PAPER 1

Personal Taxation

Part I Suggested Answers

1. Land sold by non-UK resident

The “default method” will be applied to the disposal of the plot of land by Hugo. **(½)**

The plot of land will be valued at 5 April 2019 **(½)** and so the chargeable gain is the difference between the sale proceeds **(½)** and the value at 5 April 2019. **(½)**

However, Hugo can elect **(½)** for the “retrospective method” to apply. **(½)** This would mean the gain would be calculated by deducting the original cost in June 2017 **(½)** from the sale proceeds. **(½)** This means the whole gain is chargeable. **(½)**

There is no option for Hugo to elect for the “time apportionment method”. **(½)**

Maximum 4 marks

2. CSOP

If Shaun exercises the option in November 2020 ie within 3 years of being granted the option, a charge to income tax will arise **(½).** The amount subject to income tax will be the market value of the shares at exercise **(½)** less the amount paid for the shares. **(½)**

The shares are readily convertible assets, **(½)** so exercising the shares before three years will also result in them being subject to class 1 NIC. **(½)**

There are no income tax implications for Shaun if he exercises the option after three years ie in December 2020, **(½)** nor will there be any NIC implications. **(½)**

Maximum 3 marks

3. ER

Salim – CGT for 2019/20:

	£	£
Gains qualifying for ER (W1)	1,000,000	
Gains not qualifying for ER (W2)		500,000
Less:		
Annual exempt amount		(12,000) **(½)**
Chargeable gains	1,000,000	488,000

CGT:

1,000,000 @ 10%	100,000 **(½)**
488,000 @ 20%	97,600 **(½)**
	197,600 **(½)**

(W1)

Lifetime limit remaining = £10,000,000 - £9,000,000 = £1,000,000 **(½)**

(W2)

Gain not qualifying for ER = £1,500,000 - £1,000,000 = £500,000 **(½)**

3 marks

4. Jack's FHLs

Rose House can be treated as a furnished holiday letting as it is:

- Furnished. **(½)**
- In the UK. **(½)**
- Available for commercial letting as holiday accommodation to the public for at least 210 days **(½)** in the relevant 12 month period (this is usually the tax year). **(½)**
- Actually let out for at least 105 days as holiday accommodation. **(½)**

Lily Cottage cannot be treated as a furnished holiday letting as it is let for a continuous period of more than 31 days to the same person, **(½)** and the total of such longer-term occupation exceeds 155 days. **(½)**

Brynn's Cottage does not fulfil the condition for actual let days at least 105. However an election can be made to average this with Rose House days**(½)**. The average of 133 days ((170 + 96)/2) **(½)** is at least 105 days so Brynn's Cottage can also be treated as a furnished holiday letting.

Maximum 4 marks

5. No Gain No Loss transfer

There is a disposal by Anne for CGT purposes, **(½)** but as it is to her civil partner, it is deemed to take place at "no gain no loss". **(½)**

As such, Anne's capital gain will be zero, **(½)** even though the shares have gone up in value.

For CGT purposes, Sarah is deemed to have paid Anne £12,000 for the shares **(½)**, which is the price Anne paid for them. **(½)** When Sarah comes to sell the shares, this will be her base cost for CGT purposes. **(½)**

3 marks

6. Harriet - Gain on home

	£	£	
Gain		247,500	
Less PPR relief £247,500 × 8.5/11		<u>(191,250)</u>	**(½)**
		56,250	
Less letting relief			

Lowest of			(½)
• the amount of PPR relief	191,250		(½)
• the gain arising during the period when the property was let out	56,250		(½)
• the maximum amount of lettings relief	40,000		(½)
		(40,000)	
Chargeable gain		16,250	(½)

3 marks

7. Jane

Jane's income tax calculation for 2019/20:

