Answers

1 (a) (i) Bayle Defender – Trading profit for the year ended 30 September 2010

	£
Net profit	172,400
Impairment loss	0
Gifts to customers – Clocks	3,300
– Bottles of champagne	2,480
Donations to political parties	2,900
Lease of motor car (10,360 x 15%)	1,554
Personal tax advice	600
Property expenses (46,240 x 2/5)	18,496
Parking fines	520
Professional subscription	0
Golf club membership fee	960
Trading profit	203,210

Tutorial notes:

(1) *The recovered impairment loss will have been allowed as a deduction when originally written off, so the recovery is now taxable.*

(2) *Gifts to customers are only an allowable deduction if they cost less than £50 per recipient per year, are not of food, drink, tobacco or vouchers for exchangeable goods and carry a conspicuous advertisement for the company making the gift.*

(3) *The motor car has a CO_2 emission rate in excess of 160 grams per kilometre, so 15% of the leasing costs are not allowed.*

(ii) Bayle Defender – Income tax computation 2010–11

	£	£
Trading profit (from (a)(i) above)		203,210
Employment income		
Director's remuneration	42,000	
Bonus payment	6,000	
		48,000
Interest from savings certificate		0
Interest from government stocks		3,600
Dividends (9,900 x 100/90)		11,000
		265,810
Personal allowance		0
Taxable income		265,810
Income tax		
37,400 at 20%		7,480
112,600 at 40%		45,040
104,810 (265,810 – 11,000 – 150,000) at 50%		52,405
11,000 at 42·5%		4,675
265,810		
Income tax liability		109,600
Tax suffered at source		
PAYE (48,000 at 50%)	24,000	
Dividends (11,000 at 10%)	1,100	
		(25,100)
Income tax payable		84,500

Tutorial notes:

(1) *The bonus payment of £6,000 that Bayle became entitled to on 10 March 2010 will have been treated as being received during 2009–10.*

(2) *Interest received on the maturity of savings certificates issued by National Savings & Investments is exempt.*

(3) *No personal allowance is available as Bayle's adjusted net income of £265,810 exceeds £112,950.*

(iii) Tax payments

(1) Bayle's balancing payment for 2010–11 will be £31,100 (84,500 – 53,400).

(2) In addition, she will have to make the first payment on account for 2011–12 of £42,250 (84,500 x 50%), so the total amount payable on 31 January 2012 will be £73,350 (31,100 + 42,250).

Interest and penalties

(1) Interest is charged where payments are made late. This will run from 31 January 2012 to 31 August 2012.

(2) The interest charge will be £1,284 (73,350 x 3·0% x 7/12).

(3) Two penalties of £1,555 (31,100 at 5%) will be imposed on the balancing payment, one when it is one month late and the other when it is six months late.

(b) (i) (1) The monthly earnings threshold is £476 (5,715/12).

(2) Fyle will pay employee Class 1 NIC for 2010–11 of £1,243 (2,824 (3,300 – 476) at 11% x 4).

(3) Bayle will pay employer's Class 1 NIC for 2010–11 of £1,446 (2,824 (3,300 – 476) at 12·8% x 4).

Tutorial note: *The alternative approach using the annual earnings threshold and then taking 4/12ths of an annual NIC figure is acceptable.*

(ii) Trading income assessments

(1) Fyle's trading income assessment for 2010–11 is £14,400 calculated as follows:

	£
Basis period: 1 December 2010 to 5 April 2011	
216,000 x 4/12	72,000
Profit share 72,000 x 20%	14,400

(2) The assessment for 2011–12 is £44,000 calculated as follows:

	£
Basis period: 1 December 2010 to 30 November 2011	
216,000 x 10/12	180,000
240,000 x 2/12	40,000
	220,000
Profit share 220,000 x 20%	44,000

Tutorial notes:

(1) The commencement rules apply to Fyle for 2010–11 since he will join as a partner on 1 December 2010.

(2) The assessment for 2011–12 is for the 12 months from when Fyle joins the partnership.

NIC

(1) Fyle will pay Class 2 NIC for 2010–11 of £43 (18 x 2·40).

(2) He will pay Class 4 NIC for 2010–11 of £695 (14,400 – 5,715 = 8,685 at 8%).

(3) There are no NIC implications for Bayle.

