15}$)	4,000
2007/08 Actual	6/4/07 – 5/4/08	(30,000 × $\frac{12}{15}$)	24,000
2008/09 12 months to accounting date ended in tax year	12m to 30/4/08	(30,000 × $\frac{12}{15}$)	24,000
2009/10 CYB	Y/e 30/4/09		10,000
2010/11 CYB	Y/e 30/4/10		12,000
2011/12 CYB	Y/e 30/4/11		15,000
2012/13	Y/e 30/4/12		18,000
	P/e 31/10/12		7,000
	Less: Overlap		25,000
	1/5/07 – 5/4/08	($\frac{11}{15}$× 30,000)	(22,000)
			3,000

14 Grace

The capital allowances, computed for each period of account, are as follows:

Period to 31 July 2012		*General Pool*	*Allowances*
Additions qualifying for AIA	**£**	**£**	**£**
Plant 1/5/11	163,000		
Plant 1/12/11	18,000		
	181,000		
AIA (100,000 × 17/12)	(141,667)		141,667
		39,333	
WDA × 20% × 17/12		(11,144)	11,144
			152,811
WDV c/f		28,189	
Period to 31 July 2013			
WDV b/f		28,189	
Additions qualifying for AIA			
Plant 1/10/12	40,000		
AIA	(40,000)		40,000
	–	28,189	
WDA @ 20%		(5,638)	5,638
			45,638
WDV b/f		22,551	
Period to 31 July 2014			
WDV b/f		22,551	
Additions qualifying for AIA			
Plant 1/2/14	20,000		
AIA	(20,000)		20,000
Disposal		(22,000)	
		551	
Small Pool WDA		(551)	551
			20,551
WDV c/f		–	

The Trading profits of the first three periods of account are as follows.

Period of account	*Working*	*Trading Profits*
1/3/11 - 31/7/12	£(192,111 – 152,811)	39,300
1/8/12 - 31/7/13	£(91,218 – 45,638)	45,580
1/8/13 - 31/7/14	£(71,671 – 20,551)	51,120

The assessments are as follows.

Year	*Basis of Assessment*	*Basis period*	*Working*	*Assessment*
2010/11	Actual	1/3/11 - 5/4/11	£39,300 × 1/17	2,312
2011/12	Actual	6/4/11 - 5/4/12	£39,300 × 12/17	27,741
2012/13	12 months to accounting date ended in tax year	1/8/11 - 31/7/12	£39,300 × 12/17	27,741
2013/14	CYB	1/8/12 - 31/7/13		45,580
2014/15	CYB	1/8/13 - 31/7/14		51,120

Overlap profits are those from 1/8/11 – 5/4/12 ie: 8/17 × £39,300 = £18,494.

15 David

Capital allowances for each period of account:

Accounting period ending 31/12/10		*General Pool*	*Allowances*
	£	£	£
WDV b/f		14,800	
Additions qualifying for AIA			
Plant	2,800		
AIA - 100%	(2,800)		2,800
		–	
		14,800	
WDA × 20%		(2,960)	2,960
			5,760
WDV c/f		11,840	
Y/e 31/12/11			
WDV b/f		11,840	
Additions qualifying for AIA			
Plant	4,600		
AIA - 100%	(4,600)		4,600
		11,840	
WDA × 20%		(2,368)	2,368
			6,968
WDV c/f		9,472	
Period to 30/6/12			
WDV b/f		9,472	
Disposal		(4,000)	
		5,472	
Balancing allowance		(5,472)	5,472
		–	

Profits for periods of account:

Period of account	*Working*	*Trading profit*
		£
1/1/10 - 31/12/10	(25,000 - 5,760)	19,240
1/1/11 - 31/12/11	(27,000 - 6,968)	20,032
1/1/12 - 30/06/12	(14,000 - 5,472)	8,528

	Trading profit Assessments	£	£
2010/11	CYB (Y/e 31/12/10)		19,240
2011/12	CYB (Y/e 31/12/11)		20,032
2012/13	Closing year 1/1/12 - 30/6/12	8,528	
	Less overlap profit	(2,000)	6,528

16 Max

(a) Trading profit assessments

	Trading profit assessments £	Trading loss £
2010/11 (1/1/11 - 5/4/11)		
3/12 × £(12,000) (loss)	Nil	3,000
2011/12 (1/1/11 - 31/12/11) (loss)		
(12,000-3,000)	Nil	9,000
2012/13		
Y/e 31/12/12 (loss)	Nil	4,000
		16,000
2013/14		
Y/e 31/12/13	8,000	
Less: carry forward	(8,000)	(8,000)
	Nil	
2014/15		
Y/e 31/12/14	11,500	
Less: carry forward	(8,000)	(8,000)
	3,500	
Loss carried forward		Nil

(b) Loss relief under special opening year loss relief

2010/11 loss of £3,000	This can be relieved against total income of 2007/08, 2008/09, 2009/10 in that order.
2011/12 loss of £9,000	This can be relieved against total income of 2008/09, 2009/10, 2010/11 in that order.
2012/13 loss of £4,000	This can be relieved against total income of 2009/10, 2010/11, 2011/12 in that order.

