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# May 2025 Examination

## PAPER 2

### BUSINESS TAXATION

### Suggested Answers

*Candidates will be given credit for relevant points not on the mark scheme.*

1. Alex

**1) Alex: Income tax due**

|  |  |  |  |
| --- | --- | --- | --- |
|  |  | £ |  |
| Profit per the accounts |  | 39,100 |  |
|  |  |  |  |
| Goods for self (sales value) | 1,700 x 1.5 | 2,550 | **1** |
| Depreciation |  | 6,400 | **½** |
| Alex drawings |  | 20,000 | **½** |
| Excess wages | (20,000 – 1/5 x 25,000) | 15,000 | **1** |
| Car running expenses | Replaced by mileage | 6,800 | **½** |
| Business mileage | 10,300 + 3,140 = 13,440 |  | **½** |
|  | 10,000 x 45ppm | (4,500) | **½** |
|  | 3,440 x 25ppm | (860) | **½** |
| Van leasing | No high emissions charge | - | **½** |
| Van running costs | 25% x (6,300 + 3,900) | 2,550 | **1** |
| Accountancy | Allowable | - | **)** |
| Late payment penalties |  | 800 | **)½** |
| Legal costs | All allowable | - | **½** |
| Private health care | Employee benefit | - | **½** |
| Gifts |  | 934 | **½** |
|  |  | 88,774 |  |
| Less use of home: |  |  |  |
| Council tax and insurance | (2,400 + 350) x 20% | (550) | **1½** |
| Greater of: |  |  | **½** |
| Flat rate | 18 x 12 = 216 | (216) | **½** |
| Business use | 15% x 1,300 = 195 |  | **½** |
|  |  |  |  |
| *(****½*** *for calculation of flat rate,* ***½*** *for calculation of business %,* ***½*** *for comparison)* | |  |  |
|  |  | 88,008 |  |
|  |  |  |  |
| Capital allowances |  | (9,824) | **½** |
| Taxable trading profit |  | 78,184 |  |
|  |  |  |  |
| Less Personal Allowance |  | (12,570) | **½** |
| Taxable income |  | £65,614 |  |
|  |  |  |  |
| Tax due: |  |  |  |
| 37,700 x 20% |  | 7,540 | **½** |
| 27,914 x 40% |  | 11,166 | **½** |
| Total tax due |  | £18,706 |  |

**Working:**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Capital allowances** | General pool | Special rate pool | Allowances |  |
|  | £ | £ | £ |  |
| WDV b/f | 4,800 | 16,000 |  |  |
|  |  |  |  |  |
| Additions | 8,000 |  |  |  |
| AIA | (8,000) |  | 8,000 | **½** |
| WDA 18%/6% | (864) | (960) | 1,824 | **1** |
|  | £3,936 | £15,040 |  |  |
| Total allowances |  |  | £9,824 |  |

(15)

**2)** **National Insurance payable**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  | | £ |  |
|  |  | |  |  |
| Class 1 – Alice and Sue | 25,000 + 20,000 – 2 x 9,100 = 26,800 | |  |  |
|  | 26,800 x 13.8% | | 3,698 | **1** |
|  |  | |  |  |
| Less Employment Allowance |  | | (3,698) | **½** |
| Class 1A - Private health | 1,412 x 13.8% | | 195 | **½** |
|  |  | |  |  |
|  |  | | 195 |  |
|  | £ | |  |  |
| Class 4 NIC | 37,700 x 6% | 2,262 |  | **½** |
|  | 27,914 x 2% | 558 | 2,820 | **½** |
|  |  | |  |  |
|  |  | | £3,015 | (3) |

Total (18)

1. Arefa
2. **Calculation of capital gain on disposal of the building**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Shop | Flat | ½ \* |
|  | £ | £ |  |
| Sales proceeds | 325,000 | 175,000 | ½ |
| Cost | (80,000) | (40,000) | ½ |
| Enhancement |  | (60,000) | ½ |
| Capital gain | 245,000 | 75,000 |  |
|  |  |  |  |
| Total gain |  | £320,000 |  |

(2)

Tutorial note: this mark will be awarded if the allocation is shown later in the answer.