	£
Non-savings income	34,200
Less:	
Personal allowance	(12,500) (½)
Total	21,700
Tax due:	
21,700 @ 20%	4,340 (½)
Less: MCA (W1)	
(8,915 – 2,300) = 6,615 (½) @ 10% (½)	(662) (½)
Income tax liability	3,678 (½)

(W1) Married couples allowance (MCA)

MCA restricted as above threshold of £29,600:

34,200 - 29,600 = 4,600 (½)

4,600 / 2 = 2,300 (½)

4 marks

8. Xander

	£
Loan at the start of the year	50,000 (½)
Plus:	
Loan at the end of the year	30,000 (½)
Total	80,000

Taxable benefit = (80,000 / 2) (½)
= 40,000 x 2.5% (½) (official rate of interest)
= **1,000**

2 marks

9. Amelie

Amelie's taxable income for 2019/20:

	Non-Savings	Savings	Dividends
	£	£	£
Discretionary trust (W1)	10,000 (½)		
Trust income:			
Interest (W2)		12,500 (½)	
Dividends (W3)			4,324 (½)
Less: Personal allowance (1)	(10,000)	(2,500)	
Taxable income	0	10,000	4,324

(W1) £5,500 x 100/55 = £10,000 (½)

(W2) £10,000 x 100/80 = £12,500 (½)

(W3) £4,000 x 100/92.5 = £4,324 (½)

4 marks

10. Split year treatment

The 2019/20 tax year is split for Sharon under the statutory residence test. **(½)**

She is present in the UK for at least 183 days and so is UK resident for 2019/20 **(½)**. However, the split year treatment applies as she has ceased full-time work overseas (Case 6) and returned to the UK **(½)**.

To 30 September 2019, Sharon is taxed in the UK as a non-UK resident individual **(½)** ie taxed on just her UK income.

From 1 October 2019, Sharon is taxed in the UK as a UK resident individual **(½)** ie taxed on her worldwide income.

Therefore Sharon will be subject to Income Tax on:

- her UK salary of £35,000 **(½)**
- total UK dividends of £1,250 (£600 + £650) **(½)**
- Brazilian dividends from 1 October 2019 of £100 **(½)**

4 marks

11. Jock

Jock's property income for 2019/20:

	£
Premium	60,000
Less:	
2% x 60,000 x (25-1) **(2 x 1/2 marks for calculation)**	(28,800)
	31,200 **(½)**
Plus:	
Rent received	3,000 **(½)**
Net property income	34,200 **(½)**
Less:	
Property allowance	(1,000) **(1)**
Total property income	33,200

Maximum 3 marks

12. Disengagement letter

Any three of the following points that a disengagement letter should usually address:

- A summary of services provided up to the date Gianni ceases to act; **(1)**
- A note of any further action to be taken by Gianni; **(1)**
- A note of any outstanding matters that either the ex-client or the new advisers will need to address; **(1)**
- Details of any impending deadlines and the action required; **(1)**
- How willing Gianni would be assist the new advisers to resolve outstanding issues with HMRC or provide copy papers to the new advisers; **(1)**
- Details of any outstanding fees; and **(1)**
- A note of who will advise HMRC of the change that has taken place, being either Gianni or the new adviser. **(1)**

Maximum 3 marks

PAPER 1

Personal Taxation

Part II Suggested Answers

13. JEMMA CHAPMAN

1) Income tax computation – 2019/20

	Total income	Non-savings income	Savings income	Dividend income	
	£	£	£	£	
Employment income (W1)	78,604	78,604			W
Building society interest	1,390		1,390		½
UK dividends	250			250	½
Overseas dividends (£2,310 x 100/88)	2,625			2,625	½
Total income	82,869	78,604	1,390	2,875	
Less: PA	(12,500)	(12,500)			½
Taxable income	70,369	66,104	1,390	2,875	

Income tax:	£		£	
Non-savings income – Basic rate	37,500	× 20%	7,500	
Non-savings income – Higher rate	28,604	× 40%	11,442	½
	66,104			
Savings income – Nil rate band	500	× 0%	0	
– Higher rate	890	× 40%	356	½
Dividend income – Nil rate band	2,000	× 0%	0	
– Higher rate	875	× 32.5%	284	½
	70,369			
			19,582	
Less: Double taxation relief (W4)			(284)	½
Income tax liability			19,298	

Tutorial note:

The income tax liability is required, not the income tax payable.