The revised net income for 2007/08 to 2009/10 is as follows:

	£	£
Loss sustained in 2010/11		3,000
2007/08		
Salary	9,200	
Less: special opening year loss relief	(3,000)	(3,000)
Net Income	6,200	Nil
Loss sustained in 2011/12		9,000
2008/09		
Salary	13,800	
Less: special opening year loss relief	(9,000)	(9,000)
Net Income	4,800	Nil
Loss sustained in 2012/13		4,000
2009/10		
Salary	10,100	
Less: special opening year loss relief	(4,000)	(4,000)
Net Income	6,100	Nil

17 Elliot

Assessments

	£	
2008/09		
y/e 31 Dec 2008	60,000	
2009/10		
y/e 31 Dec 2009	30,000	
2010/11		
y/e 31 Dec 2010	40,000	
2011/12		
y/e 31 Dec 2011	–	(loss of £60,000)

Income Tax Computations

	2008/09	*2009/10*	*2010/11*	*2011/12*
	£	£	£	£
Trading profit	60,000	30,000	40,000	–
Property Income	6,000	6,000	6,000	6,000
Total Income	66,000	36,000	46,000	6,000
Current year				(–)
Carryback			(46,000)	
Net income	66,000	36,000	–	6,000
Personal Allowance	(7,475)	(7,475)	(7,475)	(7,475)
Taxable income	58,525	28,525	–	–

Loss memo:

	£
Trading loss 2011/12	60,000
Carryback 2010/11	(46,000)
Trading loss available to carry forward	14,000

A current year offset could be chosen but this will waste the Personal allowance of 2011/12. As Elliot has traded for many years the special opening years loss relief allowing a 3 year carry back is not available.

18 Anne and Betty

(a) (1) Each partner is treated as a sole trader running a business and is assessed on his / her share of the adjusted trading profit of the partnership using the relevant basis of assessment for each partner. Continuing partners will be assessed using CYB.

(2) The commencement rules apply when a partner joins the partnership.

(3) The cessation rules apply when a partner leaves the partnership.

(b)

	Total	*Anne*	*Betty*	*Chloe*
A/C year ended 31/12/11	60,000			
1/1/11 – 30/6/11				
(6/12 x 60,000) PSR1:1	30,000	15,000	15,000	
1/7/11 – 31/12/11				
(6/12 x 60,000) PSR 1:1	30,000	15,000		15,000
	60,000	30,000	15,000	15,000
A/C year ended 31/12/12	72,000			
PSR 1:1		36,000		36,000

Assessments		£
Anne		
2011/12 (CYB)		
A/C year ended 31/12/11		30,000
2012/13 (CYB)		
A/C year ended 31/12/12		36,000
Betty (note 1)		
2011/12		
6 months to 30/6/11	15,000	
Less: Overlap relief	(3,000)	12,000
Chloe (note 2)		
2011/12 (Actual)		
(1/7/11 – 5/4/12)		
15,000 + (3/12 x 36,000)		24,000
2012/13 (CYB)		
A/C year ended 31/12/12		36,000

Note 1 Betty

Betty ceased trading on 30/6/11 so her final tax year of assessment is 2011/12 in which she will be assessed on all remaining profit as yet not assessed less her overlap relief. Therefore in the preceding tax year, 2010/11 she would have been assessed on her normal CYB i.e. on her share of the profit of the accounting year ended 31/12/10. The only remaining profit to be assessed is therefore for her final 6 months of trading to 30/6/11.

Note 2 Chloe

Chloe commenced trading on 1 July 2011 so her first tax year of assessment is 2011/12 in which an actual basis applies. She is able to use CYB from 2012/13 which for this year will generate an overlap profit of £9,000 (3/12 x 36,000)

(c) (1) Daniel and Frank can carry the loss forward against future trading profits.
(2) Daniel, Elvis and Frank can claim against total income for 2011/12 and/or 2010/11
(3) Frank can claim against total income for 2008/09, 2009/10 and 2010/11. (Special opening year loss relief)
(4) Elvis can claim against trading profit for 2010/11, 2009/10 and 2008/09. (Terminal loss relief)

19 Renner

Income tax computation - 2011/12

	Non-savings	*Dividends*	*Total*
	£	£	£
Earned income			
Employment income (W1)	46,464		46,464
Dividend income (20,000 × 20p × 100/90)		4,444	4,444
Total Income	46,464	4,444	50,908
Less PA	(7,475)		(7,475)
Taxable income	38,989	4,444	43,433

Income tax		£			£
Basic rate:	Non savings	35,000	@	20%	7,000
Higher rate:	Non-savings	3,989	@	40%	1,596
	Dividends	4,444	@	32.5%	1,444
Income tax liability					10,040

Workings

(W1) Employment income

	£
Salary	
($\frac{8}{12}$ × £28,500)	19,000
($\frac{4}{12}$ × £33,000)	11,000
	30,000
Bonus (February 2012)	4,200
Benefits (W2)	13,164
	47,364
Less: Occupational pension contributions (3% × £30,000)	(900)
Employment income	46,464