1. **Explain reliefs available**

The gain on the shop **(½)** but not the flat **(½)** is eligible for replacement of business assets relief (rollover relief) **(½)** as:

1. The shop was used for business purposes throughout Arefa’s ownership**(½)**.
2. The shop was a qualifying asset – land and buildings **(½)**.
3. The new shop is also a qualifying asset – land and buildings **(½).**
4. The new shop will be immediately brought into use in the business **(½).**
5. The new shop will be bought within three years after the sale of the old shop **(½).**

As she is not reinvesting the full proceeds under either option **(½)**, then there will be a gain immediately chargeable **(½)**.

If she keeps the shop for 12 years, then any gain deferred under option 1 would crystallise after 10 years **(½)**. Under option 2, the gain would be deferred until the property is sold **(½)**.

(6)

**3) Capital Gains Tax computation**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | | Shop | Flat |  |
|  | | £ | £ |  |
| Capital gain | | 245,000 | 75,000 |  |
| Gain rolled over | |  |  |  |
| (245,000 – (325,000 – 275,000)) | | 195,000 | - | **1½** |
| Chargeable gain (cash not reinvested) | | 50,000 | 75,000 | **½** |
|  | |  |  |  |
| Annual exemption | |  |  |  |
| (allocated to residential property) | | - | (3,000) | **1** |
|  | | 50,000 | 72,000 |  |
|  | |  |  |  |
| Capital Gains Tax payable | |  |  |  |
| Shop | 20% x 50,000 |  | 10,000 | **½** |
| Flat | 24% x 72,000 |  | 17,280 | **½** |
|  | |  | £27,280 |  |
|  | |  |  |  |
|  | |  |  | **(4)** |

**4) Tax planning scheme**

The tax planning scheme does not meet the requirements of PCRT Help Sheet B – Tax Advice **(½)** in relation to the Standards for Tax Planning **(½)**. The advice is not specific to Arefa’s facts and circumstances **(½)**. It also may not agree with the view of the law that would be taken by HMRC **(½)**. If included full disclosure of the facts of the scheme should be made to ensure transparency. **(½)** However you should not promote or encourage a tax planning arrangement that is highly artificial or contrived. **(½)**

Arefa should be advised of the risks of including the claim in her tax return **(½)**. Members should not include a claim in tax returns which they believe may be incorrect **(½)**. If Arefa continues to insist that the claim should be included, then the firm should consider ceasing to act **(½)**.

Max (3)

Total (15)

1. Lucia

**Taxable trading income**

The initial sale of the furniture and furnishings from Lucia’s previous home will not qualify as taxable trading income for Income Tax **(½)**. This is because, even though she made a profit on many items, the motive for the sale was not to make a profit but rather to sell things that did not suit her new house **(½)**.

During the period from 10 April 2024 to 1 June 2024, she was preparing to trade **(½)**.

However, from 1 June 2024 **(½ for date)**, she will be considered to be carrying out a trade. This is because her intention was to buy goods and sell them at a profit **(½)**. There are also other indications that she is trading:

1. The frequency of transactions **(½)** - after her initial sale, she has made repeated transactions **(½)**.
2. Sales organisation **(½)** – she has set up a website and is using social media to support her business **(½)**.
3. Financing **(½)** – she has taken out finance to enable her to increase the business **(½)**.
4. Connection to an existing trade **(½)** - the buying and selling of furnishings and furniture is closely linked to her existing business**(½)**.
5. Length of ownership – the stock is being held for a short period before being sold.

*(2 marks for badges of trading, 2 marks for application to facts given)*

Max (5)

**VAT**

The VAT registration of Lucia’s company has no impact on whether she should be registered as it is a separate ‘person’ for VAT purposes **(1)**.

Lucia will have to keep a record of the cumulative monthly turnover from June 2024 **(½)**. The earlier sale was not in furtherance of a trade and is therefore ignored **(½)**.

When the taxable supplies in the last 12 months period are more than the VAT registration threshold (currently £90,000) **(½)**, will have 30 days to register the business for VAT **(½)**. It will then start to charge VAT from the beginning of the following month **(½)**.

(3)

**Self-assessment requirements**

Lucia will have to notify HMRC of her chargeability within 6 months of the end of the tax year **(½)** in which she started **(½)** to trade. She started to trade on 1 June 2024, i.e. in 2024/25, so she will have to notify HMRC by 5 October 2025 **(½)**.