2 (a) Molten-Metal plc – Corporation tax computation for the year ended 31 March 2011

	£	£
Trading profit		1,882,600
Loan stock interest payable (22,500 + 3,700 – 4,200)	22,000	
Repairs to office building	0	
Capital allowances – P & M (working 1)	142,520	
– IBA (working 2)	7,320	
		(171,840)
		1,710,760
Property business profit (working 3)		68,400
Interest income (working 4)		8,700
Chargeable gain (working 5)		176,426
Taxable total profits		1,964,286
Corporation tax (1,964,286 at 28%)		550,000

Tutorial notes:

(1) Interest paid in respect of a loan used for trading purposes is deductible in calculating the trading profit.

(2) The repairs to the office building are not deductible, being capital in nature, as the building was not in a usable state when purchased and this fact was reflected in the reduced purchase price.

Working 1 – Plant and machinery (P & M)

	£	Main pool £	Special rate pool £	Allowances £
WDV brought forward		87,800		
Additions qualifying for AIA				
Office building	0			
Ventilation system	32,000			
Lift	46,000			
	78,000			
AIA – 100%	(78,000)		0	78,000
Machinery	81,600			
Building alterations	7,700			
Wall	0			
Partition walls	22,900			
	112,200			
AIA – 100%	(22,000)			22,000
		90,200		
Other additions				
Motor cars (17,300 x 2)		34,600		
		212,600		
WDA – 20%		(42,520)		42,520
WDV carried forward		170,080		
Total allowances				142,520

Tutorial notes:

(1) The ventilation system and lift are both integral to a building and so are included in the special rate pool. It is beneficial to claim the annual investment allowance of £100,000 initially against this expenditure, as it would otherwise only qualify for writing down allowance at the rate of 10%.

(2) The building alterations were necessary for the installation of the machinery, and therefore qualify for capital allowances. Walls are specifically excluded, with the exception of partition walls which are movable and intended to be so moved.

(3) The motor cars have CO_2 emissions between 111 and 160 grams per kilometre, and therefore qualify for writing down allowances at the rate of 20%. The private use of a motor car is irrelevant, since such usage will be assessed on the employee as a benefit.

Working 2 – Industrial buildings allowance (IBA)

	£
Eligible expenditure	732,000
Industrial buildings allowance at 1%	7,320

(1) The general offices costing £165,000 qualify as they cost less than 25% of the total cost (732,000 x 25% = £183,000).

Working 3 – Property business profit

	£
Premium received	68,000
Less: 68,000 x 2% x (6 – 1)	(6,800)
	61,200
Rent receivable (78,800 – 68,000 = 10,800 x 2/3)	7,200
Property business profit	68,400

Working 4 – Interest income

	£
Loan interest receivable (9,800 + 3,100)	12,900
Bank interest receivable	2,600
	15,500
Interest payable	(6,800)
	8,700

Working 5 – Chargeable gain

	£	£
Disposal proceeds		872,000
Incidental costs of disposal		(28,400)
		843,600
Cost	396,200	
Enhancement expenditure – Extension	146,000	
– Roof	0	
		(542,200)
		301,400
Indexation allowance		
Cost 396,200 x 0·269	106,578	
Enhancement expenditure 146,000 x 0·126	18,396	
		(124,974)
Chargeable gain		176,426

Tutorial note: *The cost of replacing part of the roof is not enhancement expenditure as the office building is simply being restored to its original state prior to the fire.*

(b) (1) The fourth and final quarterly instalment payment will be for £151,800 (550,000 – 398,200).

(2) This is due on 14 July 2011.

3 (a) (1) Bon only acquired her shareholding and became a director on 1 February 2010, so the qualifying conditions were not met for one year prior to the date of disposal.

(2) Cherry was not an officer or an employee of Alphabet Ltd.

(3) Dinah's shareholding of 3% (3,000/100,000 x 100) is less than the minimum required holding of 5%.

(b) Aloi – Capital gains tax (CGT) liability 2010–11

	£
Chargeable gain qualifying for entrepreneurs' relief	
Ordinary shares in Alphabet Ltd	
Disposal proceeds (60,000 x £6)	360,000
Cost (50,000 + 18,600)	(68,600)
	291,400
Other chargeable gain	
Investment property	22,600
Annual exempt amount	(10,100)
	12,500
CGT liability: 291,400 at 10%	29,140
12,500 at 28%	3,500
	32,640

Tutorial note: *The annual exempt amount is set against the chargeable gain from the sale of the investment property as this saves CGT at the higher rate of 28%.*

Bon – CGT liability 2010–11

	£
Ordinary shares in XYZ plc	
Deemed proceeds (10,000 x £7·12)	71,200
Cost	(36,880)
	34,320
Annual exempt amount	(10,100)
	24,220
CGT liability: 24,220 at 28%	6,782

(1) The shares in XYZ plc are valued at £7·12 (£7·10 + ¼(£7·10 – £7·18)). There is no average value as there were no recorded bargains for the date of the gift.

