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March/June 2017 Exams

ACCA Paper

F6

Taxation (UK)

FA 2015

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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 and the obligations of taxpayer and/or their agents and the implications of non-compliance
- Explain and compute the income tax liabilities of individuals and the effect of national insurance contributions (NIC) on employees, employers and the self-employed
- 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 effects of Value Added Tax on incorporated and unincorporated businesses

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 liabilities arising on chargeable lifetime transfers and on death..

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 and its administration

(a) The overall function and purpose of taxation in a modern economy
(b) Principal sources of revenue law and practice
(c) The systems for self assessment and the making of returns
(d) The time limits for the submission of information, claims and payment of tax, including payments on account
(e) The procedures relating to enquiries, appeals and disputes
(f) Penalties for non-compliance

4.2 Income tax and NIC 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) National Insurance contributions for employed and self employed persons
(g) 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)** Chargeable gains for companies
- **(d)** The comprehensive computation of corporation tax liability
- **(e)** The effect of a group corporate structure for corporation tax purposes
- **(f)** 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
- **(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 basic principles of computing transfers of value
- **(b)** The liabilities arising on chargeable lifetime transfers and on the death of an individual
- **(c)** The use of exemptions in deferring and minimising inheritance tax liabilities
- **(d)** Payment of inheritance tax

4.6 Value added tax

- **(a)** The VAT registration requirements
- **(b)** The computation of VAT liabilities
- **(c)** The effect of special schemes

5 Approach to examining the syllabus

5.1 Assessment: Taxation (GBR)

The syllabus is assessed by a three hour and 15 minute examination. The paper will be predominantly computational and all questions are compulsory.

Section A of the examination comprises 15 objective test (OT) questions of 2 marks each.

Section B of the examination comprises three objective test cases (OT cases), each of which includes five OT questions of 2 marks each.

Section C of the examination comprises one 10 mark and two 15 mark "constructed response" (requiring written answers) questions.

The two 15 mark questions will focus on income tax and corporation tax.

The section A OT questions, section B OT case questions and the other constructed response question in section C can cover any area of the syllabus.

5.2 September 2016 Examinations

For examinations from September 2016 students will have a choice of CBE or paper examinations in respect of the ACCA Fundamental Skills Level papers (F5 - F9).

The computer based and paper examinations will follow the same format,with the following exception:

OT questions in sections A and B of the paper examination will be of multiple choice style only. This means there will be four possible answers to choose from, with only one answer being correct.

OT questions in sections A and B of the computer based examination will be of varying styles. These styles include multiple choice, number entry, pull down list, multiple response, hot area, and enhanced matching.

Section C will be in the same format for both the computer based and paper examinations.

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 – £31,785	20%	10%
Higher rate	£31,786 – £150,000	40%	32.5%
Additional rate	£150,001 and over	45%	37.5%

A starting rate of 0% applies to taxable savings income where it falls within the first £5,000 of taxable income

Personal Allowance

	£
Personal Allowance	10,600
Transferable amount	1,060
Income limit	100,000

Residence status

Days in UK	**Previously resident**	**Not previously resident**
Less than 16	Automatically not resident	Automatically not resident
16 to 45	Resident if 4 UK ties (or more)	Automatically not resident
46 to 90	Resident if 3 UK ties (or more)	Resident if 4 UK ties
91 to 120	Resident if 2 UK ties (or more)	Resident if 3 UK ties (or more)
121 to 182	Resident if 1 UK tie (or more)	Resident if 2 UK ties (or more)
183 or more	Automatically resident	Automatically resident

Child benefit income tax charge

Where income is between £50,000 and £60,000, the charge is 1% of the amount of child benefit received for every £100 of income over £50,000.

Car Benefit Percentage

The base level of CO_2 emissions is 95 grams per kilometre.

The percentage rates applying to petrol cars with CO2 emissions up to this level are:

50 grams per kilometre or less	5%
51 grams to 75 grams per kilometre	9%
76 grams to 94 grams per kilometre	13%
95 grams per kilometre	14%

Car Fuel

The base figure for calculating the car fuel benefit is £22,100

Individual savings accounts (ISAs)

The overall investment limit is £15,240.

Pension Contribution Limits

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

Annual allowance	– 2014–15 and 2015-16	£40,000
	– 2012–13 and 2013–14	£50,000

The maximum contribution that can qualify for tax relief without any earnings is £3,600.

Authorised mileage allowances

All cars

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

Capital Allowances

Plant and machinery

Main pool	18%
Special rate pool	8%

Motor cars

New cars with CO_2 emissions up to 75 grams per kilometre	100%
CO_2 emissions between 76 and 130 grams per kilometre	18%
CO_2 emissions over 130 grams per kilometre	8%

Annual investment allowance

Rate of allowance	100%
Expenditure limit	£500,000

Cap on income tax reliefs

Unless otherwise restricted, reliefs are capped at the higher of £50,000 or 25% of income.

Corporation Tax

Rate of tax	20%
Profit threshold	£1,500,000

TAX RATES AND ALLOWANCES

Value Added Tax

Standard rate	20%
Registration limit	£82,000
Deregistration limit	£80,000

Inheritance Tax: Tax Rate:

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

Inheritance Tax: 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%

Rates of Interest

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

Capital Gains Tax - Individuals

Annual Exempt Amount		£11,100
Rate of tax	– lower rate	18%
	– higer rate	28%
Entrepreneurs' relief	– lifetime limit	£10,000,000
	– Rate of tax	10%

National Insurance (not contracted out rates)

		Annual		
Class 1	Employee	£1 - £8,060	@	0%
		[£8,061 – £42,385]	@	12%
		£42,386 and above	@	2%
Class 1	Employer	£1 - £8,112	@	0%
		£8,113 and above	@	13.8%
		Employment allowance		£2,000
Class 1A				13.8%
Class 2		£2.80 per week		
		Small earnings exemption limit		£5,965
Class 4		£1 - £8,060 per year	@	0%
		£8,061 – £42,385 per year	@	9%
		£42,386 and above per year	@	2%

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

2. All apportionments should be made to the nearest month.

3. All workings should be shown in Section C

Chapter 1

THE UK TAX SYSTEM

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 and a new "General anti-abuse rule" has been introduced to back up the existing specific legislation. The rule targets abusive arrangements (action that cannot be regarded as reasonable) arising from tax arrangements designed to achieve tax advantages such as decreasing a source of income or overstating a deduction.

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 taxes apply to the following situations and state whether the tax is direct or indirect

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

(b) A company has profit of £250,000 in a year and employs 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 his estate of £1,000,000 to his children

Chapter 2

INCOME TAX COMPUTATION

1 Introduction

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

The Taxable Income will 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.

In computing Taxable Income UK taxpayers may be entitled to a deduction of a Personal Allowance, a level of tax free income. The details of this are in Section 3 of this chapter, but the normal Personal Allowance available is £10,600 for the 2015/16 tax year.

One of the 15 mark questions in section C of the exam will be on income tax which in many cases will require the candidate to prepare an income tax computation.

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 2015/16 runs from April 6, 2015 to April 5, 2016. Therefore each source of taxable income requires its own basis of assessment to determine how much of that income is to be assessed to tax in each such tax year.

Proforma income tax computation for 2015/16

	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)
Other Trading Loss reliefs	(X)			(X)
NET INCOME	X	X	X	X
Less: Personal Allowance (PA)	(X)			(X)
TAXABLE INCOME	X	X	X	X

* Employment income, salaries or wages, must be included gross before deduction of taxes by the employer and will always be stated gross within the question

* * These sources of income are received net of either an actual or deemed deduction of tax at source but must always be included gross in the computation

*** Deductions from Total Income and the deduction of the PA from Net Income are deducted in order from firstly non savings income, then savings income and finally dividend income

1.1 Exempt Income

The following are the main examples of sources of income that 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

1.2 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 and on dividend income

1.3 Taxation of non-savings income.

Non-savings income is taxed at the following rates:

£1 to £31,785	20%	(basic rate)
£31,786 – 150,000	40%	(higher rate)
£150,001 +	45%	(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 has been working for many years and earns a salary of £50,000 per annum (PAYE £9,403).

Calculate the income tax payable by Mr Smith for 2015/16.

2 Savings income and Dividend Income

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

2.1 Taxable interest income received net

(a) Building society interest

(b) Bank deposit interest

(c) Company loan stock interest

Most building society interest, bank deposit interest and company debenture interest is received by individuals net of 20% income tax deducted at source by the payer and payable by them to HMRC. It must however always be included in gross form on the income tax computation - see the proforma computation on page 5 for the grossing up calculation (amount received x 100/80). This tax credit is repayable if the amount deducted at source exceeds the Tax Liability of the taxpayer.

2.2 Taxable interest received Gross:

(a) National Savings & Investment (NSI) Bank Interest

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

2.3 Basis of assessment

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

2.4 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 and may only reduce the tax liability to nil. Any tax credits then on interest income or PAYE may generate a repayment of tax to the taxpayer.

2.5 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) Taxable 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 at 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 £31,785	20%
	£31,786 – 150,000	40%
	£150,001 +	45%
Savings	• Savings income is taxed in the same way as non-savings income, however a starting rate of tax of 0% (yes zero!) will apply to the first £5,000 of savings income in the following circumstance: • The 0% rate only applies where savings income falls within the first £5,000 of taxable income. • If the first £5,000 of taxable income consists of non-savings income then the 0% rate will not apply.	
Dividends	• After considering non savings and savings income the dividend tax rates are: £1 – £31,785 @ 10% £31,786 – £150,000 @ 32.5% £150,001 + @ 37.5%	

Example 2

Billy had a trading profit of £25,600 and received bank deposit interest of £8,000 in 2015/16

Calculate Billy's income tax payable in 2015/16

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 2015/16.

Calculate Molly's income tax payable in 2015/16

Example 5

Rework the example of Molly, assuming she makes a trading profit of £11,600 in addition to the bank interest.

Example 6

Daisy received a salary of £18,600 (PAYE £1,400), received £8,000 bank deposit interest and dividend income of £1,800 in 2015/16

Calculate Daisy's income tax payable for 2015/16

Example 7

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

3 Personal allowance

The Personal Allowance (PA) is a level of tax free income available to UK taxpayers and is deducted from Net Income to derive Taxable Income on the Income Tax Computation and as can be seen on the pro forma computation on page 5 is deducted from the analysis columns in the order of firstly non-savings income, followed if necessary by savings income and finally dividend income.

- The normal PA for 2015/16 is £10,600. However if an individuals' Adjusted Net Income (ANI) exceeds £100,000 then the PA is reduced by:

  ½ × [ANI – £100,000]

- Once adjusted net income ≥ £121,200 the PA is reduced to nil.
- Net income is total income less qualifying interest payments and trading loss reliefs (see pro forma page 5)
- ANI is net income less gross personal pension contributions and less gross gift aid payments (see section 5)

Example 8

Mike received gross employment income of £108,000 in 2015/16 of which £33,130 was deducted at source under PAYE in 2015/16.

Calculate Mike's income tax payable for 2015/16.

Example 9

Ken made trading income of £130,000, received bank interest of £32,000 and dividend income of £32,400 in 2015/16.

Calculate Ken's income tax payable for 2015/16.

EXAMPLE 10

James has a trading income assessment in 2015/16 of £102,000 and received bank interest of £3,200.

Calculate the income tax payable by James for 2015/16

3.1 Transferable amount of Personal allowance

From 2015/16 an election may be made to transfer a fixed 10% of the PA to a spouse or civil partner. The election is only available when both taxpayers are either just a basic rate taxpayer or non taxpayer. The election is only likely to be made when one spouse has an amount of unused PA that would otherwise be wasted and the other spouse is only a basic rate taxpayer.

The election must be made within 4 years of the end of the tax year to which it should apply though if made within the tax year concerned the election will remain in force for future years until it is either withdrawn or the conditions are not met.

The relief is given as tax credit to be deducted in deriving the tax liability of the taxpayer and is computed as 20% of the transferred PA which for 2015/16 would be computed as (10% x 10,600) x 20% = 212. This amount can only reduce the tax liability, it cannot create a repayment. The amount of the transferable PA will be given in the tax rates and allowances provided in the exam.

This is also known as the marriage allowance or marriage tax allowance.

EXAMPLE 11

David and Victoria are married and in 2015/16 David had a trading income assessment of £8,000 and Victoria received a salary of £30,000.

Calculate the income tax liabilities of David and Victoria assuming that an election is made to transfer 10% of David's personal allowance to Victoria and state the date by which the election should be made.

4 Deductions from Total Income

4.1 Reliefs are tax deductible

The only reliefs examinable at Paper F6 are

(a) qualifying interest

(b) loss reliefs - These reliefs are deducted from total income in deriving net income and as with the deduction of the PA from net income they are deducted firstly from non savings income before savings income and then dividend income

4.2 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

4.3 Loss reliefs

These will be explained in chapter 7 section 4

Example 12

Kathy has trading profit of £50,000 in 2015/16 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 2015/16

5 Payments to charity under the Gift Aid System

5.1 The gift aid system is a tax efficient way by which to give money to charity and is available to all taxpayers

5.2 Basic rate taxpayers

Payments to charity under gift aid are treated as being paid net of the basic rate of 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 . The charity will then 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 shown as a deduction in the calculation of Taxable Income.

5.3 Higher rate tax payer

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

(a) 20% at source (as noted above), and

(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 gift aid payments made by 31 January to have been made in the previous year, ie a payment made by 31 January 2017 can be treated as if paid in tax year 2015/16. This would be advantageous if the taxpayer was likely to be a basic rate taxpayer in 2016/17 but was a higher rate taxpayer in 2015/16 and would also be better for cash flow purposes by reducing last year's tax payable instead of this year's.

This would also be advisable if in 2015/16 the taxpayer had adjusted net income between £100,000 and £121,200 and was therefore suffering a loss of their PA.

5.4 Additional rate tax payer

For additional rate taxpayers, 45% tax relief is given as follows:

(a) 20% at source (as noted above) and

(b) 25% through the income tax computation by extending both the basic rate band and higher rate band by the gross donation (so that more income is taxed at 20% instead of 40% and 40% instead of 45%)

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

See section 3 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 13

Elliot has trading profit of £48,000 in 2015/16. He paid £1,600 to charity under the gift aid system.

Calculate Elliot's income tax liability for 2015/16

Example 14

Thomas earned £160,000 trading profit in 2015/16. In the tax year he paid £6,400 to charity under the gift aid scheme.

Calculate Thomas's income tax liability for 2015/16.

Example 15

Kerry made a trading profit of £101,000 in 2015/16. 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 2015/16.

6 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.

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 allow couples to rearrange joint income between them to better use their personal allowances 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, 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 transferee 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 16

Elton is a higher rate taxpayer (but with an adjusted net income of ≤ £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 thereon. David his civil partner has no income.

Discuss how Elton and David could reduce their income tax liabilities

7 Child Benefit Income Tax Charge

Child benefit is a tax free benefit payable to parents irrespective of the level of taxpayer they may be. It was decided therefore that from the tax year 2013/14 if a person's Adjusted Net Income (ANI) (or whose partner) exceeds £50,000 and they received child benefit, that a child benefit income tax charge would be raised to gradually remove the benefit from such higher income earners such that when the ANI reached £60,000 the benefit would be entirely removed.

If both partners have income over £50,000 the partner with the higher income is liable for the charge.

Where ANI falls between £50,000 and £60,000 the income tax charge would amount to 1% of the child benefit received for every £100 of income in excess of £50,000.

The following information will therefore be provided in the tax rates and allowances section of the examination paper:

Where income is between £50,000 and £60,000 the charge is 1% of the amount of child benefit received for every £100 of income over £50,000.

The income tax charge is added in deriving the income tax liability of the taxpayer.

Illustration 1
Catherine received child benefit of £1,056 in 2015/16 and has ANI for the year of £54,000.
As Catherine's ANI is between £50,000 and £60,000 the child benefit income tax charge is £422 (£1,056 x 40% (54,000 – 50,000 / 100))

Illustration 2
Victoria receives child benefit of £3,147 in respect of her 4 children and has ANI of £77,000.
As Victoria's ANI exceeds £60,000 the child benefit income tax charge is £3,147, being the full amount of the child benefit received.

8 Residence

A taxpayer's liability to income tax, CGT and IHT is based upon their residence and / or domicile. At F6 a UK resident will be liable to income tax on worldwide income and a non UK resident will be liable on only UK income. It is essential therefore to determine the residence of the taxpayer to be able to determine their UK tax liability

These rules are detailed and the following table will therefore be given in the tax rates and allowances section of the examination paper.

Days in UK	Previously Resident (R)	Not Previously Resident (R)
<16	Automatically NOT R	Automatically NOT R
16 – 45	R if 4 UK ties	Automatically NOT R
46 – 90	R if 3 UK ties	R if 4 UK ties
91 – 120	R if 2 UK ties	R if 3 UK ties
121 – 182	R if 1 UK tie	R if 2 UK ties
>183	Automatically R	Automatically R

In the above table a taxpayer is Previously Resident if they have been resident in any of the previous 3 tax years.

The above table shows that the following persons will automatically be treated as NOT resident in the UK:

- Anyone in the UK for less than 16 days in tax year.
- A person in the UK for less than 46 days in tax year and who was not resident in previous 3 tax years

In addition a person who works full time overseas and who has not been in the UK for more than 90 days in the tax year is automatically not resident.

The above table also shows that any person in the UK for at least 183 days in the tax year is automatically RESIDENT. The following persons are also treated as automatically resident, unless they meet one of the automatic non-resident tests:

- A person whose only home is in the UK
- A person who carries out full time work in the UK

Where none of the automatic tests apply then based on the above table a person's status will be based on both how many days they are in the UK and how many ties they have with the UK in a tax year.

There are 5 UK ties as follows:

- Spouse/civil partner or minor child in the UK
- House in UK which is used during tax year
- In UK for more than 90 days in either of 2 previous tax years
- More time in UK than in any other country in tax year
- Doing substantive work in UK

A UK day is where the person is in the UK at midnight.

The detailed rules are far more complex but only the above rules are examinable.

Illustration 1
Sebastian was not previously resident in the UK but spent 35 days in the UK during 2015/16.

Sebastian is automatically not resident, as in UK for less than 46 days and not previously resident.

Illustration 2
Fernando was not previously resident in UK but bought a holiday home in the UK on 1 May, 2015 and lived in it for 140 days in the 2015/16 tax year. The remainder of the year he lived in his home in Spain.

Fernando was in the UK too long (>45 days) to be automatically treated as not resident, but not long enough to be treated as automatically resident (<183 days) nor did he have his only home in the UK.

Using the table therefore as he has been in UK for between 121 days and 182 days and has only one tie with the UK (made use of UK house), so as he was not previously UK resident he is therefore not UK resident in 2015/16.

Illustration 3
Lewis was in the UK for 80 days in 2015/16 when he lived in the only home that he owns.

Lewis has been in the UK too long to be treated as automatically not resident, irrespective of his previous residence. He will, however be treated as automatically UK resident as his only home is in the UK.

Illustration 4
Jensen has always been UK resident spending about 10 months of the year in the UK, but on 1 May, 2015 he purchased an apartment overseas where he lived for most of the tax year returning to the UK for a further 50 days in 2015/16 when he stayed at the family home with his wife and children.

Jensen has spent more than 15 days in UK in 2015/16 so will not be automatically not resident. He will also not be automatically resident in the UK as he has not spent 183 days in the UK nor does he have his only home in the UK.

As he was in the UK for between 46 and 90 days he will remain resident for 2015/16 as he has 3 UK ties:
- Spouse/children in UK
- A house in the UK that he uses
- In the UK for more than 90 days in previous 2 years

You should now work through the following part of the Finance Act 2015 technical article written by the F6 examining team - Income Tax section to example 6

Chapter 3

PROPERTY INCOME AND INVESTMENTS – INDIVIDUALS

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 computed as the rental income accrued less allowable expenses incurred.

EXAMPLE 1

Jim bought a property and rented it out for the first time on 1 July 2015. 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 2015 for redecoration and £500 in May 2016 for repairs completed in March 2016.

Calculate the Property Income for 2015/16.

1.2 Allowable deductions

(a) To be allowable an expense 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% × rental income

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

10% × (rental income less council tax / business rates and water rates)

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

Example 2

Sid owns a furnished property that is let out at an annual rent of £9,600, payable monthly in advance. During the year 2015/16 he made the following payments:

May 2015	Construction of a garage, replacing the car port	£2,000
June 2015	Insurance for year from 1 July 2015 (insurance for the previous year to 30 June 2015 was £420)	£480
November 2015	Drain clearance	£380
May 2016	Redecoration (work completed in March 2016)	£750

The tenant vacated the property during June 2015 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 2015.

Calculate the Property Income for 2015/16 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 profits 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 (see chapter 5) 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 (see chapter 14).

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 210 days in the tax year.

(e) The accommodation must actually be let for at least 105 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 exceeds £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 2015/16 by 31 January 2018 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 per year

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 2015
Annual rent £5,000 due on 1 July 2015

Term	20 years
Premium	£60,000

Calculate the Property Income assessment for Bill in 2015/16

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 Individual Savings Accounts (ISA's) have for many years been the most common form of tax efficient investment.

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 £15,240 per tax year and ISA's permit the taxpayer complete flexibility over the mix of investments in either cash or stocks and shares. This limit will be provided 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 & Investments (NS&I) products are taxable, namely:

- NS&I Easy Access account / NS&I Direct Saver Account
- NS&I Investments accounts

The income is received gross without deduction of tax at source.

The nature of the investments are historically risk free.

You should now review the ISA section of the Finance Act 2015 technical article written by the F6 examining team and then attempt Practice Questions 1 to 9

Free lectures available for Paper F6 - click here

Chapter 4

TAX ADJUSTED TRADING PROFIT – INDIVIDUALS

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) The tax adjusted trading profit for inclusion within the income tax computation is not the same as the profit shown in the individuals statement of profit or loss. Accounting profits before tax are adjusted to arrive at tax adjusted trading profit. The main adjustments are to disallow for tax certain non-allowable expenses and to exclude from the assessment any non-trading income

(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 130g/km

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

(j) Premium paid for the grant of a lease (see chapter 3).

» 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 2015 Jeremy commenced in self-employment running a retail shop. Jeremy's statement of profit or loss for the year ended 31 May 2016 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 statement of profit or loss for light, heat, rent and rates, 40% relates to the flat.

Note 2: Motor expenses

During the year ended 31 May 2016, 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 2015, and £1,050 for decorating the private flat during August 2015. 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 2016, 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 2016 are £13,060.
(In the actual examination you will be required to prepare a capital allowances computation and work out this figure. - see chapter 5)

Calculate Jeremy's tax adjusted trading profit for the year ended 31 May 2016.

After completing this chapter you may now attempt Practice Question 10

Free lectures available for Paper F6 - click here

Chapter 5

CAPITAL ALLOWANCES

1 Capital allowances

1.1 Capital Allowances replace the disallowed depreciation charge in the adjustment of profits, giving tax relief against trading profits in respect of expenditure incurred on qualifying plant and machinery.

Plant is generally defined as assets that perform an active function in the business – something with which the trade is carried on and will include office furniture and equipment including moveable office partitioning. Machinery will include motor vehicles and computers, including building alterations necessary for the installation of plant and machinery.

Capital allowances are now also available on integral features of a building including lifts and escalators, electrical systems, heating and air cooling systems

1.2 If a business is VAT registered and the input VAT is recoverable on the purchase of an asset then the VAT exclusive net cost will be available for capital allowances. If the VAT is not recoverable as on the purchase of a car or if the business is not VAT registered then the VAT inclusive price will attract capital allowances.

2 Capital Allowance Computations

2.1 Capital allowance computations will be prepared for the accounting period of the business not the tax year and will be deducted from the adjusted trading profit of that accounting period.

2.2 **There are 3 types of capital allowance available on the qualifying cost of qualifying plant and machinery.**

(1) Annual Investment Allowance (AIA)

The AIA gives an allowance of 100% for the first £500,000 of qualifying expenditure incurred in a 12 month accounting period. If the accounting period of the business is other than 12 months then the AIA will be time apportioned accordingly, for example a business that has prepared its accounts for a 6 month period would be entitled to AIA of £250,000 (6/12 x 500,000). The £500,000 limit applies in the F6 exam regardless of the period covered by the exam question

AIA is available on the purchase of all plant and machinery except motor cars.

Any expenditure in excess of the AIA limit or on the majority of motor cars will qualify instead for a writing down allowance (WDA)

(2) Writing Down Allowance (WDA)

The cost of most plant and machinery that has not qualified for AIA will be allocated to a pool of expenditure that will then be eligible for a WDA of either 18% per annum if expenditure qualifies for the main pool, or 8% per annum if allocated to the special rate pool, available on a reducing balance basis.

As with AIA the WDA will be time apportioned where the accounting period is other than 12 months.

Illustration 1

Richard commenced to trade on 1 July 2015 and prepared accounts to 31 December 2015 and to 31 December thereafter. Richard made the following acquisitions of main pool assets:

Accounting Period to 31 December 2015		**£**
1 July 2015	Plant	220,000
20 October 2015	Computer equipment	80,000
Accounting Year ended 31 December 2016		
19 October 2016	Machinery	30,000

Capital Allowance Computations

6 month period to 31 December 2015			*Main Pool*	*Allowances*
Additions (AIA)				
1 July 2015	Plant	220,000		
20 October 2015	Computers	80,000		
		300,000		
AIA (max 6/12 x 500,000)		(250,000)	50,000	250,000
WDA (max 6/12 x 18% x 50,000)			(4,500)	4,500
Total Allowances				254,500
Tax Written Down Value (TWDV) c/f			45,500	
Year Ended 31 December 2016				
TWDV b/f			45,500	
Additions (AIA)				
19 October 2016		30,000		
AIA		(30,000)		30,000
WDA (18%)			(8,190)	8,190
Total Allowances				38,190
TWDV c/f			37,310	

(3) First Year Allowance (FYA)

New cars with CO_2 emissions up to 75 grams per kilometre attract a 100% FYA. The FYA is never time apportioned.

3 Capital Allowance Rates

3.1 The capital allowances information that will be given in the tax rates and allowances section of the examination papers for the September 2016 exam through to the March 2017 exam sitting is as follows:

Rates of allowance	**%**
Plant and machinery	
Main pool	18
Special Rate Pool	8
Motor Cars	
New cars with CO_2 emissions up to 75 grams per Km	100
CO_2 emissions between 76 and 130 grams per Km	18
CO_2 emissions over 130 grams per Km	8
Annual Investment Allowance	
Rate of allowance	100
Expenditure limit	£500,000

As can be seen from this information it is therefore essential for students to know what type of allowances are available for each asset acquired during the accounting period of the business:

As stated in section 3 above new cars with low CO_2 emissions qualify for a 100% FYA.

As stated in section 2 above all plant and machinery with the exception of cars will qualify for AIA with any excess expenditure over £500,000 per annum and cars then qualifying for WDA at either 18% per annum if qualifying for the main pool or 8% per annum if allocated to the special rate pool.

If expenditure exceeds the AIA limit the AIA should therefore be allocated firstly to special rate expenditure before main pool expenditure, as any excess expenditure will only attract 8% WDA in the special rate pool, whereas 18% is available in the main pool. It is therefore necessary to know what expenditure is excluded from the main pool and allocated instead to the special rate pool.

