

# THE ASSOCIATION OF TAXATION TECHNICIANS

## ATT PAPER 2 BUSINESS TAXATION

**May 2023**

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TIME ALLOWED

3 HOURS 30 MINUTES

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- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- A maximum of two marks will be awarded for the quality of presentation in Part II.
- 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. Julia, Kamal and Larry had traded in partnership for many years and have always had a 31 December accounting year end. The partners shared profits equally, after allocating Julia an annual salary of £40,000.

On 30 September 2022, Larry left the partnership. From 1 October 2022, Julia and Kamal shared the profits 60:40. From this date, Julia was no longer allocated a salary.

The trading profits of the partnership were £220,000 for the year ended 31 December 2022.

Larry had unrelieved overlap profits of £8,000.

**Calculate each partner's assessable trading profits for 2022/23.** (4)

2. Monica is a sole trader and pays her liabilities through self-assessment.

On 31 March 2023, she paid both her balancing payment for 2021/22 and her first payment on account for 2022/23.

**Explain the consequences for Monica of these late payments.** (3)

3. Knowz is a law firm in a UK city. The firm uses Liam to arrange networking events to attract new clients.

Under his contract with Knowz, Liam runs an event each month. Knowz requires that these are held in the city centre on set dates. Liam chooses each venue and agrees costs with the venue.

Liam advertises the event and invites guests. There is no charge for guests but they must book in advance. Liam attends each event to manage it but paid a friend to do this once when he was ill.

Liam receives a set fee per event from Knowz. Out of this fee, Liam must pay the venue and meet his other costs. The event is cancelled if there are fewer than 20 guests booked a week before the event date. If the event is cancelled, Knowz do not pay Liam and he may lose a deposit with the venue.

**Explain the factors which justify the firm's treatment of Liam as a supplier and not an employee.** (4)

4. Sio began trading on 6 October 2022. His tax-adjusted trading profits for the six months ended 5 April 2023 were £100,000. He had no other income during 2022/23.

**Calculate Sio's National Insurance Contributions for 2022/23.** (3)

5. Carrie joined the ABC Partnership on 1 January 2022, investing capital of £20,000.

Carrie's allocation of profit from the partnership for the year ended 31 December 2022 was £80,000. She took drawings of £36,000 from the partnership in December 2022.

**Show the accounting double entries for the year ended 31 December 2022, which record Carrie's capital investment, her allocation of profit, and her drawings.** (3)

6. Simon is a sole trader. On 1 February 2023, he sold fixed plant for £800,000. Simon had bought the plant for £710,000 on 31 July 2019.

Simon had sold a building for £960,000 on 15 September 2018. He spent £10,000 on legal fees on the sale. The gain was £340,000 before reliefs.

Simon had used both assets solely for trading purposes. Simon made no other capital purchases or disposals. He claimed all available reliefs.

**Calculate Simon's chargeable gains for 2022/23.** (3)

7. Priya used a 10-acre plot of land in her trade for many years. She had bought the plot for £90,000 in January 2003.

In October 2022, Priya sold three of the 10 acres for £150,000. The value of the remaining seven acres was £370,000 in October 2022.

Priya was a higher rate taxpayer, and made no other capital disposals, in 2022/23.

**Calculate Priya's Capital Gains Tax payable for 2022/23.** (3)

8. Broxz Ltd had taxable total profits for recent accounting periods as follows:

	£
Year ended 30 September 2022	1,400,000
Six months ended 31 March 2023	780,000

Each March, the company receives dividends of £50,000 from quoted investments.

**Explain whether Broxz Ltd must pay Corporation Tax by instalments for the six months ended 31 March 2023.** (3)

9. Mocowe Ltd makes a trading profit exceeding £1 million each year. In the year ended 31 March 2023, the company also had a chargeable gain of £200,000.

Mocowe Ltd usually has property income and non-trading loan relationship income each year. However, in the year ended 31 March 2023 it made the following loss and deficit:

	£
UK property loss	50,000
Non-trading loan relationship deficit	80,000

Mocowe Ltd claims loss relief as early as possible.

**Explain how Mocowe Ltd uses the loss and the deficit, stating the due dates of any claims made.** (3)

10. On 1 January 2021 Water Ltd was incorporated.

On 1 February 2021 shareholders subscribed for a new issue of shares and the company deposited the cash received in an interest-bearing bank account.

On 1 March 2021 Water Ltd bought a property, which it immediately began to rent out.

On 1 April 2021 the company started to trade.

On 1 January 2023 the company sold the property for a gain and stopped receiving rental income.

The company prepared its first set of accounts for the 16-month period ended 30 April 2022 and then annually after this.