Her first return will cover her income for 2024/25 and will be due by 31 October 2025, if she is submitting a paper return or by 31 January 2026, if filed online **(½)**. If the notice to file a return is issued late then it must be filed within three months of these dates if later **(½)**.

Any liability to tax and Class 4 National Insurance for 2024/25 will be due on 31 January 2026 **(½)**, or three months after the notice to file if later **(½)**.

She may also be required to pay two payments of 50% of the 2024/25 liability by 31 January 2026 and 31 July 2026 **(½)**, unless the 2024/25 liability was less than £1,000 **(½)** or less than 20% of the total liability for 2024/25 **(½)**.

The total tax and Class 4 National Insurance for 2025/26 will be due by 31 January 2027 **(½)**, less any payments on account that have been made **(½)**.

Max (5)

**Pre-trading expenses**

Lucia can claim the following costs as pre-trading expenses:

|  |  |  |  |
| --- | --- | --- | --- |
|  |  | £ |  |
| Storage unit | 2 months at £150 per month | 300 | **1** |
| Collection costs | 60% x 320 | 192 | **1** |
| Meeting costs | Not allowable | - | **½** |
| Promotion costs |  | 289 | **½** |
|  |  | £781 |  |
|  |  |  | **3** |

If you have any queries on any of the above information, please do not hesitate to contact me.

Yours sincerely,

Anne Adviser

Total (16)

4.

1)

**Chargeable gain on sale of Miko plc shares**

|  |  |  |
| --- | --- | --- |
|  | £ |  |
| Proceeds | 27,000 | **(1/2)** |
| Less indexed cost (W) | (12,789) | **(1/2)** |
| Gain | 14,211 |  |

Working: share pool

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  | No. of shares | Indexed cost |  |
|  |  |  | £ |  |
| January 2010 | Purchase | 10,000 | 30,000 | **(1/2)** |
|  |  |  |  |  |
|  | Indexation to Dec 2017 |  | 8,288 |  |
|  | [(278.1 – 217.9)/217.9] × £30,000 |  |  | **(1/2)+(1/2)** |
|  |  |  |  |  |
| September 2019 | Rights issue,10,000/4 @ £6 | 2,500 | 15,000 | **(1/2)+(1/2)** |
|  |  | 12,500 | 53,288 |  |
| March 2025 | Disposal (£53,288 x 3,000/12,500) | (3,000) | (12,789) | **(1/2)** |
|  |  | 9,500 | 40,499 |  |

**(4 marks)**

2)

**Corporation tax payable**

|  |  |  |  |
| --- | --- | --- | --- |
|  | Year ended 31 December 2024 | 3m ended 31 March 2025 | **(1)** |
|  | £ | £ |  |
| Trading profits before allowances: £2,100,000 (12:3) | 1,680,000 | 420,000 | **(1/2)** |
| Less SBA : |  |  |  |
| (£(2,500,000 - 500,000) **(1/2)** × 3% **(1/2)** × 11/12 **(1)** | (55,000) |  |  |
|  | 1,625,000 |  |  |
| Gain (£14,211 - £6,000 **(1/2)**) |  | 8,211 | **(1/2)+(1/2)** |
| NTLR | 14,000 | 3,600 | **(1/2)+(1/2)** |
| *no deduction for political donation anywhere* |  |  | **(1/2)** |
| QCDs | (8,000) |  | **(1/2)+(1/2)** |
| Taxable total profits *not incl dividends* | 1,631,000 | 431,811 | **(1/2)** |
|  |  |  |  |
| CT |  |  |  |
| £1,631,000 × 25% | 407,750 |  | **(1/2)** |
| £431,811 × 25% |  | 107,953 | **(1/2)** |

*½ mark out of first 1 for two periods but wrong dates eg 3m/e 31.3.24 and y/e 31.3.25, then follow-through marks available*

**(9 marks)**

3)

**Due dates for payments and filings**

**Year ended 31 December 2024**

Quarterly instalments are due if augmented profits (taxable total profits plus dividends) exceed £1,500,000 **(1/2)**.