4 Special Rate Pool

The following asset acquisitions should be allocated to the special rate pool:

(1) Integral features of a building

- Lifts and escalators
- Electrical and general lighting systems
- Cold water systems
- Space or water heating systems
- Systems of ventilation, air cooling or purification

(2) Long life assets

Assets, when new, with an expected economic working life of 25 years or more when total expenditure based on a 12 month accounting period exceeds £100,000

(3) Thermal insulation of a building, and

(4) Motor cars with CO2 emissions over 130 grams per Km

Note however that this expenditure being on cars does NOT qualify for AIA and only the 8% WDA is available

Illustration 2

Steven prepares accounts to 5 April

The WDV of the main pool at 6 April 2015 is £40,000. The following transactions took place during the year ended 5 April 2016:

4 May 2015	Purchased plant for £50,000
30 June 2015	Purchased a motor car for £11,200 CO_2 of 120g/km
6 July 2015	Purchased a motor car for £14,100 CO_2 of 170g/km
15 March 2016	Purchased a motor car for £14,400 CO_2 of 65g/km

Calculate the capital allowances for the year ended 5 April 2016.

Accounting period to 5 April 2016

		Main Pool	*Special Rate Pool*	*Allowances*
		£	*£*	*£*
WDV b/f		40,000		
Additions qualifying for AIA				
Plant	50,000			
AIA	(50,000)			50,000
Other additions				
Motor car (120g/km)		11,200		
Motor car (170 g/km)			14,100	
		51,200	14,100	
WDA @ 18%		(9,216)		9,216
WDA @ 8%			(1,128)	1,128
Additions qualifying for 100% FYA				
Motor car (65g/km)	14,400			
FYA @ 100%	(14,400)			14,400
				74,744
WDV c/f		41,984	12,972	

Illustration 3

Kenny prepares accounts to 5 April. As at 6 April 2015 the WDV brought forward on the main pool was £22,000.
The following transactions occurred in the year ended 5 April 2016.

22 July 2015	Purchased machinery	£45,000
13 November 2015	Purchased a long life asset	£530,000
25 February 2016	Purchased a motor car CO_2 emissions of 125g/km	£8,000

Calculate Kenny's capital allowances for year ended 5 April 2016

Accounting period to 5 April 2016

		Main Pool	*Special Rate Pool*	*Allowances*
	£	£	£	£
WDV b/f		22,000		
Additions qualifying for AIA				
Long life asset	530,000			
AIA (Maximum)	(500,000)			500,000
			30,000	
Additions qualifying for AIA				
Machinery	45,000			
AIA	(–)			
		45,000		
Other additions				
Motor car (emissions 125g/km)		8,000		
		75,000	30,000	
WDA @ 18%		(13,500)		13,500
WDA @ 8%			(2,400)	2.400
				515,900
WDV c/f		61,500	27,600	

5 Sale of plant and machinery

When plant and machinery is sold in the accounting period the sale proceeds, up to a maximum of the original cost of the asset, is deducted from the balance of the unrelieved expenditure of the relevant pool.

6 The Small Pools WDA

Where the tax wdv of either the main 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 1

Beth prepares accounts to 5 April. The WDV as at 6 April 2015 of her main pool is £1,250. She purchases machinery for £10,000 in the year and sells an item of plant for £500 (cost £3,000).

Calculate her capital allowances for the year ended 5 April 2016

7 Non Pool Assets

In the following circumstances assets will not go to either the main or special rate pools but will instead have their own separate column on the capital allowance computation:

(1) Assets with private use by the business owner, or

(2) Short life assets on which the taxpayer has made a depooling election.

7.1 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 main or special rate pool, but must be the subject of a separate column on the 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 deducting sale proceeds from the tax wdv (there is a balancing charge if sale proceeds exceed tax wdv, and a balancing allowance if sale proceeds are less than tax wdv). Having computed the balancing adjustment, the amount assessed or allowed is then reduced to the business proportion. A balancing allowance is then added in to the capital allowances of the period whereas a balancing charge will reduce the capital allowances.

(d) Private use by an employee of an asset owned by the business has no 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 an employment income assessment as a benefit charge on the employee or director (see chapter 9).

EXAMPLE 2

Jane prepares accounts to 5 April. At 6 April 2015 the WDVs brought forward are as follows:

	£
Main Pool	21,200
Motor car (115g/km) (used 30% for private purposes by Jane)	13,600

The following transactions took place during the year ended 31 December 2015:

10 May 2015	Purchased plant for £6,600
25 June 2015	Purchased a motor car for £10,600 CO_2 emissions of 100g/km to be used by an employee who will use it 80% for business purposes
15 October 2015	Sold the motor car used privately by Jane for £9,400
16 October 2015	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 2016.

7.2 Short-life assets

(a) An election can be made to omit short life assets from the main 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 at a low residual value or scrapped within 8 years following the end of the accounting period in which it was acquired.

(c) Any plant and machinery that would normally go to the main pool, **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. Clearly the election would only be worthwhile if a balancing allowance was anticipated.

(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 main pool items will qualify for a WDA of 18%.

(h) The AIA could be matched with short life assets. However if total expenditure on plant and machinery is above £500,000 the AIA would be allocated to the main pool additions first, as no balancing allowance occurs on sale. If the AIA is allocated to main pool items first then a short life asset election could be made on any short-life assets, with balancing allowances hopefully crystalising on disposal.

(i) Given the increase in AIA to £500,000 it is very unlikely that the election would now be worthwhile for most unincorporated traders. An exam question may still be set of course for an unincorporated trader selling a short life asset where the election had beeen made when AIA was previously at a much lower level. Example 3 below, however shows both the election being made and the resultant effect on the disposal of the asset.

Example 3

John prepares accounts to 5 April in each year.
At 6 April 2015 the WDV of the main pool was £16,000.
On 1 July 2015 John purchased machinery for £520,000
On 1 September 2015 John purchased a photocopier for £4,000 and made a short life asset election.
On 1 July 2016 the photocopier was sold for £1,500.

Calculate the capital allowances for years ended 5 April 2016 and 2017

7.3 Balancing adjustments on the Main or Special Rate Pools

(a) A balancing charge can arise at any time on the main pool or special rate pool if disposal proceeds exceed the balance on the pool. If a net balancing charge arises on the capital allowances computation this would be added to the adjusted trading profit of the accounting period.

Example 4

Peter prepares accounts to 5 April. In the year ended 5 April 2016 the following transactions took place:

10 April 2015	Plant sold (originally purchased for £10,200) for £8,600
1 October 2015	Second hand motor car (emissions 125g/km) purchased for £2,000

The WDV on the main pool as at 6 April 2015 was £4,000.

Calculate the balancing adjustment for the year ended 5 April 2016

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

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

Example 5

Kris prepares accounts to 31 December.
Kris ceased to trade on 31 March 2016 on which date all plant and machinery was sold for £5,000.
The WDV on the main pool as at 1 January 2016 was £12,000.
Machinery was purchased on 1 February 2016 for £4,000

Calculate the balancing allowance for the accounting period ended 31 March 2016

8 Preparing the Capital Allowance Computation

It is essential to follow a set format in dealing with the additions and disposals of assets in the accounting period in the preparation of the capital allowance computation:

(1) List any tax written down values (unrelieved expenditure) on the pools and any non-pool assets at the start of the accounting period as given within the question.

(2) List expenditure qualifying for AIA, in order, firstly special rate pool and then main pool

(3) Add any expenditure in excess of the AIA limit to the relevant pool

(4) Add to relevant pool the cost of any cars qualifying for WDA ie cars with CO_2 emissions in excess of 75 grams per Km

(5) Deduct sale proceeds, to a maximum of original cost, of assets sold during the accounting period from the relevant pool balance

(6) Deduct sale proceeds, to a maximum of original cost from the tax WDV of any non-pool assets and compute the relevant balancing adjustment

(7) Compute available WDA's on the Tax WDV's computed and deduct therefrom

(8) List any new low emission cars purchased during the accounting period and claim the available 100% FYA

9 Full Pro forma Capital Allowances Computation

		Main pool	*Special Rate Pool*	*Short life asset (1)*	*(Business %) Private use Asset*	*Allowances*
	£	£	£	£	£	£
WDV b/f		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 76-130g/km		X				
emissions >130 g/km			X			
Disposals		(X)		(X)		
		X	X	X	X	
(Note b)						
WDA × 18%		(X)				X
WDA × 18%/8%					(X)	X
					(× Business use)	
WDA × 8%			(X)			X
Balancing allowance				(X)		X
Additions qualifying for FYA						
Motor car emissions ≤ 75g/km	X					
FYA @ 100%	(X)					X
Allowances for period						X
WDV c/fwd		X	X	–	X	

Notes

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

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

Example 6 (Comprehensive)

Ling prepares accounts to 5 April. The WDV of the main pool at 6 April 2015 was £30,000, and on a car (120g/km) £14,000. The car was used by Ling 20% for private use. The following transactions took place during the year ended 5 April 2016.

6 May 2015	Purchased a motor car (emissions 70g/km)	£17,000
10 June 2015	Purchased computer equipment	£60,000
25 June 2015	Purchased a machine	£184,000
7 September 2015	Purchased plant	£260,000
10 November 2015	Purchased a motor car (emissions 115g/km)	£11,200
3 December 2015	Purchased thermal insulation for the business building	£28,000
9 December 2015	Disposed of the car used privately by Ling	£8,000

Calculate the capital allowances for year ended 5 April 2016 assuming that no short life asset election is to be made in respect of the computer equipment.

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team - Capital Allowances section

You may now attempt Practice Question 11

Chapter 6

TRADING PROFIT – BASIS PERIODS

1 Basis periods

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

The problem is that not all traders will prepare their accounts to 5th April so a basis of assessment is required that will allow HMRC to relate any accounting period of profit to the tax year in which it will be charged to tax. Traders are assessed on their trading profit using a current year basis (CYB), this is the tax adjusted trading profit of the accounting year ending in the tax year of assessment.

If a trader makes accounts to 31 October each year, his 2015/16 assessment will be based on the trading profit for the accounting year ending 31 October 2015.

Example 1

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

In which tax year will the trading profits for the accounting year ended 31 March 2015 be assessed?

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

In which tax year will the trading profits for the accounting year ended 31 August 2015 be assessed?

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

In which tax year will the trading profits for the accounting year ended 30 April 2015 be assessed?

1.1 Opening years rules

(a) There are special rules that apply for the opening tax years of a new trade until a CYB assessment is available:

(b) A new business is unlikely to start trading on 6th April and prepare accounts to following 5th April and therefore permit the CYB assessment to apply in its first tax year of trading: Indeed as we will discover it may not be until the third or even fourth tax year of trading before there will be an accounting YEAR ended in a tax year and thus allow CYB to apply.

(c) HMRC will however assess a taxpayer from the first tax year in which they trade.

(d) As you will see in the detailed rules that follow, the first tax year is quite easy to deal with as we will always use an ACTUAL basis of assessment and assess the profit actually made from the date the trade commenced through to the following 5th April. The only issue here is that some time apportionment of a profit period will be required if the taxpayer has prepared accounts to a date other than 5th April (or 31st March as apportionments will be made to the nearest month)

(e) It is the second tax year where there are alternative bases of assessment that may apply depending on the choice of accounting date and the detailed rules for this and the third tax year of assesment follow overleaf .

Tax year	Basis of assessment
Year 1	Actual profits from commencement of trade to the following 5 April
Year 2	Is there an accounting period which ends in tax year 2?

yes → How long is this accounting period?

- < 12 months long → Assess profits for the first 12 months of trading
- ≥ 12 months long → Assess profits for the 12 months to the accounting period end date ending in year 2

no → Assess the actual profits in tax year 2 i.e 6 April to 5 April

Year 3	Assess profits for the 12 months to the accounting period end date ending in year 3

(f) 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, overlap relief will be available on cessation of trading allowing the overlap profit to be deducted in the final tax year of assessment - see section 1.2.

Example 2

Andrew started to trade on 1 January 2013 and makes up his first accounts to 30 June 2013 and then 30 June annually thereafter. His trading profits are as follows:

6 months	to 30 June 2013	£30,000
Year	to 30 June 2014	£70,000
Year	to 30 June 2015	£82,000

What are the assessments for 2012/13 to 2015/16?

How much overlap relief is available?

Example 3

Chris started to trade on 1 May 2014 and makes up his first accounts to 31 October 2015 and then 31 October annually thereafter.

He made £36,000 trading profits in the 18 months to 31 October 2015 and £30,000 in the year ended 31 October 2016.

Compute the assessments for the relevant tax years so far as the above information will allow.

How much overlap profit arises?

1.2 Closing years rules

The rules for dealing with the closing years of a taxpayer ceasing to trade are much more straightforward than opening years with CYB being used up to and including the penultimate tax year (one before last). The basis of assessment for the final tax year is then as follows:

(a) The actual trading profits from the end of the basis period for the previous (penultimate) year of assessment until the date of cessation (al profits not yet taxed).

(b) Any overlap profit / relief from the opening years of the trade is then 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 2015 with trading profits as follows:

	Trading Profit
	£
Year to 31 January 2015	47,000
4 months to 31 May 2015	8,000

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

Compute the assessments for the final tax years of trading as far as the available information will allow.

2 Basis periods for capital allowances

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

2.1 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 ≤ 75g/km, is never time apportioned.

Example 5

Until 30 June 2015 Wendy was employed as a management consultant at an annual salary of £40,000.

On 1 July 2015 Wendy commenced in self-employment running a music-recording studio. The following information relates to the period of self-employment from 1 July 2015 to 5 April 2016:

1 The Adjusted profit for the period 1 July 2015 to 5 April 2016 is £89,000. This figure is before taking account of capital allowances.
2 Wendy purchased the following assets:

		£
1 July 2015	Recording equipment	30,000
15 August 2015	Motor car (CO_2 emissions are 170 g/km) used by Wendy - 60% business use	14,800
20 October 2015	Motor car (CO_2 emissions are 125 g/km) used privately by employee - 20% private use)	10,400
4 March 2016	Computer	2,600

Compute Wendy's income tax liability for 2015/16

2.2 Cessation of trade

(a) No WDA, AIA or FYA are available in the final period of trading and a balancing adjustment on cessation is instead computed.

(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 the net balance is still positive then a balancing allowance will arise whereas if the net balance is a negative figure then a balancing charge arises.

3 Cash Basis for Small Businesses

Certain small unincorporated businesses (sole traders and partnerships) may elect to use a cash basis to determine their tax adjusted trading profits instead of the normal accruals basis.

The election is available to those businesses with receipts for a 12 month accounting period assessable in the tax year that do not exceed the VAT registration limit of £82,000.

A trader must leave the scheme if receipts assessable in the previous tax year exceed twice the VAT registration limit (£164,000).

The cash basis will assess a business on its cash receipts less cash payments of allowable business expenses. Payables, receivables and inventory are ignored.

The accounting profit must be adjusted for taxation purposes mostly as for accruals accounting with the main difference being in relation to capital expenditure.

Expenditure on plant and machinery which would normally attract capital allowances will now attract tax relief with capital payments for plant and machinery (except cars) being deductible and capital receipts from sale of plant and machinery (except cars) being included in the calculation of the adjusted trading profit.

In respect of cars instead of claiming capital allowances the trader may instead use a fixed (or flat) rate deduction for tax purposes. The actual capital cost of acquiring a car for use in the business, the running costs and the sale proceeds are excluded from the profit calculation. The trader can instead claim as a deduction against the trading profit a mileage allowance for the business mileage. The allowance is at a rate of 45p per mile for the first 10,000 business miles and 25p thereafter.

Taxable trading profits for an accounting period under the cash basis are computed as:

	£
Receipts (inc. sale of plant & machinery)	xxx
Expense payments (inc. purchase of plant & machinery)	(xxx)
Tax adjusted trading profit / (loss)	xx

Example 6

Adam commenced trading as a sole trader selling fresh fruit on June 1, 2015 and prepared his first set of accounts to May 31, 2016, for which the following information is available:
Sales for the period were £61,000 of which £4,000 was still owed by business customers at the end of the period.
Inventory at May 31, 2016 amounted to £1.800.
Purchases and expenses of the period (all allowable) amounted to £29,000 of which £2,000 was still owed to suppliers at the end of the period.
On June 1, 2015 Adam purchased equipment for use within the trade costing £8,000 and on 1 October, 2015 a motor car costing £12,000 with CO_2 emissions of 122 grams per kilometre. Adam uses the car 40% for private use and incurred motor expenses during the period of £3,600 in driving a total of 10,000 miles.

Calculate Adam's adjusted trading profit for the accounting period ended May 31, 2016 using the normal basis and using the cash basis.

If a trading loss arises under the cash basis then the only relief available to the trader is to carry forward the loss to set off against future trading profits of the same trade.

This compares unfavourably with the normal loss reliefs available to a trader which are detailed in Chapter 7 and may be a critical issue especially for new businesses in making the decision as to whether to elect for the cash basis to apply and may also be a reason for a business in the future to withdraw the election.

Premises used as both home and business premises such as a small hotel, guest house, bed and breakfast or public house can elect for a flat rate private use adjustment to apply under the cash basis in respect of private use of the property for such expenses as food and heat and light. Note this is an add back not a deduction.

The relevant flat rates will be provided in an examination question and are based on the number of occupants. For example if the property had one occupant the add back would be £350 per month or part thereof (£4,200 per annum) and for two occupants it would be £500 per month (£6,000 per annum).

The flat rate add back does not include other property expenses such as rent or loan interest payments.

Example 7

Eve, a single lady, runs a small guest house in which she lives and prepares accounts to April 5 each year. For the year ended April 5, 2016 she has a trading profit before any private use adjustment of £23,000. The total cost for food, heating and lighting charged for this period amounted to £14,000.

State how the total cost of food and heat and light may be dealt with for tax purposes and calculate Eve's adjusted trading profit assuming the election for the flat rate private use adjustment has been made.

Students may now attempt Practice Questions 12 to 15

Free lectures available for Paper F6 - click here

Chapter 7

TAX ADJUSTED TRADING LOSSES – INDIVIDUALS

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 of the same trade

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

(c) Opening years 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 in full against the next available trading profit 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 2013	Loss	(5,000)
Year to 31 December 2014	Profit	3,000
Year to 31 December 2015	Profit	10,000

Assume that Albert chose to carry forward the loss.

Calculate his assessable amounts for all relevant tax years.

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 preceding tax year.

» the loss is calculated on an accounting period basis.

» a loss for the year ended 30 June 2015 maybe relieved against total income of 2015/16 (the tax year of loss) and/or 2014/15 (the preceding tax year)

(b) If relief against total income is taken,

» the loss must be set off to the maximum possible extent subject to a newly introduced cap on income tax reliefs - see section (c) below

» personal allowances may therefore be lost as total income is before the deduction of the personal allowance and partial claims are not allowed.

» a claim against total income may be made for either the tax year of the loss or 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 2013	32,000
Year ended 31 December 2014	25,000
Year ended 31 December 2015	(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 2015/16 applies in all tax years.

(c) A cap applies that limits the amount of loss relief available against a person's total income. The cap is the higher of:

- £50,000, or
- 25% of person's adjusted total income

Adjusted total income is after deducting the gross amount of any personal pension contributions.

Importantly the cap does not apply to any trading profits within the total income figure (this would be relevant to a claim made in respect of the preceding tax year).

The cap will only be tested at F6 within this section of relief against the total income of current and / or the preceding tax year.

Illustration

Louise Serr has always prepared accounts to April 5 in each year in respect of her trade while also receiving employment income of £60,000 each tax year. For the year ended April 5, 2016 she made a trading loss of £125,000 having made a trading profit of £20,000 in the year ended April 5, 2015.

Assume the personal allowance for 2015/16 also applied in 2014/15 and compute the taxable income for each of these tax years assuming that loss relief claims against total income are made in both tax years.

	2014/15	*2015/16*
	£	*£*
Trading Profit	20,000	Nil
Employment Income	60,000	60,000
	80,000	60,000
Loss Relief	(70,000)	(50,000)
	10,000	10,000
Personal Allowance	(10,600)	(10,600)
Taxable Income	-	-

Loss relief claim in 2015/16 is capped at £50,000 as this is higher than £15,000 (25% x 60,000).

In 2014/15 the loss relief claim is made in full against the trading profit but the cap of £50,000 then applies against the remaining total income (employment income).

The cap can here be seen in fact to be of advantage to Louise as it leaves sufficient total income in both years to absorb the majority of the available personal allowance.

The remaining trading loss of the year of £5,000 (125,000 – 50,000 – 70,000) will be carried forward to set off against the next available trading profit of the business.

(d) Relief of trading losses against capital gains

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

(ii) A trading loss may be relieved against capital gains, but only after the total income of the tax year in question has been reduced to zero by the trading loss under a normal claim, and an unrelieved loss still remains.

(iii) The remaining unrelieved trading loss (restricted to a maximum loss as shown below) is then deducted from the net gains (gains less losses) of the tax year. This deduction is made BEFORE then deducting any capital losses brought forward and the Annual Exempt Amount (a level of tax free gains).

(iv) The maximum loss available for use in this relief is computed as the net gains of the tax year LESS any capital losses brought forward. The detail of chargeable gains and allowable losses is dealt with in chapter 12.

Example 3

For 2015/16 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 has been made.

Calculate Kathy's chargeable gain for 2015/16, assuming that Kathy makes the election.

5 Losses in opening years

In the first tax year of the trade the assessable profit (or loss) is measured from the day trade commences to the following 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 computing the assessment of one tax year, it is treated as nil when calculating the next assessment.

Example 4

Matthew starts trading on 1 August 2014. His trading results, as adjusted for tax purposes are:

		£
10 months to 31 May 2015	Loss	(20,000)
Year ended 31 May 2016	Profit	48,000

Calculate Matthew's trading profit assessments and the losses available for relief in respect of all relevant tax years.

5.1 Opening years loss relief

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

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

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

(c) The relief operates against all three preceding tax years on a FIFO basis. As with current and preceding year relief partial claims are not available and hence personal allowances may again be lost

(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 years loss relief
- Relief against total income of the current and/or previous tax year, including possible extended claim against gains
- Carry forward against future trading profit

Example 5

Fiona started trading on 1 July 2014. Her results, as adjusted for tax purposes, for the first two years are as follows:

		£
Year ended 30 June 2015	Loss	(12,000)
Year ended 30 June 2016	Profit	2,500

Fiona had previously been employed.

Her remuneration from this employment, which ceased on 30 September 2013, for recent years was:

	£
2013/14	5,868
2012/13	11,050
2011/12	12,800

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

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

Assume the personal allowance for 2015/16 applies throughout.

6 Terminal loss relief

(a) The terminal loss is set against trading profit for the tax year of cessation (if any - note this is usually a nil assessment given the loss arising) and then the previous three tax years on a LIFO basis.

(b) The terminal loss is the loss of the final 12 months of trading computed in 2 parts dividing the last 12 months of trading between the final and penultimate tax years, calculated as follows:

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

(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 6

David has the following trading results before ceasing to trade on 31 May 2016

		£
Year ended	31 July 2014	18,000
Year ended	31 July 2015	6,000
10 months	31 May 2016	(20,000)

Show the loss available for relief under terminal loss relief, assuming overlap profits on commencement were £500 and state how this loss would then be relieved

Students may now attempt Practice Questions 16 & 17

Chapter 8

PARTNERSHIPS

1 Introduction

A partnership is a single trading entity, but for taxation purposes 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 as expenses as these are simply an allocation of trading profit by the ownwers of the business.

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 in force during the accounting period.

(b) Partners may firstly be entitled to salaries and interest on capital. The balance of any trading profit (or loss) will then be allocated in the profit sharing ratio (PSR).

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 under the different agreements.

Example 1

Doug and Rob are in partnership. The trading income for the year ended 30 September 2015 was £18,000

Up to 30 June 2015 profits were shared between Doug and Rob 3:2, after paying salaries of £3,000 and £2,000 per annum.

From 1 July 2015 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 2015.

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 on his/her share of the adjusted trading profit

(d) Continuing partners will be assessed using CYB

(e) When a new partner joins a partnership, he is treated as commencing a new trade and hence the opening years rules apply

(f) When an old partner leaves a partnership he is treated as ceasing a trade and hence the closing years rules apply

(g) 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 only to the individuals joining or leaving the partnership.

Example 2

Ann and Beryl have been in partnership since 1 July 2013 making up their accounts to 30 June each year. On 1 July 2015 Clair joins the partnership.
The partnership's trading profit is as follows:

	£
Year ended 30 June 2014	12,000
Year ended 30 June 2015	14,000
Year ended 30 June 2016	24,000

Profits are shared equally.

Show the amounts assessed on the individual partners for all relevant tax years of assessment.

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 years loss relief, for losses in the first four tax 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 2015/16 Paul left the partnership and George joined in his place.

For the year ended 5 April 2016 the partnership made a trading loss of £40,000.

State the loss relief claims that will be available to the partners. No calculation of the loss reliefs available is required

Students may now attempt Practice Question 18

Chapter 9

EMPLOYMENT INCOME

1 The scope of employment income

An employee is taxable under Employment Income rules

A self employed person is taxable under Trading Income rules

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. The date received is taken as the earlier of the date when the employee became entitled to the payment or the date when it was actually received by the employee.

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 relevant 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 2015/16 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 2015/16 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) Qualifying removal expenses up to £8,000.

(c) Car parking spaces at or near place of work.

(d) Workplace nurseries (crèches).

(e) Childcare voucher up to £55 per week for basic rate taxpayers, £28 per week for higher rate and £25 per week for additional rate taxpayers.

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

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

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

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

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

(k) Annual exemption of £500 per employee where employer pays for medical treatment to assist the employee in returning to work after a period of absence due to ill health or injury

(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 £4 per week 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 2012 for £120,000.

Calculate the total benefit assessable on Jones for 2015/16 assuming an official rate of interest of 3%

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 2014, costing £900. On 6 April 2015 Gerald was given the dishwasher by his employer (its market value then being £150).

Calculate the benefit assessable on Gerald in respect of the gift, 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*
50g/km or less	5%
51 to 75 g/km	9%
76 to 94 g/km	13%
95 g/km	14%
> 95g/km	Add an additional 1% for every complete 5g/km above 95 g/km
Maximum percentage	37%

The percentage rates are increased by 3% for diesel cars but not beyond the maximum 37%

(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 A pool car is one provided for the use of any employee to use for business purposes and is kept at the business place of work..

Example 4

During 2015/16 Speed Merchants plc provided the following employees with company motor cars:

Lewis was provided with a new diesel powered company car on 6 August 2015. The motor car has a list price of £13,500 and an official CO_2 emission rate of 122 grams per kilometre.

Nico was provided with a new petrol powered company car throughout 2015/16. The motor car has a list price of £16,400 and an official CO_2 emission rate of 187 grams per kilometre.

Fernando was provided with a new petrol powered company car throughout 2015/16. The motor car has a list price of £22,600 and an official CO_2 emission rate of 249 grams per kilometre. Fernando paid Speed Merchants plc £1,200 during 2015/16 for the use of the motor car.

Jenson was provided with a new petrol powered company car throughout 2015/16. The motor car had a list price of £16,000 and an official CO_2 emission rate of 90 grams per kilometre.

Sebastian was provided with a new diesel car throughout 2015/16. 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 2015/16 for Lewis, Nico, Fernando, Jenson and Sebastian.

(f) Fuel provided for private use

(i) The car benefit also covers the running costs of the car BUT does not take account of fuel provided for private use.

(ii) The amount of fuel benefit is computed on a base figure of £22,100 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 Lewis, Nico, Fernando, Jenson and Sebastian assuming also that Fernando pays Speed Merchants plc £600 during 2015/16 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 £3,150 p.a.

(iii) An additional charge is made for fuel provided for unrestricted private use equal to £594p.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 (3% for 2015/16)

(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 £10,000 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 2015. Interest is payable on the loan at 1% p.a. On 1 June 2015 Jack repaid £5,000 and on 1 December 2015 a further £15,000. The remaining £15,000 was still outstanding on 5 April 2016. Jack earns £30,000 p.a.