**State the dates of all Corporation Tax accounting periods from 1 January 2021 to 30 April 2023.** (4)

11. Earthee Ltd, a trading company, prepared accounts for the year ended 30 June 2022.

The company's financial controller has calculated draft tax-adjusted trading profits after capital allowances of £1,840,000. However, she has not yet adjusted for the following items which were deducted in the accounts:

	£
Legal fees for the issue of share capital	13,000
Cash gift to registered charity	20,000
Interest payable on overdue Corporation Tax payment	160
Interest payable on a loan used to buy a machine	8,000
Bank arrangement fee on the machine loan	500
Running costs of directors' cars used 20% for business purposes	18,000
Penalty for security breach concerning clients' data	50,000
Dividends paid to shareholders	100,000

**Calculate Earthee Ltd's tax-adjusted trading profits for the year ended 30 June 2022, showing clearly your treatment of each item listed.** (4)

12. Hoak Ltd is a standalone company and does not pay Corporation Tax by instalments. The company always pays its Corporation Tax on the due date for payment. It submits its Corporation Tax return on the same date.

HMRC opened a CTSA enquiry into the return for the year ended 31 March 2022. The HMRC Inspector found out that the company had incorrectly claimed a trading deduction for capital expenditure, included within 'costs of sale' in the accounts.

The Inspector believes that this has also been done in the return for the year ended 31 March 2021. However, by May 2023 it is too late for HMRC to open a CTSA enquiry into that return.

1) **Explain why it is too late for HMRC to open a CTSA enquiry into the return for the year ended 31 March 2021; and**

2) **Explain the alternative action which HMRC may be able to take for the year ended 31 March 2021.** (3)

## PART II

**Presentation skills** – awarded for quality of presentation.

(2 marks)

13. Joseph has been trading for many years as a dairy farmer, preparing accounts to 31 December. Due to falling profits, Joseph decided to stop dairy farming and sold his dairy herd in June 2022. He had made a herd basis election when he bought the farm.

The draft accounts for the six months ended 30 June 2022 are as follows:

	£	£
Sales		675,000
Cost of sales		<u>(486,000)</u>
Gross profit		189,000
<u>Expenses</u>		
Wages and contractors	35,700	
Premises costs	16,400	
Motor and travel expenses	12,600	
Repairs	28,500	
Administrative expenses	12,500	
Legal and professional fees	6,700	
Depreciation	17,000	
Loss on disposal of fixed assets	<u>16,000</u>	
		<u>(145,400)</u>
Net profit		<u>43,600</u>

You are given the following information:

- 1) Sales includes £240,000 for the sale of the herd. Cost of sales includes £57,000, which is the herd value for tax purposes.
- 2) Wages and contractor costs include a redundancy payment of £15,000 to Edward, an employee. He was entitled to statutory redundancy of £3,560.
- 3) Premises costs are:

	£
Farmhouse costs	6,760
Farm cottage costs	4,640
Rental of farm buildings	<u>5,000</u>
	<u>16,400</u>

The farmhouse is occupied by Joseph and used 60% for business purposes. The farm cottage is occupied by Edward and used 15% for business purposes.

- 4) Motor expenses are:

	£
Joseph's car	6,250
Other vehicle costs	5,750
Parking and speeding fines	<u>600</u>
	<u>12,600</u>

Joseph's car was used 75% for business purposes. Joseph incurred all of the fines.

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Continuation

5) Repairs include:

	£
Repainting farmhouse	3,470
Repairs to farm buildings	2,680

The repairs to the farm buildings were to restore the buildings to their original condition, at the end of the lease.

- 6) Administrative expenses include £400 for a waterproof jacket bought by Joseph in a general outdoor shop.
- 7) Legal and professional fees include legal fees of £1,500 to terminate the lease of the farm buildings.
- 8) During the period, Joseph took milk for personal use with a sale value of £200 and a cost of £100. No entry has been made in the accounts for this.
- 9) In March 2022, Joseph bought a trailer for £6,000. All the plant and machinery, apart from Joseph's car and the trailer, were sold in an auction for £54,000. Joseph kept the car and the trailer. The market values at 30 June 2022 of the car and trailer were £8,000 and £5,200. The tax written down values at 1 January 2022 were £5,600 on the general pool and £4,400 on Joseph's car. Joseph's car had emissions of 185g/km and cost £15,000 when bought.

Prior to the period ended 30 June 2022, Joseph's profits were as follows:

<u>Year ended</u>	£
31 December 2021	10,800
31 December 2020	17,900
31 December 2019	32,600

Joseph has overlap relief brought forward of £16,000.

Joseph's only other income was his salary from a contracting company as follows:

<u>Tax year</u>	£
2022/23	36,000
2021/22	14,000
2020/21	28,000
2019/20	25,000

**Requirements:**

- 1) Calculate the tax-adjusted trading profit/loss from dairy farming for the six months ended 30 June 2022. Show clearly your treatment of items 1) to 9). (12)
- 2) Assuming a tax-adjusted trading loss for the six months ended 30 June 2022 of £50,000:
- a) Calculate the terminal loss available. (2)
- b) Calculate Joseph's net income for 2019/20 to 2022/23 assuming relief is claimed as early as possible. Ignore averaging. (6)

Total (20)

14. Seblat Ltd trades as an electrical engineering company. The company was incorporated in September 2018. The company's share capital was divided into 10,000 £1 ordinary shares and 1,000 £1 non-voting preference shares. The 10,000 ordinary shares were subscribed for at par as follows:

<u>Shareholder</u>	<u>Number</u>
Elish	9,000
Li	400
Sam	<u>600</u>
	<u>10,000</u>

The non-voting preference shares were all subscribed for by Rafael.

