



Practical Tax People
Association of
Taxation Technicians

May 2017 Examination

PAPER 1

Personal Taxation

Part II Suggested Answers

ANSWER Q1**Sarah Bray Income Tax computation 2016/17**

1)

	Non-Savings income	Savings income	Dividend income
	£	£	£
Employment income (W1)	54,625 (1/2)		
Private medical insurance	570 (1/2)		
REIT (N1)	475 (1)		
Interest income		425	(1/2)
Dividend income			<u>2,300</u> (1/2)
Total income	55,670	425	2,300
Less:			
Personal allowance	<u>(11,000)</u> (1/2)		
Taxable income	44,670	425	2,300

Tax	Non-savings income (W2)	36,625 @ 20%	7,325 (1/2)
	Non-savings income	8,045 @ 40%	3,218 (1/2)
	Savings income (N2)	425 @ 0%	0 (1/2)
	Dividend income (N3)	2,300 @ 0%	<u>0</u> (1/2)
			10,543
	Plus: High Income Benefit Charge (W3)		<u>398</u> (1/2)
	Tax liability		10,941
	Less: Tax deducted at source:		
	PAYE deducted		(10,200) (1/2)
	REIT		<u>(95)</u> (1/2)
	Income Tax payable for 2016/17		646 (1/2)

This is due for payment by 31 January 2018. (1/2)

Workings

		£
(W1) Business mileage		
Amount reimbursed by Rello Ltd:	12,500 x 22ppm	2,750 (1/2)
Less: HMRC approved mileage allowance	10,000 x 45ppm	(4,500) (1/2)
	2,500 x 25ppm	<u>(625)</u> (1/2)
Shortfall		(2,375)

The shortfall is deductible from earnings.

		£
Annual salary		57,000
Less: Mileage shortfall		<u>(2,375)</u> (1/2)
Taxable Employment income		54,625

		£
(W2) Basic Rate Band extension		
Basic Rate Band for 2016/17		32,000
Plus: Grossed up gift aid donations		
January 2017 – one off contribution	2,500 x 100/80	3,125 (1/2)
Regular monthly contributions (12 x £100)	1,200 x 100/80	<u>1,500</u> (1/2)
Revised Basic Rate Band		<u>36,625</u> (1/2)

(W3) High Income Child Benefit Charge (HIBC)

		£
Net income (W4)		53,770
Less:		
Child benefit charge threshold		<u>(50,000)</u> (1/2)
Excess		3,770 (1/2)
3,770/100 x 1% =		37% (1/2)
Total Child Benefit received =		1,076
HIBC @ 37% =		398 (1)

(W4) Net income for the purposes of the HIBC

	<u>£</u>	<u>£</u>
Total income (N4)		58,395 (1)
Less:		
Gross gift aid donations		<u>(4,625)</u> (1)
Adjusted Net Income		53,770

Notes

(N1) UK REIT

UK REIT dividends are paid net of basic rate tax and are taxable as non-savings income.

(N2) Interest income

As a higher rate taxpayer, Sarah is entitled to a Personal Savings Allowance of £500 for 2016/17.

The entire £425 interest from bank accounts is therefore taxable at 0%.

(N3) Dividend income

Sarah is entitled to a dividend allowance of £5,000 for 2016/17 irrespective of whether she is a basic, higher or additional rate taxpayer.

Her dividend income of £2,300 is therefore taxable at 0%.

(N4) HIBC income

Although Sarah's UK interest and dividend income is taxable at 0% for income tax purposes, it is still counted as income when establishing her net income for the HIBC.

2)

If Sarah pays her Income Tax late, she will be subject to penalties.

The first penalty is charged where tax due is paid more than 30 days after the payment due date and is levied at the rate of 5%. (1/2)

This results in a penalty of £646 x 5% = £32. (1/2)

There is a second penalty charge, a further 5%, if Sarah has still not paid the tax due more than 5 months after the first penalty has been levied. (1/2)

So Sarah will have a further penalty of £32, making total penalties due of £64. (1/2)

3)

The two factors required to make the clause enforceable are:

- the employer has a legitimate business interest to protect, (1) and
- the restrictions in the covenants are reasonable in terms of the length of time they apply and the geographic area covered. (1)

ANSWER Q2

Sanjay pension contributions – draft letter

1)

Client's address (1 mark for presentation)

Our address

Date

Dear Sanjay

Congratulations on your promotion to the Head of Sales at Hutton Ltd. You have queried whether you can pay your full £30,000 bonus in 2017/18 into your pension and what the tax implications will be if you do this.

Method of obtaining tax relief

If you were to pay your £30,000 bonus into your pension, you would receive tax relief via the payroll. This means Hutton Ltd would take your total pay for 2017/18 of (£70,000 + £30,000) and deduct your additional £30,000 contribution, (1/2) as well as your regular annual contribution of £13,000, (1/2) from your salary before you pay tax. (1/2) As a higher rate taxpayer, this means you automatically get 40% tax relief on your pension contributions in the year. (1/2)

However, there are a couple of things we need to check to ensure you are entitled to full tax relief on your pension contributions.

