



July 2026 Examination

PAPER 1

Personal Taxation

Suggested Answers

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

1. Leo and Layla

1) Capital gains tax implications

(a) Leo's wedding present to Layla on 1 October 2013

Leo's transfer of a half share in his flat to Layla occurs after the wedding and is therefore an inter-spouse transfer. (½)

The disposal is deemed to take place at 'no gain no loss' (NGNL). (½)

Layla is deemed to have bought her half of the house from Leo for £170,000 (£340,000 x 50%), being 50% of Leo's historic cost in 2011. (½)

(b) The couple's separation on 1 January 2023

The couple's separation itself is not a chargeable event for capital gains tax purposes. (½)

(c) The capital transactions in 2025

For disposals from 6 April 2023, transfers between spouses continue to take place at NGNL (½) until the earlier of: (½)

(i) **5 April 2026** (i.e. three years from the end of the tax year of separation) (½)

(ii) **1 September 2026** (i.e. the date of divorce) (½)

Accordingly, the transfer of the vase from Leo to Layla is a NGNL event, and Layla is deemed to have acquired the vase from Leo for £2,500 (i.e. Leo's historic cost in 2009). (½)

The transfer of the painting from Layla to Leo is a NGNL event, and Leo is deemed to have acquired the painting from Layla for £6,300 (i.e. Layla's historic cost in 2023). (½)

(d) Leo's birthday present to Layla on 31 July 2026

As the gift is after 5 April 2026, even though the couple are not yet legally divorced, the transfer takes place at full market value (½) as they are now connected persons. (½)

A chargeable gain of £3,333 (W) arises. (½)

Leo will be assessed on the gain in the tax year 2026/27 (½) at 24% as he is a higher rate taxpayer (½), subject to the availability of the annual exempt amount. (½)

Working: Chargeable gain on necklace (non-wasting chattel) in 2026/27

	£	£	
Lower of:			
(1) Normal gain			
Market value	8,000		½
Less: Probate value	(4,000)		½
	<u>4,000</u>		
	=====		
(2) 5/3 rule			
5/3 x (£8,000 – £6,000)	3,333	3,333	1½
	=====	=====	

(e) The couple's financial divorce settlement on 1 September 2026

All capital transfers which take place as part of a formal divorce settlement are NGNL events. (½)

Accordingly, Layla acquires the additional 50% ownership and now has full ownership of the family home with a deemed cost of £815,000 (i.e. historic cost in 2013). (½)

Leo acquires the additional 50% ownership and now has full ownership of the flat with a deemed cost of £340,000 (i.e. historic cost in 2011). (½)

The transfer of cash (i.e. bank and building society accounts) is exempt from capital gains tax as cash is an exempt asset. (½)

Max: 10 marks

2) Planned sale of marital home in 2027

Capital gains tax consequences for Layla

As Layla lived in the property from the date of purchase to the date of sale, (½) private residence relief (PRR) is available and her portion of the gain will be fully exempt. (½)

Capital gains tax consequences for Leo

When Leo moved out of the marital home on 1 January 2023, it ceased to be his main residence. (½)

On 1 October 2027 Leo will receive £126,000 ((£1,175,000 – £815,000) x 35%) in accordance with the deferred sale agreement. (½)

This capital sum is treated as a chargeable gain attributable to the transfer of his 50% interest to Layla on 1 September 2026. (½)

Leo will be entitled to the PRR he would have been entitled to on 1 September 2026 (i.e. the date of Leo's transfer of his 50% share to Layla). (½)

Leo's chargeable gain will be:

	£	
Capital sum received	126,000	½
Less: PRR		
(£126,000 x 120/155) (W)	(97,548)	½
Chargeable gain	<u>28,452</u>	
	=====	

Leo will be taxed on the gain in the tax year 2027/28 (½) (i.e. when the deferred proceeds are received) at 24% (½) as he is a higher rate taxpayer (½), subject to the availability of the annual exempt amount. (½)

