

THE ASSOCIATION OF TAXATION TECHNICIANS

ATT PAPER 2 BUSINESS TAXATION

May 2022

TIME ALLOWED

3 HOURS 30 MINUTES

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

PART I

1. Rachvik started trading on 1 July 2021 and prepared accounts for the nine months to 31 March 2022. Rachvik uses the cash basis for tax purposes. He is not VAT registered. Rachvik has provided the following information for the nine-month period:

	£
Total amount invoiced to customers	66,000
Invoices unpaid by customers at 31 March 2022	4,300
Payments to suppliers	26,000
Payment to buy machinery	8,500
Interest paid on bank loan to buy machinery	700
Payment to a restaurant for entertaining a potential supplier	140
Payments to lease a car (CO ₂ 145g/km) used 100% for business	2,500
Rent for six months paid on 1 July 2021	3,000
Rent for six months paid on 1 January 2022	3,000

Calculate Rachvik’s tax adjusted trading profit for the nine months ended 31 March 2022. (4)

2. Bayley owns a manufacturing business and prepares accounts to 31 March 2022. He bought the following assets in December 2021:

- 1) A van costing £22,800 with emissions of 165g/km.
- 2) A new car costing £14,000 with zero emissions. This car is used by an employee and the proportion of private use is 20%.
- 3) A new car costing £23,000 with emissions of 145g/km. This car is used by Bayley and the private use is 70%.

The tax written down value of the general pool at 1 April 2021 was £30,000. All costs are stated inclusive of VAT. Bayley is VAT registered.

Calculate the maximum capital allowances for the year ended 31 March 2022. Show all tax written down values carried forward at 31 March 2022. (4)

3. Kev is a self-employed project manager and now works exclusively for Ridly Ltd. He invoices for hours worked each month and is paid a few days later.

Kev works on whichever projects he is allocated by Ridly Ltd and has to complete them in line with the schedules he is given.

Kev cannot send anyone else to do his work. It is a specialised role and he has had to undertake some training paid for by Ridly Ltd. Kev has not been asked to reimburse Ridly Ltd for the loss of revenue they incurred when he forgot to invoice a client for additional work.

Explain the factors that indicate that Kev should be treated as an employee for tax purposes. (4)

4. Jason submitted his 2019/20 self-assessment tax return on 15 March 2021. HMRC opened an enquiry into this return on 1 April 2022. HMRC issued an amendment to the tax return on 1 May 2022 and require him to pay an additional £6,000 of Income Tax. Jason believes that the enquiry was opened after the deadline for doing so had passed, and that the amount of the amendment is incorrect.

Briefly explain if the enquiry was opened within the correct time limit and how Jason should make an appeal against the amendment. (2)

5. Megan lives with her civil partner in a flat within her business premises, a guesthouse. Megan wants to know how much of the total electricity and food costs she can deduct from her tax adjusted trading profit.

Explain how Megan can use the fixed rate expenses rule to calculate the tax adjustment to trading profits for the year ended 31 March 2022. (3)

6. Carbis Ltd has the following recent results:

	<u>Year ended</u> <u>31 March</u> <u>2018</u> £	<u>Year ended</u> <u>31 March</u> <u>2019</u> £	<u>Year ended</u> <u>31 March</u> <u>2020</u> £	<u>Year ended</u> <u>31 March</u> <u>2021</u> £	<u>Year ended</u> <u>31 March</u> <u>2022</u> £
Trade profits/(loss)	28,000	32,000	47,000	(135,000)	15,000
Non-trading loan relationships	3,000	3,000	3,000	3,000	3,000
Chargeable gain/(loss)	(10,000)		8,000		
Donation to charity	(1,000)	(1,000)	(1,500)	(500)	(1,000)

The company claims loss relief as soon as possible.

Calculate the taxable total profits for each year, showing clearly the use of the trading loss. State any amounts unrelieved at 1 April 2022. (4)

7. Sage Ltd prepared accounts for the year ended 31 March 2020. HMRC served the company a notice to file a tax return for this period on 10 February 2021. Sage Ltd then changed its accounting date and prepared accounts for a 16-month period ended 31 July 2021. Sage Ltd was served notices to file the tax returns for this period on 25 August 2021.