(W2) Benefits

		£	£
(a)	Use of yacht (Two weeks use only)		
	Annual value		
	20% × (M.V. when first made available to any employee)		
	(20% × £42,000 × 2/52)	323	
	Running expenses (£6,000 × 2/52)	231	
			554
(b)	Private medical insurance - Cost to employer		270
(c)	Subsidised canteen - Exempt benefit		-
(e)	Car scale charges		
	Pool car - exempt benefit		–
	Rover (W3)		2,916
	Fuel charge (petrol)		
	Rover (W3)		3,572
(f)	Employer's contribution into pension - Exempt benefit		-
(g)	Beneficial loan £20,000 × (4% – 3%)		200
(h)	Use of computer equipment		
	MV when first provided		
	Use of asset (20% × £2,010)		402
(i)	Living accommodation		
	Annual value for ten months	900	
	Additional charge for expensive accommodation		
	[(£138,000 – £75,000) × 4% × $\frac{10}{12}$]	2,100	
	Council tax	550	
	Electricity	260	
	Telephone	110	
	Cleaning	130	
	Use of furniture (20% × £7,200 × 10/12)	1,200	
			5,250
	Total assessable benefits		13,164

(W3) Rover - Car and fuel benefits

CO_2 emissions = 145g/km (rounded down to the nearest 5g/km)

Petrol engine

Appropriate percentage = 15% + (145 - 125)=20/5 = 4%
= 19%

Car benefit	(19% × £15,348)	£2,916
Fuel benefit	(19% × £18,800)	£3,572

20 George

(a) The maximum allowable contribution that George may make into his pension scheme, subject to his earnings level for a year is his annual allowance limit of £50,000 plus any unused allowance brought forward from the previous 3 years. For this purpose we compare the gross amount of contributions made in the year with a deemed £50,000 annual limit for each year so long as he was a member of a pension scheme for the tax year in question.

His payment of £60,000 will represent a gross pension contribution of £75,000 (60,000 x 100/80). As this exceeds the annual allowance of 2011/12 he will now be able to use any unused allowance brought forward from the previous 3 years on a FIFO basis i.e. 2008/09, 2009/10 and 2010/11.

As George was not a member of a pension scheme in 2008/09 no unused allowance will be available to carry forward from this year. £22,000 of unused allowance (50,000 – 28.000) is available from 2009/10 and will now be fully utilised, followed by £3,000 of the £17.000 (50,000 – 33,000) unused allowance from 2010/11.

Tax relief will therefore be available on the full contribution of £75,000 (gross) made in 2011/12 and George will have £14,000 of unused allowance to carry forward to 2012/13 which will permit a maximum allowable gross contribution of £64,000 to be made in 2012/13.

(b) **Osbourne – Income Tax Computation 2011/12**

	£
Employment Income	200,000
Annual Allowance Charge (note 1)	20,000
	220,000
Personal Allowance (note 2)	Nil
Taxable Income	220,000

Income Tax Liability

125,000	@ 20%	25,000
95,000	@ 40%	38,000
220,000		63,000

The basic and higher rate bands are extended by the gross amount of personal pension contributions (35, 000 + 90,000 = 125,000) and (150,000 + 90,000 = 240,000)

Osbourne has employment income of £200,000pa and hence all of the £90,000 pension contribution will attract tax relief.

Note 1 Osbourne has his annual allowance for 2011/12 of £50,000 and £20,000 brought forward unused allowance from 2009/10. Therefore an Annual Allowance Charge will arise of £20,000 (90,000 – 70,000)

Note 2 Osbourne has an adjusted net income of £130,000 (220,000 – 90,000) which exceeds £114,950 and thus no personal allowance is available

21 Tony

(a) Class 1 NICs

Employees		
Jack	(8,200 – 7,225) × 12% =	117
Jill	(12,480 – 7,225) × 12% =	631
Employer's		
Jack	(8,200 - 7,072) × 13.8% =	156
Jill	(12,480 – 7,072) × 13.8% =	746
Total Class 1 NICs		1,650

(b) Class 2 NICs

52 × £2.50	130

Class 4 NICs

(18,479 – 7,225) × 9%	1,013

22 Chorley Ltd

	£
Profit before tax per Accounts	6,868
Deduct	
Profit on sale of business premises	(1,750)
Add back:	
Advertising	–
Irrecoverable debts	–
Depreciation	2,381
Light and heat	–
Subscription to printer association	–
Contribution to local Enterprise agency	–
Gifts to customers:	
Calendars	–
Food hampers (1)	95
Director use of car (2)	–
Refurbishing press (3)	522
Redecorating adm offices	–
Building extension (3)	1,647
Staff Christmas lunch and wages (4)	–
Telephone	–
Adjusted profit	9,763

Notes

(1) Gifts to customers are disallowed unless they amount to £50 or less per customer during the year and display a conspicuous advert for the business. Gifts of food (or drink or tobacco) are disallowed irrespective of their cost.

(2) Motor car expenses are all allowable for the company although the director will be taxed as an employee on the private use of the car.

(3) Refurbishment of the second hand press is disallowed on the grounds that the expenditure was necessary before it was brought into use in the business. The extension of the paper store created a new asset and was not the repair of part of an existing one.

(4) The expenditure on the Christmas lunch is allowable in the hands of the employer.