By definition, income tax liability is after deducting DTR. However, there is no credit for deducting the PAYE given in the question.

Class 1 primary contributions – payable by Jemma

Payable on cash earnings of £62,128

ie salary of £61,000 plus private mileage of £1,128 ((17,900 – 15,215) x 42p) ½

	£	
(£50,000 – £8,632) × 12%	4,964	1
(£62,128 – £50,000) × 2%	243	½
Class 1 primary NICs	5,207	

Tutorial note:

Benefits are not assessed to Class 1 NICs.

There are no allowable deductions in the calculation of Class 1 NICs (i.e. cannot deduct pension contributions).

Workings

(W1) Employment income

	£	£	
Salary		61,000	½
Less: Occupational pension contributions			
(5% x £61,000)		(3,050)	½
		57,950	
Benefits:			
Employer pension contributions	Exempt		½
Use of own car (W2)	1,714		W
Living accommodation (Note)			
– Annual value	10,150		½
– Additional yearly rent benefit (W3)	8,790		W
		20,654	
Employment income		78,604	

Tutorial note:

Jemma (not the employer) provides her own furniture in the flat and pays the expenses relating to the flat, therefore there are no employment benefits for the use of furniture nor the expenses of the flat.

(W2) Use of own car

Jemma was paid for 17,900 miles, of which 15,215 (17,900 x 85%) are for business. ½

		£	£	
Mileage allowance received (17,900 x 42p)			7,518	½
Less: ITEPA mileage rates				
	10,000 x 45p	4,500		½
	5,215 x 25p	1,304		½
	15,215		(5,804)	
	======			
Benefit			1,714	

(W3) Additional yearly rent benefit

	£	
Original cost (October 2013)	409,900	½
Capital improvement (February 2014)	16,700	½
'Cost of property' (Note)	426,600	
Less: Limit	(75,000)	½
	351,600	
Benefit (£351,600 x 2.5%)	8,790	½

Tutorial note:

The company purchased the accommodation less than six years before Jemma moved in. Accordingly, the 'cost of the property' up to the beginning of the tax year (6.4.2019) is used to calculate the benefit. The market value when she moved in is not relevant.

(W4) Double taxation relief – Unilateral relief

	£	£	
Overseas dividends			
Lower of:			
(i) Overseas tax suffered (£2,625 – £2,310)	315		½
(ii) UK tax suffered (£875 x 32.5%)	284	284	½

Tutorial note:

In the absence of a DTR treaty agreement, relief is given under the unilateral provisions.

The UK tax suffered on the source of income is the reduction in the total income tax liability as a result of removing the overseas source of income from the computation.

2) Grace Chapman – Property income

	£	£	
Rent received			
(£1,620 × 8 months) + (£1,760 × 4 months) (Note 1)		20,000	1
Agency fees (7% × £20,000)	1,400		½
Loan interest (£7,440 × 25%) (Note 2)	1,860		1
Insurance	1,120		½
		(4,380)	
Property income		15,620	

Tutorial note:

1. *The default basis of assessment for property income is the cash basis.*

   Grace received rent in advance on the first day of the month, therefore if the rent changed on 1 January 2020, Grace will have received:

– *Rent at the old rate from 1 May to 1 December 2019 inclusive*

(i.e. 8 months), and

– *Rent at the new rate on 1 January to 1 April 2020 inclusive (i.e. 4 months).*

2. *Mortgage interest on a buy-to-let property is tax allowable but in 2019/20 the transitional provisions apply. 25% of the interest is allowable as a deduction in the property income computation. The remaining 75% can only obtain basic rate relief and therefore £1,116 (£7,440 x 75% x 20%) can be deducted in Grace's income tax liability computation.*