Explain the dates by which Sage Ltd must file its Corporation Tax returns for all accounting periods between 1 April 2019 and 31 July 2021. (3)

8. Helix Ltd had the following interest income and expenditure during the year ended 31 December 2021.

	£
Interest payable on loan to buy plant for use in its trade	4,800
Bank overdraft interest	1,300
Interest payable on late payment of Corporation Tax	450
Interest receivable on loan to an employee	200
Debenture interest receivable	8,000
Interest payable on loan to buy an investment property	6,000
Costs of securing the loan to buy the investment property	1,000

Explain how each item of interest income and expenditure is treated for Corporation Tax purposes. (4)

9. Evos Ltd sold a warehouse for £500,000 on 30 November 2021. Evos Ltd had bought the warehouse for £270,000 on 30 November 2011. For the whole period of ownership, Evos Ltd had used 80% of the warehouse in the business and had rented out the remaining 20%. Evos Ltd bought a new freehold warehouse in September 2021 for £350,000. Evos Ltd uses all of the new warehouse in the business.

Calculate the chargeable gain after reliefs on the sale of the warehouse. (3)

10. Esther bought a freehold property for £120,000 on 30 June 2011, for use in her business. In January 2019, Esther spent £12,000 on repairs to the roof following wind damage.

In November 2021, Esther granted a 25-year lease on the property to Freeda. Freeda paid a premium of £90,000. The freehold reversion was valued at £200,000 in November 2021. Esther incurred legal fees of £4,000 on the grant of the lease. Esther spent £5,600 on redecoration of the property prior to granting the lease.

Calculate the chargeable gain arising on the grant of the lease. State the treatment of each item of cost incurred by Esther. (4)

11. Khubaib sold a painting in October 2021 for £110,000, realising a gain of £75,000. Khubaib used £60,000 of the proceeds to subscribe for qualifying EIS shares in January 2022. Khubaib sold no other chargeable assets during 2021/22. He has capital losses brought forward at 6 April 2021 of £5,000.

Explain the optimal amount of reinvestment relief that Khubaib should claim for 2021/22. (2)

12. Jeraldine, a VAT registered sole trader, ordered garden furniture for resale costing £12,000 (inclusive of VAT at the standard rate). She paid a deposit of £3,000 plus VAT on 10 November 2021. The furniture was delivered on 28 March 2022. She received an invoice for the furniture dated 3 April 2022 and paid the balance owing on 30 April 2022.

Explain when Jeraldine must account for the VAT on the purchase of the garden furniture and state the relevant VAT amounts. (3)

PART II

13. Tarias Ltd is an engineering company with no related 51% group companies. It has been trading for many years, preparing accounts to 31 March each year.

You have been provided with the following draft profit and loss account for the year ended 31 March 2022:

	£	£
Sales		1,350,000
Cost of sales		<u>(685,000)</u>
Gross profit		665,000
Rent, rates and utility expenses	47,000	
Staff costs	186,000	
Administration costs	18,450	
Motor and travel expenses	23,000	
Legal and professional fees	13,900	
Interest costs	3,500	
Depreciation	<u>7,400</u>	
		<u>(299,250)</u>
Net profit before taxation		<u>365,750</u>

In addition, you are provided with the following information:

- (a) Staff costs include bonuses of £17,000 and pension contributions of £2,300 for March 2022, both paid on 10 April 2022.
- (b) Administration costs include a suit bought for a director for £450.
- (c) Motor and travel expenses include £1,050 for football tickets for nine customers and £350 for concert tickets for three staff.
- (d) Legal and professional fees are analysed as follows:

	£
Accountancy costs	5,400
Debt collection costs	6,100
Legal costs for new office lease	<u>2,400</u>
	<u>13,900</u>

- (e) Interest costs of £2,300 relate to assets leased on finance leases.
- (f) Depreciation includes £2,300 for assets leased on finance leases.
- (g) During the year, the company renovated a disused warehouse and fitted it out to use as a workshop. The following costs were incurred and capitalised in the accounts:

<u>Date</u>		£
August 2021	Cost of additional land	75,000
September 2021	Legal and planning fees	7,600
October 2021	Demolition costs	9,600
November 2021	Construction costs	160,000
December 2021	Laser cutter (bought second hand)	50,000
December 2021	Electrical and water systems	8,375
February 2022	Computer equipment (new)	15,000

The estimated useful life of the laser cutter is 20 years. The workshop was first used on 1 March 2022.

Continued

- (h) The balances brought forward at 1 April 2021 on the general pool and the special rate pool were £14,000 and £6,780 respectively.

Since the year end, the accountant at Tarias Ltd went on sick leave and their assistant has asked how to record the disposal of a car in April 2022. The cost of the car was £8,000 and the depreciation to the date of disposal was £4,500. The car was sold for £2,500.

Requirements:

- 1) Calculate the taxable total profits for the year ended 31 March 2022. Show your treatment of items (a) to (g) above. Ignore VAT. (15)
- 2) Show the journal entries to record the sale of the car. (3)
- Total (18)

14. Sadiq, Anya and John have been trading in partnership as planning consultants for many years preparing accounts to 31 December each year.