Latun Ltd’s augmented profits for the year ended 31 December 2024 clearly exceed £1,500,000 **(1/2)**.

However, augmented profits for the previous year ended 31 December 2023 did not exceed £1,500,000 (£1,450,000 + £7,000 = £1,457,000) **(1/2)**. The augmented profits for the year ended 31 December 2024 also do not exceed £10 million **(1/2)** and so Latun Ltd does not have to make quarterly instalments for the year ended 31 December 2024 **(1/2)**. Instead, corporation tax is due by 1 October 2025 **(1/2)**.

**Three months ended 31 March 2025**

The limit for the short period is £375,000 (£1,500,000 × 3/12) **(1/2)** and so the augmented profits of £431,811 exceed this and quarterly instalment payments are due **(1/2)**. There is one payment due on 14 July 2025 **(1/2)**.

**Filing corporation tax returns**

Two returns are due, one for each accounting period **(1/2)** but both are due on the same date **(1/2)** which is 12 months after the end of the period of account **(1/2)** ie 31 March 2026 **(1/2)**.

**(maximum 6 marks)**

**Total 19 marks**

5.

1)

**Tax points**

Car: Basic tax point is the date of collection, being 1 February 2024 (Note VAT is not recoverable on this car) **(1/2)**.

Hot water system: Payment is made before the date of installation (delivery) ie before the basic tax point **(1/2)**\* and so the date of payment (31 March 2024) becomes the actual tax point **(1/2)**.

Packaging machinery:

The actual tax point for the £210,000 payment is 28 May 2024 **(1/2)** being before the basic tax point.

The invoice has been issued within 14 days of the basic tax point (date of delivery) **(1/2)** and so the tax point for the remaining £630,000 payment is the date of the invoice (4 July 2024) **(1/2)**.

Relevance: The tax point determines which quarterly VAT returns the purchases are included on **(1/2)** for the recovery of input VAT (where possible) **(1/2)**.

*\*Give credit whether explained here, or for the first payment for the packaging machinery*

**(4 marks)**

2)

**Capital allowances**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | AIA/FYA @ 100% | General pool | Special rate pool | Total allowances |  |
|  |  | £ | £ | £ |  |
| TWDV b/f |  | 68,000 | 43,000 |  |  |
| Additions: |  |  |  |  |  |
| Car |  |  | 30,000 |  | **(1/2) + (1/2)** |
|  |  |  |  |  |  |
| Hot water system  (5/6 × £600,000) | 500,000 |  |  |  | **\*** *amounts* |
| AIA @ 100% | (500,000) |  |  | 500,000 | **(1/2)** |
|  |  |  |  |  |  |
| Packaging machine  (5/6 × £840,000) | 700,000 |  |  |  | **\*(1/2)** |
| Remaining AIA (9/12 × £1,000,000) - £500,000 | (250,000) |  |  | 250,000 | **(1/2) + (1/2)** |
| FYA @ 100% | (450,000) |  |  | 450,000 | **(1/2)** |
|  |  |  |  |  |  |
| Disposals: |  |  |  |  |  |
| Solar panels (50% × £20,000) |  |  | (10,000) |  | **(1/2)** |
| Zero-emission car |  | (11,000) |  |  | **(1/2)** |
|  |  | 57,000 | 63,000 |  |  |
| WDA @ 18% × 9/12 |  | (7,695) |  | 7,695 | **(1/2) + (1/2)** |
| WDA @ 6% × 9/12 |  |  | (2,835) | 2,835 | **(1/2)** |
|  |  | 49,305 | 60,165 | 1,210,530 |  |

Balancing charge on solar panels = £20,000 × 50% = £10,000 **(1/2)**

Total capital allowances = £1,210,530 - £10,000 **(1/2)** = £1,200,530

**(7 marks)**

3)

**Categories of deduction for costs relating to the building**

The letting agent’s fees are deductible against property business income and so not deductible against either chargeable gains or trading income **(1/2)**.

The proportion of interest (75%) which relates to the floors used in the company’s trade is deductible against trading profits **(1/2)**. The other 25%, relating to the part let out, is deductible against non-trading loan relationship income **(1/2)**.

The replacement window (repair) in the part used for trading is deducted against trading profits **(1/2)**.