3) Lasting power of attorney

A lasting power of attorney (LPA), introduced by the Mental Capacity Act 2005, is a power created by a person (the donor) and given to another person (the donee or attorney) so that the attorney can act in law as agent of the donor. **(½)**

An LPA gives the attorney authority to make decisions (defined in the terms of the LPA) on behalf of the donor **(½)** including situations where the donor no longer has capacity to act on their own behalf. **(½)**

For example, decisions in relation to the donor's:

- personal welfare,
- property, and
- financial affairs. **(½)**

- The legal instrument must include:
  - two statements by the donor:
    - that they have read the document,**(½)** and intend the authority granted to be exercised when they no longer have capacity **(½)**; and
    - the name of the person to be notified in the event the LPA is registered) **(½)**
  - a statement by the donee (the person given the power of attorney):
    - that they have read the document, **(½)** and
    - understand the duties imposed **(½)**
  - an LPA certificate made (and signed) by the donor **(½)** confirming they understand the purpose and scope of the power **(½)** and that it has been created without duress. **(½)**
  - signatures of the donor and the donee **(½)** made in the presence of a witnesses. **(½)**

Maximum 4 marks

14.

		£	£
George Ltd £1 Ordinary shares			
Proceeds		1,100,000 **(½)**	
Cost	(W1)	(312,500) **(½)**	
			787,500
Manu Ltd £10 Ordinary shares			
Gain realised on £1m of the investment **(½)**, i.e. on 100,000 shares, is not chargeable **(½)**			
Chargeable proceeds	20,000/120,000 x £5m **(½)**	833,333	
Cost	20,000 x £10 **(½)**	(200,000)	
			633,333
Land – 1st sale			
Proceeds		260,000 **(½)**	
Cost	(W2)	(97,307) **(½)**	
Legal costs		(10,000) **(½)**	
			152,693
Land – 2nd sale			
Disposal date for conditional contract is date on which condition is met - so this is a 2020/21 disposal **(½ – for excluding from calculation and ½ for flagging exclusion)**			
Loan stock **(½ - recognise chargeable)**			
Proceeds	\$410,000 / 1.25	328,000 **(½)**	
Cost	(W3)	(291,282) **(½)**	
			36,718
Loan to Eddie			
A simple debt is not a chargeable asset **(½ – for excluding from calculation and ½ for flagging exclusion)**			-
2nd hand loan to Eddie **(½ - recognise chargeable)**			
Proceeds		15,000 **(½)**	
Cost		(12,000) **(½)**	
			3,000
Statue			
Insurance proceeds			
Insurance receipt		25,000 **(½)**	
Cost – A/(A+B) x acquisition cost **(½)**	25,000/(25,000 + 50,000) x 40,000 **(1)**	(13,333)	
			11,667
Sale			
Proceeds		80,000 **(½)**	
Cost	40,000 – 13,333 **(½)** + 16,000 **(½)**	(42,667)	
			37,333
Net capital gains			1,662,244
Annual exempt amount			(12,000) **(½)**
Taxable gain			1,650,244

W1 George Ltd

Date		Nominal	£
March 2016	Purchase @ £5 each	25,000	125,000 (½)
June 2018	Purchase @ £10 each	35,000	350,000 (½)
		60,000	475,000
January 2019	Bonus issue 2 for 3	40,000 (½)	- (½)
		100,000	475,000
September 2019	Rights issue 1 for 10 @ £15	10,000 (½)	150,000 (½)
		110,000	625,000
March 2020	Disposal	(55,000)	(312,500) (½)
		55,000	312,500

W2 Land – 1st sale

Probate value	£9,000 x 42		378,000 (½)
Cost of 14 acres sold	A/(A + B) (½)	378,000 x (260,000/(260,000 + 750,000)) (1)	97,307

W3 Loan stock

Date		Nominal	£
May 2015	$200,000 / 1.5	$200,000	133,333 (½)
June 2018	$300,000 / 1.3	$300,000	230,769 (½)
		$500,000	364,102
		($400,000)	(291,282) (½)
		$100,000	72,820

[Max: 20 marks]

15.