The capital gains tax will be due 30 November 2027 (i.e. 60 days after the completion of the sale of the house). (½)

Working: Private residence relief

		Total months	Exempt months	Chargeable months	
1.10.13 to 1.1.23	Owner occupation	111	111		1
1.1.23 to 1.9.26	Not PPR/ Not owned by Leo	44	Last 9	35	1
		<u>155</u>	<u>120</u>	<u>35</u>	
		=====	=====	=====	

Max: 6 marks

3) Income tax consequences

(a) Renting the flat

Whilst in joint ownership, the rental income is taxed 50% on Leo and 50% on Layla in the tax year of receipt. (½)

Transferring income-producing assets in the divorce settlement means that Leo will receive all the rental income from 1 October 2026 (½) and the tax burden on the rental income will be the sole responsibility of Leo after that transfer date. (½)

(b) Transfer of bank and building society accounts to Leo

Cash payments from one spouse to another as part of a financial settlement is not treated as taxable income for Leo. (½)

(c) Maintenance payments paid by Leo

Spousal and child maintenance payments are tax free receipts for Layla, (½) and are not tax allowable deductions for Leo. (½)

Max: 2 marks

Total: 18 marks

(a) Retirement payments

State pension

Hilary's state pension is taxable income and is assessed as non-savings income (½) in the tax year of receipt. (½)

In 2025/26, £2,070 is received (£230 x 9 weeks) and in a full year £11,960 would be received (£230 x 52). (½)

Tax is usually collected by adjusting the taxpayer's tax code if they have other taxable income (e.g. other pension income or other employment income). (½) If not, the tax is collected via self-assessment if the taxpayer already submits an annual return. (½) If not, HMRC will issue a simple assessment detailing what tax is owed and how to pay. (½)

Lump sum payment into occupational pension scheme

Lump sum payment into a registered pension scheme is exempt from income tax and NICs. (½)
Accordingly, the £10,000 is not taxable on Hilary.

Non-contractual cash payment and gift of company car

Ex gratia payments are partially exempt from income tax (½) and fully exempt from NICs for Hilary. (½)

There is a £30,000 exemption in total. (½)

Hilary will be taxed on the ex gratia amounts on a cash receipts basis. (½)

As the ex gratia payments are received over two tax years, the exemption is applied to payments in the earliest tax year first. (½)

As different payments are made in the same tax year, the limit is allocated to cash receipts before benefits received. (½)

		£	
Tax year: 2025/26 (½)			
20.3.26	Ex gratia cash payment (£56,000/2)	28,000	½
	Less: Exemption	(28,000)	½

	Taxable amount	Nil	
		=====	
28.2.26	Gift of car	12,250	
	Less: Exemption (£30,000 – £28,000)	(2,000)	½

	Taxable amount	10,250	
		=====	
Tax year: 2026/27 (½)			
20.9.26	Ex gratia cash payment	28,000	
	Less: Exemption (none remaining)	(Nil)	

	Taxable amount	28,000	½
		=====	

The taxable amounts are treated as the top slice of Hilary's taxable income (i.e. taxed after dividends) (½) and are taxed at her highest marginal rate of tax in that tax year. (½)

The tax on the £10,250 will be taxed under PAYE as it arises before the P45 is issued. (½)

The tax on the £28,000 assessed in 2026/27 will be paid net of Niche plc's estimate of Hilary's marginal rate of tax in that year, and any under or over payments are dealt with through self-assessment. (½)

Tutorial note:

Whilst Hilary pays no NICs on the taxable element of ex gratia payments, Niche plc will pay Class 1A NICs on the excess amounts over the £30,000 limit.