On incorporation Elish was the only director of the company. Li, Sam and Rafael have never worked for Seblat Ltd.

The company operates from offices which had been bought by Elish personally in October 2018. Elish charged a rent to the company equivalent to 75% of the market rent.

In May 2019, Sam sold his shares to Li. Two new directors (who were not shareholders) were appointed and Elish reduced her working time for the company, to 10 hours per week.

In January 2023, Belkoy plc purchased all of the shares in Seblat Ltd and the offices owned by Elish for a total of £2 million.

Elish, Li and Rafael have not made any other capital disposals in 2022/23. None of them has made any previous claim for relief against their chargeable gains.

**Requirement:**

**Explain whether there are any reliefs and exemptions available to Elish, Li and Rafael on the disposals and the rates of tax payable on each disposal.** (12)

15. Scalit Ltd has been trading for many years providing printing services to advertising and exhibition customers. The company is not part of a group and has no businesses under common control. Accounts have always been prepared to 31 March each year.

You are given the following information:

- 1) The accounts to 31 March 2023 show a trading profit of £245,000 after deduction of the following:

	£
Legal costs	17,000
Planning costs	14,000
Depreciation	26,000
Loss on sale of equipment	8,500

- 2) The legal and planning costs relate to the construction of a new factory which will be completed in September 2023. The land for the development was bought in November 2022 at a cost of £60,000. The expected costs to be incurred in the year to 31 March 2024 are as follows:

	£
Demolition of existing building	8,000
Construction of new building	160,000

- 3) The company incurred the following additional capital expenditure during the year to 31 March 2023:

<u>Date expenditure incurred</u>	<u>Detail</u>	£
1 July 2022	New electric car for director (30% private use)	40,000
1 September 2022	New digital printer	65,000
15 November 2022	Electrical installation for new offices	15,000
1 February 2023	Second hand printing machine	50,000

- 4) The company disposed of equipment that it had bought new in May 2021 at a cost of £37,000. The equipment was sold for £12,000.
- 5) The balances at 1 April 2022 on the general and special rate pools were £48,000 and £18,000 respectively. The company always claims maximum capital allowances.
- 6) The company had no other income, outgoings or gains during the year.

The managing director, Mary, wants to raise money to finance future expansion of the company. She was approached by Sam who wants to buy shares in the company. Sam will not be involved in the running of the company. He wants to share in the future profits of the company but has asked for some reassurance that he will receive at least a fixed amount of dividend each year.

**Requirements:**

- 1) **Calculate Scalit Ltd's Corporation Tax liability for the year ended 31 March 2023.** (9)
- 2) **Explain the relief available for the costs associated with the construction of the new factory, together with how allowances are treated when the building is sold.** (4)
- 3) **Explain the type of shares that the company can offer to Sam, and how these shares fulfil his requirement for a minimum dividend.** (3)

Total (16)



16. You have recently been engaged by Sonja to act on her behalf.

Sonja has traded for many years in partnership with Olaf as an agent for holiday cottage holidays. The business is VAT registered with a turnover of £375,000 for the last financial year.

Sonja has decided to set up a business in her own name to provide cleaning and maintenance services for holiday home owners and members of the public. Initially the turnover is expected to be approximately £5,000 per month, but Sonja expects this to grow steadily to over £14,000 per month in approximately 18 months time.

Sonja has sent an email asking three questions:

- 1) Will the new business be part of the existing VAT registration and so be registered immediately for VAT?; and
- 2) If it isn't registered immediately, what are the advantages and disadvantages of voluntary registering?
- 3) I have bought cleaning products I also paid a solicitor to draw up a draft contract to use with holiday home owners wanting to use my services. I have invoices (including 20% VAT) for all of this. I have used some of the cleaning products at home, most will still be available when I start the business. Is it possible to claim back the VAT on the invoices even though they are from before the business started, and, if so, how do I do it?

Sonja's previous advisers has involved the partnership in a tax avoidance scheme. There were no comments in the last tax returns about the scheme. After reviewing HMRC manuals, you decide that the scheme documentation indicates that there is a loophole in legislation which can be exploited using several unusual steps to pay less tax. You think the previous advisers may not have complied with the 'Advising on Tax Planning Arrangements' standard within the Standards for Tax Planning.

**Requirement:**

**Write a letter to Sonja which includes:**

- 1) **A response to her three questions about VAT registration.** (6)
- 2) **An explanation of why the tax scheme does not comply with the 'Advising on Tax Planning Arrangements' standard, the action that should be taken by Sonja and the possible consequences.** (4)

Total (10)