23 Sail Ltd

Corporation tax computation for the year ended 31 March 2012

	£
Trading profit	380,000
Interest receivable	9,000
Property Income	12,000
Chargeable gains	21,000
	422,000
Less: Gift Aid	(22,000)
Taxable Total profits	400,000
Franked investment income (£45,000 × 100/90)	50,000
'Augmented profits'	450,000
Corporation tax liability	
£400,000 at 26%	104,000
Marginal relief 3/200 × (750,000 - 450,000) × $\frac{400,000}{450,000}$ (Note 1)	(4,000)
	100,000

Note 1: Upper limit 1,500,000 ÷ 2 (Sail Ltd plus one associated company) = £750,000 reduced upper limit.

24 Swish Ltd

(a) Computation of Trading loss for the year ended 31/3/12

		£	£
Net loss per accounts			(116,500)
Add back:	Depreciation	10,800	
	Entertaining	1,200	
			12,000
			(104,500)
Less:	Capital allowances £20,000 × 20%		(4,000)
Trading Loss			(108,500)

(b)

	Year ended 31 March 2011	2012
	£	£
Trading profit	40,000	–
Interest receivable	2,000	3,500
Chargeable gain	–	44,500
	42,000	48,000
Less: Current Year / Carry back	(42,000)	(48,000)
Taxable Total Profit	Nil	Nil

Loss memorandum

Loss for y/e 31/3/12 (part (a))	108,500
Less: Current Year relief y/e 31/3/12	(48,000)
Carry back relief y/e 31/3/11	(42,000)
Loss available to carry forward	18,500

25 Trunk Limited

Matching rules

- same day ✗
- previous 9 days ✓ 1,000

Calculate the gain:

	£
Proceeds $\frac{1,000}{2,500} \times 40,000$	16,000
Less cost	(15,000)
Chargeable Gain	1,000

FA85 Share Pool

	Number	Cost	Indexed cost
July 1994	1,000	10,000	10,000
Index up to February 1996 $\frac{150.9 - 144.0}{144.0} \times 10,000$			479
	1,000	10,000	10,479
Purchase February 1996	500	6,000	6,000
	1,500	16,000	16,479
Bonus issue 1:2	750	–	–
	2,250	16,000	16,479
Index up to October 1998 $\frac{164.5 - 150.9}{150.9} \times 16,479$			1,485
	2,250	16,000	17,964
Rights issue 1:3 @ £9 per share	750	6,750	6,750
	3,000	22,750	24,714
Index up to December 2011 $\frac{229.2 - 164.5}{164.5} \times 24,714$			9,720
	3,000	22,750	34,434
Sale December 2011	(1,500)	(11,375)	(17,217)

Calculate the gain

	£
Proceeds $\frac{1{,}500}{2{,}500} \times 40{,}000$	24,000
Less cost	(11,375)
Unindexed gain	12,625
Less indexation allowance (17,217 – 11,375)	(5,842)
Chargeable gain	6,783
Total chargeable gains:	
Previous 9 days	1,000
Pool	6,783
Chargeable gains to include in Corporation tax computation	7,783

26 Granger Limited

(1) Sale of land

	£
Proceeds	4,500
Less cost $5{,}000 \times \frac{4{,}500}{4{,}500 + 20{,}500}$	(900)
Unindexed gain	3,600
Less indexation allowance $\frac{220.7 - 130.2}{130.2} = 0.695 \times 900$	(626)
Chargeable Gain	2,974

(2) Sale of antique furniture - Non wasting chattels rules

	£
Deemed Proceeds	6,000
Less cost	(8,000)
Capital loss	(2,000)

(3) Sale of painting - Non wasting chattel rules

(a) Normal calculation

	£
Proceeds	6,600
Less cost	(2,000)
Unindexed gain	4,600
Less indexation allowance $\frac{219.2 - 152.4}{152.4} = 0.438 \times 2{,}000$	(876)
Chargeable Gain	3,724

(b) Restricted to

5⁄3 [6,600 – 6,000] = 1,000

Take lower gain = £1,000

Total chargeable Gains

	£
Land	2,974
Painting	1,000
Antique	(2,000)
Net Chargeable Gains	1,974

27 Westcroft Limited

		£
Disposal proceeds		500,000
Less cost		(100,000)
Unindexed gain		400,000
Less indexation allowance	$\frac{229.2-197.7}{197.7}=0.159\times 100,000$	(15,900)
Chargeable Gain		384,100

As the proceeds have been used within 12 months of receiving the monies to buy a replacement asset, therefore some of the gain can be deferred. However as only part of the proceeds have been used, some of the gain is chargeable immediately.

Proceeds	500,000
Cost of replacement	(450,000)
Chargeable now	50,000

Available to defer
£384,100 – £50,000 = £334,100

When the replacement painting is sold the base cost is:

Actual cost	450,000
Less Gain Deferred	(334,100)
Base cost	115,900

28 Mighty Ltd

The chargeable gain on the disposal of the freehold factory is £40,000 (£160,000 - £120,000).