Calculate the taxable benefit for 2015/16 under

(a) the average method and

(b) the accurate method

You should assume that the official rate of interest is 3% 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 deduction

(d) Employers must send income tax and NIC information to HMRC electronically every time employees are paid (weekly or monthly) and make their monthly PAYE payments electronically on the 22nd of the month under the Real Time Information reporting system.

(e) For the tax year 2015/16 there are now penalties if submissions made during the tax year are made late, though there is no penalty for the first month in a tax year that submissions are paid late. Thereafter a monthly late filing penalty of between £100 and £400 is charged depending on the number of employees. An additional penalty of 5% of the tax and NIC due may be charged where the submisssion is more than 3 months late.

(f) send appropriate returns in addition to the to the employee 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 allowance	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) × 100/20 × 100/40 × 100/45 for basic/higher/additional rate taxpayers	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 pa and is single, She has annual benefits of £440 and her unpaid employment income tax for 2014/15 was £132. Annabel pays income tax at the marginal rate of 20%

Calculate Annabel's tax code for 2015/16.

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 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.

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team - Employment Income section

In addition the article on Benefits should be fully reviewed

Students should now attempt Practice Question 19

Chapter 10

PENSION SCHEMES

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 only 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, or
- £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 occupational 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 £32,785 and £151,000 respectively.

2 Annual Allowance (AA)

The AA determining the total pension input allowed for tax relief each year is limited to £40,000 in the tax years 2014/15 and 2015/16 having been set at £50,000 for the tax years 2012/13 and 2013/14 (this information will be provided in the tax rates and allowances section of the exam paper).

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 possible to carry forward any unused amount for 3 years.

Although tax relief is given on pension contributions up to the level of relevant earnings of the taxpayer for a tax year, if the tax relieved contributions exceed the AA (including any unused allowances brought forward) there will be an AA charge chargeable to income tax at the taxpayer's marginal rate (see note 3 below)

Example 1

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

2012/13	£62,000
2013/14	£30,000
2014/15	£25,000

Aston has an annual salary of £120,000.

Compute the total pension input allowed for Aston for the 2015/16 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 2015/16 tax year of £250,000 and made his first contribution into a personal pension scheme during this year of £70,000 (gross).

Compute the annual allowance charge that will arise in 2015/16 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 £70,000 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 (70,000 – 40,000).

As Villa has contributed to a personal pension scheme not an occupational scheme his basic and higher rate band limits will be increased by the gross contribution of £70,000, to £101,785 and £220,000 respectively. As personal pension scheme contributions are made net of basic rate tax relief, Villa will actually have made a payment of £56,000 (70,000 x 80%) into the pension scheme.

Villa's Income Tax computation for 2015/16 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	101,785 @ 20%	=	20,357	
Higher rate	118,215 @ 40%	=	47,286	
Additional rate	60,000 @45%	=	27,000	
Income Tax Liability				94,643

Note 1 Villa's Adjusted Net Income for purposes of computing his personal allowance is £210,000 (280,000 – 70,000). As this exceeds £121,200, his personal allowance will be reduced to zero.

4 Lifetime Allowance

When the taxpayer takes their pension a tax free lump sum of 25% of the pension fund may be taken and whereas previously the remainder would have to be used to buy a pension annuity, the taxpayer may now withdraw the balance of the pension fund as taxable income whenever they wish.

In addition to the AA limiting the tax relief available on yearly contributions a Lifetime Allowance of £1.25M 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. These calculations however are not within the syllabus!

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team - Pension Schemes section

Students should now attempt Practice Question 20

Chapter 11

NATIONAL INSURANCE CONTRIBUTIONS (NIC)

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 2015/16 the rate of employee Class 1 NIC is at 12%. It is paid where **cash** earnings exceed a threshold of £8,060 per annum, but only up to an upper limit of £42,385 per annum, however for earnings above £42,385 per annum there is a rate of 2% payable with no limit. The contributions cease when the employee reaches pensionable age.

(c) Employers

The rate of employer Class 1 NIC is 13.8%. It is paid on **cash** earnings that exceed a threshold of £8,112 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 only by employers on taxable benefits provided to employees. The rate is 13.8% multiplied by the assessable value of the benefits.

2 Employment Allowance

HMRC have introduced an annual employment allowance of £2,000 per EMPLOYER to reduce the Employer's Class 1 NIC payable. For example if the employer's Class 1 NIC for the tax year is £5,000 the amount payable will be reduced by the £2,000 employment allowance to £3,000. If the total employer's Class 1 NIC was say £1,500 then this would be reduced to nil.

The employment allowance does not reduce the amount of employer Class 1A NIC payable nor will it serve to reduce the amount of Class 1 employee's NIC.

Example 1

An employee of Riga Ltd is paid £50,000 per annum, and was provided with the following taxable benefits during 2015/16:

	£
Company motor car	6,400
Fuel	4,320

Calculate the Class 1 and Class 1A NIC liability in respect of this employee.

3 Self-employed earners

3.1 Class 2 contribution

(a) Self-employed earners pay a flat rate contribution of £2.80 per week from their 16th birthday until they reach pensionable age when the tax adjusted trading profit assessed for the tax year exceed a small profits threshold of £5,965. Class 2 NIC is now payable under the self-assessment system and will be due on 31 January following the tax year. Thus for 2015/16 it will be due on 31 January 2017 along with the class 4 NIC below.

3.2 Class 4 contribution

(a) The self employed also pay Class 4 contributions which are based on the assessable trading profits of the tax year.

(b) The rate of Class 4 is 9% and is payable on trading income between £8,061 and £42,385.

(c) For trading income in excess of £42,385, 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 reaches pensionable age at the start of the relevant tax year

Example 2

Jerome, a trader, has trading profit of £50,000 for 2015/16.

Calculate his Class 4 NIC and Class 2 NIC for 2015/16

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team: National Insurance Contributions section

You may now attempt Practice Question 21

Chapter 12

CAPITAL GAINS TAX – INDIVIDUALS

1 Individuals and Companies

Individuals pay Capital Gains Tax (CGT) on their chargeable gains of the tax year, whereas the chargeable gains of a company are included on the company's Corporation Tax Computation along with its other taxable income and the company's overall taxable total profits are then subjected to Corporation Tax, as you will see later in these course notes.

A chargeable gain or allowable loss arises on a chargeable disposal of a chargeable asset by a chargeable person.

The basic calculation of the chargeable gain is a simple one, deducting the allowable costs of an asset from its net proceeds upon its sale. A company NOT an individual may then further reduce any gain for the effects of inflation by the deduction of Indexation Allowance.

Qualifying gains may then be eligible for certain reliefs that will allow such gains or parts thereof to be either exempted from tax or and more commonly, deferred from immediate chargeability to tax.

1.1 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. 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).

1.2 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 (Government Securities such as Exchequer Stock)
- Qualifying Corporate Bonds (Corporate loan stock)
- Certain Chattels (tangible moveable property)
- Investments held in an ISA

1.3 Chargeable Person

An individual who is resident in the UK is a Chargeable Person and is therefore liable on their worldwide assets.

1.4 CGT computation

(a) Capital gains and losses 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 exempt amount	(11,100)
Taxable Gains	X
CGT × 10%, 18% or 28%	X
Due (for 2015/16)	31/1/17

A chargeable gain or allowable loss of an individual is computed as follows:

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 Exempt Amount which is not available to companies.

1.5 Annual Exempt Amount (AEA)

(a) Every individual has an exempt amount of gains for each tax year. For 2015/16 it is £11,100

(b) If the annual exempt amount is not used it is wasted.

1.6 Payment of CGT

CGT is due in one amount on 31 January following the tax year (2015/16 by 31 January 2017)

No payments on account of the CGT liability are required.

1.7 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, then on those gains qualifying a CGT rate of 10% is applied.

(b) The taxpayer's Taxable Income from his Income tax Computation is then used as the basis for applying the relevant CGT rates to his figure of Taxable Gains. 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 (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).

For example if the taxpayer had taxable gains of £15,000 (none qualifying for entrepreneurs relief) and taxable income of £21,785, then the first £10,000 of his taxable gains would use up his remaining basic rate band (31,785 - 21,785) and be taxed at 18% leaving £5,000 of his taxable gains to be taxed at 28%

Example 1

Tina sold a painting on 1 July 2015 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 2015 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 2016 which had cost her £15,000 in September 2013.
Tina had capital losses brought forward from previous tax years of £12,000. Tina's taxable income for 2015/16 is £50,000.

Calculate Tina's Capital Gains Tax for 2015/16

Example 2

Matthew has trading profit of £20,000 assessed in 2015/16 and sold an antique vase giving rise to a capital gain of £18,000.

Calculate Matthew's capital gains tax for 2015/16

Example 3

Katie has trading profit of £40,600 assessed in 2015/16. In addition she sold an investment property giving rise to a capital gain of £30,000.

Calculate Katie's capital gains tax for 2015/16

Example 4

Elliot has trading profit of £44,600 assessed in 2015/16. 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 2015/16.

Calculate Elliot's capital gains tax for 2015/16

1.8 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 should be calculated as the mid price based on the day's quoted prices

Example 5

Jenny gifted 1,000 shares in M plc when they were quoted at £4.00 - £4.08p

Calculate the value to be used for capital gains disposal proceeds

1.9 Incidental costs would include:

(a) legal fees

(b) advertising fees

(c) auctioneers fees

(d) agency fees

1.10 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 Exempt Amount (AEA)

(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, however only reduce capital gains to the level of the AEA, and therefore do not waste the AEA

(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 2014/15 and 2015/16 as set out below:

	Fiona	*Jane*
2014/15		
Capital gains	15,000	7,000
Capital losses	10,000	10,000
2015/16		
Capital gains	17,000	13,700
Capital losses	5,200	2,000

Calculate the taxable gains for Fiona and Jane for both 2014/15 and 2015/16 and the amount of any losses carried forward at the end of 2015/16

3 Transfer of assets between a husband and wife or between civil partners

The transfer of assets between spouses and civil partners is for CGT purposes deemed to take place at a value that would give rise to neither a gain nor a loss. The transfer is said to be a nil gain/ nil loss or no gain / no loss transfer. Essentially the transferor is deemed to make the disposal at cost and the transferee acquires the asset at the original cost of the transferor.

The no gain / no loss transfer rules may be used by these taxpayers to utilise both parties annual exempt amounts, and to take advantage of capital losses and lower capital gains tax rates. For example it would be better for each spouse to yield gains of £10,000 each rather than one spouse make gains of £20,000. It would also be better for a basic rate taxpayer to yield taxable gains, taxed at 18% instead of a higher rate taxpayer who would be taxed at 28% on the same gains.

Example 7

Gollum bought a ring in July 1993 for £12,000. He transferred it to his civil partner Frodo in December 2015. Frodo sold the ring in January 2016 for £20,000.

Calculate Frodo's capital gain in 2015/16

4 Part Disposals

(a) A chargeable asset may be only partly disposed of, for example a taxpayer acquires 100 hectares of land and subsequently goes on to sell 40 of those hectares. This will give rise to a chargeable gain computed in the normal way, but a specific problem arises however regarding what figure of cost should be used in the gains calculation. It may seem appropriate to use 40/100 of the original cost, given the quantity of land purchased and then sold. This, however is not the basis used and a value based apportionement of the total cost should instead be used

(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 (this will be given in the question)

Example 8

ST owned 10 hectares of land which originally cost £26,000 in March 2013. ST sold 2 hectares of the land in December 2015 for £16,000. The remaining 8 hectares were valued at £34,000 in December 2015.

Calculate the chargeable gain on the disposal of the 2 hectares of land in December 2015

5 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, greyhounds (dogs) and yachts (boats).

(c) There is an exception for plant & machinery on which capital allowances have been claimed, these assets are treated as non wasting chattels. If plant and machinery is not covered by the non wasting chattel exemption in note (d) below, then a gain would need to be computed upon its disposal. Such a calculation is seldom required however as it would normally be sold for less than cost. A capital loss will not however arise in this situation as capital allowances will already have given tax relief for the net cost of ownership of the asset.

(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 a maximum 5/3 x [Gross proceeds – 6,000]
> £6,000	<£6,000	Deemed Gross Proceeds = £6,000
> £6,000	> £6,000	Normal calculation

Example 9

JM sold the following assets in December 2015

(a) an antique table which had cost £3,000 in February 2010 and sold for £5,000

(b) a painting which had cost £2,000 in January 2013 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

Calculate the net chargeable gains or losses arising for JM in December 2015

6 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 original cost is therefore reduced BY

$$\frac{P}{L} \times (C - S)$$

where

P = Period of ownership of seller

L = Predictable Life of asset on acquisition

C = Cost of the asset

S = Scrap / residual value at the end of the assets' predictable life

Example 10

On 1 December 2003 Z bought a copyright at a cost of £25,000. It had an estimated useful life of 30 years, and an estimated residual value of £1,000.
Z sold the asset for £38,000 on 1 December 2015.

Calculate the chargeable gain arising on the sale of the copyright in December 2015.

You should now attempt Practice Questions 29 & 30

Chapter 13

CAPITAL GAINS TAX – INDIVIDUALS – SHARES

1 Shares and securities

1.1 Gift edged securities and Qualifying Corporate Bonds

Disposal of these investments are exempt.

1.2 Disposal of shares

Where shares are disposed of a problem arises in computing the allowable cost as shares may have been acquired over several acquisitions at different costs at different dates. Therefore HMRC have deemed that when shares are disposed of, 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. Bonus issues are where a company issues free shares on a proportionate basis to its existing shareholders. Rights Issues are where a company seeks to raise new share capital and offers its existing shareholders the right to acquire on a proportionate basis additional shares in the company at an advantageous share price.

(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 rather than companies as no indexation allowance 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 2013 for £20,000, and 500 shares on 30 June 2014 for £10,000. On 7 March 2016 Jane bought a further 200 shares in ABC Ltd for £4,000.
Jane sold 1,000 shares in ABC Ltd on 28 February 2016 for £25,000. She is not an employee of ABC Ltd.

Calculate Jane's capital gain on the disposal of the shares in February 2016.

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 Alderholt Ltd shares:

February 2014	Purchased 7,000 shares for £15,000
June 2014	Purchased 1,000 shares for £4,000
July 2014	Bonus issue of one for five
October 2015	Sold 5,000 shares for £20,000

Calculate the capital gain arising on the disposal in October 2015.

3 Rights issue

The share pool is increased by the number and cost of the shares acquired via the rights issue.

EXAMPLE 3

Mark in an employee of Romsey Ltd. He had the following transactions in the company shares:

February 2014	Purchased 6,000 shares for £15,000
June 2014	Purchased 900 shares for £2,700
July 2014	Took up 1 for 3 rights issue for £3.00 per share
September 2015	Sold 6,000 shares for £24,000

Calculate the capital gain on the disposal in September 2015.

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) If more than one type of share, for example ordinary and preference shares, are acquired in the takeover company then 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. Thus if a shareholder acquired on takeover £300,000 of ordinary shares and £100,000 of preference shares in the takeover company they would acquire respectively 3/4 and 1/4 of the original shareholding's cost. These costs may then be used to compute any subsequent gain arising on the sale of either those ordinary or preference shares. See example 4 below.

(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. (see example 5 below)

Example 4

In May 2012 Mark purchased 4,000 ordinary shares in Silver Ltd for £12,000. In June 2015 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 2016 Mark sold all his holding ordinary shares in Gold Ltd for £35,000.
Mark was not an employee of Silver Ltd or Gold Ltd.

Calculate the capital gain arising on the disposal in January 2016.

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 2015

You may now attempt Practice Questions 32 & 33

Chapter 14

CAPITAL GAINS TAX – INDIVIDUALS – RELIEFS

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). The relief is not therefore available if a trader simply disposes of an asset that is used in the trade. The assets must be used for the purpose of the business, so the relief is not available on investments.

» Individual business 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% shareholding in the company AND is also an employee (part time or full time) of the company for the 12 months prior to disposal. There is no restriction of the relief if the company owns 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 2015/16 by 31 January 2018

Example 1

Daisy disposed of the following assets in 2015/16
On 30 September 2015 Daisy sold a business that she ran as a sole trader since February 2009. The sale resulted in the following capital gains and capital losses

Goodwill	250,000
Factory	320,000
Warehouse	(90,000)

In December 2015 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 2010. The gain arising was £370,000

Calculate Daisy's Capital Gains Tax in 2015/16

1.4 Further points

- The gains qualifying for entrepreneurs' relief must be taken into account when establishing which tax rate applies to other capital gains in the tax year, in that they are deemed to firstly use any amount of unused basic rate band.
- The AEA and any capital losses should however be deducted firstly 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 2015/16. 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 2014/15 and her taxable income for 2015/16 was £18,000.

Calculate Anne's capital gains tax for 2015/16 and state the due date for payment.

2 Replacement of business assets (Rollover Relief)

2.1 Definition

A gain may be 'rolled over' (deferred) where it arises on the disposal of a qualifying business asset whose sale proceeds are reinvested in another qualifying business asset.

2.2 Qualifying assets

Both the old and new assets must fall into one of the following categories:

(a) Land and buildings

(b) Fixed plant and machinery

Both the old and new assets must be used in the business.

2.3 The relief

(a) The gain is not taxed immediately but is postponed until the trader 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) 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.

(f) A claim must be made within 4 years from the end of the tax year in which the disposal occurred. For disposals in 2015/16 by 5 April 2020.

Example 3

Jones purchased a property for use in his business in March 1990 for £250,000. In August 2015 he sold the property for £300,000 and spent £320,000 in July 2015 on a new business property.

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 2015 wishing to move to a more convenient location, he sold the factory for £800,000. He moved into a rented factory until January 2016 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

2.4 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 limited in proportion to the 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 2015 he sold the factory for £600,000 and bought another factory in August 2015 for £650,000 claiming rollover relief.

(a) what is the chargeable gain arising on the disposal in July 2015?

(b) what is the base cost of a new factory?

2.5 Reinvestment in depreciating asset

2.6 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 leasehold property with a life of 60 years or less.

2.7 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.

(c) 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 2014 he sold it for £500,000 and in July 2014 bought a 55 year leasehold factory building for £600,000. In February 2016 Charles sold the leasehold factory for £640,000 and moved into rented premises.

Calculate the chargeable gains arising in 2015/16 assuming Charles claims to defer gains where possible.

2.8 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

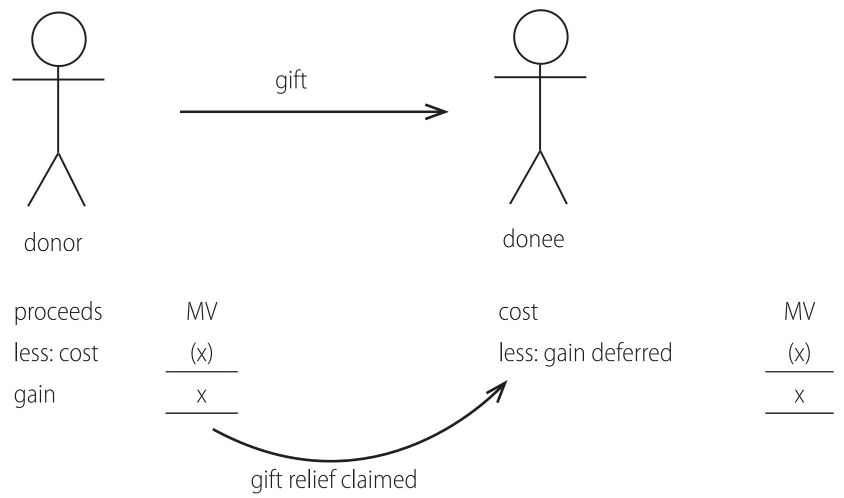
(a) A gift is subject to capital gains tax

(b) The donor (the person making the gift) is treated as making a disposalof the asset at market value.

The donee (the person receiving the gift) is treated as if he had acquired the asset at market value.

(c) When gift relief is claimed, the donor's gain is deferred. 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 2013. In September 2015 he gifted it to Tommy, when its market value was £100,000. The asset qualified for gift relief.

Assuming David and Tommy make a claim for gift relief calculate Tommy's base cost of the asset.

3.2 Interaction with 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 2015/16 the claim must be made by 5 April 2020.

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 in excess of the original cost are chargeable to CGT immediately.

(c) The gain deferred, the gift relief, 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 2016 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 asset.

(a) What is the chargeable gain, if any, incurred by Richard?

(b) What is the base cost of the shares 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 any 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 This will include all chargeable assets held by the company, both those used in the business and those held as investments.

(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 2015 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 2001. At the time of the gift John Ltd owned the following assets.

	£
Freehold trading premises	500,000
Goodwill	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 Principal Private Residence Relief

4.1 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

$$\text{Gain} \times \frac{\text{Period of occupation}}{\text{Period of ownership}}$$

4.2 There are however periods of absence which are deemed to be full occupation

(a) Last 18 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 10

David bought a house on 1 April 1986 for £10,000. he lived in it until 30 June 1986. He worked abroad for 2 years and then moved back into the house on his return on 1 July 1988. He lived in the house until 31 December 2002 before leaving to live and work elsewhere in UK. David did not return to the house and the house was sold on 31 December 2015 for £150,000.

Calculate the chargeable gain arising.

4.3 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 18 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.

4.4 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 11

Ken bought a house on 1 April 1986 for £30,000 and occupied as follows:

1/4/1986 – 31/3/1988	lived in it
1/4/1988 – 30/9/1993	travels the world and lets the house
1/10/1993 – 31/3/2003	lived in it
1/4/2003 – 31/3/2016	Moved out of the house to live with his girlfriend and the property was empty.

Ken sold the house on 31 March 2016 for £250,000.

Calculate the chargeable gain arising.

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team: Capital Gains Tax section

You may now attempt Practice Questions 34 to 37

Chapter 15

SELF-ASSESSMENT AND PAYMENT OF TAX FOR INDIVIDUALS

1 Due dates for payment

Type of income		*Dates for 2015/16 assessment*
Trading income Property Business profit	due	31/1/2016 Payment on account (50% of 14/15 income tax payable by self assessment) 31/7/2016 Payment on account (50% of 14/15 income tax payable by self assessment) 31/1/2017 Balancing payment
Employment Income	due	PAYE payments made electronically on the 22nd of the month under the Real Time Information reporting system.
Savings income Dividend	due	31/1/2017 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 2 and Class 4 NIC are payable at the same time as the income tax on trading income.

Note, the taxpayer can claim to reduce payments on account at any time before 31 January following the tax year. This would be done if 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 2014/15 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 2015/16 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 2015/16 liability will be settled and determine the total amount of tax to be paid on January 31, 2017.

Ignore Class 2 NIC

2 Interest on tax

2.1 Late payments

(a) Interest is charged on late payment of tax at a rate of 3.0%.

For 2015/16

Payment on account:	Interest runs from 31/1/2016 or 31/7/2016
Other payments:	Interest runs from 31/1/2017

(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 2017 for 2015/16.

(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 taxpayer 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 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 2015/16 return are therefore 31 October 2016 (paper returns) and 31 January 2017 (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) HMRC can amend a taxpayer self assessment to correct obvious errors or mistakes within nine months of receiving the return.

(h) The taxpayer can give notice to an officer to amend his tax return within 12 months of the 31 January 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 due 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 2022 for the year 2015/16 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 2018 for the year 2015/16 if not in business.

(b) 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 2015/16 this will be 5 April 2020.

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.

(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 makes a genuine 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

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team - Tax Management section

You may now attempt Practice Questions 43 & 44

Chapter 16

CORPORATION TAX

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 and for which the Taxable Total Profit (TTP) is computed. If the period of account exceeds 12 months then 2 corporation tax computations will be required, the first for 12 months and the second for the remainder of the period (see chapter 17)

- The tax rates to be used however, are set for **Financial Years** (FY) which run from April 1 to following March 31 and are denoted by reference to the year in which they start.

  FY 2015 = 1 April 2015 to 31 March 2016.

  From FY 2015 however there is a single 20% rate of corporation tax that applies to all companies irrespective of the level of profits. For purposes of the F6 exam students will only need to use this rate irrespective of whether the CAP spans an earlier or later FY.

  Despite the introduction of the single universal rate of corporate tax it will still be necessary to determine whther a company is a large company as large companies are required to make quarterly instalment payments to settle their corporation tax liability.

  A large company is a company whose "profits" exceed £1.5M. "Profits" are defined as the TTP of the company plus franked investment income (FII). FII is computed as the gross equivalent of dividends received (dividends received x 100/90) excluding dividends from related 51% group companies.

  Companies are related 51% group companies where one company controls another or two or more companies are both 51% subsidiaries of another company. Dormant companies are excluded.

  The limit of £1.5M is used for a single company with a 12 month CAP. It is therefore divided by the number of related 51% group companies at the end of the immediately preceding accounting period and must also be time apportioned for a CAP of less than 12 months.

  Example

  Large Ltd prepares its accounts to 31 March in each year and for the accounting year ended 31 March 2016 it had a TTP of £600,000 and also received dividends from a number of companies including its two wholly owned subsidiary companies. This was its lowest profit recorded in several years.

  As Large Ltd has two subsidiary companies there are three related 51% group companies which will reduce the profit limit for each group company to £500,000 (£1.5M / 3) As Large Ltd has a TTP of £600,000 then even without including FII, its "profits" exceed the relevant profit limit and it will therefore be required to make quarterly instalment payments to settle its CT liability for the accounting period. See chapter 23 for details of the quarterly instalment payment system.

1.3 Chargeable 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 (TTP)

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

Pro forma corporation tax computation
Corporation Tax Computation for the year ended 31 March 2016

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: Qualifying Charitable Donations		(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 (see chapters 19 - 21)

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 are no private use assets and note only one AIA is allowable to a group of companies.

5.4 Basis periods

The complicated rules for unincorporated traders 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 deduction of qualifying charitable donations of the current period and any excess is carried forward against total profits before qualifying charitable donations 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 Qualifying Charitable Donations

For companies to ensure tax relief is achieved on their charitable donations they should make such payments under the qualifying charitable donations system. The payment is GROSS and deductible on a paid basis. Thus in the adjustment of trading profit any such payments should be added back and instead included as a separate 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 2016.

	£
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
Qualifying charitable donations	(10,000)

Compute the Taxable Total Profits for the year ending 31 March 2016.

You may now attempt Practice Question 22 and 23

Chapter 17

LONG PERIOD OF ACCOUNT

1 Apportioning income and expenditure

(a) 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

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

Adjusted profit	Time apportioned	
Capital allowances	Two calculations	(WDA and AIA will be restricted in the second short period, but note that FYAs on motor cars with emissions ≤ 75 g/km are never restricted for short accounting periods)
Property Income	Accruals basis	
Interest receivable	Accruals basis	
Qualifying charitable donations Chargeable gains	Date of disposal/payment	
Dividends	Date received	

Example 1

A plc prepared accounts for a 15 month period to 30 June 2016. The results for the period are as follows:

	£
Adjusted profit	4,000,000
Chargeable gain (sale of asset on 6 May 2016)	80,000
Qualifying charitable donations (paid annually on 31 July)	20,000

The tax written down value of plant and machinery qualifying for capital allowances at 1 April 2015 was nil. The capital transactions during the 15 month period was the purchase of new vans for £68,000 on 12 May 2015 and plant and machinery costing £152,500 on April14, 2016.

Calculate the corporation tax liabilities for the relevant CAP's

Chapter 18

TAX ADJUSTED LOSSES – COMPANIES

1 Trading and Non-Trading losses

1.1 Trading losses

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) against total profits and / or by carry forward to relieve against future trading profits.