(2) Following the takeover Bon received 25,000 ordinary shares in XYZ plc. The cost of the original shareholding is passed on to the new shareholding, so the cost attributable to the 10,000 shares sold is £36,880 (92,200 x 10,000/25,000).

Cherry – CGT liability 2010–11

	£
Ordinary shares in Alphabet Ltd	
Disposal proceeds (12,000 x £6)	72,000
Cost	(23,900)
	48,100
Annual exempt amount	(10,100)
	38,000
CGT liability: 9,800 at 18%	1,764
28,200 at 28%	7,896
	9,660

(1) Cherry's basic rate tax band is extended to £40,800 (37,400 + 3,400), of which £9,800 (40,800 – 31,000) is unused.

Dinah

(1) There is no CGT liability on the sale of the XYZ plc shares as the gain of £5,000 (6,600 – (4,800 x 1,000/3,000)) is less than the annual exempt amount.

(2) The transfer of the XYZ plc shares on Dinah's death is an exempt disposal.

4 **(a)** (1) Aston would have been liable to compulsory value added tax (VAT) registration when his taxable supplies during any 12-month period exceeded £70,000.

(2) This happened on 31 January 2011 when taxable supplies amounted to £75,200 (2,300 + 6,400 + 25,700 + 10,700 + 16,100 + 14,000).

(3) Registration is required from the end of the month following the month in which the limit is exceeded, so Aston will have been registered from 1 March 2011 or from an agreed earlier date.

(b) The following information is required:

(1) Aston's VAT registration number.
(2) An identifying number (invoice number).
(3) The rate of VAT for each supply.
(4) The amount of VAT payable.

(c) (1) VAT will have to be accounted for according to the time of supply. This is the earlier of the date that the service is completed or the date it is paid for.

(2) The VAT charged at the UK VAT rate should be declared on Aston's VAT return as output VAT, but will then be reclaimed as input VAT on the same VAT return. This is known as the reverse charge procedure.

(d) (1) HM Revenue and Customs will not charge a penalty if Aston has taken reasonable care, provided he informs them of any errors upon subsequent discovery.

(2) However, applying the incorrect rate of VAT is more likely to be treated as careless, since Aston would be expected to check the VAT classification of his supplies.

(3) The maximum amount of penalty will therefore be 30% of the VAT underpaid, but this penalty could be reduced to nil as a result of a subsequent unprompted disclosure to HM Revenue and Customs.

(e) **(i)** (1) Aston, as a newly registered business, will have to file his VAT returns online and pay the VAT that is due electronically.

(2) The deadline for doing this is one month and seven days after the end of each quarter. For example, for the quarter ended 31 May 2011 Aston will have until 7 July 2011 to file his VAT return and pay the VAT that is due.

Tutorial note: *The deadline is extended to one month and 10 days after the end of each quarter where payment is made by direct debit.*

(ii) (1) Aston will have to make nine payments on account of VAT commencing in month four of the annual VAT return period. These will be due electronically.

(2) Each payment on account will be 10% of the VAT payable for the previous year, although for the first year an estimated figure will be used.

(3) The annual VAT return, along with the balancing payment, will be due two months after the end of the annual VAT period. The VAT return will have to be filed online.

Tutorial note: *An additional seven days is not given for filing an annual VAT return online as the deadline is already longer than normal.*

5 **(a)** (1) A potentially exempt transfer only becomes chargeable to inheritance tax (IHT) if the donor dies within seven years of making the gift.

(2) In contrast, a chargeable lifetime transfer is immediately charged to IHT. An additional IHT liability may then arise if the donor dies within seven years of making the gift.

(b) **Jimmy – Inheritance tax computation**

Lifetime transfers
2 August 2009

		£	£
Value transferred			50,000
Marriage exemption		2,500	
Annual exemptions	2009–10	3,000	
	2008–09	3,000	
			(8,500)
Potentially exempt transfer			41,500

14 November 2009

	£
Net chargeable transfer	800,000
Inheritance tax liability 325,000 at nil%	0
475,000 x 20/80	118,750
Gross chargeable transfer	918,750

Additional liabilities arising on death
2 August 2009

	£
Potentially exempt transfer	41,500

14 November 2009

	£
Gross chargeable transfer	918,750
IHT liability 283,500 at nil%	0
635,250 at 40%	254,100
IHT already paid	(118,750)
Additional liability	135,350

Tutorial note: *The potentially exempt transfer utilises £41,500 of the nil rate band of £325,000 for 2010–11, so only £283,500 (325,000 – 41,500) is available against the chargeable lifetime transfer.*

Death estate

	£
Property	260,000
Building society deposits	515,600
Proceeds of life assurance policy	210,000
	985,600
Funeral expenses	(5,600)
Value of estate	980,000
Spouse exemption	(300,000)
Chargeable estate	680,000
IHT liability 680,000 at 40%	272,000

(c) (1) The due date on which the IHT liability of £272,000 will be payable by the personal representatives of Jimmy's estate is the earlier of 31 August 2011 or the date when they deliver their account to HM Revenue and Customs.