(a) Larger freehold factory

The gain will be rolled over against the base cost of the new factory as all the proceeds are reinvested:

	£
Cost of factory	170,000
Gain rolled over	(40,000)
Base cost of new factory	130,000

(b) Smaller freehold factory

As only part of the proceeds are reinvested, the capital gain element that cannot be rolled over will be £5,000 (£160,000 - £155,000). This will be immediately chargeable to corporation tax. The balance of the gain will be rolled over as above.

	£
Cost of factory	155,000
Gain rolled over (£40,000 - £5,000)	(35,000)
Base cost of new factory	120,000

(c) Lease

If all the proceeds are used to acquire a depreciating asset (one with an expected life of less than 60 years), the capital gain is not rolled over but is instead held over. It will become chargeable to corporation tax on the earlier of:

- the date that the lease is sold
- the date when the lease ceases to be used in Mighty Ltd's trade
- the expiry of ten years from the acquisition date.

Therefore the base cost of the lease remains at £180,000. If, before the held over gain becomes chargeable, a non-depreciating asset is acquired, the capital gain can be rolled over in the usual way. In this question, if the freehold of the factory is acquired in the next two to three years, all the proceeds will be reinvested and so the rollover claim would switch to the freehold factory cost of £200,000.

In all the cases above the reinvestment must take place within 1 year before to 3 years after the disposal date if the gain is to be eligible for relief

29 Claude

Claude 2011/12 Capital Gains Tax

	£
Capital Gain	31,000
Capital Gain	24,000
Capital Loss	(7,000)
Net Capital gains arising in 2011/12	48,000
Less Capital loss brought forward	(10,000)
Net Capital Gains	38,000
Less Annual Exemption	(10,600)
Taxable Gains	27,400
Capital Gains Tax payable £27,400 × 28%	£7,672

Due for payment 31 January 2013

30 Cheryl

	£
Chargeable Gain	40,000
Less annual exemption	(10,600)
Taxable gains	29,400
Capital Gains Tax (W1)	£7,732
Due	31/1/13

(W1) Basic rate band remaining
(£35,000 + £1,600 × 100/80) – £32,000 = £5,000)

	£
5,000 × 18% =	900
24,400 × 28% =	6,832
29,400	7,732

31 Shamus

As all proceeds have been used in restoring the asset, and a claim has been made to deduct the proceeds from the cost on a future disposal, there is no gain arising in January 2012.

Base cost of restoration property when sold

Original cost	124,000
Restoration cost	60,000
Less Insurance Proceeds	(50,000)
Base cost	134,000

If no claim was made – the receipt of the proceeds would be a part disposal in January 2012.

	£
Proceeds	50,000
Less cost $124{,}000 \times \dfrac{50{,}000}{50{,}000 + 160{,}000}$	(29,524)
Gain	20,476

On subsequent sale of the restored asset

Original cost (124,000 – 29,524)	=	94,476	Oct 2011
Restoration	=	60,000	Feb 2012
Base cost		154,476	

32 Zoe

Apply matching rules

i)	same day	X		
ii)	Next 30 days	✓	10/2/11	200 shares
	Calculate a Gain			
	Proceeds $^{200}/_{1000} \times 20{,}000$		4,000	
	less cost		(3,600)	
	Capital Gain		400	

iii)	Share Pool	✓		
			Number	*Cost*
	30/4/10		1,500	18,000
	31/5/10		500	7,000
			2,000	25,000
	Disposal		(800)	(10,000)
			1,200	15,000

Calculate the Gain	
Proceeds $^{800}/_{1000} \times 20{,}000$	16,000
Less cost	(10,000)
Capital Gain	6,000

Summary	
Next 30 days	400
Share Pool	6,000
Total Capital Gains	6,400

33 Michael

Apply matching rules

i)	same day	X
ii)	Next 30 days	X
iii)	Share Pool	✓

	Number	*Cost*
January 2011	2,700	5,400
May 2011	600	1,500
June 2011 Rights issue 1:3 @ £2:30	1,100	2,530
	4,400	9,430
Disposal August 2011	(4,000)	(8,573)
	400	857

Calculate the Gain	
Proceeds	14,000
Less cost	(8,573)
Capital Gain	5,427

34 Jenny

Gains not qualifying for ER

	£
Investment asset	80,000
Less capital loss b/f	(15,000)
	65,000
Less Annual exemption	(10,600)
	54,400
CGT @ 28% (Note 1)	£15,232

Gains qualifying for ER

	£
Sale of business	
Goodwill	100,000
Factory	250,000
Warehouse	(50,000)
	300,000
Sale of shares	145,000
	445,000
CGT @ 10%	£44,500

Total CGT £44,500 + £15,232 = **£59,732** Due 31 January 2013

Note:

(1) Jenny's taxable income is below the basic rate band but the gains qualifying for ER effectively use up the remaining basic rate band such that gains not qualifying for ER are taxed at 28%

(2) The remaining gains eligible for ER in future year are (10,000,000 – 445,000) = £9,555,000

35 Beth

(a) New factory purchased for £700,000

	£	£
Purchase cost of new factory		700,000
Capital gain on old factory (£750,000 - £635,000)	115,000	
Restriction on rollover (£750,000 - £700,000)	(50,000)	
Gain rolled over		(65,000)
Base cost of new factory		635,000

Entrepreneurs' relief is not available on the £50,000 gain chargeable as it is not the disposal of the entire business.