The advertising costs are deductible in the gains calculation on the sale of the building **(1/2)**. The legal fees on the sale are also deductible in the gains calculation **(1/2)**.

The proportion of the insurance (75%) relating to the floors used in the trade is deductible against trading profits **(1/2)**, with the remainder deductible from property business income **(1/2)**.

**(4 marks)**

**Total 15 marks**

6.

1)

**Partnership profit allocation**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Total | Caro | Eniola | Megan |  |
|  | £ | £ | £ | £ |  |
| Y/e 30.4.2024 | 90,000 |  |  |  |  |
| 2:1:2 |  | 36,000 | 18,000 | 36,000 | **(1/2)** |
|  |  |  |  |  |  |
| Y/e 30.4.2025 |  |  |  |  |  |
| 1.5.24 – 31.10.24 |  |  |  |  |  |
| 6/12 × 102,000\* | 51,000 |  |  |  | **(1/2)\*** |
| 2:1:2 |  | 20,400 | 10,200 | 20,400 | **(1/2)** |
|  |  |  |  |  |  |
| 1.11.24 – 30.4.25 |  |  |  |  |  |
| 6/12 × 102,000\* | 51,000 |  |  |  |  |
| Salary: **(1/2)** |  |  |  |  |  |
| 6/12 **(1/2)** × 30,000 |  | 15,000 |  |  |  |
|  | (15,000) |  |  |  | **(1/2)** |
|  | 36,000 |  |  |  |  |
| Split 1:1 |  | 18,000 | 18,000 |  | **(1/2)** |
| Total for 30.4.2025 |  | 53,400 | 28,200 | 20,400 | **(1/2)** |

**(4 marks)**

2)

**Taxable trading profits 2024/25**

Caro

|  |  |  |
| --- | --- | --- |
|  | £ |  |
| 6 April 2024 – 5 April 2025 |  |  |
| 1/12 × £36,000 + 11/12 × £53,400 | 51,950 | **(1/2)** |
| Plus transition profit spread £24,000/5 | 4,800 | **(1/2)** |
|  | 56,750 |  |

Eniola

|  |  |  |
| --- | --- | --- |
|  | £ |  |
| 6 April 2024 – 5 April 2025 |  |  |
| 1/12 × £18,000 + 11/12 × £28,200 | 27,350 | **(1/2)** |
| Plus transition profits spread (£12,000 - £10,000)/4 | 500 | **(1/2) + (1/2)** |
|  | 27,850 |  |

Megan

|  |  |  |
| --- | --- | --- |
|  | £ |  |
| 6 April 2024 – 31 October 2024 |  |  |
| 1/12 × £36,000 + £20,400 | 23,400 | **(1/2)** |
| Plus remaining transition profits £24,000 × 4/5 | 19,200 | **(1/2) + (1/2)** |
|  | 42,600 |  |

**(4 marks)**

3)

**Transfer of partnership assets to leaving partner**

The car is an exempt asset for capital gains tax – no implications **(1/2)**.

The transfer of the building is a chargeable disposal for each of Caro and Eniola **(1/2)**. The gain is their share (one third each) **(1/2)** of the market value of the building on transfer less original cost to the partnership **(1/2)**. Each partner then deducts their own annual exempt amount **(1/2)**.

The rate of capital gains tax charged is 10% for any gain falling in the remaining basic rate band (for Eniola) and 20% thereafter **(1/2)**. The transition profits are ignored when determining Eniola’s basic rate band remaining **(1/2)**.

**(maximum 3 marks)**

4)

**Retainer arrangement** Ch 8, Section 8.4, Ethics Manual 6th Edition

The firm should set out the retainer arrangement in writing **(1/2)** in the letter of engagement **(1/2)** making clear the point at which further charges may be levied **(1/2)** so that the firm and the client clearly understand the extent and limitations of the arrangement **(1/2)**.

Before agreeing to an arrangement where the partnership can call on the firm’s services at any time **(1/2)**, the firm should consider their ability to fulfil their obligations to other clients *(alternatively, this can be worded in terms of considering resources, or not neglecting other clients)* **(1/2)**. The firm should consider all implications before entering into the arrangements **(1/2)** and should include termination arrangements in the letter of engagement **(1/2)**.

**(4 marks)**

**Total 15 marks**