Profits and losses were shared 50:30:20 (Sadiq, Anya, John) after allowing interest of 8% per annum on capital of £245,000 contributed by Sadiq.

From 1 April 2021, no further interest is provided on capital accounts. Profits and losses are shared 50:40:10 (Sadiq, Anya, John) after allowing for a salary of £50,000 per annum for John.

The partnership normally makes a profit. However, due to problems with a large contract there was a tax adjusted loss for the year ended 31 December 2021 of £85,000. The partnership expects a return to profit for the year ended 31 December 2022.

Sadiq has other income each year from property and dividends.

In November 2021, the partners had a meeting to discuss the potential loss for the year. They disagreed about the strategy to follow going forward. Sadiq wanted to invest in staff and resources to expand the business, but John wanted to make no changes. At the end of December, Sadiq recruited a new employee Tina. John was unaware of the appointment and is unhappy with this and other decisions taken by Sadiq. Sadiq has concerns about John's abilities as a partner. They have both approached your firm for advice.

Requirements:

- 1) Calculate the allocation of the loss for the year ended 31 December 2021 to the three partners. (4)
- 2) Explain the loss relief claims available to Sadiq and any restrictions, assuming no carry forward claims are made. Calculations are not required. (4)
- 3) Explain whether the partnership is bound by Sadiq's decision to employ Tina. (3)
- 4) Explain the options available to your firm to advise John and Sadiq in accordance with the Professional Rules and Practice Guidelines of the ATT. (4)

Total (15)

15. Sasha is the sole director and shareholder of Sashenka Ltd which has traded since 1985 as a design consultancy.

The company's only chargeable asset is an office purchased for £75,000 in 1990.

The company also operates from a high street shop, which is owned by Sasha. Sasha has charged the company rent at 50% of the market value from the date she bought the shop in April 2000.

Sasha has been approached by Telstet Ltd with two options:

- (a) Sasha can sell the shares in Sashenka Ltd to Telstet Ltd for £300,000. The shares cost £100 when she started the company; or
- (b) Sashenka Ltd can sell the office for £250,000.

Whichever option Sasha chooses, Telstet Ltd will also buy the shop from Sasha giving her a gain of £50,000.

Although Sasha sometimes sells capital assets for gains and losses, she has not made any previous gains which qualified for business asset disposal relief.

Requirement:

Write a letter to Sasha in which you explain the gains implications for Sasha and Sashenka Ltd of the disposals above. No computations are required.

(12)

16. Robert commenced trading as a software developer on 1 February 2020. He prepared his first set of accounts to 30 April 2021 using the accruals basis. His draft accounting profit for the 15 months of trading was £36,000.

You are given the following additional information:

- (a) Expenses claimed include 15 months of Robert's home broadband connection. The monthly cost is £48 and he estimates that there is 70% business use.
- (b) Travel costs include rail tickets totalling £2,875 in respect of travel from his home to an office where he has a contract to work on site for three days per month.
- (c) Before he started trading he incurred the following costs which have not been deducted in the accounts:

	<u>Notes</u>	£
Training costs	(i)	2,600
Repairs to garden office	(ii)	4,600
Website development	(iii)	1,200
Computer equipment	(iv)	6,000

- (i) The training costs were the cost of two courses for Robert to become an accredited software engineer.
- (ii) He had been using a building in his garden as an office for some time, but in order to make it more presentable to customers in online meetings he replaced the door and windows and repainted the inside.
- (iii) The website is used to promote his business and is expected to last for three years.
- (iv) The computer equipment had a cost of £6,000 when Robert bought it in January 2019. The market value at 1 February 2020 was £5,400.

Robert's turnover for the 12 months to 30 April 2022 was £75,000. He expects his turnover to continue to increase slowly. He is also a 50% shareholder in a company with Jaime selling computer parts, which has an annual turnover of £25,000. The company is not VAT registered.

Robert has asked whether he will be able to recover the VAT on office equipment bought in January 2022.

Requirements:

- 1) **Calculate Robert's assessable profit for 2019/20, 2020/21 and 2021/22, showing clearly the basis periods and any overlap profits arising. Show your treatment of items (a) to (c) above. Ignore VAT.** (8)
- 2) **Explain when Robert will be required to register for VAT. Explain whether he can then recover VAT on the office equipment purchased in January 2022.** (4)
- 3) **Explain the National Insurance contributions Robert is liable for in respect of his business for 2019/20 and any options available. Calculations are not required.** (3)

Total (15)