(b) New factory purchased for £550,000

In this case the amount of proceeds not reinvested of £200,000 (750,000 -550,000) exceeds the gain made on the old factory. Thus none of the gain is eligible to be rolled over and so there is no adjustment to the base cost of the new factory. It remains at the purchase price of £550,000.

As above entrepreneurs' relief is not available.

36 Wendy

(a) Wendy - Capital gain on shares sold in January 2012

	£	£
Market value of shares in January 2012		165,000
Less: cost		(40,000)
		125,000
Less: Gain deferred with gift relief claim		
Gain	125,000	
Less: Proceeds received - Actual cost (70,000 - 40,000)	(30,000)	
		(95,000)
Chargeable Gain		30,000

(b) Wendy's grandson - Base cost

	£
Market value of shares, January 2012	165,000
Less: Gain deferred	(95,000)
Base cost	70,000

37 Smithers

Capital gain on incorporation - May 2011

		£
Total gains		43,000
Less: Gain rolled over	$\frac{80,000}{80,000 + 20,000} \times 43,000$	(34,400)
Chargeable Gain		8,600

Disposal of shares - February 2012

	£	£
Disposal proceeds		150,000
Less: Cost	80,000	
Less: Rolled over gain	(34,400)	
		(45,600)
Gain		104,400

Total chargeable Gains in 2011/12 = £113,000 (8,600 + 104,400)
The gains would be taxed at different rates due to the impact of entrepreneurs' relief.

38 Amy

Proceeds	400,000
Less cost	(190,270)
Gain	209,730
Less PPR relief (W1)	(84,428)
Less letting relief (W2)	(12,542)
Chargeable Gain	109,394

(W1)

	Actual & Deemed	*Letting*	*Non occupation*	*Total*
1/4/85 – 1/4/86	1yr			
1/4/86 – 30/9/90 (any reason)	3 yrs	1yr 6m		
1/10/90 – 1/4/94	3 yrs 6m			
1/4/94 – 1/5/11 (last 36 months)	3 yrs		14yrs 1m	
	10yrs 6m	1yr 6m	14yrs 1m	26yrs 1m

PPR $209{,}730 \times \frac{10\text{yrs } 6\text{m}}{26\text{yrs } 1\text{m}} = 84{,}428$

(W2) Letting relief

Lower of

- 84,428
- 40,000
- $\frac{1\text{yr } 6\text{m}}{26\text{yrs } 1\text{m}} \times 209{,}730 = 12{,}061$

Letting relief = £12,061

39 Nathan

(a)

Chargeable transfers	23/10/02	17/09/06	26/08/09
	CLT	CLT	CLT
Transfer value	356,000	47,000	276,000
Less: Exemptions:			
AE 02/03	(3,000)		
AE 01/02	(3,000)		
Marriage		(1,000)	
AE 06/07		(3,000)	
AE 05/06		(3,000)	
AE 09/10			(3,000)
AE 08/09			(3,000)
Chargeable Transfer	350,000	40,000	270,000

Note: Transfer to civil partner on 14/02/08 is exempt

Computation of IHT on lifetime transfers chargeable when made

	£	Gross	IHT
23/10/02 CLT	350,000	377,000	27,000
242,000 @ NRB = nil			
108,000 @ 25% = 27,000			
Tax paid by Nathan due 30/04/03			
26/08/09 CLT	270,000	270,000	54,000
NRB of £325,000 deemed used by Gross Chargeable Transfers(GCT's) in previous 7 years		647,000	
∴ 270,000 @ 20%			
Tax paid by trustees due 30/04/10			

(b) Computation of IHT on lifetime transfers chargeable on death - 30 November, 2011

	Gross	IHT
GCT's in 7 years before 17/09/06	377,000	–
27/09/06 PET	40,000	16,000
∴ All £325,000 NRB deemed used = 40,000 @ 40%	417,000	
Less: Taper relief (60%)		(9,600)
Tax payable and borne by donee (nephew)		6,400
26/08/09 CLT	270,000	108,000
GCT's in previous 7 years exceed NRB	687,000	
∴ 270,000 @ 40%		
Less: Taper relief (NIL)		–
Lifetime Tax Paid		(54,000)
Additional Tax Due on Death paid by trustees, borne by beneficiaries		54,000
23/10/09 GCT (23/10/02) Removed from cumulative total	(377,000)	
GCT's in 7 years before death	310,000	

Nathan chargeable Estate at death – 30 November, 2011

	£	£
Property	500,000	

Less: Mortgage	(150,000)	350,000
Quaoted shares		120,000
Paintings		205,000
Cars		50,000
Building Society Accounts		36,000
Life insurance proceeds		105,000
Less: Debts (Note)	2,500	
Funeral expenses	5,000	(7,500)
Less: Exempt transfers		
Civil partner		(100,000)
		758,500
NRB @ death	325,000	
GCT's in 7 years before death	(310,000)	
Remaining NRB	15,000 @ Nil	NIl
Balance of Estate	743,500 @ 40%	297,400
	758,500	

The tax is payable by the Personal Representatives (Executors) and is borne by the residuary legattee (Nathan's nephew).
Note - legal fees of friend not allowable deduction as not legally enforceable debt.