As all companies now pay corporation tax at the same rate of 20% the choice of loss relief will be based on achieving relief at the earliest available opportunity and seeking to avoid wasting relief for qualifying charitable donations as both the current and carry back claims target total profits which is before the deduction of such donations.

1.2 Non-Trading losses

(a) Capital losses

Capital losses are relieved against:

(i) Current year capital gains, then
(ii) Net capital gains in future accounting periods.

(b) Property Business losses

Property Business losses are relieved by

(iii) Setting them off against total profits before deduction of qualifying charitable donations of the current period, then
(iv) By carrying them forward against total profits before qualifying charitable donations of future periods.

2 Trading losses

2.1 Current period relief

The loss may be relieved against total profits before deduction of qualifying charitable donations in the period that the loss arose.

EXAMPLE 1

A Ltd had the following results for the year ended 31 March 2016

	£
Trading loss	(45,000)
Interest receivable	20,000
Chargeable gain	50,000
Qualifying charitable donations	15,000

Show how current year relief would be obtained in the year ended 31 March 2016

2.2 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 deduction of qualifying charitable donations 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 qualifying charitable donation, are not allowed. These claims may therefore result in no tax relief being achieved for the qualifying charitable donations.

EXAMPLE 2

A Ltd has produced the following results over recent years.

	Year ended 31 March		
	2014	*2015*	*2016*
	£	*£*	*£*
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	*9 months to*	*y/e*
	31/3/14	*31/12/14*	*31/12/2015*
	£	*£*	*£*
Trading profit / (loss)	25,000	20,000	(40,000)
Bank interest	3,000	1,000	1,000
Chargeable gains / (losses)	(1,000)	6,000	–
Qualifying charitable donations	(500)	(500)	(500)

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

2.3 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 deduction of qualifying charitable donations of the 36 months preceding the loss making period on a LIFO basis.

Example 4

A Ltd ceased trading on 31 March 2016. It had the following results for the five accounting periods to 31 March 2016.

	y/e 30/9/12	*6 months to 31/3/13*	*y/e 31/3/14*	*y/e 31/3/15*	*y/e 31/3/16*
	£	*£*	*£*	*£*	*£*
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
Qualifying charitable donations	500	-	500	500	-

Show the Taxable Total Profits for all accounting periods.

2.4 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 and losses must be relieved as soon as possible.

EXAMPLE 5

A plc had the following results since it started trading on 1 April 2011

	y/e 31/3/12	*y/e 31/3/13*	*y/e 31/3/14*	*y/e 31/3/15*
	£	*£*	*£*	*£*
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
Qualifying charitable donations	(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.

You may now attempt Practice Question 24

Chapter 19

CHARGEABLE GAINS – COMPANIES

1 General

As seen in Chapter 16 companies pay corporation tax on their chargeable gains.

A chargeable gain arises on a chargeable disposal of a chargeable asset by a chargeable person as seen in Chapter 12 for individuals.

A UK resident company is chargeable on its worldwide gains and may dispose of a chargeable asset not only by sale but also on the loss or destruction of an asset.

As you will see in note 1.2 below the calculation of the gain contains one new component not applicable to individuals. Companies are given a deduction from the gain to remove the effect of inflation from when the asset was purchased to when it is sold, this deduction is known as indexation allowance.

All assets are chareable assets unless they are specifically exempt.

1.1 Exempt assets

A more complete list of the main exempt assets may be found in Chapter 12 dealing with individuals but the main exempt assets that a company may dispose of would be motor vehicles, qualifying corporate bonds (corporate loan stock) and certain chattels.

The main chargeable assets that a company will dispose of will be shares, land and buildings and plant and machinery.

This and subsequent chapters will deal with these main assets.

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) For companies only, NOT individuals, 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 and is computed by reference to the movement in the Retail Prices Index (RPI)

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

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

(f) 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 2015 (RPI assume = 259.5).
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 net proceeds are less than allowable cost. Indexation allowance may not be used to either create or increase a loss.

(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.

(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 or allowable loss. It is difficult however to identify which shares are being sold, and therefore establish the cost of those shares sold where it is only some of the shareholding being sold and the shares had been acquired over a period of time at different costs. We need to identify the shares sold by using matching rules as laid down by HMRC which, as you may expect, are not exactly the same as the matching rules that we used when dealing with the same problem for individuals disposing of shares as we saw back in Chapter 13. Thus the shares sold are deemed disposed of in the following order::

- shares acquired on same day
- shares acquired in previous 9 days
- shares contained within the share pool which is made up of any shares acquired more than 9 days previous.

The share pool records the number and cost of shares for each acquisition and disposal as it did for individuals but also has to deal with the fact that companies are entitled to indexation allowance. Thus 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 which is recorded in a separate Indexed Cost column 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 2015 (RPI 259.5) 500 shares at a cost of £5,000

A Ltd sold 3,000 shares on 10 October 2015 (RPI 259.5) for £36,000
The company has a 31 March year end.

Calculate the gain to include in the Corporation Tax Computation for year ended 31 March 2016.

4 Bonus issues

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

(b) The bonus shares are simply added to the number of shares column in the pool.

(c) Do not however index the cost of the original shares to the date of the bonus as no new cost is incurred.

5 Rights issues

(a) A rights issue again increases the number of shares held, but this time there is also a cost associated with the shares. It is therefore dealt with in the same way as any other acquisition

(b) The indexed cost in the pool is indexed to the date of the rights issue. The rights shares are added to the number of shares column and the cost is then added to both the cost and indexed cost columns in the pool. The only problem you face is computing how many shares are acquired under the rights issue

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 October 2015 for £12,000.

Calculate the gain on the disposal of the shares in October 2015

RPI are as follows:

October 2015	259.5
February 1995	146.9
July 1993	140.7

6 Takeovers

(a) Where a takeover is a share for share deal or 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 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 the market value of what is received at the time of the takeover. See example 4

(d) If at takeover, cash is received, a chargeable gain needs to be calculated at takeover for the cash element received. See example 5

Example 4

Z Ltd acquired 10,000 A Ltd shares in July 1989 for £10,000. In July 2015 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 2015 for £15,000 and the indexed rise from July 1989 to October 2015 is 1.247

Calculate the Gain arising as a result of the takeover in July 2015, and the sale of the B plc preference shares in October 2015

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 2015 is 1.239.

You may now attempt Practice Question 25

Chapter 20

CHARGEABLE GAINS – COMPANIES – FURTHER ASPECTS

1 Part Disposals, Chattels, Non chattel wasting assets

1.1 When a company disposes of a part but not all of an asset the allowable cost is computed as we saw for individuals in Chapter 12. This same calculation will be performed for a company but in addition the allowable cost computed will then be available for indexation allowance in the normal way.

Example 1

ST Ltd owned 10 hectares of land which originally cost £26,000 in March 2011 (RPI 220.7). ST sold 2 hectares of the land in October 2015 (RPI 259.5) for £16,000.
The remaining 8 hectares were valued at £34,000 in October 2015.

Calculate the chargeable gain on the disposal of the 2 hectares of land in October 2015.

1.2 A chattel disposal is also dealt with in the same way as for an individual but again with the availability in a normal gains calculation of indexation allowance

Example 2

JM Ltd sold the following assets in October 2015

(a) an antique table which had cost £3,000 in February 2009 and sold for £5,000
(b) a painting which had cost £2,000 in January 2011 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's

February 2009	211.4
January 2011	217.9
August 2002	176.4
July 1999	165.1
October 2015	259.5

Calculate the net chargeable gains or losses arising for JM Ltd in October 2015

1.3 A non chattel wasting asset disposed of by a company will again be dealt with as for individuals but again with indexation allowance available on the allowable cost

Example 3

On 1 October 2003 Z Ltd bought a copyright at a cost of £25,000. It had an estimated useful life of 30 years, and an estimated residual value of £1,000.

Z Ltd sold the asset for £38,000 on 1 October 2015.

Assume an indexation factor of 0.486.

Calculate the chargeable gain arising on the sale of the copyright in October 2015.

2 Assets damaged, lost or destroyed

2.1 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

Ml Ltd bought a painting on 1 April 2000 for £10,000. The painting was damaged on 1 May 2015 when it was worth £50,000. After the damage it was only worth £25,000. On 1 July 2015 insurance proceeds of £30,000 were received and were not used to restore the painting. Assume an indexation factor from April 2000 to July 2015 = 0.505.

Calculate the chargeable gain 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 2015 when it was worth £50,000. After the damage it was worth £40,000.
On 1 July 2015 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.

2.2 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 2009, It was destroyed in March 2015. Insurance proceeds of £34,000 were received in October 2015. SC Ltd spent £30,000 on a replacement asset.

Calculate the chargeable gain and the base cost of the new asset.

RPI is	October 2015	259.5
	June 2009	216.8

Students may now attempt Practice Questions 26 & 27 and 31

Chapter 21

CHARGEABLE GAINS – COMPANIES – RELIEFS

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 qualifying 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 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 October 2015 RPI (259.5) for £400,000. In December 2015 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 2003 (RPI 181.5) for £200,000. The land was sold in October 2015 (RPI 259.5) for £350,000.. In September 2015 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 leasehold property 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 2010 (RPI 212.8).
In March 2011 YR Ltd bought fixed plant for use in the business, costing £390,000.
YR Ltd sold the plant in February 2016. (YR Ltd has a 31 March year end)

Calculate the chargeable gains as far as the above information allows for y/e 31/3/2011 and y/e 31/3/2016

(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..

You should now review the following technical articles written by the F6 examining team: Chargeable Gains parts 1 and 2

You may now attempt Practice Question 28

Chapter 22

CORPORATION TAX – GROUPS

1 Introduction

If companies are within a group then each such company must still prepare its own corporation tax computation. There is no taxation equivalent of consolidation as in financial reporting! Group companies will benefit from certain reliefs but will also have certain additional rules and regulations placed upon them.

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

- related 51% group companies

- Group VAT registration (see Chapter 24)

- Availability of AIA

(2) 75% groups issues

- group relief of losses

- gains group membership

2 Related 51% group companies

2.1 Definition

Companies are related 51% group companies if:

(a) One company is a 51% subsidiary of the other or

(b) They are 51% subsidiaries of another company

2.2 Control

A company is a related 51% group company if the parent company owns directly or indirectly more than 50% of the share capital of the subsidiary company at the end of the previous chargeable accounting period:

Dormant companies are excluded but overseas companies are included.

2.3 The tax implications

(a) The profit limit of £1.5M used to determine if the company is large and required to make quarterly instalment payments is divided between the number of related 51% group companies.

Example 1

A Ltd owns 100% of the share capital of V Ltd, F Ltd and C Ltd and has a Taxable Total Profit of £400,000. Is A Ltd a large company for purposes of making quarterly instalment payments?

3 The Annual Investment (AIA)

Only one AIA is available to a group of companies but the group members can allocate the AIA in any way it chooses across the group if the qualifying AIA expenditure is more than the AIA limit of £500,000. A group therefore may choose to allocate the available AIA to firstly reduce the profits of large companies below the profit limit of £1.5M and as always in a company to special rate pool expenditure before main pool expenditure

4 Group relief

4.1 Introduction

The relief allows companies in a 75% group to transfer any part of a current year trading loss of one such group company to set off against any part of another company's taxable total profit (TTP) of a corresponding accounting period.

Group relief is also available in respect of:

- excess qualifying charitable donations and

- excess property income losses

Such losses are only excess if they exceed the total profits of the company concerned before any other losses have been applied.

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 profits on a distribution.

4.3 Sub-subsidiaries

The holding company must have an EFFECTIVE interest in any sub-subsidiary of at least 75% for them to be in the same group for group relief purposes, for example if a parent company owns 90% of the shares in a subsidiary which in turn owns 90% of its subsidiary then all 3 companies would be able to group relieve with one another as the parent company has an effective 81% interest (90% x 90%) in the sub-subsidiary.

If the subsidiary owned only 80% of the shares in the sub-subsidiary, then the parent company may only group relieve with its direct subsidiary as its effective holding in the sub-subsidiary is only 72% (90% x 80%). The sub -subsidiary may only group relieve with the subsidiary company, but the subsidiary company is able to group relieve with either its parent company or its own subsidiary.

EXAMPLE 2

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 2016 Z plc has a trading loss.

State the companies to which Z plc may surrender its trading loss in y/e 31/3/16.

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.

4.5 The surrendering company

(a) The surrendering company may surrender as much of its trading loss as it wants to

(b) It is not necessary to relieve a trading loss against its own income and gains first.

(c) The losses which may be surrendered are:

- any amount of a current trade loss
- unrelieved qualifying charitable donations
- 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 the TTP of the same period as the surrendering company's loss making period

4.7 Group relief

(a) The important points to remember as regards group relief are:

- Losses can be group relieved against 100% of a 75% subsidiary's TTP, 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 brought back from a later period.

(b) Where the accounting periods of two group companies are different, then group relief will be restricted to the corresponding or coterminous period. It is therefore necessary to time apportion both the loss making period and the profit making periods to calculalate how much loss may be set against how much profit in each CAP

(c) In F6 only UK resident companies are eligible for group relief though two UK resident subsidiaries of an overseas resident parent company would be able to group relieve though neither could group relieve with its overseas parent company

Example 3

Continuing with Example 2 suppose that B Ltd had commenced trading on 1 October 2015 preparing accounts for the six-month period to 31 March 2016

Discuss the group relief available in respect of Z plc trading loss for y/e 31/3/16 if it were to consider surrendering the trading loss to B Ltd.

Example 4

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 2016 and made a trading profit of £50,000 in its 3 month period to 31 March 2016. Beyonce made a trading loss of £240,000 in its year ended 31 March 2016 while J Ltd has Taxable Total Profits of £160,000 for the year ended 30 June 2015 and £280,000 for the year ended 30 June 2016.

Compute the maximum group relief claims available to J Ltd and Z Ltd in respect of Beyonce's loss of £240,000.

4.8 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 their subsidiaries.

(b) The parent company must only have an effective interest of over 50% in any sub-subsidiary companies.

(c) Groups may be established through a parent company 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 a 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 of Gains Group membership

(a) The group's capital losses can be better utilised

(b) Rollover relief is available on a group wide basis

(c) Gains may be moved to a company with insufficient profits to cover its qualifying charitable donations

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 current period 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.
- » 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 any part of a capital gain or capital loss.

EXAMPLE 5

During the year ended 31 March 2016 Large Ltd disposed of an asset that resulted in a capital loss of £35,000. Smaller 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 Smaller Ltd has Taxable Total Profits of £800,000 including the chargeable gain and anticipates larger profits in the next accounting period. Large Ltd holds no other shareholdings.

Discuss the elections available to the group companies and how they may best be used.

You should now review the following technical article written by the F6 examining team - Groups

Chapter 23

SELF ASSESSMENT AND PAYMENT OF TAX FOR COMPANIES

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. Payment must be made electronically

(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 with a profit exceeding £1.5M based on a single company with no related 51% group companies and which prepares accounts for a 12 month period. The profit limit must be divided by the number of 51% related group companies and time apportioned for a chargeable accounting period of less than 12 months.

(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. Thus for the accounting year ended 31 March 2016 the first quarterly instalment payment would be due October 14, 2015 followed by further payments due January 14, April 14 and July 14, 2016

(e) Quarterly payments are not required if

» current augmented profits do not exceed £10 million

and

» the company was not large in previous CAP.

Example 1

Photo plc has Taxable Total Profits for the year ended 31 December 2015 of £2M, its lowest profit figure for several years.

Show how the liability for the year ended 31 December 2015 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 financial accounting period (this is called the filing date). If the accounts and computations are filed late there is a fixed penalty of £100. If the return is filed more than 3months after the filing date the fixed penalty is increased to £200 (This becomes £500 and £1,000 if it is the third consecutive time the return is late).

Returns 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 HMRC's intention to make an enquiry is given within 12 months from the date the return is received by HMRC.

(d) 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.

(e) 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.

(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 genuine 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 the error is deliberate and 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.

Students may now attempt Practice Question 45

Chapter 24

INHERITANCE TAX

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

The "available" nil rate band is deducted from the value of the chargeable estate. The nil rate band is £325,000 in 2015/16.

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 (never married), died on 1st February, 2016 leaving an estate valued at £0..75M. She had made no chargeable transfers of value in her lifetime and now bequeathed her estate 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, 2016	*£'000*
Net Assets	750
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 2016 (6 months after the end of the month in which the taxpayer died). 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 lifetime chargeable transfer of value of £200,000 in June 2013.

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, 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 an additional amount of tax of £130,000 (40% x £325,000) to be saved.
Note that irrespective of the level of nil rate band that existed at the date of her husband's death, Dee will now benefit from an extra 100% of the available nil rate band when she dies.

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 a lifetime gift made by an individual to another individual.

With a PET, the original assumption is that the gift will be exempt IHT. There is therefore no IHT 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 from the date of the gift, 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 2013 and the second in August 2013.

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 2013	PET	200,000	nil
August 2013	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 2010 and June 2012 respectively.

Compute the amount of IHT payable as a result of Dee's death.

Lifetime Transfers Chargeable on Death

			Gross Transfers	*IHT*
January 2010		PET	200,000	nil
June 2012		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 made in lifetime 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. For transfers made before 2015/16 the relevant nil rate band limit will be provided by the examiner. 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.

For example tax payable on a CLT made in December 2015 will be payable by June 30, 2016, whereas if the CLT was made in June 2015 then the IHT would not be payable until April 30, 2016.

The gross rate of IHT on transfers above the nil rate band is 20% and is applied 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 transfer is said to be a net transfer and the gift has to be "grossed up" as the IHT payable by the donor effectively becomes part of the gift. The simple solution to this problem is to apply a net IHT rate of 25% to any part of the net gift in excess of the available nil rate band at that date. The gross amount of this transfer is then computed by adding the amount of IHT to the net transfer.

Illustration 8

Kay Babb made a chargeable transfer into a trust of £400,000 in June 2011. She has made no previous lifetime transfers. The nil rate band in the 2011/12 tax year was £325,000.

Compute the amount of IHT payable, assuming firstly the trustees paid any IHT due, and then that Kay paid 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 paid 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 given for taper relief and then any lifetime tax paid.

Illustration 9

Having made the chargeable transfer of £400,000 into the trust in June 2011 Kay then died in December 2015 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.

Lifetime Transfers Chargeable on Death

		Gross Transfers	*IHT*
June 2011	CLT	400,000	30,000
325,000 @ Nil	= Nil		
75,000 @ 40%	= 30,000		

(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)	(12,000)
		18,000
Less:	Lifetime Tax Paid	(15,000)
Additional Tax Due on Death		3,000

If the lifetime tax paid exceeded the amount of tax now due, no additional tax would be payable, but equally there would be no repayment of lifetime tax paid.

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.
- Normal expenditure 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 2014	a gift to her daughter of £2,000
2)	12 August 2014	a wedding present to her son of £5,500
3)	19 September 2014	a gift to her husband of £20,000
4)	9 July 2015	a gift to her nephew as a wedding gift of £8,000
5)	25 December 2015	gifts of £200 each to two friends as a Christmas gift
6)	25 March 2016	a gift to a trust of a valuable painting worth £100,000

The gift on 19 September 2014 is exempt as a transfer between spouses and the gifts on 25 December 2015 are exempt as they are covered by the small gifts exemption.

The chargeable transfer figures are then computed as follows:

	7/6/2014	*12/8/2014*	*9/7/2015*	*25/3/2016*
	PET	PET	PET	CLT
Transfer of value	2,000	5,500	8,000	100,000
Less: Exemptions				
AE 2014/15	(2,000)			
Marriage		(5,000)		
AE 2014/15		(500)		
Marriage			(1,000)	
AE 2015/16			(3,000)	
AE 2014/15 (b/f balance unused)			(500)	
Chargeable Transfer	nil	nil	3,500	100,000

Note: although the 2013/14 AE is unused and would be brought forward into the 2014/15 tax year, it may only be used after the 2014/15 AE has itself been fully utilised. The 2014/15 AE is not however fully used and a balance of £500 is carried forward into 2015/16 for use after that year's own AE, while the 2013/14 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 2016, 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 2016 of £125,000 from which proceeds of £140,000 were received following Joe's death.

Joe had outstanding credit card bills of £6,000 at the date of his death and had also verbally promised to pay the medical expenses of £1,000 of a friend. Funeral expenses amounted to £6,000.

During his lifetime he had made the following lifetime transfers:

(1) On 20 November 2009 a cash gift of £40,000 to his son on the occasion of his wedding.

(2) On 15 July 2010 he transferred £405,000 into a trust and paid the IHT due thereon

(3) On 8 December 2014 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 the tax year 08/09 was £312,000 and £325,000 for 09/10.

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 2016 having made a CLT in June 2005, 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 2011 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 2005 CLT as it had been made within the 7 years prior to the PET.

Example 2

Dee Ceased died on 1 March 2016 with a Chargeable Estate of £500,000 having made the following lifetime gifts:

1 October 2003	£100,000 cash to son
1 June 2004	£278,000 cash into a trust
1 September 2010	£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:

03/04	£255,000
04/05	£263,000
10/11	£325,000

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. In addition the taxpayer has available each year an annual exemption of £3,000 and may also take advantage of the marriage exemption.

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

You should now review the following technical article written by the F6 examining team -IHT parts 1 and 2, plus the Finance Act 2015 article - Inheritance Tax section

You may now attempt Practice Question 38

Chapter 25

VALUE ADDED TAX – VAT

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. Trader is able to register for VAT and must then account for output VAT on sales but may reclaim input VAT on purchases and expenses, both capital and revenue expenditure. If a trader only makes exempt supplies he is unable to register for VAT and cannot reclaim input VAT

(b) A trader making taxable supplies must register for VAT if during the previous 12 months the value of taxable supplies exceeded £82,000. However, VAT registration is not required if taxable supplies in the following 12 months will not exceed £80,000. These figures are exclusive of VAT.

(c) HMRC must be notified within 30 days after the end of the period when taxable supplies exceeded £82,000.

(d) The trader will be registered from the end of the month following the month in which the limit was exceeded, or from an earlier agreed date.

EXAMPLE 1

Orchid Ltd commenced trading on 1 June 2015. Its sales are as follows:

		£			£
2015	June	3,900	2016	January	4,800
	July	3,800		February	6,000
	August	4,300		March	6,100
	September	5,100		April	7,900
	October	4,700		May	8,200
	November	4,700		June	11,800
	December	4,900		July	14,500

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 trader must also register for VAT if taxable supplies will exceed £82,000 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 2016, and its forecast income is £90,000 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 £82,000 registration limit. This will be beneficial when:

- » The trader makes zero-rated supplies. Input VAT will be reclaimed, but no VAT will be charged on the zero-rated outputs.
- » The trader 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 £78,000.

The company is planning to put up its prices, and this will increase annual income to £84,000. 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 trader stops being liable to VAT registration when it ceases to make taxable supplies. The trader must notify HMRC within 30 days, and will then be deregistered from the date of cessation or from an agreed later date.

(b) A trader can also request voluntarily VAT deregistration if expected taxable supplies in next 12 months are less than £80,000

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 2016 and 2017 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 £80,000.
- 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

(d) If a business disposes of its assets and trade as a going concern no output VAT will be charged as it will be outsaide the scope of VAT. The conditions for this treatment are:
- the business is transferred as a going concern
- no significant break in trading
- same type of trade pursued by transferee
- the transferee is or will become VAT registered

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 2016. 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 exam points regarding output VAT and input VAT as follows:

(a) VAT is chargeable on the actual amount received where a discount is offered for prompt payment. If the discount is not taken the VAT is charged on the full sale price and if the discount is taken then the VAT is based on the discounted price.

(b) Relief for irrecoverable (impaired) debts is only available if the output VAT has been accounted for and paid and debt is over six months old as measured from the time that payment was due. The relief is claimed as input VAT on the VAT return

(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).

(d) Input VAT cannot be recovered in relation to private use by a proprietor of a business

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 2016:

(1) Standard rated sales amounted to £120,000. Rose Ltd offers its customers a 5% discount for prompt payment and half of the customers took advantage of this discount.
(2) Standard rated purchases and expenses amounted to £35,640. This figure includes £480 for entertaining UK customers.
(3) On 15 March 2016 the company wrote off irrecoverable debts of £2,000 and £840 in respect of invoices due for payment on 10 May and 5 December 2015 respectively.
(4) On 31 March 2016 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 2016.

3.2 The refund of VAT

The refund of VAT that has been overpaid is subject to a four-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 a scale charge based on the cars CO_2 emissions.

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 2016 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 2016.

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. All businesses are now required to file VAT returns and make VAT payments online. VAT returns must be filed online and electronic payment made by one month and seven days after the end of the VAT return period. For example for the quarter ended 30 June 2016 a business has until 7 August 2016 to file its VAT return online and electronically make its VAT payment

Illustration 3
For the quarter ended 31 March 2016 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 2016 should be submitted by 7 May 2016. VAT of £5,300 (£12,400 - £7,100) is payable, and this is due by 7 May 2016 when the VAT return is submitted..

(b) Because VAT is a self-assessed tax, HMRC make control visits to VAT registered traders. The purpose of a control visit is to provide an opportunity for HMRC to check the accuracy of VAT returns.

(c) A business may choose to submit monthly returns but would only do so if it received regular VAT repayments. This would arise where the business had standard rated purchases and expenses but made zero rated sales and hence always had more input tax than output tax and therefore would claim a repayment.

(d) If a trader's VAT liability exceeds £2,300,000 over a 12 month period; they must make monthly payments on account of the VAT liability.

6 VAT Invoices

A VAT registered trader 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 new penalty system is being introduced over a period of years for the late filing of VAT returns and late payment of tax. This system has not yet been implemented by HMRC and hence the examiner has stated that it will be the existing penalty / default surcharge system that will continue to be examined in the September 2016 to March 2017 examinations.

(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 end 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%, the minimum surcharge is £30.

(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 2014	3,100	5 December 2014
31 December 2014	21,300	2 March 2015
31 March 2015	4,300	25 April 2015
30 June 2015	7,600	24 July 2015
30 September 2015	1,900	25 October 2015
31 December 2015	3,200	27 January 2016
31 March 2016	6,900	16 May 2016

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 2015. 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 an extended period of credit is taken by customers, and it also results in automatic bad debt relief. The disadvantage is that input VAT will only be recovered in relation to when payments are made.

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. It will also allow easier budgeting for cashflow.

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 and payments.
3. Under the scheme only one VAT return is submitted each year. This is due within two months of the end of the year.
4. Nine monthly payments are made on account, each being 10% of the previous year's VAT, in months 4 to 12 of the period with any balancing payment being made with the VAT return, or they may choose to pay quarterly instead
5. 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 (given by HMRC based on trade sector) to total income inclusive of VAT and any exempt supplies. 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 £120,000, all of which are standard rated and are to the general public. The company's standard rated expenses are £6,000 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 (120,000 × 20/120)	20,000
Input VAT 6,000 × 20/120)	(1,000)
VAT payable	19,000

If Snowdrop Ltd uses the flat rate scheme then it will pay VAT of £18,000 (120,000 × 15%). There is a VAT saving of £1,000 (19,000 – 18,000) 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 £96,000, 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 £30,000 p.a. These figures are inclusive of VAT. The relevant flat rate percentage for Primrose Ltd's trade is 6%. Using the normal basis of calculating its VAT liability, Primrose Ltd will have to pay VAT as follows:

	£
Output VAT (96,000 x 50% x 20/120)	8,000
Input VAT (30,000 x 20/120)	(5,000)
VAT payable	3,000

If Primrose Ltd uses the flat rate scheme then it will pay VAT of £5,760 (96,000 × 6%). Although the flat rate scheme will result in simplified administration, it is not beneficial as additional VAT of £2,760 (5,760 – 3,000) is payable and Primrose Ltd would 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. It would be beneficial to exclude a company making zero rated sales as it would then be able to continue making monthly returns to get the improved cash flow of monthly VAT repayments.