Amount of available relief

Firstly, there is a maximum contribution to a pension fund that an individual can obtain tax relief for in any one tax year, which is 100% of their "relevant earnings" for that year. (1/2) Relevant earnings include your salary and the cash equivalent of any benefits you receive from your employer. (1/2) Whilst you do not receive any benefits from Hutton Ltd, you clearly have sufficient relevant earnings (1/2) to make total personal pension contributions of (£30,000 + £13,000) = £43,000 in 2017/18.

There are also other items that can be included as relevant earnings, such as profits from a furnished holiday letting, (1/2) and please let me know if you want more details on what other items qualify.

The annual allowance

Secondly, there is an annual allowance for 2017/18 of £40,000 (1/2) and, if this is exceeded, the excess is charged to income tax at your marginal rate. (1/2) Whilst the contributions by Hutton Ltd are a tax-free benefit, (1/2) the annual allowance takes into account both your own and Hutton Ltd's pension contributions in a tax year. (1/2)

You will see in Appendix 1 that, on the face of it, you will exceed the annual allowance by £8,000 (1/2) for 2017/18. However, your annual allowance can be increased by any unused annual allowance for the previous three tax years. (1/2)

When calculating the amount of any unused annual allowance, it is important to note that the current year's annual allowance is deemed to be used first. (1/2) Then any unused allowances from the previous three years are utilised on a "first in, first out" basis, (1/2) which means any unused allowance from 2014/15 will be used first as you will be fully utilising your £40,000 allowance for 2017/18. (1/2)

As you will see in Appendix 2, you have an unused allowance to carry forward from 2014/15 of £24,000. Appendix 3 shows you how this will be set against the excess pension contributions in 2017/18, which means you will not be subject to any excess charge. (1/2)

However, the remaining unused amount carried forward from 2014/15 will not be able to be carried forward to 2018/19. (1/2) For 2018/19, you will have the unused annual allowance amounts brought forward from 2015/16 and 2016/17, as you paid less than £40,000 into your pension in each of these tax years. (1/2)

If you need any further information, please let me know.

Yours sincerely

A Manager

(Maximum 12 marks)

Appendix 1

2017/18

	<u>£</u>
Hutton Ltd pension contribution	5,000
Bonus	30,000
Regular annual amount	<u>13,000</u>
Gross pension contributions in 2017/18	48,000
Less:	
Annual allowance for 2017/18	<u>(40,000)</u>
Excess pension contributions in 2017/18	8,000

Appendix 2

2014/15

		<u>£</u>
Hutton Ltd pension contribution		5,000
Regular annual amount		<u>11,000</u>
Gross pension contributions in 2014/15	(1/2)	16,000
Less:		
Annual allowance		<u>(40,000)</u>
Unused allowance to carry forward	(1/2)	24,000

Appendix 3

		£
Unused allowance brought forward from 2014/15		24,000
Less:		
Excess pension contributions in 2017/18	(1/2)	<u>(8,000)</u>
Unused allowance from 2014/15 remaining		16,000

Note

Credit is also available for stating that the employer could make a pension contribution of £30,000 rather than paying a bonus.

(Max 12 marks)

2)

An ATT member should keep a proper professional record of all dealings with clients in order that:

- the member and colleagues/successors can gain access to a complete record of the client's history. This is important to inform future client service. (1)
- the member is able to resolve any misunderstandings/complaints, for example with regard to fees. (1)
- the member is able to defend themselves in the event of any allegation of negligence. (1)

ANSWER Q3

1)

a) PPR complications

PPR can exempt the gain that arises on the disposal of your home from tax. In your circumstances, the complications that could prevent full relief being available are:

1. Size of grounds

PPR relief will normally only apply to grounds of up to ½ hectare (½); therefore the capital gain applicable to the additional ½ hectare of land may be exposed to CGT (½). However, HM Revenue & Customs may accept that a larger area can be included within PPR relief if the additional grounds are required for the “reasonable enjoyment” (½) of the property.

2. Not occupying immediately

PPR relief applies to the extent that the property is actually occupied or deemed to be occupied (½). The initial non-occupation could therefore expose some of the gain to CGT (½). However, there is an Extra Statutory Concession (ESC D49) that allows you a period of absence from the property of up to 12 months when you first buy the property (½). As your period of absence is 18 months there may still be some exposure to CGT (½) although HM Revenue & Customs can allow a period of absence of up to 2 years (½) where there are good reasons that are outside of your control (½).