40 VAT

(a) Traders become liable to register for VAT if at the end of any month the value of taxable supplies in the previous 12 months exceeds 73,000, or if the value of the taxable supplies to be made in the next 30 days will exceed £73,000.

Kite Ltd will therefore be liable to register for VAT from 29 February 2012 (36,000 + 19,000 + 19,000 = 74,000), and the company must notify HMRC by 30 March 2012. Kite Ltd will be registered from 1 April 2012.

(b) **VAT Return - Quarter ended 31 December 2011**

	£	£
Output VAT		
Sales (240,000 × 95% (100% - 5%) × 20%)		45,600
Input VAT		
Purchases and expenses (71,280 - 960 = 70,320 × 20%)	14,064	
Irrecoverable debt (4,000 × 20%)	800	
Machinery (42,300 × 20/120)	7,050	(21,914)
VAT payable 31 January 2012		23,686

Notes

1 The calculation of output VAT must take into account the discount for prompt payment, even if customers do not take it.
2 Input VAT on entertaining UK customers cannot be reclaimed.
3 Relief for an irrecoverable debt is not given until six months from the time that payment is due.
4 Input VAT on motor cars not used wholly for business purposes cannot be reclaimed.

41 Geewizz Ltd

(a) The default surcharge

Geewizz Ltd's first VAT return for quarter to 30 June 2011 was due on 31 July 2011 was submitted late, that is on 20 August 2011 so HMRC will have issued a surcharge liability notice specifying a surcharge period running to 30 June 2012.

Although the second and third returns were submitted by the due dates of 31 October 2011 and 31 January 2012 respectively, the VAT due was paid late in each case.

Surcharges of 2% and 5% will therefore have been charged. The surcharge period will have been extended to 31 December 2012.

If the return to 31 March 2012 is late, a surcharge at the rate of 10% will be imposed and the surcharge period will be extended to 31 March 2013.

(b) Cash accounting scheme

Geewizz Ltd can use the cash accounting scheme if:

- its annual taxable turnover does not exceed £1,350,000
- it is up to date with its VAT returns and VAT payments.

(c) The scheme will result in the tax point becoming the date that payment is received from customers. This should be advantageous where customers take extended credit periods since it delays the payment of output VAT until the cash is actually received.

It also provides for automatic bad debt relief should a customer not pay.

OR

(a) Annual accounting scheme

Geewizz Ltd can apply to use the annual accounting scheme if:

- it has been VAT registered for 12 months (unless its turnover is less than £1,350,000, in which case it can join the scheme as soon as it registers for VAT)
- its annual taxable turnover does not exceed £1,350,000
- it is up to date with VAT returns.

(b) Under the scheme only one VAT return is submitted each year, with nine monthly payments being made on account or quarterly payments on account. The payments are based on the VAT liability of the previous year or in the case of a new business on an estimate of the VAT liability for the year. The balancing payment is due two months after the end of the annual VAT period.

The scheme can be beneficial since there is less administration involved in only preparing one VAT return each year. There is also less chance of incurring a VAT penalty.

42 Factor Limited

(a) Selling to non EU customers – the VAT treatment is that sales to non EU customers (VAT registered or non VAT registered) are zero rated.

(b) Selling to EU customers depends on the VAT status of the customer

- sales to VAT registered EU customer are zero rated
- sales to non VAT registered EU customer are standard rated (20%)

(c) Purchases of goods from non EU suppliers involves the goods being charged UK VAT (20%) at the point of entry unless the UK customer has elected for the duty deferment scheme, whereby the associated VAT is paid within 30 days from the end of the month the goods entered the UK.

(d) Purchases of goods from EU suppliers depends upon the VAT status of the EU supplier.

- VAT registered EU suppliers will zero rate the transaction and the UK customer will account for UK VAT on the value of the goods as output VAT on their own VAT return. This will be treated as input VAT in the same period, so recoverable, if the UK customer makes wholly taxable supplies
- Non VAT registered EU supplier will not charge VAT and the are no VAT consequences for the UK customer

43 Group relief

Calculate the upper and lower limits for small companies rate purposes and calculate the tax payable.

Upper limit $\frac{£1,500,000}{5} = £300,000$

Lower limit $\frac{£300,000}{5} = £60,000$

(a) Corporation tax liability without group relief:

	A Ltd	*B Ltd*	*C Ltd*	*D Ltd*	*E Ltd*
	£	*£*	*£*	*£*	*£*
Taxable Total Profits	Nil	20,000	83,000	96,000	375,000
Corporation tax					
at 20%		4,000			
at 26%			21,580	24,960	97,500

Less:					
$\frac{3}{200} \times$ (300,000 – 83,000)			(3,255)		
$\frac{3}{200} \times$ (300,000 – 96,000)				(3,060)	
Corporation tax liability	Nil	4,200	18,325	21,900	97,500

(b) The loss should be surrendered first to companies paying tax in the marginal relief band so as to bring their augmented profits down to the lower limit, as they are paying an effective rate of 27.5% in the marginal band. The loss should then be surrendered to companies paying tax at 26% to bring their augmented profits down to the lower limit. Any remaining loss should be surrendered to companies paying tax at 20%.