(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 businesses trading within and outside the European Union.

UK businesses frequently trade with companies/individuals within other European Union (EU) and non EU countries. The VAT treatment of exports and imports must be appreciated on these transactions.

12.1 Supply of goods

(a) Trading with **non EU** countries

» Exports

- The supply of goods is zero rated

» 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.

(b) Trading with EU 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.

(ii) Imports (Acquisitions)

- The VAT registered EU supplier will zero rate the transaction and the UK VAT registered business will "self supply" under the reverse charge system 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.

12.2 Supply of Services

- To overseas business customer = outside scope of VAT
- To overseas non business customer = standard rated
- Service from an overseas business = Self supply / reverse charge system applies as above

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 2016.

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)

You should now review the following part of the Finance Act 2015 technical article written by the F6 examining team - VAT section, plus VAT parts 1 and 2 articles, plus article on Motor Cars

You may now attempt Practice Questions 39 to 42

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 (companies pay corporation tax on their chargeable gains) - direct tax
(f) Inheritance tax - direct tax

Chapter 2

Answer to Example 1

Mr Smith Income tax computation 2015/16

	Non-savings	*Total*
	£	*£*
Employment Income	50,000	50,000
Total income	50,000	50,000
Less: Personal Allowance	(10,600)	(10,600)
Taxable income	39,400	39,400
Tax calculation:		
Non Savings		
31,785 × 20% =		6,357
7,615 × 40% =		3,046
39,400		
Tax liability		9,403
Less: tax suffered at source (PAYE)		(9,403)
Tax payable		–

Answer to Example 2

Billy Income Tax Computation 2015/16

	Non-savings income	*Savings income*	*Total*
	£	*£*	*£*
Trading income	25,600		25,600
Bank Deposit interest (8,000 × 100/80)		10,000	10,000
Total Income	25,600	10,000	35,600
Less: Personal Allowance	(10,600)		(10,600)
Taxable Income	15,000	10,000	25,000
Tax calculation:			
Non Savings			
15,000 @ 20% =			3,000
Savings			
10,000 @ 20% =			2,000
Tax liability			5,000
Less tax deducted @ source:			
Bank deposit interest 10,000 @ 20% =			(2,000)
Tax payable			3,000

Note: The 0% starting rate for savings income is not applicable as non savings taxable income exceeds £ 5,000

Answer to Example 3

Billy Income Tax Computation 2015/16

	Non-savings income	Savings income	Total
	£	£	£
Trading income	25,600		25,600
Bank Deposit interest 16,000 × 100/80		20,000	20,000
Total Income	25,600	20,000	45,600
Less: Personal Allowance	(10,600)		(10,600)
Taxable income	15,000	20,000	35,000

Tax calculation:		
Non Savings		
	15,000 @ 20% =	3,000
Savings		
	16,785 @ 20% =	3,357
	3,215 @ 40% =	1,286
	35,000	
Tax liability		7,643
Less tax deducted @ source:		
Bank deposit interest 20,000 @ 20% =		(4,000)
Tax payable		3,643

Note: The starting rate for savings income is not applicable as non savings taxable income exceeds £5,000

Answer to Example 4

Molly Income Tax Computation 2015/16

	Savings	Total
	£	£
Bank interest 16,000 × 100/80	20,000	20,000
Total Income	20,000	20,000
Less: Personal Allowance	(10,600)	(10,600)
Taxable income	9,400	9,400

Tax calculation:	
Savings	
5,000 @ 0% =	nil
4,400 @ 20% =	880
9,400	
Income Tax liability	880
Less tax deducted @ source:	
Bank Deposit interest £20,000 @ 20% =	(4,000)
Income Tax repayable	(3,120)

As Molly has no non savings taxable income, the full £5,000 zero rate band is available on the taxing of the savings income

Answer to Example 5

Molly Income Tax Computation 2015/16

	Non-savings income	Savings income	Total
	£	£	£
Trading income	11,600		11,600
Bank interest 16,000 × 100/80		20,000	20,000
Total Income	11,600	20,000	31,600
Less: Personal Allowance	(10,600)		(10,600)
Taxable income	1000	20,000	21,000

Tax calculation	
Non Savings	
1000 @ 20% =	200
Savings	
(5,000 – 1000 = 4,000)	
4,000 @ 0% =	nil
16,000 @ 20% =	3,200
21,000	
Income tax liability	3,400
Less tax deducted at source	
Bank deposit interest 20,000 @ 20% =	(4,000)
Income Tax Repayable	(600)

Answer to Example 6

Daisy Income Tax Computation 2015/16

	Non-savings income	Savings income	Dividends	Total
	£	£	£	£
Employment Income	18,600			18,600
Bank deposit interest 8,000 × 100/80		10,000		10,000
Dividends 1,800 × 100/90			2,000	2,000
Total Income	18,600	10,000	2,000	30,600
Less: Personal Allowance	(10,600)			(10,600)
Taxable income	8,000	10,000	2,000	20,000

Tax calculation:	
Non Savings	
8,000 @ 20% =	1,600
Savings	
10,000 @ 20% =	2,000
Dividends	
2,000 @ 10% =	200
Income Tax liability	3,800
Less tax deducted @ source	
Dividends 2,000 @10% =	(200)
Bank Deposit Interest 10,000 @ 20% =	(2,000)
PAYE	(1,400)
Income Tax Payable	200

Note: The starting rate for savings income is not applicable as non savings taxable income exceeds £5,000

Answer to Example 7

Daisy Income Tax Computation 2015/16

	Non-savings income	Savings income	Dividends	Total
	£	£	£	£
Employment Income	35,600			35,600
Bank interest 9,600 × 100/80		12,000		12,000
Dividends 1,800 × 100/90			2,000	2,000
Total Income	35,600	12,000	2,000	49,600
Less: Personal Allowance	(10,600)			(10,600)
Taxable income	25,000	12,000	2,000	39,000

Tax calculation:

	£
Non savings	
25,000 × 20% =	5,000
Savings	
6,785 × 20% =	1,357
5,215 × 40% =	2,086
12,000	
Dividends:	
2,000 × 32.5% =	650
Income Tax liability	9,093
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	788

Note: The starting rate for savings income is not applicable as non savings taxable income exceeds £5,000

Answer to Example 8

Mike Income Tax Computation 2015/16

	Non-savings	Total
	£	£
Employment income	108,000	108,000
Total income	108,000	108,000
Less: Personal Allowance (W1)	(6,600)	(6,600)
Taxable Income	101,400	101,400

Income Tax calculation:	
Non Savings	
31,785 @ 20% =	6,357
69,615 @ 40% =	27,846
101,400	
Income Tax Liability	34,203
Less: Tax deducted at source	
PAYE	(33,130)
Income tax Payable	1,073

(W1)	Normal personal allowance	10,600
	Less ½ [108,000 – 100,000]	(4,000)
	Revised Personal Allowance	6,600

ANSWERS TO EXAMPLES

Answer to Example 9

Ken Income Tax Computation 2015/16

	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		
	31,785 @ 20% =	6,357
	98,215 @ 40% =	39,286
	130,000	
Savings		
	20,000 @ 40% =	8,000
	20,000 @ 45% =	9,000
	40,000	
Dividends		
	36,000 × 37.5% =	13,500
Income Tax Liability		76,143
Less: Tax deducted at source		
Dividends 36,000 × 10% =		(3,600)
Bank Interest 40,000 × 20% =		(8,000)
Income tax Payable		64,543

(W1)	Normal personal allowance	10,600
	Less ½ [206,000 – 100,000]	(53,000)
	Restricted to	Nil

[Alternatively simply state that as adjusted net income > £121,200 the personal allowance is reduced to nil]

Answer to Example 10

James Income Tax Computation 2015/16

	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)	(7,600)		(7,600)
Taxable income	94,400	4,000	98,400

Income Tax calculation:		
Non Savings		
	31,785 @ 20% =	6,357
	62,615 @ 40% =	25,046
	94,400	
Savings	4,000 × 40% =	1,600
Income Tax Liability		33,003
Less: Tax deducted at source		
Bank Interest 4,000 × 20% =		(800)
Income tax Payable		32,203

(W1) As adjusted net income exceeds £100,000, the normal personal allowance is then restricted

Normal personal allowance	10,600
Less ½ [106,000 – 100,000]	(3,000)
Revised personal allowance	7,600

Answer to Example 11

David Income Tax Computation 2015/16	£
Trading Profit	8,000
Revised PA (10,600 - 1,060)	(9,540)
Taxable Income	Nil

Victoria Income Tax Computation 2015/16	£
Employment Income	30,000
PA	(10,600)
Taxable Income	19,400
Tax Calculation	
Non Savings 19,400 x 20% =	3,880
PA tax reduction (1,060 x 20%) =	(212)
Tax Liability	3,668

The election must be made within 4 years of the end of the tax year ie by 5 April 2020

Answer to Example 12

Kathy Income Tax Computation 2015/16

	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 Allowance	(10,600)	(10,600)
Taxable Income	38,400	38,400

Tax calculation:	
Non Savings	
31,785 @ 20% =	6,357
6,615 @ 40% =	2,646
38,400	
Income Tax Liability	9,003

Answer to Example 13

Elliot Income Tax Computation 2015/16

	Non-savings	*Total*
	£	*£*
Trading income	48,000	48,000
Total Income	48,000	48,000
Less: Personal Allowance	(10,600)	(10,600)
Taxable income	37,400	37,400

Tax calculation

Non Savings

33,785 (W1) @ 20% =	6,757
3,615 @ 40% =	1,446
37,400	
Income Tax Liability	8,203

(W1) $31,785 + (1,600 \times 100/80) = 33,785$

Answer to Example 14

Thomas Income Tax Computation 2015/16

	Non-savings	*Total*
	£	*£*
Trading income	160,000	160,000
Total Income	160,000	160,000
Less: PA (note 1)	(–)	(–)
Taxable income	160,000	160,000

Income Tax Non savings

	Non Savings	
(W2)	39,785 @ 20% =	7,957
(W3)	118,215 @ 40% =	47,286
	2,000 @ 45% =	900
	160,000	
	Income Tax Liability	56,143

note 1 The PA is reduced to nil as the adjusted net income exceeds 121,200

(W1)	Net Income	160,000
	Less Gross gift aid payment ($6,400 \times 100/80$)	(8,000)
	Adjusted Net income	152,000

(W2) $31,785 + (6,400 \times 100/80) = 39,785$
$150,000 + (6,400 \times 100/80) = 158,000$
(W3) $158,000 - 39,785 = 118,215$

Answer to Example 15

Kerry Income Tax Computation 2015/16

	Non-savings	Savings	Dividends	Total
	£	£	£	£
Trading income	101,000			101,000
Bank interest 3,200 × 100/80		4,000		4,000
Dividends 2,700 × 100/90			3,000	3,000
Total Income	101,000	4,000	3,000	108,000
Less reliefs:				
Qualifying interest	(3,000)			(3,000)
Net Income	98,000	4,000	3,000	105,000
Less: PA (W1)	(10,600)			(10,600)
Taxable income	87,400	4,000	3,000	94,400

Income Tax		
Non Savings		
(W3)	37,785 @ 20% =	7,557
	49,615 @ 40% =	19,846
	87,400	
Savings		
	4,000 × 40% =	1,600
Dividends		
	3,000 × 32.5% =	975
	94,400	
Income Tax Liability		29,978
Less: Tax deducted at source		
Dividends		
3,000 × 10%		(300)
Bank Interest		
4,000 × 20%		(800)
Income tax payable		28,878

(W1) As Adjusted Net Income does not exceed 100,000 the PA is not reduced

(W2)	Net Income	105,000
	Less Gross gift aid payment (4,800 × 100/80)	(6,000)
	Adjusted Net income	99,000

(W3) 31,785 + (4,800 × 100/80) = 37,785
150,000 + (4,800 × 100/80) = 156,000

Answer to Example 16

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 be computed as:

	£
Property income	10,000
Less: Personal Allowance	(10,600)
	nil
Tax liability	nil

This will save the couple £4,000

If Elton transferred the ownership of the entire asset then all the income would be assessed on David and his taxable income of £9,400 (20,000 - 10,600) would be taxed at 20% giving a tax liability of £1,880 compared to Elton's current tax liability on the property income of £8,000 achieving a total tax saving therefore of £6,120

Chapter 3

Answer to Example 1

The rent assessable in each case is the rent due for the period 1 July 2015 to 5 April 2016
Expenses incurred in the same period are deductible.

	£	£
Rent due $\frac{9}{12} \times 6{,}000$		4,500
Expenses:		
Redecoration	300	
Repairs	500	
		800
Property Income for 2015/16		3,700

Answer to Example 2

	£	£
Rent due £800 × 12		9,600
Expenses		
Bad debt – June 2015 rent	800	
Insurance ($\frac{3}{12}$× £420) + ($\frac{9}{12}$ × £480)	465	
Drain clearance	380	
Redecoration	750	
Wear and tear (10% × £8,800)	880	
		(3,275)
Property Income for 2015/16		6,325

The garage is an improvement, not a repair, and is therefore not deductible. The redecoration cost was incurred in 2015/16

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

As gross rents exceed £4,250 Barbara must elect for the rent a room relief to apply if she wants it. Barbara should elect for the alternative treatment in 2015/16 by 31 January 2018

Answer to Example 4

		£
Premium	$\frac{51-20}{50} \times 60{,}000$	37,200
Rent	($\frac{9}{12}$× 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 2016

	£	£
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 Year Ended 5 April 2016		*Main Pool*	*Allowances*
	£	£	£
WDV b/f at 6 April 2015		1,250	
Additions Qualifying for AIA	10,000		
AIA	(10,000)	–	10,000
Disposals		(500)	
		750	
Small pool WDA		(750)	750
WDV c/f		–	10,750

Answer to Example 2

Accounting Year ended 5 April 2016			70%	70%	
		Main Pool	*Business use car (1)*	*Business use car (2)*	*Allowances*
	£	£	£	£	£
WDV b/f at 6 April 2015		21,200	13,600		
Additions Qualifying for AIA					
Plant	6,600				
AIA	(6,600)				6,600
Other additions					
Motor car (CO_2 100g/km)		10,600			
Motor car (CO_2 180g/km)				16,000	
Disposal			(9,400)		
		31,800	4,200	16,000	
WDA @ 18%		(5,724)			5,724
Balancing allowance			(4,200) × 70%		2,940
WDA @ 8%				(1,280) × 70%	896
					16,160
WDV c/f		26,076	–	14,720	

Answer to Example 3

Accounting period to 5 April 2016

		Main Pool	*Short life Asset*	*Allowances*
	£	£	£	£
WDV b/f		16,000		
Additions qualifying for AIA				
Machinery	520,000			
Photocopier	4,000			
	524,000			
AIA (Maximum)	(500,000)			500,000
		20,000	4,000	
		36,000	4,000	
WDA @ 18%		(6,480)		6,480
WDA @ 18%			(720)	720
				507,200
WDV c/f		29,520	3,280	

Accounting period to 5 April 2017

	Main Pool	*Short life Asset*	*Allowances*
	£	£	£
WDV b/f	29,520	3,280	
Disposal		(1,500)	
	29,520	1,780	
WDA @ 18%	(5,314)		5,314
Balancing allowance		(1,780)	1,780
			7,094
WDV c/f	24,206	–	

Answer to Example 4

Year ended 5 April 2016

	Main Pool	*Allowances*
	£	*£*
WDV b/f at 6 April 2015	4,000	
Addition – 1/10/15	2,000	
	6,000	
Less Disposal 10/04/15	(8,600)	
	(2,600)	
Balancing charge	2,600	(2,600)

Answer to Example 5

Accounting Period ended 31 March 2016

	Main Pool	*Allowances*
	£	£
WDV b/ at 1 January 2016	12,000	
Addition – 1 February 2016	4,000	
	16,000	
Less Disposals – 31 March16	(5,000)	
	11,000	
Balancing allowance	(11,000)	11,000
	–	

Answer to Example 6

Accounting period to 5 April 2016

		Main Pool	*Special rate pool*	*80% Business use car*	*Allowances*
	£	£	£	£	£
WDV b/f		30,000		14,000	
Additions Qualifying for AIA (Special Rate)					
Thermal insulation for business building	28,000				
AIA	(28,000)				28,000
			–		
Additions Qualifying for AIA (Main)					
Computer	60,000				
Machine	184,000				
Plant	260,000				
	504,000				
AIA (500,000 – 28,000)	(472,000)				472,000
		32,000			
Other additions					
Motor car (76 -130g/km)		11,200			
Disposals				(8,000)	
		73,200		6,000	
WDA @ 18%		(13,176)			13,176
Balancing allowance				(6,000) × 80%	4,800
Additions Qualifying for FYA					
Motor car (≤ 75g/km)	17,000				
FYA @ 100%	(17,000)				17,000
					534,976
WDV c/f		60,024	–	–	

Chapter 6

Answer to Example 1

(a) 2014/15
(b) 2015/16
(c) 2015/16

Answer to Example 2

				£
2012/13	Actual (1/01/13 – 5/04/13)	3/6 × 30,000		15,000
2013/14	First 12 months (1/01/13– 31/12/2013)			
	1/01/13 – 30/06/13		30,000	
	1/07/13 – 31/12/2013	6/12 × 70,000	35,000	65,000
2014/15	CYB (year to 30/06/14)			70,000
2015/16	CYB (year to 30/06/15)			82,000
Overlap profits:	1/01/13 – 5/04/13		15,000	
	1/07/13 – 31/12/2013		35,000	50,000

Answer to Example 3

			£
2014/15	Actual (1/05/14 – 5/04/15)	11/18 × 36,000	22,000
2015/16	12 months to 31/10/15	12/18 × 36,000	24,000
2016/17	CYB (y/e 31/10/16)		30,000
Overlap profits	1/11/14 – 5/04/15	5/18 × 36,000	10,000

Answer to Example 4

		£
2014/15	CYB (y/e 31/01/15)	47,000
2015/16	4 months: 1/02/15 – 31/05/15	8,000
	Less: overlap relief	(6,000)
		2,000

Answer to Example 5

Income tax computation 2015/16

	Non savings
Employment Income (3/12 x 40,000)	10,000
Trading Profit (W1)	54,463
Total Income	64,463
Personal allowance	(10,600)
Taxable income	53,863
Tax calculation:	
31,785 @ 20%	6,357
22,078 @ 40 %	8,831
53,863	
Income Tax Liability	15,188

As Wendy started to trade on 1 July 2015 the first tax year of assessment is 2015/16,
2015/16 (Actual) (1.7.15 - 5.4.16)
= 54,463

(W1)	Adjusted profit	89,000
	Less capital allowance (W2)	(34,537)
	Trading income	54,463

(W2)

		Main Pool	60% Business use asset (1)	Allowances
	£	£	£	£
Accounting Period to 5 April 2016		–		
Additions qualifying for AIA (max 9/12 x 500,000)				
Recording equipment	30,000			
Computer	2,600			32,600
Other Additions				
Motor car (76-130g/km)		10,400		
Motor car (>130g/km)			14,800	
		10,400	14,800	
WDA × 18% x 9/12		(1,404)		1,404
WDA × 8% x 9/12			(888) × 60%	533
				34,537
WDV c/f		8,996	13,912	

Answer to Example 6

Normal Basis

		£
Revenues		61,000
Cost of sales (29,000 – 1,800)		(27,200)
		33,800
Motor expenses (3,600 x 60%)		(2,160)
Capital allowances (8,000 + (12,000 x 18% x 60%)		(9,296)
Adjusted Trading Profit		22,344

Cash Basis

Receipts (61,000 – 4,000)		57,000
Payments		
Purchases & Expenses (29,000 – 2,000)	27,000	
Equipment	8,000	
Motor expenses (10,000 x 60% x 45p)	2,700	(37,700)
Adjusted Trading Profit		19,300

Answer to Example 7

Eve may either establish an agreed split between business and private use and add back the private use proportion or simply use the flat rate private use adjustment and add back £4,200, giving an adjusted trading profit figure of £27,200 (23,000 + 4,200).

If a question is set using the cash basis it should be assumed that the election to use the relevant flat rate scheme has been made.

Although the flat rate scheme applies to unincorporated businesses generally it will only be examined within the cash basis.

If the cash basis is to be used in the examination it will be specifically mentioned and should only be used therefore if specifically required.

ANSWERS TO EXAMPLES

Chapter 7

Answer to Example 1

	2013/14	2014/15	2015/16
	£	£	£
Trading income	nil	3,000	10,000
Less: carry forward relief	nil	(3,000)	(2,000)
Revised trading income	nil	nil	8,000

Working – loss memorandum	£
Trading loss	5,000
Less: carry forward relief in 2014/15	(3,000)
	2,000
Less: carry forward relief in 2015/16	(2,000)
Loss carried forward to 2016/17	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 2014/15 and the remainder carried forward to 2015/16.

Answer to Example 2

Trading profit assessments:	£
2013/14	
Year ended 31 December 2013	32,000
2014/15	
Year ended 31 December 2014	25,000
2015/16	
Year ended 31 December 2015	NIL

Income tax computations

	2013/14	2014/15	2015/16
	£	£	£
Trading profit	32,000	25,000	Nil
Property income	6,000	6,000	6,000
Total income	38,000	31,000	6,000
Less relief's			
Loss relief against total income		(31,000)	(–)
Net income	38,000	–	6,000
PA	(10,600)	(10,600)	(10,600)
Taxable income	27,400	–	–

- A claim against total income in 2015/16 would waste the personal allowance for 2015/16 and save no income tax. The claim in 2014/15 will also waste the PA but will generate a repayment of tax of 20% on a taxable income of £20,400 (31,000 - 10,600).
- The balance of the trading loss £53,000 (£84,000 - £31,000) will then be carried forward against the first available future trading profits that arise from the same trade.
- As the total non trading income for the tax year 2014/15 is less than £50,000 the cap on the income tax loss relief available is not relevant (explained in section 4 part (c) of this chapter).

Answer to Example 3

Provided an election is made, the whole of the trading loss available can be offset against the capital gains as follows:

	£
Capital gains	44,000
Loss relief	(24,000)
	20,000
Annual Exempt Amount	(11,100)
Taxable gain	8,900

Answer to Example 4

Trading income assessable amounts:

	Assessment	*Loss*
2014/15 (Actual basis)		
1/8/14 – 5/4/15 (8/10 × (20,000))	Nil	(£16,000)
2015/16 (First 12 months)		
1/8/14 – 31/7/15		
Loss	(20,000)	
Less: Used in 2014/15	16,000	
	(4,000)	
Profits 2/12 × 48,000	8,000	
	4,000	
2016/17 (CYB)		
A/C year ended 31/5/16	48,000	

When calculating the amount assessable for 2015/16, the loss already taken into account in 2014/15 must be deducted. The loss of £4,000 allocated to 2015/16 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 2014/15. A loss may only be relieved once hence there is no concept of "overlap loss"

Answer to Example 5

Taxable income computations

	2011/12	*2012/13*	*2013/14*	*2014/15*	*2015/16*	*2016/17*
	£	*£*	*£*	*£*	*£*	*£*
Employment Income	12,800	11,050	5,868			
Trading profit (W1)				Nil	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 years relief	(9,000)	(3,000)	–	–	–	–
Net Income	8,300	12,550	10,368	4,500	4,500	7,000
Less: Personal Allowances	(10,600)	(10,600)	(10,600)	(10,600)	(10,600)	(10,600)
Taxable income	Nil	1,950	Nil	Nil	Nil	Nil

Under opening years loss relief the loss of 2014/15 (£9,000) is set initially against Total Income of 2011/12. Any loss remaining would then be set automatically against Total Income of 2012/13 and finally against Total Income of 2013/14. In this example there is clearly sufficient income in 2011/12 to absorb all the available loss of 2014/15. It does however result in some wastage of the personal allowance for 2011/12. The loss of 2015/16 (£3,000) is then set against Total Income of 2012/13 (before relieving 2013/14 and 2014/15 had any loss remained).

Workings

(W1) New business – assessments

			Assessment	Loss
2014/15 (Actual)	1/7/2014 – 5/4/2015		Nil	
	9/12 × (12,000)			(9,000)
2015/16 (CYB)	y/e 30/6/2015		Nil	(12,000)
	Less: used in 2014/15			9,000
				(3,000)
2016/17	(y/e 30/6/2016)		2,500	
Loss available for relief				
2014/15			(9,000)	
2015/16			(3,000)	

Answer to Example 6

Trading loss arising in final 12m of trading available for terminal loss relief is calculated as

2016/17		
6/4/2016 –31/5/2016		
2/10 × (20,000)		(4,000)
Overlap Relief		(500)
2015/16		
1/6/2015 – 5/4/2016		
2/12 × 6,000	1,000	
+ 8/10 × (20,000)	(16,000)	(15,000)
Trading Loss available under terminal loss relief		(19,500)

The loss of £19,500 would then be set off against the trading profits of firstly 2015/16 of £6,000 leaving the remaining £13,500 to be used against the £18,000 trading profit assessment of 2014/15

Chapter 8

Answer to Example 1

	Total	Doug	Rob
	£	£	£
A/C Year Ended 30/9/2015	18,000		
1/10/2014 to 30/6/2015			
(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
1/7/2015 to 30/9/2015			
(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 then be assessed on their share of the profit in 2015/16 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 30/6/2014	12,000	6,000	6,000	–
y/e 30/6/2015	14,000	7,000	7,000	–
y/e 30/6/2016	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 2013:

		£
2013/14 (Actual)	1 July 2013 to 5 April 2014 £6,000 × 9/12	4,500
2014/15 (CYB)	Year ended 30 June 2014	6,000
2015/16 (CYB)	Year ended 30 June 2015	7,000
2016/17 (CYB)	Year ended 30 June 2016	8,000

They will both carry forward overlap profits of £4,500.

Clair will be treated as commencing on 1 July 2015, and will be assessed on her share of the partnership profits as follow:

2015/16 (Actual)	1 July 2015 to 5 April 2016 £8,000 × 9/12	6,000
2016/17 (CYB)	Year ended 30 June 2016	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 carry forward relief.

Chapter 9

Answer to Example 1

The mileage allowance of £3,600 (12,000 at 30p) received is tax free and Kerry will be entitled to a deduction of £1,400 computed as follows:

Authorised rate	£
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) × 3%	1,350
Total assessable benefit	4,850

Answer to Example 3

(a) Gift of dishwasher

	£
Market value when first made available to Gerald	900
Less: Benefit already assessed 2014/15 : (900 × 20% × 10/12)	(150)
Taxable benefit on gift: 2015/16	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: 2015/16	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 2014/15 – use £150
   Taxed in 2015/16 – Gift 750 (a) or £600 (b)

Answer to Example 4

Lewis

The CO_2 emissions are above 95g/km, so the relevant percentage is 22% (14% + 3%(diesel car) + 5% (1% for every complete 5g/km above 95g/km ie 120-95 = 25 / 5 = 5%). The motor car was only available for eight months of 2015/16, so the benefit is £1,980 (13,500 × 22% × 8/12).

Nico

The CO_2 emissions are above the base level figure of 95 grams per kilometre. The CO_2 emissions figure of 187 is rounded down to 185 so that it is divisible by five. The base level percentage of 14% is increased in 1% steps for each complete 5 grams per kilometre above the base level, so the relevant percentage is 32% (14% + 18% (185 – 95 = 90/5)). The motor car was available throughout 2015/16 so the benefit is £5,248 (16,400 × 32%).