Our Address

Your address

Date

[Format **(1)**]

Dear Maria

Penalties for non-compliance

Thank you for your letter.

I understand that you would like me to explain the financial penalties that you have already incurred for late compliance with your tax reporting and payment obligations and any additional penalty that HMRC could impose, aside from interest, in light of your circumstances.

Late submission of your tax return **(½ for linking these penalties to late submission)**

Now that you have approved your tax return we will submit it to HMRC immediately.

However, as the deadline for submission was 31 January 2020 **(½)** the following penalties have already been incurred:

- A £100 penalty for filing your tax return late **(½).**
- A possible £900 penalty **(½)**, incurred at £10 per day **(½)** once the return was more than 3 months late **(½)**.
- A £500 penalty (5% of £10,000) **(½)** once the return was 6 months late **(½)**, being the greater **(½)** of 5% of the tax liability and £300 **(½)**.

Late payment of tax **(½ for linking these penalties to late payment)**

Two **(½)** £500 penalties **(½)** have already been incurred as a 5% penalty is applied to the outstanding tax liability once the tax is 30 days late **(½)** and, again, 5 months later **(½)**.

If you do not receive the gift from your parents **(½)** and are therefore unable to pay the tax before 11 months **(½)** have elapsed since the first 30 day penalty you will incur a further 5% penalty **(½)**.

I hope that this answers your question but please let me know if you have any queries.

Kind regards,

ATT

16. Notes for meeting

Andy

Income Tax consequences for him of receiving free shares and dividend shares:

Free shares - No Income Tax charge on value received **(½)**

Dividend shares - Dividends used to buy the shares are tax free **(½)**

Additional shares he could acquire:

Andy can buy partnership shares. As his salary is less than £18,000 the maximum value of the partnership shares is £1,700 (i.e. 10% **(½ - for the 10%)** of Andy's salary **(½ - for knowing there is a limit by reference to salary)**). Therefore, he can buy 680 partnership shares (£1,700/£2.50). **(½)**

Andy's salary will be reduced by the £1,700 and so he will receive Income Tax relief **(½)** on this amount, saving him £340 (£1,700 × 20%) in Income Tax **(½)**.

Andy can also acquire matching shares as Oldfield plc can offer up to 1,360 additional shares **(½)** (i.e. two shares for every one partnership share purchased **(½)**). There is no Income Tax charge on the award of matching shares **(½)**.

Carol

The tax charge associated with withdrawing the free shares from the SIP depends on the time that has elapsed between acquisition and withdrawal **(½)**.

Income Tax consequences of withdrawing free shares from the SIP

1) Withdrawn within three years **(½)** (i.e. those awarded on 1 March 2019 and 2020)

   Income Tax is charged on the value at the date of withdrawal **(½)**. So, Carol will be taxed on £7,500 **(1)** (1,500 × £2.50 × 2) in relation to these two awards.

2) Withdrawn within three to five years **(½)** (i.e. those awarded on 1 March 2017 and 2018)

   Income Tax is charged on the lower of the value at the date of award and the date of withdrawal **(½)**.

   So, relating to the award on 1 March 2018 Carol is taxed on £3,600 **(½)** and the award on 1 March 2017 she is taxed on £3,475 (1,390 × £2.50) **(1)**.

3) Withdrawn after five years **(½)** (i.e. awarded on 1 March 2015 and 2016)

   There is no Income Tax charge **(½)**.

[Max: 10 marks]