	A Ltd	*B Ltd*	*C Ltd*	*D Ltd*	*E Ltd*
	£	*£*	*£*	*£*	*£*
Taxable Total Profits	Nil	20,000	83,000	96,000	375,000
Less: Group relief			(23,000)	(36,000)	(41,000)
Revised Taxable Total Profits	Nil	20,000	60,000	60,000	334,000
Corporation tax					
at 20%		4,000	12,000	12,000	
at 26%					86,840
Corporation tax liability	Nil	4,000	12,000	12,000	97,500

The loss is first surrendered to C Ltd and D Ltd to bring their profits down to £60,000. The balance of the loss is surrendered to E Ltd.

(c) Companies can form a VAT group if they are more than 50% held by another company. As A Ltd owns > 50% of B Ltd, C Ltd, D Ltd and E Ltd, all companies can be a part of a VAT group.

The advantages and disadvantages of companies forming a VAT group are:

The advantages of group VAT registration are:

- No VAT is accounted for on transactions between members within the VAT group
- Only one VAT return is submitted for the group therefore an administrative advantage.
- The group can choose which companies to include or exclude A cash flow advantage would be achieved by leaving out of the group VAT registration a company which makes zero rated supplies and is therefore submitting monthly VAT returns to get monthly repayments of VAT from HMRC.

The disadvantages of group VAT registration are:

- The limits for cash and annual accounting will apply to the group as a whole and not on an individual company basis.
- Joint and several liability of each company in the VAT group for VAT debts, not just the representative member who submits the VAT return.
- Possible administration issues collecting information to be passed on to the representative member.

44 MN plc

The dividend from AB Inc is exempt from UK corporation tax and as AB Inc is an as associated company the dividend will not be classed as FII in the calculation of augmented profits.

Corporation tax computation: year ended 31 March 2012

	Total	*UK*	*Overseas rent*
	£	*£*	*£*
Trading profit	2,000,000	2,000,000	
Overseas rent	400,000		400,000
Taxable Total Profits	2,400,000	2,000,000	400,000
Corporation tax @ 26%	624,000	520,000	104,000
Less: Double taxation relief	(97,750)		(97,750)
UK Corporation tax liability	526,250	520,000	6,250

DTR on the overseas rents is the lower of:

- the overseas tax paid of £97,750
- the UK corporation tax on the overseas rent of £104,000.

Note that the use of a columnar layout makes the DTR calculations easier to follow. and is the method preferred by the examiner. It also makes it easier to demonstrate how either loss reliefs or gift aid payments will be deducted firstly from UK profits before overseas profits when determining the available DTR.

If in the above example MN plc had made a £100,000 gift aid payment during the period this would be deducted in the UK profits column reducing it to £1.9M and would have no effect on the available DTR. If the gift aid payment had instead been deducted from the overseas rent this would have reduced that profit to only £300,000, thus making the UK taxation thereon (at 26%) only £78,000 and with it reducing the DTR to just £78,000 and losing £19,750 (97,750 - 78,000) of foreign tax credit!

45 Jim

Payments on Account for 2011/12 will be based on the tax payable by self assessment in 2010/11

Due Dates

31 Jan 2012	5,100/2 = 2,550
31 Jul 2012	5,100/2 = 2,550
31 Jan 2013	Balancing payment

Tax payable by self assessment	7,629
Less Payments on Accounts	(5,100)
	2,529
Plus CGT Liability	1,000
Balancing payment	3,529

The first payment on account for 2012/13 is based on tax payable by self assessment in 2011/12

	31 Jan 2013	£7,629/2	= £3,814
Total due	31 Jan 2013	= £3,529 + £3,814	= £7,343

46 Enquiries

(a) HM Revenue and Customs (HMRC) must normally give written notice within 12 months of the actual filing date.

(b) HM Revenue and Customs can extend the above deadline by making a discovery assessment to prevent loss of tax. This may be done if the HMRC make a discovery which they could not reasonably have been expected to make from the information provided in the return. This assessment can be made up to 4 years from the end of the tax year, 6 years if the taxpayer has been careless and up to 20 years if the error is deliberate.

(c) An enquiry is normally commenced due to:

- Under-declaration of income.
- Overstatement of deductions.
- Selection for a random review.

(d) The taxpayer can either:

- Accept the HMRC's amendment to the return; or
- Request a review of the decision by a HMRC officer and/or
- Appeal to a tribunal within 30 days of notification of any additional tax due to the enquiry.

47 Cannock Limited

Corporation tax due

	£
FY 2010	
2/12 x 2,400,000 = 400,000 @ 28% =	112,000
FY 2011	
10/12 x 2,400,000 = 2,000,000 @ 26% =	520,000
Total =	632,000

Each instalment is 25% × £632,000 = £158,000

Due Dates for y/e 31 January 2012

	£
14 Aug 2011	158,000
14 Nov 2011	158,000
14 Feb 2012	158,000
14 May 2012	158,000

The return filing date is 31 January 2013

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