Fernando

The CO_2 emissions are above the base level figure of 95 grams per kilometre. The relevant percentage is 44% (14% + 30% (245 – 95 = 150/5)), but this is restricted to the maximum of 37%. The motor car was available throughout 2015/16 so the benefit is £7,162 (22,600 × 37% = 8,362 - 1,200). The contribution by Carla towards the use of the motor car reduces the benefit.

Jenson

The CO_2 emissions are between 76 grams per kilometre and 94 grams per kilometre so the relevant percentage is 13% as it is a petrol car. The benefit is £16,000 × 13% = £2,080 for 2015/16.

Sebastian

The CO_2 emissions are between 51 grams to 75 grams per kilometre and the relevant percentage is 12% (9% + 3% (diesel car)). The benefit is £11,000 × 12% = £1,320 for 2015/16.

Answer to Example 5

Lewis

£22,100 × 22% × 8/12 = £3,241
The fuel was not available for first 4 months

Nico

£22,100 × 32% = £7,072

Fernando

£22,100 × 37% = £8,177

There is no reduction for the contribution made by Fernando since the cost of private fuel was not fully reimbursed.

Jenson

£22,100 × 13% = £ 2,873

Sebastian

£22,100 × 12% = £2,652

Answer to Example 6

(a) Average method

		£
$\frac{35,000 + 15,000}{2}$ x 3%		750
Less: interest paid (as below)		(258)
		492
6/4/2015 – 31/5/2015	£35,000 × 1% × 2/12	58
1/6/2015 – 30/11/2015	£30,000 × 1% × 6/12	150
1/12/2015 – 5/4/2016	£15,000 × 1% × 4/12	50
		258

(b) Accurate method

		£
6/4/2015 – 31/5/2015	£35,000 × 3% × 2/12	175
1/6/2015 – 30/11/2015	£30,000 × 3% × 6/12	450
1/12/2015 – 5/4/2016	£15,000 × 3% × 4/12	150
		775
Less: Interest paid (as above)		(258)
		517

HMRC would be entitled to opt for the accurate basis as this gives a higher assessment.

Answer to Example 7

	£
Personal Allowance	10,600
Benefits	(440)
Tax underpaid: 132 × 100/20	(660)
	9,500
Tax code	950L

Chapter 10

Answer to Example 1

The total pension input allowed is made up as follows:

AA for 2015/16	40,000
Unused AA b/f	
- 2012/13 fully used	nil
- 2013/14 (50,000 – 30,000)	20,000
- 2014/15 (40,000 – 25,000)	15,000
Maximum gross contribution	75,000

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 2015/16 Aston made a gross contribution of £55,000, this would be less than his relevant earnings for the year (£120,000) and would therefore qualify for relief and would utilise all of the 2015/16 AA of £40,000 and £15,000 of the £20,000 unused AA brought forward from 2013/14.

The remaining £5,000 would be carried forward for one more year to 2016/17. If a £30,000 payment were then made this would be within the AA for 2016/17 so no unused AA brought forward would be utilised.

The £5,000 unused AA from 2013/14 would now lapse so that in 2017/18 after that year's AA is used there would be unused AA brought forward for use as follows:

- 2014/15		£15,000
- 2015/16		£NIL
- 2016/17	(40,000 – 30,000)	£10,000

Chapter 11

Answer to Example 1

The Class 1 and Class 1A NIC liability is as follows:

Class 1		£
Employee	. ≤ £8,060 @ 0%	Nil
	. [£42,385 – £8,060] × 12%	4,119
	. [£50,000 – £42,385] × 2%	152
		4,271
Employer	. ≤ £8,112 @ 0%	Nil
	. [£50,000 – £8,112] × 13.8%	5,781
		5,781
	Employment Allowance	(2,000)
		3,781

Class 1A
Employer   6,400 + 4,320 = 10,720 @ 13.8% = £1,479

Answer to Example 2

Class 4	£
(£42,385 – £8,060) × 9%	3,089
(£50,000 – £42,385) × 2%	152
	3,241
Class 2	
£2.80 × 52 weeks	£146

Chapter 12

Answer to Example 1

Tina – Capital Gains tax computation as 2015/16

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 2015/16		240,000
Less capital losses b/f		(12,000)
Net Capital Gains		228,000
Less Annual Exempt Amount		(11,100)
Taxable Gains		216,900
CGT × 28% (Note)		£60,732
Due		31/1/2017

Note: Tina's taxable income of £50,000 exceeds the basic rate band of £31,785 so all of the taxable gain is taxed at 28%

Answer to Example 2

	£
Capital Gain	18,000
Less AEA	(11,100)
Taxable Gain	6,900
Capital Gains Tax (W1)	
6,900 × 18%	£1,242
Due	31/1/2017

Income Tax Computation

Trading profit	20,000
Less PA	(10,600)
Taxable income	9,400

Basic rate band remaining.
31,785 – 9,400 = £22,385. The taxable gains of £6,900 therefore fall wholly into the remaining basic rate band so the CGT rate is 18%

Answer to Example 3

	£
Capital Gain	30,000
Less AEA	(11,100)
Taxable Gain	18,900
Capital Gains Tax (W1)	
1,785 × 18%	321
17,115 × 28%	4,792
18,900	£5,113
CGT Due	31/1/2017

Income Tax Computation

Trading profit	40,600
Less Personal allowance	(10,600)
Taxable income	30,000

Basic rate band remaining.
31,785 – 30,000 = £1,785.
Part of the taxable gain falls within the remaining basic rate band so will be taxed at 18%, but (£18,900 – £1,785) £17,115 exceeds the basic rate band so will be taxed at 28%.

Answer to Example 4

	£
Capital Gain	26,000
Less AEA	(11,100)
Taxable Gain	14,900
Capital Gains Tax (W1)	
785 × 18%	141
14,115 × 28%	3,952
14,900	£4,093
CGT Due	31/1/2017

W1 Income Tax Computation

Trading profit	44,600
Less Personal allowance	(10,600)
Taxable income	34,000

Basic rate band remaining £34,785 – £34,000 = £785

Part of the taxable gain falls into the remaining basic rate band so will be taxed at 18%, but (£14,900 – £785) £14,115 exceeds the basic rate band so will be taxed at 28%.

The basic rate band is extended by the gross gift aid payment: (£31,785 + 2,400 × 100/80) = 34,785

Answer to Example 5

(£4.00 + £4.08) / 2 = £4.04p

Value 1,000 × £4.04p = £4,040

Answer to Example 6

Fiona

	£
2014/15	
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 AEA. No losses to carry forward to 2015/16.

2015/16	
Capital gains in the tax year	17,000
Capital losses in the tax year	(5,200)
Net Capital gains in the tax year	11,800
AEA	(11,100)
Taxable gains	700

Fiona is taxed on taxable gains of £700 in 2015/16. No losses to carry forward.

Jane

2014/15	
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 2014/15 AEA since her gains are covered by current year losses. She has net losses of £3,000 (10,000 - 7,000) to carry forward to 2015/16.

2015/16	
Capital gains in the tax year	13,700
Capital losses in the tax year	(2,000)
Net Capital Gains in the tax year	11,700
Less capital loss b/f (restrict)	(600)
Net Capital Gains	11,100
Less AEA	(11,100)
Taxable Gain	–

The capital loss b/f is used so as to only reduce the net gains of the year down to the level of the AEA. Capital loss to carry forward is then 3,000 – 600 = £2,400

Answer to Example 7

Gollum transfers the ring at no gain / no loss in December 2015
Frodo sells the ring

	£
Disposal Proceeds	20,000
Less Cost	(12,000)
Capital gain	8,000

Frodo simply takes on the original cost of the asset from Gollum as if he acquired it himself in July 1993

Answer to Example 8

		£
Proceeds		16,000
Less Acquisition cost	$26{,}000 \times \dfrac{16{,}000}{16{,}000 + 34{,}000}$	(8,320)
Chargeable gain		7,680

Answer to Example 9

(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)
Chargeable gain	8,000

Restricted to ⁵⁄₃ [10,000 – 6,000] = **£6,667**

(c) Antique vase – non wasting chattel

	£
Disposal proceeds (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 10

	£	£
Proceeds		38,000
Less Acquisition cost		
Purchase	25,000	
Less 12/30 × [25,000 – 1,000]	(9,600)	
		(15,400)
Chargeable gain		22,600

Chapter 13

Answer to Example 1

(a) Match with acquisitions on same day as sale — none

(b) Match with acquisitions in next 30 days

7 March 2016		200 shares
	£	
Disposal proceeds (200/1,000 × £25,000)	5,000	
Less: cost	(4,000)	
Capital gain		1,000

(c) Match with share pool

	Number	Cost
31 May 2013	1,500	20,000
30 June 2014	500	10,000
	2,000	30,000
Disposal	(800)	(12,000)
	1,200	18,000

Calculate Gain	£	
Disposal proceeds (800/1,000 × £25,000)	20,000	
Less: cost	(12,000)	
Capital gain		8,000
Capital Gains 2015/16		9,000

Answer to Example 2

(a) Match with acquisitions on same day — none
(b) Match with acquisitions in next 30 days — none
(c) Match with share pool

	Number	Cost
Feb 2014	7,000	15,000
June 2014	1,000	4,000
	8,000	19,000
July 2014 Bonus 1:5	1,600	–
	9,600	19,000
October 2015 Disposal	(5,000)	(9,896)
	4,600	9,104

Calculate Gain

	£
Disposal proceeds	20,000
Less: cost	(9,896)
Capital gain	10,104

Answer to Example 3

(a) Match with acquisitions on same day none

(b) Match with acquisitions in next 30 days none

(c) Match with share pool

	Number	Cost
Feb 2014	6,000	15,000
June 2014	900	2,700
	6,900	17,700
July 2014 Rights 1: 3 @ £3.00	2,300	6,900
	9,200	24,600
September 2015 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	35,000
Less Cost (W)	(10,000)
Capital gain	25,000

Working: Cost of ordinary shares in Gold Ltd

Mark received:

8,000 ordinary shares, valued at £5 =	40,000
4,000 preference shares, valued at £2 =	8,000
Total	48,000

The cost attributable to the ordinary shares is therefore: £12,000 x $\frac{40{,}000}{48{,}000}$ = £10,000

Answer to Example 5

Mark receives at takeover:

	Market value	Cost
8,000 Gold Ltd ordinary shares	£40,000	£10,000
Cash	£8,000	£2,000
Total	£48,000	£12,000

The original Silver Ltd share cost of £12,000 is divided between the shares and cash received from Gold Ltd proportionate to the value received. As cash has now been received at the time of the takeover an immediate gain arises.

Capital gain in June 2015:

(Computed from working above)	£
Proceeds (cash received)	8,000
Less Cost	(2,000)
Capital gain	6,000

ANSWERS TO EXAMPLES

Chapter 14

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 AEA	(11,100)
Taxable gain	838,900
Capital Gains Tax £838,900 × 10%	£83,890
Due	31/1/2017

Entrepreneurs relief is available on both disposals, the sale of the business and the sale of the shares where Daisy had owned at least 5% of the shares and been an employee for a period of at least 12 months

Daisy has utilised £850,000 (£480,000 + £370,000) of entrepreneurs' relief in 2015/16 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 AEA		(11,100)
Taxable gain		63,900
Capital Gains Tax (W1)	£450,000	£17,920
Due date	31/1/2017	31/1/2017

(W1)	£
£4,500,000 × 10%	450,000
£63,900 × 28% (Note)	17,892
Capital Gains Tax	467,892

Note: £13,785 (£31,785 – £18,000) of Anne's basic rate band is unused, but this is deemed to be 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.

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

As all the sale proceeds have been reinvested in a new qualifying business asset the entire gain is eligible for rollover relief. If rollover relief was not claimed entrepreneurs' relief would not be available as this is the disposal of an individual asset used in the business, not the disposal of the business itself.

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

As £50,000 of the sale proceeds has not been reinvested this amount of the gain remains chargeable. 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 business. If a further £50,000 were to be reinvested in other qualifying business assets by August 2018 (3 years from disposal date) a further rollover relief claim could be made to defer the remaining gain

(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 2015/16 as it is not the disposal of the whole of the business.

If however further reinvestment in qualifying assets within the relevant time period (by August 2018) is made then claims for rollover relief may then be available.

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) As all the business proportion of the sale proceeds has been reinvested in a business asset the business proportion of the gain (85%) may be rolled over in full. 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 a 55 year leasehold factory, a depreciating asset, the entire gain may be held over. The held over gain on the sale of the factory in June 2014 becomes chargeable in 2015/16, as the depreciating asset has been sold in February 2016. The capital gain is £200,000 (£500,000 - £300,000). A further gain of £40,000 (640,000 - 600,000) arises on the sale of the leasehold factory. Entrepreneurs' relief is not available as Charles did not dispose of the whole business.

ANSWERS TO EXAMPLES

Answer to Example 7

David has made a disposal in September 2015 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 deemed base cost to set against a future disposal, calculated as follows.

	£
Market value of asset acquired	100,000
Less: gain deferred	(40,000)
	60,000

Answer to Example 8

(a) Richard – Chargeable gain on shares sold at undervalue in March 2016

	£	£
Market value of shares in March 2016		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 AEA		(11,100)
Taxable gain		13,900
CGT @ 10%		£1,390

(b) Richard's son – Base cost

	£
Market value of shares in March 2016	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 AEA	(11,100)
Taxable gain	63,900
CGT @ 10%	£6,390

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

The shares in the unquoted trading company will qualify for gift relief but as £100,000 (investments) of the £800,000 (investments, premises and goodwill) chargeable assets are investments the relief is restricted as follows:

$$600{,}000 \times \frac{700{,}000}{800{,}000} = 525{,}000$$

Answer to Example 10

	£
Disposal proceeds	150,000
less cost	(10,000)
Capital gain	140,000
less PPR relief (W1)	(104,706)
Chargeble Gain	35,294

(W1)

		Actual & Deemed Occupation (months)	Absent (months)
1/4/86 – 30/6/86	(actual)	3	
1/7/86 – 30/6/88	(working overseas)	24	
1/7/88 –31/12/02	(actual)	174	
1/1/03 –31/12/2015	(4 years work in UK/last 18 months)	66	90
		267	90

PPR relief $\frac{267}{357} \times 140{,}000 = 104{,}706$

Answer to Example 11

	£
Disposal proceeds	250,000
Less cost	(30,000)
Capital Gain	220,000
Less PPR relief (W1)	(117,333)
	102,667
Less Letting relief (W2)	(18,333)
Chargeable Gain	84,334

(W1)

	Actual & Deemed (months)	Absent (months)	
1/4/1986 – 31/3/1988 (actual)	24		
1/4/1988 – 30/9/1993 (Any reason)	36	30 (house let)	
1/10/1993 –31/3/2003 (actual)	114		
1/4/2003 –31/3/2016 (last 18 months)	18	138	
	192	168	360

PPR relief $\frac{192}{360} \times 220{,}000 = 117{,}333$

(W2) (i) £117,333

(ii) £40,000

(iii) $\frac{30}{360} \times 220{,}000 = 18{,}333$

Chapter 15

Answer to Example 1

The payments on account for 2015/16 will be based on the tax payable by self assessment and the class 4 (NIC) liability in 2014/15

Due dates:

31/1/2016 13,000/2 = £6,500
31/7/2016 13,000/2 = £6,500

The Balancing payment for 2015/16 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 31/1/2017	3,200

The payments on Account for 2016/17 will be based on the income tax payable by self assessment and class 4 NIC liability in 2015/16

31/1/2017 (12,000 + 2,500)/2 = 7,250
31/7/2017 = 7,250

Total payment to be made on 31 January 2017 is 10,450 (3,200 + 7,250)

Chapter 16

Answer to Example 1

Corporation tax computation for the chargeable accounting period of 12 months ended 31 March 2016

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: Qualifying charitable donations		(10,000)
Taxable Total Profits		1,516,500

Note: Dividends from other companies (UK or overseas) are exempt and therefore are ignored when calculating Taxable Total Profits

Chapter 17

Answer to Example 1

	12 months to 31/3/2016	*3 months to 30/6/2016*
	£	£
Adjusted profit (12 : 3)	3,200,000	800,000
Less: CA (W1)	(68,000)	(126,238)
Tax adjusted trading profit	3,132,000	673,762
Chargeable Gain (6/5/2016)	–	80,000
Qualifying charitable donations (31/7/2015)	(20,000)	–
Taxable Total Profits	3,112,000	753,762
Corporation Tax @ 20%	£622,400	£150,752

(W1) *12 months to 31/3/2016*

		Main pool	*Allowances*
WDV b/f		nil	
Additions qualifying for AIA - Vans	68,000		
	(68,000)		68.000
3 months to 30/6/2016			
WDV b/f		nil	
Additions qualifying for AIA			
Plant & Machinery	152,500		
AIA - (Maximum 500,000 × 3/12)	(125,000)		125,000
		27,500	
		27,500	
WDA × 18% × 3/12		(1,238)	1,238
			126,238
WDV c/f		26,262	

Chapter 18

Answer to Example 1

Current year relief

	y/e 31/3/16
	£
Trading profit	–
Interest receivable	20,000
Chargeable gain	50,000
	70,000
Current year relief	(45,000)
	25,000
Qualifying charitable donations	(15,000)
Taxable Total Profits	10,000

Answer to Example 2

	y/e 31/3/14	*y/e 31/3/15*	*y/e 31/3/16*
	£	*£*	*£*
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)
Carry back relief		(70,000) (ii)	
Taxable Total Profits	40,000	–	–

Loss memorandum

Loss arising		
y/e 31/3/16		90,000
Current year relief	y/e 31/3/16	(10,000) (i)
Carry back relief	y/e 31/3/15	(70,000) (ii)
Available to carry forward		10,000

Answer to Example 3

	y/e 31/3/14	9m to 31/12/2014	y/e 31/12/2015
	£	£	£
Trading profit	25,000	20,000	–
Interest Income	3,000	1,000	1,000
Chargeable Gain	– (W1)	5,000 (W1)	–
Total profit before Qualifying charitable donations	28,000	26,000	1,000
Current year relief			(1,000)
Carry back relief (3/12 x 28,000)	(7,000)	(26,000)	
	21,000	–	–
Less Qualifying charitable donations	(500)	(500)(w2)	(500)(w2)
Taxable Total Profits	20,500	–	–

W1 The capital loss of £1000 is c/f to set off against the £6000 gain of next CAP
W2 Qualifying charitable donations are unrelieved
Loss memorandum

Trading loss	
y/e 31/12/2015	40,000
Current year 31/12/2015	(1,000)
	39,000
Carry back to 9m to 31/12/2014 & 3m of y/e 31/3/14 (26,000 + 7,000)	(33,000)
Available to carry forward	6,000

Answer to Example 4

	y/e 30/9/12	6 months 31/3/13	y/e 31/3/14	y/e 31/3/15	y/e 31/3/16
	£	£	£	£	£
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)	–
Qualifying charitable donations	(500)	–	–	–	–
Taxable Total Profits	5,500	–	–	–	–
Qualifying charitable donations unrelieved			500	500	–

Loss memorandum		£
Loss arising y/e 31/3/2016		97,000
Current year relief	y/e 31/3/2016	(10,000)
Carry back relief	y/e 31/3/2015	(34,000)
Carry back relief	y/e 31/3/2014	(28,000)
Carry back relief	6m to 31/3/2013	(16,000)
Carry back relief	y/e 30/9/2012 £12,000 × 6/12 = £6,000 maximum set off	(6,000)
Loss unrelieved		3,000

Answer to Example 5

		y/e 31/03/12		y/e 31/03/13		y/e 31/3/14		y/e 31/3/15
				£		£		£
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)		
Carry back relief			(ii)	(26,000)				
		47,000		–		–		17,000
Less Qualifying charitable donations		(1,000)		–		–		(1,000)
Taxable Total Profits		46,000		–		–		16,000
Unrelieved Qualifying charitable donations				1,000		1,000		

Loss memo			£
Loss arising y/e 31/3/14			43,000
Current year relief	31/3/14	(i)	(8,000)
			35,000
Carry back relief	31/3/13	(ii)	(26,000)
			9,000
Carry forward y/e 31/3/15		(iii)	(9,000)
			–

Chapter 19

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	$20{,}000 \times \frac{259.5 - 97.85}{97.85}$	(1.652)	33,040	
On enhancement	$6{,}000 \times \frac{259.5 - 128.1}{128.1}$	(1.026)	6,156	
				(39,196)
Chargeable gain				33,804

Answer to Example 2

1) Same day X
2) Previous 9 days 500 shares

		£
Proceeds	$\frac{500}{3,000}$ x 36,000	6,000
Less cost		(5,000)
Chargeable gain		1,000

3) Share pool

Share Pool		*Number*	*Cost*	*Indexed cost*
		£	£	£
20 August 1989		1,000	5,000	5,000
Index up to November 1996	$\frac{153.9 - 115.8}{115.8}$ x 5,000			1,645
		1,000	5,000	6,645
Addition 16 November 1996		2,000	12,000	12,000
		3,000	17,000	18,645
Index up to October 2015	$\frac{259.5 - 153.9}{153.9}$ x 18,645			12,793
		3,000	17,000	31,438
Disposal 10 October 2015	2500/3000 x 17,000: 2500/3000 x 31438	(2,500)	(14,167)	(26,198)
		500	2,833	5,240

Note: when reindexing the indexed cost in the share pool we do not round the indexation factor to 3 decimal places. However in the examination the examiner may simply give you indexation factors from one relevant date to another for ease of calculation, in which case use the given indexation factors where applicable.

Calculate the gain on the 2,500 shares

		£
Proceeds	$\frac{2,500}{3,000}$ x 36,000	30,000
Cost		(14,167)
Unindexed gain		15,833
I.A (26,198 – 14,167)		(12,031)
Chargeable gain		3,802

Total Gains	*Gains*
Previous 9 days	1,000
Pool	3,802
Chargeable Gains to include in the corporation tax computation	4,802

Answer to Example 3

Matching rules

Same day	×
Previous 9 days	×
Share pool	✓

Share pool	Number	Cost	Indexed cost
	£	£	£
July 1993	3,000	10,000	10,000
February 1995 Bonus 1:3	1,000	–	–
No reindexation of pool (though examiner will still give the RPI for that date - ignore!)	4,000	10,000	10,000
Index up to October 2015 from July 1993 $\frac{259.5 - 140.7}{140.7} \times 10{,}000$			8,443
	4,000	10,000	18,443
Sale	(2,000)	(5,000)	(9,221)
	2,000	5,000	9,222

Calculate the Gain

	£
Proceeds	12,000
Less Cost	(5,000)
Unindexed Gain	7,000
Less Indexation allowance (9,221 – 5,000)	(4,221)
Chargeable gain	2,779

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

As the terms of the takeover are a share for share transfer no gain will arise at the the time of the takeover with the new shares in B plc taking on the same original cost as the old shares in A Ltd. As 2 types of share are issued at takeover we use the market values of those shares as the basis of dividing the A Ltd share cost, hence the ordinary shares take 30/40 and the preference shares take 10/40 of the £10,000 share cost.

Calculate Gain on sale of preference shares in October 2015:

	£
Proceeds	15,000
Cost	(2,500)
Less: indexation allowance 1.247 × 2,500	(3,117)
Chargeable gain	9,383

The cost of B plc ordinary shares when they are sold will be £7,500. If the examiner gives you an indexation factor rather than the RPI's to use then just apply as in a normal indexation allowance calculation.

Answer to Example 5

As Z Ltd now receives some cash at the time of the takeover an immediate gain will arise thereon as computed below.

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 2015:

	£
Proceeds	10,000
Less Cost	(2,500)
Indexation allowance (1.239 × £2,500)	(3,097)
Chargeable gain	4,403

Chapter 20

Answer to Example 1

		£
Proceeds		16,000
Less: Cost	$26{,}000 \times \dfrac{16{,}000}{16{,}000 + 34{,}000}$	(8,320)
Unindexed gain		7,680
Less: I.A	$\dfrac{259.5 - 220.7}{220.7} = 0.176 \times 8{,}320$	(1,464)
Chargeable gain		6,216

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	$\dfrac{259.5 - 217.9}{217.9}$ = 0.191 x 2.000	(382)
Gain		7,618

Restricted to 5/3 [10,000 – 6,000] = **£6,667**

(c) Antique vase – non wasting chattel

	£
Disposal proceeds (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 12/30 × [25,000 – 1,000]	(9,600)	
		(15,400)
Unindexed gain		22,600
Less indexation allowance 0.486 × 15,400		(7,484)
Chargeable gain		15,116

Answer to Example 4

		£
Proceeds (July 2015)		30,000
Less Acquisition cost	$10{,}000 \times \frac{30{,}000}{30{,}000 + 25{,}000}$	(5,455)
Unindexed gain		24,545
Less indexation allowance 0.505 × 5,455		(2,755)
Chargeable gain		21,790

Answer to Example 5

On 1 July 2015 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: I.A	$\frac{259.5 - 216.8}{216.8} = 0.197 \times 23{,}000$	(4,531)
Chargeable gain		6,469
Less gain rolled over		(2.469)
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 £2,469 (£6.469 – £4,000) can be deferred.

Base cost of the replacement asset

Cost	30,000
Less Gain Deferred	(2,469)
Base cost	27,531

Chapter 21

Answer to Example 1

		£
Proceeds		400,000
Less Cost		(150,000)
Unindexed Gain		250,000
Less: I.A	$\frac{259.5 - 145.2}{145.2} = 0.787 \times 150{,}000$	(118,050)
Chargeable gain		131,950

Proceeds are fully reinvested into a qualifying asset within the specified time period, so the entire gain of £131,950 can be deferred until the sale of the land.

Base cost of the land

Cost	500,000
Less Gain deferred	(131.950)
Base cost	368,050

Answer to Example 2

		£
Proceeds		350,000
Cost		(200,000)
		150,000
Less: I.A	$\frac{259.5 - 181.5}{181.5} = 0.430 \times 200{,}000$	(86,000)
Chargeable gain		64,000

Proceeds not reinvested = 350,000 – 335,000 = £15,000
.£15,000 will be taxed in y/e 31/12/2015
The remaining gain £49,000 (64,000 – 15,000) can be deferred

Base cost of new asset:

Cost	335,000
Gain deferred	(49,000)
	286,000

Answer to Example 3

		£
Proceeds		350,000
Cost		(200,000)
		150,000
I.A	$\frac{212.8 - 156.3}{156.3} = 0.361 \times 200{,}000$	(72,200)
		77,800

The gain is deferred due to the purchase of the fixed plant and will be chargeable in year ended 31 March 2016, when the depreciating asset is sold/ceases to be used in the trade (Feb 2016). This is earlier than 10 years from its date of acquisition (March 2021).

Chapter 22

Answer to Example 1

A Ltd has three wholly owned subsidiaries and thus there are four related 51% group companies, meaning that each group member will have a revised profit limit of £375,000 (£1.5M / 4).
A Ltd with a TTP of £400,000 will therefore be a large company and if it was large in the previous CAP should have made quarterly instalment payments for this period and will be required to make quarterly instalment payments for the next CAP if its estimated profits for that period will exceed £375,000.

Answer to Example 2

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 that where sub - subsidiaries (indirect subsidiaries) exist there will be more than one group for purposes of group relief.

Answer to Example 3

(1) Group relief to B Ltd will be restricted to 6/12ths of Z plc's trading loss for the year ended 31 March 2016.
(2) The set–off will be against B Ltd's Taxable Total Profits for the six–month period to 31 March 2016.