3. Absence from property whilst in Newcastle

PPR relief is available for periods of actual and deemed occupation. Deemed occupation includes a period of absence of up to 4 years whilst working elsewhere in the UK (½) – this includes both employment and self-employment (½) - and up to 3 years for any other reason (½). These two periods can be combined to secure deemed occupation for the period from July 2000 to July 2007 (½). The gain arising in the period from July 2007 until your return to the property in July 2010 will be exposed to CGT (½).

4. No other property qualifying for relief

Deemed periods of occupation are only available if there is no other residence eligible for relief (½). The let flat in Newcastle could qualify as a residence eligible for relief even though you do not own it (½); HM Revenue & Customs rarely take the point but it would be advisable to elect your Exeter property to be your main residence (½) to avoid this potential problem. The normal deadline for making such an election is two years from when the 2nd residence was acquired (½) but ESC D21 allows this deadline to be extended where the interest in one of the residences is of negligible capital value and the taxpayer is unaware that an election could be made (½).

(Max 6 marks)

b) Protection for commercial premises

The Landlord and Tenant Act 1954 provides that:

- A business tenancy does not end when a fixed term runs out (½) or the landlord serves a notice to quit, (½) but the tenancy continues on the terms of the lease (½), and
- The tenant has the right to a new lease (½).

A landlord who wants to bring a business tenancy to an end, other than by forfeiture, generally has to follow a statutory notice procedure (½).

A tenant who wants a new tenancy can apply to the court against the statutory notice (½). The court must generally grant the new tenancy (½) on substantially the same terms as the old one (½) unless the landlord can establish one of the stated grounds of opposition (½).

(Max 3 marks)

Scots law

Even when the term of the lease comes to an end, the tenant is not required to leave unless the landlord serves a notice to quit. (1)

If a notice to quit is not served, the lease continues for one further year on the same terms and conditions as before. (1)

None of the statutory provisions which give security to tenants under English legislation relating to business tenancies have any application in Scotland. (1) The only leases in Scots law which now provide such security to a commercial tenant are a limited class of shops under the Tenancy of Shops Act 1949. (1)

(Max 3 marks)

2) CGT calculation

Proceeds	£	£	
		1,600,000	(½)
Cost	200,000		
Conversion costs	<u>145,000</u>		
		<u>(345,000)</u>	(½)
Capital gain		1,255,000	
PPR relief	(12.5 + 8.5)/24 x 1,255,000	<u>(1,098,125)</u>	(1)
Chargeable gain		156,875	
Less: Annual exempt amount		<u>(11,100)</u>	(½)
Taxable gain		<u>145,755</u>	
CGT @ 28%		<u>40,817</u>	(½)

		Actual occupation Years	Deemed occupation Years	Absence Years	
July 1992 – Jan 1994	Extension of ESC D49		1.5		(½)
Jan 1994 – July 2000		6.5			(½)
July 2000 – July 2004	Working elsewhere in UK		4.0		(½)
July 2004 – July 2007	Absence for any reason		3.0		(½)
July 2007 – July 2010				3.0	(½)
July 2010 – July 2016		6.0			(½)
		<u>12.5</u>	<u>8.5</u>	<u>3.0</u>	

(6 marks)

ANSWER Q4

To: Jennifer.client@hitmail.com

From: candidate@examroom.co.uk

Subject: Exposure to UK taxes (**layout – ½**)

Jennifer

I understand that you would like me to explain how you acquire a domicile of origin and a domicile of choice and the bases on which you are currently subject to Income Tax and Capital Gains Tax on your UK properties and the shareholding in Emerald Ltd. I will also explain how this would change if you were to become non-UK resident.

Domicile

From a UK perspective, everyone is born with a domicile of origin – this is derived from your father (½) if your parents were married (½) or from your mother if not (½). If you move to another country (½) and form an intention to reside there permanently or indefinitely (½) you will obtain a domicile of choice in that other country (½) which overrides your domicile of origin (½).

(Max 3 marks)

Tax exposure whilst UK resident and non-UK domiciled

Currently, you are subject to Income Tax at 45% (½) on the net rental income that arises (½) from your UK rental property in the year, calculated on the accruals basis (½). Equally you are subject to Capital Gains Tax at 28% (½) on any gain that arises (½) on the disposal of property in the year, with the timing of the disposal being dictated by the date of exchange (½).

You are only subject to Income Tax on the dividends from your overseas shareholding or gains from the disposal of the shareholding if the income and/or gains are remitted to the UK (½ : ½). Remitted gains will be taxed at 20% (½) and remitted dividends at 45% (½).

Tax exposure whilst non-UK resident

You will remain subject to Income Tax and Capital Gains Tax on the net rental income and capital gains arising from your UK residential property (½ : ½).

You will have no exposure to either Income Tax or Capital Gains Tax on your non-UK shareholding (½ : ½).

I hope that this answers your queries. Please let me know if I can be of further assistance.

Kind regards

T. Adviser

(Max 10 marks)