				Marks	
1	(a)	(i)	Impairment loss	½	
			Gifts to customers	1	
			Donations to political parties	½	
			Lease of motor car	1	
			Personal tax advice	½	
			Property expenses	1	
			Parking fines	½	
			Professional subscription	½	
			Golf club membership fee	½	
					6
		(ii)	Trading profit	½	
			Director's remuneration	½	
			Bonus payments	1	
			Interest from government stocks	½	
			Interest from savings certificate	½	
			Dividends	½	
			Personal allowance	1	
			Income tax	2	
			Tax suffered at source	1½	
					8
		(iii)	**Tax payments**		
			Balancing payment	1	
			Payment on account	1	
			Interest and penalties		
			Interest	1½	
			Penalties	1½	
					5
	(b)	(i)	Monthly earnings threshold	1	
			Employee Class 1 NIC	1½	
			Employer Class 1 NIC	1½	
					4
		(ii)	**Trading income assessments**		
			2010–11	1½	
			2011–12	2½	
					4
			NIC		
			Class 2 NIC	1½	
			Class 4 NIC	1	
			Bayle	½	
					3
					30

			Marks	
2	**(a)**	Trading profit	½	
		Loan stock interest payable	1½	
		Repairs to office building	1	
		P & M – Office building	½	
		– Ventilation system and lift	1	
		– AIA	1	
		– Machinery	½	
		– Building alterations	½	
		– Wall	½	
		– Partition walls	1	
		– AIA	1	
		– Main pool	2	
		IBA – Eligible expenditure	1	
		– General offices	1	
		– Allowance	½	
		Property business profit – Premium received	1½	
		– Rent	1	
		Interest income	2	
		Chargeable gain – Disposal proceeds	½	
		– Costs of disposal	½	
		– Cost	½	
		– Enhancement expenditure	1½	
		– Indexation allowance	1½	
		Corporation tax	½	
				23
	(b)	Instalment payment	1	
		Due date	1	
				2
				25
3	**(a)**	Bon	1	
		Cherry	1	
		Dinah	1	
				3
	(b)	**Aloi**		
		Alphabet Ltd – Disposal proceeds	½	
		– Cost	1	
		Investment property	½	
		Annual exempt amount	1	
		Capital gains tax	1	
		Bon		
		Deemed proceeds	1	
		Cost	1	
		Annual exempt amount	½	
		Capital gains tax	½	
		Cherry		
		Disposal proceeds	½	
		Cost	½	
		Annual exempt amount	½	
		Capital gains tax	2	
		Dinah		
		Sale of shares	1	
		Exempt disposal on death	½	
				12
				15

			Marks	
4	**(a)**	Registration limit	½	
		31 January 2011	2	
		Date of registration	½	
				3
	(b)	Aston's VAT registration number	½	
		An identifying number	½	
		The rate of VAT for each supply	½	
		The amount of VAT payable	½	
				2
	(c)	Time of supply	1	
		Entries on VAT return	1	
				2
	(d)	No penalty if reasonable care	1	
		Treated as careless	1	
		Amount of penalty	1	
				3
	(e)	**(i)** Online filing	½	
		Electronic payment	½	
		Deadline	1	
				2
		(ii) Payments on account	1	
		Amount of each payment	1	
		Deadline	1	
				3
				15
5	**(a)**	PET	1	
		CLT	1	
				2
	(b)	**Lifetime transfers**		
		PET – Recognition as a PET	½	
		– Marriage exemption	1	
		– Annual exemptions	1	
		CLT – Recognition as a CLT	½	
		– IHT liability	2	
		Additional liabilities arising on death		
		PET	1	
		CLT – IHT liability	1	
		– IHT already paid	½	
		Death estate		
		Property	½	
		Building society deposits	½	
		Life assurance policy	1	
		Funeral expenses	1	
		Spouse exemption	1	
		IHT liability	½	
				12
	(c)	Due date		1
				15