Answer to Example 4

Both Beyonce Ltd and Z Ltd prepare accounts to 31 March but as Z Ltd only commenced trading on 1 January, 2016 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 2015, hence maximum group relief in this period is lower of:
3/12 × (240,000) = (60,000)

3/12 × 160,000 = 40,000
Maximum group relief is therefore£40,000.

9 months of Beyonce's loss corresponds with 9 months of J's profit for the year ended 30 June 2016, hence group relief in this period is restricted to lower of:
9/12 × (240,000) = 180,000
9/12 × 280,000 = 210,000
Maximum group relief is therefore £180,000

Answer to Example 5

An election may be made, the matching election, to deem any part of a gain or loss made by one gains group member to have been made by any other gains group member. This will allow gains and losses to be set off within the group rather than carrying forward an unused capital loss in one group company while being taxed on a gain in another group company. Initially therefore it would appear that electing to either deem the loss made by Large Ltd to have been made by Smaller Ltd, or deeming £35,000 of Smaller Ltd's gain to have been made by Large Ltd would have the same effect of matching the gains with the losses and either approach may be proposed, but there is a further issue to be identified that will suggest that it would be preferable to transfer any amount of the gain in excess of £50,000 from Smaller Ltd to Large Ltd. Both companies are large companies which notwithstanding their size in the previous chargeable accounting period (CAP) will mean that they will both be required to make quarterly instalment payments in relation to the next CAP if they are both estimating large profits for that period.. This will result in an adverse cash flow position for both group companies. They are large companies as their profits are above the profits threshold of £750,000 (£1.5M divided between two 51% related group companies)
It would be beneficial therefore to transfer any amount of the gain in excess of £50,000 from Smaller Ltd to Large Ltd which will bring Smaller Ltd's profits down from £800,000 to below £750,000 and will therefore remove the requirement for Smaller Ltd to make quarterly instalment payments for the next CAP. This result would not be achieved if the loss was transferred to Smaller Ltd as this would still leave Smaller Ltd with profits in excess of £750,000.

Chapter 23

Answer to Example 1

Photo Plc
Corporation tax liability
=
£2M x 20% = 400,000

All payable by instalments
This will be paid as follows:

£100,000	on	14 July 2015
£100,000	on	14 October 2015
£100,000	on	14 January 2016
£100,000	on	14 April 2016

In reality of course as the payments are based on an estimate of the current year's liability and the first payment is made in only the 7th month of the accounting period the amounts paid are likely to change at each payment date as that estimate is updated.

Chapter 24

Answer to Example 1

Chargeable Transfers	*20/11/09*	*15/7/10*	*8/12/2014*
	PET	*CLT*	*PET*
Transfer of value	40,000	405,000	184,000 (W1)
Less: Exemptions			
Marriage	(5,000)		
AE 2009/10	(3,000)		
AE 2008/09	(3,000)		
AE 2010/11		(3,000)	
AE 2014/15			(3,000)
AE 2013/14			(3,000)
	29,000	402,000	178,000

ANSWERS TO EXAMPLES

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
15/7/10	CLT		402,000	421,250	19,250
	325,000 @ nil	= nil			
	77,000 @ 25%	= 19,250			
	402,000				

Lifetime Transfers Chargeable on Death – April 1, 2016

			Gross Transfers	IHT
20/11/09 PET			29,000	nil
15/7/10 CLT			421,250	50,100
	Available nil rate band (325,000 - 29,000) = 296,000			
	296,000 @ nil	= nil	450,250	
	125,250 @ 40%	= 50,100		
	421,250			
Less:	Taper Relief (60%) (5-6 years)			(30,060)
				20,040
Less:	Lifetime tax paid			(19,250)
Additional tax due on death				790
8/12/2014PET			178,000	71,200
	178,000 @ 40%	=71,200	628,250	

Chargeable Estate at Death – April 1, 2016.

	£	£
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		628,250
Nil Rate Band fully used therefore entire estate taxed @ 40%		
£758,000 @ 40%		£303,200

Answer to Example 2

The gift on 1 October 2003 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 03/04 and 02/03.

Answer to Example 3

The gift on 1 June 2004 is a CLT and was chargeable when made but not on death as again Dee survived for 7 years.
The gift on 1 September 2010 is a PET and will be chargeable on death as Dee died within the next 7 years.

Step 1 Compute the Chargeable Transfers

	1/6/04	*1/9/10*
	CLT	*PET*
Transfer of value	278,000	296,000
Less: Exemptions		
AE 04/05	(3,000)	
AE 10/11		(3,000)
AE 09/10		(3,000)
Chargeable Transfer	275,000	290,000

AE 03/04 will have been applied to the 1 October 2003 PET despite it never becoming chargeable.

Step 2 Lifetime Transfers Chargeable When Made

	£	*Gross Transfers*	*IHT*
1/6/04 CLT	275,000	278,000	3,000
263,000 @ 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 1/9/10. However in computing any IHT payable on this transfer 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 < 1/9/10	278,000	
1/9/10 PET	290,000	97,200
Available nil rate band = 325,000 – 278,000	568,000	
= 47,000 @ nil = nil		
243,000 @ 40% = 97,200		
290,000		
Less: Taper Relief ((5-6 years) 60%)		(58,320)
		38,880

Although the CLT of 1 June 2004 has drastically affected the tax payable on the PET of 1 September 2010 it will only be relevant for transfers within the following 7 years hence any transfer after that date (1 June 2011), 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 September 2010 in determining any available nil rate band.

If the taxpayer had taken advice before making the PET in September 2010 she may have delayed the gift until after 1 June 2011 such that then if the PET were to become chargeable as a result of her death the CLT of 1 June 2003 would not then be taken into account in computing the IHT on the PET and no IHT would then be payable upon it as it would be entirely within the available nil rate band at the date of death.

Step 4 Chargeable Estate at Death – 1 March 2016

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 £82,000.

The taxable supplies for the first 12 months of trading to 31 May 2016 amount to only 64,400 so we now move forward adding in the next month, June 2016 and removing the sales of what is now 13 months ago, June 2015, as this revised 12 month total is only 72,300 compulsory registration is still not required. When we move forward to the end of July 2016, however taxable supplies will amount to £83,000 (4,300 + 5,100 + 4,700 + 4,700 + 4,900 + 4,800 + 6,000 + 6,100 + 7,900 + 8,200 +11,800 + 14,500).

(b) Orchid Ltd will have to notify HMRC by 30 August 2016, being 30 days after the end of the period.

(c) The company will be registered from 1 September 2016 or from an agreed earlier date.

Answer to Example 2

A business must register for VAT if there are reasonable grounds for believing that taxable supplies will exceed £82,000 in the following 30 days.

Forecast income is £90,000 per month, and so taxable supplies for the 30-day period to 30 April 2016 will exceed £82,000.

Tulip Ltd will have to notify HMRC by 30 April 2016, being the end of the 30-day period, and will be registered from 1 April 2016.

Answer to Example 3

Prior to putting up its prices, Vine Ltd's net profit is £73,200 (£78,000 - £4,800).

If Vine Ltd puts up its prices, then it will exceed the VAT registration limit of £82,000, and the business 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 (84,000 × 100/120)	70,000
Expenses (4,800 × 100/120)	(4,000)
Net profit	66,000

This is a decrease in net profit of £7,200 (73,200 – 66,000), and so it is not beneficial for Vine Ltd to put up its prices.

Answer to Example 4

VAT Return - Quarter ended 31 March 2016

	£	£
Output VAT		
Sales (60,000 x 95% (100% - 5%) x 20%)		11,400
(60,000 x 20%)		12,000
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	
		10,937
VAT payable		12,463
Due date (see Section 5 of chapter)		7/05/16

Notes:

(1) The calculation of output VAT will only take into account the discount for prompt payment if customers do take it.

(2) Input VAT on UK customer entertaining cannot be reclaimed If they had been overseas customers the input tax would be recoverable..

(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.

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 2014 will have resulted in HMRC issuing a surcharge liability notice specifying a surcharge period running to 30 September 2015.

The late payment of VAT for the quarter ended 31 December 2014 will result in a surcharge of £426 (£21,300 × 2%).

The surcharge period will have been extended to 31 December 2015.

Bluebell Ltd then submitted four VAT returns on time.

The late submission of the VAT return for the quarter ended 31 March 2016 will therefore only result in a surcharge liability notice (specifying a surcharge period running to 31 March 2017).

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 2016. 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 on the VAT Return.

(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 2016. 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 2016

	£
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)

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 2015/16:

	£
Trading profit	36,535
Employment Income	8,000
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 2015/16.

3 Jessica

Jessica had the following income and outgoings for 2015/16

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 2015/16

4 Karl

Karl has the following income and outgoings for 2015/16

	£
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 2015/16

5 Mr & Mrs Elderely

Mr Elderely receives Property Income of £35,000 in the tax year 2015/16
His wife Mrs Elderely earns no income in 2015/16.

Calculate Mr Elderely's income tax liability assuming any beneficial elections are made and recommend what course of action you would advise the couple to take to reduce this liability.

6 Michael

Michael received employment income of £116,000 and paid a personal pension contribution of £8,000 in 2015/16

Calculate his income tax liability

7 Peter

Peter acquired two properties on 1 June 2015 that were first let on 1 July 2015.
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 2016.

		£
20 June 2015	Repairs to roof following a violent storm on 15 June 2015	1,600
29 June 2015	Insurance for y/e 31/5/16	420
01 February 2016	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 31 March 2016, and this was not received until 15 April 2016. Peter incurred the following expenditure in respect of this property during the period to 5 April 2016.

		£
4 June 2015	Letting expenses paid to agent	40
29 June 2015	Insurance for y/e 31/5/16	585

You are required to calculate Peter's Property Income for the tax year 2015/16.

8 Matthew

Matthew owns three cottages that are let out. For the tax year 2015/16 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 2015/16 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 2015/16, 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 2014/15.

Advise 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 statement of profit or loss for the year ended 31 December 2015 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 2015 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 2015.

You should indicate by the use of zero any items in the statement of profit or loss for which no adjustment is required.

11 Carl

Carl prepares accounts to 5 April.
The written down value on the main pool as at 6 April 2015 was £23,500.
In the two years ended 5 April 2017 the following transactions took place.

Year ended 5 April 2016

1 Nov 2015	Purchased machinery costing £476,000.
10 Nov 2015	Sold two lorries (purchased for £8,450 each) for £2,500 each. Purchased two replacement lorries for £15,250 each.
1 Dec 2015	Purchased a motor car with CO_2 emissions of 170 g/km for £16,600 for use by the sales manager.

Year ended 5 April 2017

1 July 2016	Purchased thermal insulation for a business building of £120,000
1 Nov 2016	Purchased a motor car with CO_2 emissions of 120 g/km for £7,500.
1 Dec 2016	Sold the motor car purchased on 1 December 2015 for £12,000.

Calculate the capital allowances available to Carl for the years ended 5 April 2016 and 5 April 2017.

12 Jason

Jason commenced trading on 1 July 2014 drawing up accounts to 31 May each year.
Trading profit for each accounting period is as follows:

	£
1 July 2014 to 31 May 2015	33,000
Year ended 31 May 2016	24,000
Year ended 31 May 2017	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 2010 and ceased trading on 31 October 2015. His accounts shows the following trading income.

	£
P/e 30 April 2011	30,000
Y/e 30 April 2012	10,000
Y/e 30 April 2013	12,000
Y/e 30 April 2014	15,000
Y/e 30 April 2015	18,000
P/e 31 October 2015	7,000

Calculate the trading profit assessments for all relevant tax years.

14 Grace

Grace starts a trade on 1 May 2015, and has the following results (before capital allowances).

Period of account	*Profit*
	£
1 May 2015 – 31 July 2016	128,360
1 August 2016 – 31 July 2017	88,013
1 August 2017 – 31 July 2018	75,727

Plant is bought as follows:

Date	*Cost*
	£
1 May 2015 Plant	69,500
1 Dec 2015 Car (115g /km)	21,600
1 Oct 2016 Machinery	40,000
1 Feb 2018 Plant	25,000

On 1 May 2018, the car purchased on 1 December 2015 was sold for £13,000.

Calculate the trading profit assessments for the opening tax years as far as the available information permits, assuming maximum capital allowances are claimed.

Assume that the capital allowance rates applicable to the 15/16 tax year apply throughout.

15 David

David traded for many years preparing accounts to 5 April when he ceased trading at 30 June 2017. Trading profits (before capital allowances) have been as follows:

Year ended	£
5 April 2016	25,000
5 April 2017	27,000
Period to 30 June 2017	14,000

Expenditure on plant had been as follows:

	£
Date	*Cost*
1 June 2015	2,800
1 October 2016	4,600

All items of plant were sold on 30 June 2017 for £4,000 (no item was sold for more than cost).
The written down value of the main pool as at 6 April 2015 was £14,800.
Overlap profit from commencement was £2,000

Calculate the trading profit assessments for the last three tax years of assessments.

Assume that the capital allowance rates applicable to the 2015/16 tax year apply throughout

16 Max

Max began trading on 1 January 2015. He prepares accounts to 31 December annually, with results as follows:

	Trading profit
	£
Year ended 31 December 2015 Loss	(12,000)
Year ended 31 December 2016 Loss (estimated)	(4,000)
Year ended 31 December 2017 Profit (estimated)	8,000
Year ended 31 December 2018 Profit (estimated)	11,500

Prior to commencing self-employment, Max had the following income from employment:

2011/12	19,200
2012/13	23,800
2013/14	20,100
2014/15	11,400

(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 years 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 2012	£60,000
y/e 31 Dec 2013	£30,000
y/e 31 Dec 2014	£40,000
y/e 31 Dec 2015	(£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. Assume the 2015/16 personal allowance applies in all years

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 2015 Betty resigned as a partner, and was replaced on 1 July 2015 by Chloe. The profits were then split in the ratio of 2:1 between Anne and Chloe. The partnership's trading profit is as follows:

	£
Year ended 31 December 2015	60,000
Year ended 31 December 2016	72,000

As at 6 April 2015 Anne and Betty each have unrelieved overlap profits of £3,000.

Calculate the trading profit assessments of Anne, Betty and Chloe for 2015/16 and 2016/17.

(c) Daniel and Elvis have been in partnership since 6 April 1995, making up accounts to 5 April. On 31 December 2015 Elvis resigned as a partner, and was replaced on 1 January 2016 by Frank. For 2015/16 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 2015/16.

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	*2015*	*2016*
	£	*£*
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 2015/16.

(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 2010 (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 fully subsidised canteen was available for the other staff.

(4) When at the company premises Renner has use of a 3,500 cc Range Rover car owned by the company which emits 268 g/km of CO_2 . It had a list price of £62,000 when new in 2010 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 for business purposes.

Renner is also provided with a three year old 2 litre Mini (list price £16,500) 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 2% 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 2013. The market value of the equipment when it was first provided to Renner on the 6 April 2015 was £2,010.

(8) From 6 June 2015 he lived in Southampton in a house owned by the company which cost £80,000 in 1995. Its market value on 6 June 2015 was £138,000. The annual value for the period from 6 June 2015 to 5 April 2016 can be taken as £900. The company paid the following expenses in connection with the house during his period of residence in 2015/16.

	£
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 2015.

Compute Renner's income tax liability for 2015/16
Assume the official rate of interest for 2015/16 is 3.25%.

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 2013:

2013/14	£28,000
2014/15	£23,000

During 2015/16 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 2016/17.

(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 2014/15 when his gross contributions were only £20,000. In 2015/16 Osbourne has made gross pension contributions of £90,000.

Compute Osbourne's Income Tax liability for 2015/16.

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 2016 was £18,479.
(2) Tony employed Jack and Jill during 2015/16. Their gross wages were £18,200 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 2015/16.

(d) The Class 2 and Class 4 NICs payable by Tony for 2015/16.

22 Chorley Ltd

You are presented with the accounts of Chorley Ltd for the year to 31 December 2015 (see below). Chorley Ltd runs a small printing business and the managing director wishes to know the amount of the companies' Adjusted trading profit for the year ended 31 December 2015.

	£	£
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 trading profit for year ended 31 December 2015.

You should indicate by the use of zero any items in the accounts for which no adjustment is required

23 Sail Ltd

Sail Ltd has the following results for the year ended 31 March 2016. 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
Qualifying charitable donations	22,000

Calculate the amount of corporation tax payable by Sail Ltd for the year ended 31 March 2016 and state the due date for payment.

24 Swish Ltd

Swish Ltd has the following results for the year ended 31 March 2016

	£
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 main pool at 1 April 2015 was £20,000. There were no purchases or sales during the year ended 31 March 2016.

(4) Swish Ltd has the following results for the previous year:

	31/3/15
Trading profit	40,000
Interest receivable	2,000
Chargeable gain	–
	42,000

(a) To compute the trading loss for the year ended 31 March 2016.

(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 October 2015 Trunk Limited acquired a further 1,000 shares in Branch Limited costing £15,000 and on 20th October 2015 sold 2,500 shares in Branch Limited for £40,000

Calculate the chargeable gain arising on the sale of the Branch Limited shares in October 2015

RPI's to be used are

July 1994	144.0
February 1996	150.9
September 1998	164.4
October 1998	164.5
October 2015	259.5

26 Granger Limited

Granger Limited bought a piece of land in January 1991 for £5,000. In December 2015 the company sold part of the land for £4,500 at which time the remaining part was valued at £20,500.
In addition the company sold some antique furniture for £5,000 in September 2015. It had originally purchased the furniture in August 1996 for £8,000.
It also sold a painting for £6,600 in October 2015. 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
September 2015	259.6
October 2015	259.5
December 2015	260.6

27 Westcroft Limited

Westcroft Ltd purchased a painting in February 2010 for £100,000. In September 2015 it was stolen and never recovered. In December 2015 the company received insurance proceeds of £500,000 and immediately acquired a replacement painting for £450,000.

Calculate the chargeable gain arising in December 2015 and the base cost of the replacement painting.

RPI's to be used

February 2010	211.4
September 2015	259.6
December 2015	260.6

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 2015/16 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 2013 and were sold during September 2015.

Calculate the CGT in 2015/16 assuming his taxable income is £50,000

30 Cheryl

Cheryl disposed of various assets in 2015/16 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 2015/16 and state the due date for payment

31 Shamus

Shamus acquired a property in October 2014 for £124,000. This was damaged by flooding in December 2015. In January 2016 the insurance company made a payment of £50,000. In February 2016 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 2016 and the base cost of the property on a future disposal. Recompute these figures assuming that no election was made.

32 Zoe

Zoe acquired 1,500 shares in XYZ Ltd on 30 April 2015 for £18,000, and 500 shares on 31 May 2015 for £7,000.
On 10 February 2016 Zoe bought a further 200 shares in the company for £3,600.

Zoe sold 1,000 shares in XYZ Ltd on 31 January 2016 for £20,000.

Calculate Zoe's capital gain on the disposal of the shares

33 Michael

Michael had the following transactions in the shares of Saint Ltd:

January 2015	Purchased 2,700 shares for £5,400
May 2015	Purchased 600 shares for £1,500
June 2015	Took up 1 for 3 rights issue at £2.30 per share
August 2015	Sold 4,000 shares for £14,000

Calculate the capital gain on the disposal in August 2015.

34 Jenny

Jenny disposed of her entire business in October 2015 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 2015 of £15,000 and her taxable income for 2015/16 was £30,000.

Calculate Jenny's Capital Gains Tax for 2015/16 and state the due date for payment.

35 Beth

Beth bought a factory in September 1998 for £635,000. In December 2015, wishing to move to a more convenient location, she sold the factory for £750,000. She moved into a rented factory until March 2016 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 1999 for £40,000. In January 2016 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 of the shares for Wendy's grandson?

37 Amy

Amy bought a house on 1 April 1985 and occupied as follows:

1/4/1985	–	1/4/1986	lived in it
1/4/1986	–	30/9/1990	travels the world and lets the house
1/10/1990	–	1/4/1994	lived in it
1/4/1994	–	1/5/2015	house empty

Amy sold the house on 1 May 2015 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

38 Nathan

(a) Nathan made the following lifetime gifts:

(1)	23 October 2005	– A gift of £356,000 into a trust
(2)	17 September 2009	– A gift of £47,000 to his nephew on the occasion of his marriage
(3)	14 February 2011	– A gift to his civil partner of £100,000
(4)	26 August 2012	– A gift of £276,000 to a trust.

Calculate the IHT payable on the lifetime transfers assuming that Nathan pays any IHT due on the first transfer into trust and the trustees pay any IHT due on the second transfer into trust. Clearly state who is responsible for paying the tax and the due date for payment.

The nil rate bands are as follows

2005/06	275,000
2009/10	325,000
2010/11	325,000
2012/13	325,000

(b) Nathan died on 30 November 2015 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 from which the proceeds received were £105,000

Nathan had credit card debts of £2,500 and 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

39 VAT

(a) Kite Ltd started trading on 1 December 2015, and its forecast turnover is as follows:

	£
One month ended 31 December 2015	27,000
Quarter ended 31 March 2016	84,000
Quarter ended 30 June 2016	68,000
Quarter ended 30 September 2016	81,000

Assume that the quarterly sales figures accrue evenly within the period.

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 2015:

(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 2015 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 2015 respectively.
(4) On 30 December 2015 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 2015.

40 Geewizz Ltd

Geewizz Ltd commenced trading as a manufacturer of children's toys on 1 April 2015 and immediately registered for VAT. The company is in the process of completing its VAT return for the quarter ended 31 March 2016.

All of Geewizz Ltd's sales are standard rated. It has recently been suffering some debt collection problems with a number of slow paying customers and 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 2015, 26 October 2015 and 25 January 2016 respectively. The VAT payable in respect of the second and third returns was not paid until 11 November 2015 and 5 March 2016 respectively.

(a) **Explain the implications if the VAT return and the VAT payable for the quarter ended 31 March 2016 are not submitted to HMRC until 20 May 2016.**

(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.**

41 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.

42 Groups

Explain the circumstances in which companies may enter into a group VAT registration and state the advantages and disadvantages of joining a group VAT registration

43 Jim

Jim is required to make payments on account. His income tax payable by self assessment for 2014/15 was £5,100.
His income tax payable by self assessment in 2015/16 is £7,629, and he has a capital gains tax liability for the year of £1,000.

State the due dates for payments for tax year 2015/16 and the amount of payment due on each due date.

44 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.**

45 Cannock Limited

Cannock limited is a large company and has Taxable Total Profits in year ended 31 January 2016 of £2,400,000.

Calculate the corporation tax liability of Cannock Limited for the accounting period ended 31 January 2016 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 2015/16

	Non savings	*Savings*	*Dividends*	*Total*
	£	*£*	*£*	*£*
Trading profit	36,535			36,535
Employment Income	8,000			8,000
Interest 2,800 × $^{100}/_{80}$		3,500		3,500
Dividends 1,800 × $^{100}/_{90}$			2,000	2,000
Total Income	44,535	3,500	2,000	50,035
Less: Reliefs - Qualifying Interest	(1,000)			(1,000)
Net Income	43,535	3,500	2,000	49,035
Less: Personal Allowance	(10,600)			(10,600)
Taxable income	32,935	3,500	2,000	38,435

Tax calculation		
Non Savings:		
(W1)	32,935× 20% =	6,587
Savings [34,285 – 32,935 = 1,350]		
	1,350 @ 20% =	270
-	2,150 @ 40% =	860
Dividends	2,000 @32.5% =	650
	38,435	
Income Tax liability		8,367
Less: tax deducted at source		
Dividends (2,000 × 10%) =		(200)
Savings (3,500 × 20%) =		(700)
PAYE		(505)
Tax payable		6,962

(W1) The basic rate band is extended by the gross amount of the gift aid payment
31,785 + (2,000 × $^{100}/_{80}$) = 34,285

Note: The starting rate for savings income is not available as non savings taxable income exceeds £5,000

3 Jessica

Jessica Income tax computation 2015/16

		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)		(6,600)		(6,600)
Taxable income		83,400	20,000	103,400
Tax calculation				
Non savings				
(W2)	33,785 × 20% =	6,757		
	49,615 × 40% =	19,846		
	83,400			
Savings	20,000 x 40% =	8,000		
	103,400			
Income tax liability		34,603		
Less tax deducted at source				
Bank interest 20,000 × 20% =		(4,000)		
Income tax payable		30,603		

(W1)	Total income = Net Income	110,000
	Less Gift aid payment 1,600 × 100/80 =	(2,000)
	Adjusted net income	108,000
	Personal allowance	10,600
	Less	
	½ × (108,000 – 100,000) =	(4,000)
	Revised personal allowance	6,600

(W2) 31,785 + 2,000 = 33,785
150,000 + 2,000 = 152,000
Note: The starting rate for savings income is not available as non savings taxable income exceeds £5,000.

4 Karl

Karl Income tax computation 2015/16

		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)		*£*		
	35,785 × 20% =	7,157		
	101,215 × 40% =	40,486		
	137,000			

Dividends

(154,000 – 137,000 = 17,000)

	17,000 × 32.5% =	5,525
	13,000 × 37.5% =	4,875
	167,000	
Income tax liability		58,043
Less tax deducted of source		
Dividends 30,000 × 10% =		(3,000)
PAYE		(48,520)
Income tax payable		6,523

(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 £121,200 the personal allowance is reduced to nil.

(W2) Basic rate band £31,785 + £4,000 = £35,785
Additional rate band £150,000 + £4,000 = £154,000

5 Mr & Mrs Elderely

Mr Elderly Income tax Computation 2015/16

	Non savings	*Total*
	£	*£*
Property Income	35,000	35,000
Total Income	35,000	35,000
Less: Personal Allowance	(10,600)	(10,600)
Taxable income	24,400	24,400

Tax calculation	
24,400 @ 20% =	4,880
Less: Marriage allowance (1,060 x 20%) (note 1)	(212)
Tax liability	£4,668

note 1

As Mrs Elderely is not using at least 10% of her personal allowance and Mr Elderely is only a basic rate taxpayer an election should be made to transfer 10% of her personal allowance to him which will result in a tax saving on his computation of £212.

The election must be made within 4 years of the end of the tax year, hence by 5 April 2020 and will only apply to the 2015/16 tax year.

If the election is then made during the 2016/17 tax year it will remain in force until it is withdrawn or the conditions do not apply. This should not however be necessary if the following tax advice is taken by the Elderely's.

As 90% of Mrs Elderely's personal allowance is being wasted it would be advised that the property should be put into joint ownership and as such the income from a jointly owned asset will be split 50:50 between the spouses allowing Mrs Elderely to use all of her personal allowance and thus remove a significant amount of the property income from tax,

If this advice is followed then based on the 2015/16 figures a tax saving of £1,841 would be achieved (see below).

Revised calculations

	Mr Elderely		*Mrs Elderely*
Property Income	17,500		17,500
Total Income	17,500		17,500
Less: Personal Allowance	(10,600)		(10,600)
Taxable income	6,900		6,900
Tax calculation			
6,900 @ 20%	1,380	6,900 @ 20%	1,380
Tax liability	1,380		1,380

Combined liability	£2,760
Original liability	£4,668
Tax Saving	£1,841

6 Michael

Michael Income tax computation 2015/16

	Non savings
Employment income	116,000
Total income	116,000
Less personal allowance (W1)	(7,600)
Taxable income	108,400
Tax calculation	£
Non savings	
41,785 (W2) × 20%	8,357
66,615 × 40%	26,646
108,400	
Income tax liability	35,003

(W1)

Net Income	116,000
Less: PPC (8,000 x 100/80)	(10,000)
	106,000
Personal allowance	10,600
Less ½ × (106,000 – 100,000)	(3,000)
Revised Personal allowance	7,600

W2 The basic rate band is extended by the gross amount of the personal pension contributions paid (10,000)

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 2015/16		3,088

8 Matthew

The Property loss for the tax year 2015/16 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 2015/16

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	0	
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	0	
John's business travel	0	
Christmas presents for staff	0	
Entertaining UK customers	5,050	
Gifts of chocolate to customers	125	
Gifts of calendars	0	
Trading debt written off	0	
Increase in allowance	0	
Non trading loan written off	200	
Trade debt recovered (Taxable)	0	
Depreciation of vehicles	7,500	
Private motor expenses: £3,300 × 4,000/12,000 (W1)	1,100	
Salesman's motor car expenses	0	
Donation to national charity	50	
Donation to local charity	0	
Political donation	100	
Subscription to chamber of commerce	0	
Gift to employee on marriage	0	
Squash club subscription	250	
Advertising in trade press	0	
Cost of renewing 21 year lease	0	
Accountancy:		
Taxation services re capital gains tax	750	
Balance	0	
Interest on bank overdraft	0	
Van expenses	0	
Telephone	0	
Repairs to office photocopier	0	
New printer	650	
Central heating	2,200	
Decorating the office	0	
Goods for own consumption: £450 × ¹³⁰⁄₁₀₀	585	
		22,100
Adjusted trading 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 5 April 2016		*Main Pool*	*Special Rate Pool*	*Allowances*
	£	£	£	£
WDV b/f		23,500		
Additions Qualifying for AIA				
Machinery	476,000			
Lorries	30,500			
	506,500			
AIA(Maximum)	(500,000)			500000
		6,500		
Other additions				
Motor car > 130 g/km			16,600	
Disposals		(5,000)		
		25,000	16,600	
WDA @ 18%		(4,500)		4,500
WDA @ 8%			(1,328)	1,328
				505,828
WDV c/f		20,500	15,272	
Year ended 5 April 2017				
WDV b/f		20,500	15,272	
Additions Qualifying for AIA				
Thermal insulation for business building	120,000			
AIA	(120,000)			120,000
			-	
Other Additions				
Motor car (76 - 130g/km)		7,500		
Disposals			(12,000)	
		28,000	3,272	
WDA @ 18%		(5,040)		5,040
WDA @ 8%			(262)	262
				125,302
WDV c/f		22,960	3,010	

12 Jason

		£
2014/15: Actual		
1 July 2014 - 5 April 2015	(9/11 × 33,000)	27,000
2015/16: 1st 12 months (no CYB)		
1 July 2014 - 30 June 2015	33,000 + (1/12 × 24,000)	35,000
2016/17 (CYB)		
Year ended 31 May 2016		24,000
2017/18: (CYB)		
Year ended 31 May 2017		36,000

			£
Overlap profits	1 July 2014 - 5 April 2015		27,000
	1 June 2015 - 30 June 2015	(1/12× 24,000)	2,000
			29,000

13 Stephen

				£
2009/10	Actual	1/2/2010 – 5/4/2010	(30,000 × 2/15)	4,000
2010/11	Actual	6/4/2010 – 5/4/2011	(30,000 × 12/15)	24,000
2011/12	12 months to accounting date ended in tax year	12m to 30/4/2011	(30,000 × 12/15)	24,000
2012/13	CYB	Y/e 30/4/2012		10,000
2013/14	CYB	Y/e 30/4/2013		12,000
2014/15	CYB	Y/e 30/4/2014		15,000
2015/16		Y/e 30/4/2015		18,000
		P/e 31/10/2015		7,000
		Less: Overlap		25,000
		1/5/2010 – 5/4/2011	(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 2016		*Main Pool*	*Allowances*
Additions qualifying for AIA	**£**	**£**	**£**
Plant 1/5/2015	69,500		
AIA (max 15/12 x 500,000)	69,500		69,500
Other Additions - Car (76 - 130g/km) 1/12/2015		21,600	
WDA (18% x 15/12 x 21,600)		(4,860)	4,860
			74,360
WDV c/f		16,740	
Accounting Year ended 31 July 2017			
WDV b/f		16,740	
Additions qualifying for AIA			
Plant 1/10/2016	40,000		
AIA	(40,000)	-	40,000
	–		
WDA @ 18%		(3,013)	3,013
			43,013
WDV c/f		13,727	
Accounting Year ended 31 July 2018			
WDV b/f		13,727	
Additions qualifying for AIA			
Plant 1/2/2018	25,000		
AIA	(25,000)		25,000
Disposal		(13,000)	
		727	
Small Pool WDA		(727)	727
			25,727
WDV c/f		–	

The Trading profits of the first three periods of account are as follows.

Period of account	*Working*	*Trading Profits*
1/5/2015 - 31/7/2016	£(128,360 – 74,360)	54,000
1/8/2016 - 31/7/2017	£(88,013 – 43,013)	45,000
1/8/2017 - 31/7/2018	£(75,727 – 25,727)	50,000

The assessments are as follows.

Year	*Basis of Assessment*	*Basis period*	*Working*	*Assessment*
2015/2016	Actual	1/5/2015 - 5/4/2016	£54,000 × 11/15	39,600
2016/2017	12 months to accounting date ended in tax year	1/8/2015 - 31/7/2016	£54,000 × 12/15	43,200
2017/2018	CYB	A/C y/e 31/7/2017		45,000
2018/2019	CYB	A/C y/e 31/7/2018		50,000

Overlap profits are those from 1/8/2015 – 5/4/2016 ie: 8/15 × £54,000 = £28,800

15 David

Capital allowances for each period of account:

		Main Pool	Allowances
Year ended 5 April 2016	£	£	£
WDV b/f		14,800	
Additions qualifying for AIA			
Plant	2,800		
AIA - 100%	(2,800)		2,800
		–	
		14,800	
WDA @ 18%		(2,664)	2,664
			5,464
WDV c/f		12,136	
Year ended 5 April 2017			
WDV b/f		12,136	
Additions qualifying for AIA			
Plant	4,600		
AIA - 100%	(4,600)		4,600
		12,136	
WDA @ 18%		(2,184)	2,184
			6,784
WDV c/f		9,952	
Period to 30 June 2017			
WDV b/f		9,952	
Disposal		(4,000)	
		5,952	
Balancing allowance		(5,952)	5,952
		–	

Profits for periods of account:

Period of account	*Working*	*Trading profit*
		£
6/4/2015 - 5/4/2016	(25,000 – 5,464)	19,536
6/4/2016 - 5/4/2017	(27,000 – 6,784)	20,216
6/4/2017 - 30/06/2017	(14,000 – 5,952)	8,048

	Trading profit Assessments	£	£
2015/16	CYB (y/e 5/4/2016)		19,536
2016/17	CYB (y/e 5/4/2017)		20,216
2017/18	6/4/2017 - 30/6/2017	8,048	
	Less overlap profit	(2,000)	6,048

16 Max

(a) Trading profit assessments

	Trading profit assessments £	Trading loss £
2014/15 (1/1/2015 - 5/4/2015)		
3/12 × (12,000) (loss)	Nil	3,000
2015/16 (1/1/2015 - 31/12/2015) (loss)		
(12,000-3,000 (used in 14/15))	Nil	9,000
2016/17		
Y/e 31/12/2016 (loss)	Nil	4,000
		16,000
2017/18		
Y/e 31/12/2017	8,000	
Less: brought forward loss	(8,000)	(8,000)
	Nil	
2018/15		
Y/e 31/12/2018	11,500	
Less: brought forward loss	(8,000)	(8,000)
	3,500	
Loss carried forward		Nil

(b) Opening years loss relief

2014/15 loss of £3,000	This can be relieved against total income of 2011/12, 2012/13, 2013/14 in that order.
2015/16 loss of £9,000	This can be relieved against total income of 2012/13, 2013/14, 2014/15 in that order.
2016/17 loss of £4,000	This can be relieved against total income of 2013/14, 2014/15, 2015/16 in that order.

The revised net income for 2011/12 to 2014/15 is as follows:

	£	£
Loss sustained in 2014/15		3,000
2011/12		
Salary	19,200	
Less: opening years loss relief	(3,000)	(3,000)
Net Income	16,200	Nil
Loss sustained in 2015/16		9,000
2012/13		
Salary	23,800	
Less: opening years loss relief	(9,000)	(9,000)
Net Income	14,800	Nil
Loss sustained in 2016/17		4,000
2013/14		
Salary	20,100	
Less: opening years loss relief	(4,000)	(4,000)
Net Income	16,100	Nil

17 Elliot

Assessments

	£	
2012/13		
y/e 31 Dec 2012	60,000	
2013/14		
y/e 31 Dec 2013	30,000	
2014/15		
y/e 31 Dec 2014	40,000	
2015/16		
y/e 31 Dec 2015	NIL	(loss of £60,000)

Income Tax Computations

	2012/13	*2013/14*	*2014/15*	*2015/16*
	£	£	£	£
Trading profit	60,000	30,000	40,000	NIL
Property Income	6,000	6,000	6,000	6,000
Total Income	66,000	36,000	46,000	6,000
Current year (no claim)				(–)
Carryback			(46,000)	
Net income	66,000	36,000	Nil	6,000
Personal Allowance	(10,600)	(10,600)	(10,600)	(10,600)
Taxable income	55,400	25,400	Nil	Nil

Loss memo:

	£
Trading loss 2015/16	60,000
Carryback 2014/15	(46,000)
Trading loss available to carry forward	14,000

A current year offset could be chosen but this would waste the Personal allowance of 2015/16 without achieving any tax saving. The carry back against total income in 2014/15 is unrestricted as the non trading total income (6,000), does not exceed £50,000. 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 new partner joins the partnership.

(3) The cessation rules apply when an existing partner leaves the partnership.

(b)

	Total	*Anne*	*Betty*	*Chloe*
A/C year ended 31/12/2015	60,000			
1/1/2015 – 30/6/2015				
(6/12 x 60,000) PSR1:1	30,000	15,000	15,000	
1/7/2015 – 31/12/2015				
(6/12 x 60,000) PSR 2:1	30,000	20,000		10,000
	60,000	35,000	15,000	10,000
A/C year ended 31/12/2016	72,000			
PSR 2:1		48,000		24,000

Assessments		£
Anne		
2015/16 (CYB)		
A/C year ended 31/12/2015		35,000
2016/17 (CYB)		
A/C year ended 31/12/2016		48,000
Betty (note 1)		
2015/16		
6 months to 30/6/2015	15,000	
Less: Overlap relief	(3,000)	12,000
Chloe (note 2)		
2015/16 (Actual)		
(1/7/2015 – 5/4/2016)		
10,000 + (3/12 x 24,000)		16,000
2016/17 (CYB)		
A/C year ended 31/12/2015		24,000

Note 1 Betty

Betty ceased trading on 30/6/2015 so her final tax year of assessment is 2015/16 in which she will be assessed on all remaining profit as yet not assessed less her overlap relief. Therefore in the preceding tax year, 2014/15 she would have been assessed on her normal CYB i.e. on her share of the profit of the accounting year ended 31/12/2014. The only remaining profit to be assessed is therefore for her final 6 months of trading to 30/6/2015 which is then reduced by the available overlap relief.

Note 2 Chloe

Chloe commenced trading on 1 July 2015 so her first tax year of assessment is 2015/16 in which an actual basis applies. She is able to use CYB from 2016/17 which will generate an overlap profit of £6,000 (3/12 x 24,000)

(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 2015/16 and/or 2014/15
(3) Frank can claim against total income for 2012/13, 2013/14 and 2014/15. (Special opening year loss relief)
(4) Elvis can claim against trading profit for 2014/15, 2013/14 and 2012/13. (Terminal loss relief)

19 Renner

Income tax computation - 2015/16

	Non-savings	*Dividends*	*Total*
	£	£	£
Employment income (W1)	48,715		48,715
Dividend income (20,000 × 20p × $\frac{100}{90}$)		4,444	4,444
Total Income	48,715	4,444	53,159
Less PA	(10,600)		(10.600)
Taxable income	38,115	4,444	42,559

Income tax		£			£
Basic rate:	Non savings	31,785	@	20%	6,357
Higher rate:	Non-savings	6,330	@	40%	2,532
	Dividends	4,444	@	32.5%	1,444
Income tax liability					10,333

Workings

(W1) Employment income

	£
Salary	
($8/12 \times$ £28,500)	19,000
($4/12 \times$ £33,000)	11,000
	30,000
Bonus (February 2016)	4,200
Benefits (W2)	15,415
	49,615
Less: Occupational pension contributions (3% × £30,000)	(900)
Employment income	48,715

(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		–
	Mini (W3)		3,960
	Fuel charge (petrol)		
	Mini (W3)		5,304
(f)	Employer's contribution into pension - Exempt benefit		-
(g)	Beneficial loan £20,000 × (3% – 2%)		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) × 3% × $10/12$]	1,575	
	Council tax	550	
	Electricity	260	
	Telephone	110	
	Cleaning	130	
	Use of furniture (20% × £7,200 × 10/12)	1,200	
			4,725
	Total assessable benefits		15,415

(W3) Mini - Car and fuel benefits

CO_2 emissions = 145g/km (rounded down to the nearest 5g/km)

Petrol engine

Appropriate percentage = 14% + (145 - 95) = 50/5 = 10%
= 24%

Car benefit	(24% × £16,500)	£3,960
Fuel benefit	(24% × £22,100)	£5,304

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 £40,000 for 2015/16 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 annual limits of £50,000 (pre 14/15) and £40,000 for 2014/15 for each tax 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 £40,000 for 2015/16 he will now be able to use any unused allowance brought forward from the previous 3 years on a FIFO basis i.e. 2012/13, 2013/14 and 2014/15.

As George was not a member of a pension scheme in 2012/13 no unused allowance will be available to carry forward from this year. £22,000 of unused allowance (50,000 – 28.000) is available from 2013/14 and will now be fully utilised, followed by £13,000 of the £17.000 (40,000 – 23,000) unused allowance from 2014/15.

Tax relief will therefore be available on the full contribution of £75,000 (gross) made in 2015/16 and George will have £4,000 (17,000 - 13,000)of unused allowance to carry forward to 2016/17 which will permit a maximum allowable gross contribution of £44,000 to be made in 2016/17.

(b) **Osbourne – Income Tax Computation 2015/16**

	£
Employment Income	200,000
Annual Allowance Charge (note 1)	30,000
	230,000
Personal Allowance (note 2)	Nil
Taxable Income	230,000

Income Tax Liability

121,785	@ 20%	24,357
108,215	@ 40%	43,286
230,000		67,643

The basic and higher rate bands are extended by the gross amount of personal pension contributions (31,785+ 90,000 = 121,785) 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 2015/16 of £40,000 and £20,000 (40,000 - 20,000) brought forward unused allowance from 2014/15. Therefore an Annual Allowance Charge will arise of £30,000 (90,000 – 60,000)

Note 2 Osbourne has an adjusted net income of £140,000 (230,000 – 90,000) which exceeds £121,200 and thus no personal allowance is available

21 Tony

(a) Class 1 NICs

Employees

Jack	(18,200 – 8,060) × 12% =		1,217
Jill	(12,480 – 8,060) × 12% =		530

Employer's

Jack	(18,200 - 8,112) × 13.8% =	1,392
Jill	(12,480 – 8,112) × 13.8% =	603
		1,995
Less: Employment allowance		(2,000)
		Nil
Total Class 1 NIC		1,747

(b) Class 2 NICs

52 × £2.80 146

Class 4 NICs

(18,479 – 8,060) × 9% 938

22 Chorley Ltd

Adjustment of Trading Profit - Year ended 31 December 2015	£
Profit before tax per Accounts	6,868
Deduct	
Profit on sale of business premises	(1,750)
Add back:	
Advertising	0
Irrecoverable debts	0
Depreciation	2,381
Light and heat	0
Subscription to printer association	0
Contribution to local Enterprise agency	0
Gifts to customers:	
Calendars	0
Food hampers (1)	95
Director use of car (2)	0
Refurbishing press (3)	522
Redecorating adm offices	0
Building extension (3)	1,647
Staff Christmas lunch and wages (4)	0
Telephone	0
Adjusted trading 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, 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 for the employer.

23 Sail Ltd

Corporation tax computation for the year ended 31 March 2016

	£
Trading profit	380,000
Interest receivable	9,000
Property Income	12,000
Chargeable gains	21,000
	422,000
Less: Qualifying charitable donations	(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 20%	80,000

Note 1: Profit limit 1,500,000 ÷ 2 (Sail Ltd plus one associated company) = £750,000 reduced profit limit.
As the augmented profit of Sail Ltd does not exceed the profit limit of £750,000, then irrespective of the level of profits in the previous period it will not be required to make quarterly instalment payments. The corporation tax will therefore need to be paid nine months and one day after the end of the accounting period ie by 1 January 2017.

24 Swish Ltd

(a) Computation of Trading loss for the year ended 31 March 2016

		£	£
Net loss per accounts			(116,500)
Add back:	Depreciation	10,800	
	Entertaining	1,200	
			12,000
			(104,500)
Less:	Capital allowances £20,000 × 18%		(3,600)
Trading Loss			(108,100)

(b)

	Year ended 31 March	
	2015	*2016*
	£	£
Trading profit	40,000	Nil
Interest receivable	2,000	3,500
Chargeable gain	–	44,500
Total Profits	42,000	48,000
Less: Current Year / Carry back	(42,000)	(48,000)
Taxable Total Profit	Nil	Nil

Loss memorandum

Loss for y/e 31/3/16 (part (a))	108,100
Less: Current Year relief y/e 31/3/16	(48,000)
Carry back relief y/e 31/3/15	(42,000)
Loss available to carry forward	18,100

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

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 October 2015	$\frac{259.5 - 164.5}{164.5} \times 24,714$			14,273
		3,000	22,750	38,987
Sale October 2015		(1,500)	(11,375)	(19,493)

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 (19,493 – 11,375)		(8,118)
Chargeable gain		4,507
Total chargeable gains:		
Previous 9 days		1,000
Pool		4,507
Chargeable gains to include in Corporation tax computation		5,507

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	$\frac{260.6 - 130.2}{130.2}$	$= 1.002 \times 900$	(902)
			2,698
Chargeable Gain			

(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	$\frac{259.5 - 152.4}{152.4}$	$= 0.703 \times 2,000$	(1,406)
Chargeable Gain			3,194

(b) Restricted to

⁵⁄₃ [6,600 – 6,000] = 1,000

Take lower gain = £1,000

Total chargeable Gains

	£
Land	2,698
Painting	1,000
Antique	(2,000)
Net Chargeable Gains	1,698

27 Westcroft Limited

		£
Disposal proceeds		500,000
Less cost		(100,000)
Unindexed gain		400,000
Less indexation allowance	$\frac{260.6 - 211.4}{211.4} = 0.233 \times 100{,}000$	(23,300)
Chargeable Gain		376,700

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
£376,700 – £50,000 = £326,700

When the replacement painting is sold the base cost is:

Actual cost	450,000
Less Gain Deferred	(326,700)
Base cost	123,300

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 full 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 not all of the proceeds are reinvested, the capital gain element that cannot be rolled over and will remain chargeable 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 follows:

	£
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 no more 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 leasehold property 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 2015/16 Capital Gains Tax

	£
Capital Gain	31,000
Capital Gain	24,000
Capital Loss	(7,000)
Net Capital gains arising in 2015/16	48,000
Less: Capital loss brought forward	(10,000)
Net Capital Gains	38,000
Less: Annual Exempt Amount (AEA)	(11,100)
Taxable Gains	26,900
Capital Gains Tax payable £26,900 × 28%	£7,532

Claude is a higher rate taxpayer and hence all the taxable gains are taxed at 28%. The CGT will be due for payment on 31 January 2017

30 Cheryl

	£
Chargeable Gain	40,000
Less: AEA	(11,100)
Taxable gains	28,900
Capital Gains Tax (W1)	£7,913
Due	31/1/2017

(W1) Basic rate band remaining
£31,785 + (£1,600 × 100/80) = £33,785 – £32,000 = £1,785

	£
1,785 × 18% =	321
27,115 × 28% =	7,592
28,900	7,913

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 2016.

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 2016.

	£
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 2014
Restoration	=	60,000	Feb 2016
Base cost		154,476	

32 Zoe

Apply matching rules

i)	same day	X		
ii)	Next 30 days	✓	10/2/2016	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
30/4/2015 Acquisition	1,500	18,000
31/5/2015 Acquisition	500	7,000
	2,000	25,000
31/1/2016 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 2015	2,700	5,400
May 2015	600	1,500
June 2015 Rights issue 1:3 @ £2:30	1,100	2,530
	4,400	9,430
Disposal August 2015	(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 Entrepreneurs Relief (ER)

	£
Investment asset	80,000
Less capital loss b/f	(15,000)
	65,000
Less AEA	(11,100)
	53,900
CGT @ 28% (Note 1)	£15,092

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 + £15,092 = **£59,592** Due 31 January 2017

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 capital loss brought forward and the annual exempt amount are used in priority against those gains taxed at the highest tax rate.

(3) The remaining gains eligible for ER in future years 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	
Gain immediately chargeable (£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 only the disposal of an asset used in the business 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.

If further qualifying business assets were to be acquired by December 2018 (within 3 years of disposal date) then claims for rollover relief against those assets may become available

As above entrepreneurs' relief is not available.

36 Wendy

(a) Wendy - Capital gain on shares sold in January 2016

	£	£
Market value of shares in January 2016		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

Gift relief is available as shares in an unquoted trading company are qualifying business assets. As the disposal was a sale at undervalue it is still the OMV of the shares that is used in computing the gain but as the actual proceeds received exceed the actual cost of the shares then that part of the gain remains chargeable on Wendy and only the remaining part of the gain is eligible for gift relief

(b) Wendy's grandson - Base cost

	£
Market value of shares, January 2016	165,000
Less: Gain deferred	(95,000)
Base cost	70,000

37 Amy

Proceeds	400,000
Less cost	(190,270)
Gain	209,730
Less PPR relief (W1)	(62,745)
Less letting relief (W2)	(10,457)
Chargeable Gain	136,528

(W1)

	Actual & Deemed	*Letting*	*Non occupation*	*Total*
1/4/85 – 1/4/86	12m			
1/4/86 – 30/9/90 (any reason)	36m	18m		
1/10/90 – 1/4/94	42m			
1/4/94 – 1/5/15 (last 18 months)	18m		235m	
	108m	18m	235m	361m

PPR $209{,}730 \times \frac{108}{361} = 62{,}745$

(W2) Letting relief
Lower of

- 62,745
- 40,000
- $\frac{18}{361} \times 209{,}730 = 10{,}457$

Letting relief = £10,457

38 Nathan

(a) Chargeable transfers

	23/10/2005	17/09/2009	26/08/2012
	CLT	*PET*	*CLT*
Transfer value	356,000	47,000	276,000
Less: Exemptions:			
AE 2005/06	(3,000)		
AE 2004/05	(3,000)		
Marriage exemption		(1,000)	
AE 2009/10		(3,000)	
AE 2008/09		(3,000)	
AE 2012/13			(3,000)
AE 2011/12			(3,000)
Chargeable Transfer	350,000	40,000	270,000

Note: Transfer to civil partner on 14/02/2011 is exempt

Computation of IHT on lifetime transfers chargeable when made

	£	Gross	IHT
23/10/2005 CLT	350,000	368,750	18,750
275,000 @ NRB = nil			
75,000 @ 25% = 18,750			
Tax paid by Nathan due 30/04/2006			
26/08/2012 CLT	270,000	270,000	54,000
NRB of £325,000 deemed used by Gross Chargeable Transfers(GCT's) in previous 7 years		638,750	
∴ 270,000 @ 20%			
Tax paid by trustees due 30/04/2013			

(b) **Computation of IHT on lifetime transfers chargeable on death - 30 November, 2015**

	Gross	IHT
GCT's in 7 years before 17/09/2009	368,750	–
17/09/2009 PET	40,000	16,000
∴ All £325,000 NRB deemed used = 40,000 @ 40%	408,750	
Less: Taper relief (80%)		(12,800)
Tax payable and borne by donee (nephew)		3,200
26/08/2012 CLT	270,000	108,000
GCT's in previous 7 years exceed NRB	678,750	
∴ 270,000 @ 40%		
Less: Taper relief (20%)		(21,600)
Lifetime Tax Paid		(54,000)
Additional Tax Due on Death paid by trustees, borne by beneficiaries		32,400
23/10/2012 GCT (23/10/2005) Removed from cumulative total	(368,750)	
GCT's in 7 years before death	310,000	

Nathan chargeable Estate at death – 30 November, 2015

		£		£
Property		500,000		
Less: Mortgage		(150,000)		350,000
Quoted 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 legatee (Nathan's nephew).
Note - legal fees of friend not allowable deduction as not legally enforceable debt and as the mortgage is not an endowment mortgage it is deducted from the value of the property.

39 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 £82,000, or if the value of the taxable supplies to be made in the next 30 days will exceed £82,000.

Kite Ltd will therefore be liable to register for VAT from 29 February 2016 (27,000 + 28,000 + 28,000 = 83,000), and the company must notify HMRC by 30 March 2016. Kite Ltd will be registered from 1 April 2016.

(b) **VAT Return - Quarter ended 31 December 2015**

	£	£
Output VAT		
Sales (240,000 x 50% x 20%) + (240,000 x 50% × 95% (100% - 5%) × 20%)		46,800
Input VAT		
Purchases and expenses (71,280 - 960 = 70,320 × 20%)	14,064	
Irrecoverable debt (4,000 x 20%)	800	
Machinery (42,300 × 20/120)	7,050	(21,914)
VAT payable 7 February 2016		24,886

Notes

1 The calculation of output VAT will only take into account the discount for prompt payment if customers 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.

40 Geewizz Ltd

(a) The default surcharge

Geewizz Ltd's first VAT return for quarter to 30 June 2015 was due on 7 August 2015 but was submitted late, on 20 August 2015 so HMRC will have issued a surcharge liability notice specifying a surcharge period running to 30 June 2016.

Although the second and third returns were submitted by the due dates of 7 November 2015 and 7 February 2016 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 2016.

If the return to 31 March 2016 is late, a surcharge at the rate of 10% will be imposed and the surcharge period will be extended to 31 March 2017.

(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 as if no cash is received no output tax will need to be paid. Input tax however may only be recovered if the payment has been made within the return period.

OR

(b) 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.

(c) Under the scheme only one VAT return is submitted each year, with nine monthly payments being made on account between month 4 and month 12 of the period, 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 along with the VAT return 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 and cash budgeting is made easier.

41 Factor Limited

(a) Selling to non EU customers – the VAT treatment is that sales to non EU customers 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 so there are no VAT consequences for the UK custome.

42 Groups

(a) 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 of 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.

43 Jim

Payments on Account for 2015/16 will be based on the income tax payable by self assessment in 2014/15
Due Dates

31 Jan 2016	5,100/2 = 2,550
31 Jul 2016	5,100/2 = 2,550
31 Jan 2017	Balancing payment

Income 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 2016/17 is based on income tax payable by self assessment in 2015/16

	31 Jan 2017	£7,629/2	= £3,814
Total due	31 Jan 2017	= £3,529 + £3,814	= £7,343

44 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.

45 Cannock Limited

Corporation tax due

	£
2,400,000 @ 20% =	480,000

Each instalment is 25% × 480,000 = £ 120,000

Due Dates for y/e 31 January 2016

	£
14 Aug 2015	120,000
14 Nov 2015	120,000
14 Feb 2016	120,000
14 May 2016	120,000

The return filing date is 31 January 2017