Max 7 marks

(b) Net cash impact of sale of shares

	£	
Sale proceeds received (6,000 x £5.20)	31,200	1/2
Less: Cost of option (paid in July 2016) (6,000 x £0.05)	(300)	1/2
Less: Cost of shares (paid in January 2026 by repaying company loan) (6,000 x £1.60)	(9,600)	1/2
Less: Total tax charges (see below)	(7,434)	1/2
Net cash inflow	13,866	
	=====	

Tax charges in respect of Niche plc's share options

	£	£	
<i>Grant of option – July 2016</i>			
No tax implications		Nil	1/2
<i>Exercise of option – November 2021</i>			
MV at exercise date (6,000 x £3.80)	22,800		1/2
Less: Cost of option	(300)		1/2
Less: Cost of shares	(9,600)		1/2
	=====		
Employment income	12,900		
	=====		
Income tax – taxed in 2021/22			1/2
- £12,900 x 40%		5,160	1/2
National insurance – taxed in 2021/22			
As the shares are readily convertible into cash (plc shares), Class 1 primary NICs are payable (<i>Tutorial note</i>)			1/2
- £12,900 x 2%		258	1/2
<i>Sale of shares – January 2026</i>			
Sale proceeds (6,000 x £5.20)	31,200		1/2
Less: MV at exercise date	(22,800)		1/2
	=====		
Chargeable gain	8,400		
	=====		
CGT – taxed in 2025/26			1/2
- £8,400 x 24% (<i>Tutorial note</i>)		2,016	1/2
		7,434	
		=====	

Business Asset Disposal Relief (BADR)

BADR is not available as although Niche plc is a trading company, (1/2) Hilary is an employee (1/2) and she has owned the shares for more than two years, (1/2) she does not own at least a 5% interest in the company (6,000/2 million = 0.3%). (1/2)

Tax treatment of the loan for Hilary

From 6 November 2021 to 15 January 2026, Hilary had the benefit of an interest free loan from Niche plc. (1/2)

However, as the amount of the loan is £9,600 (1/2) it is an exempt benefit as at no point in any tax year does the loan exceed £10,000. (1/2)

Tutorial notes:

- (i) As Niche plc shares are readily marketable, Niche plc must also pay Class 1 secondary NICs on the £12,900 employment income. However, the question only asks for the tax implications for Hilary, not the employer.

- (ii) *Hilary has already used her AEA, therefore all of the chargeable gain calculated is taxable.
As she is a higher rate taxpayer, the gain is taxed at 24% as BADR is not available.*

Max 9 marks

Total: 16 marks

3.

To: Peter
From: Candidate
Date: 28 July 2026
Re: CGT exposures

Hi Peter

Your exposure to UK capital gains tax and reporting obligations depends on whether or not you are UK tax resident for the 2025/26 tax year. I will deal with each of these scenarios in turn.

1) Calculation of chargeable gains

UK resident

If you are UK tax resident, your chargeable gains will be your net gains (½) for the year across all three disposals (½). The gain/loss on each disposal will be calculated as disposal proceeds less acquisition cost (½). The acquisition cost of the Landgrab Ltd shares will be their probate value (½).

Non-UK resident

If you are non-UK tax resident, your chargeable gain on Foxglove Cottage will be that arising since 6 April 2015 (½). There are three ways that this gain can be calculated:

1. The default method (½) by reference to a valuation of the property on 6 April 2015 (½),
2. The straight-line method (½), whereby the gain over the whole of your period of ownership is allocated to the pre- and post-6 April 2015 period on a straight-line basis (½), or
3. The retrospective method (½), whereby the gain is calculated by reference to your initial cost of acquisition (½).

The loss on the disposal of the shares in Landgrab plc will only be an allowable loss and therefore relievably against the gain on Foxglove Cottage if it is the disposal of shares in a property rich company (½) i.e.:

- 75% or more of the company's gross assets are comprised of UK land/property (½),
- You owned 25% or more of the shares (½) at any point in the two years prior to the disposal (½), and
- Less than 90% of the land is used for trading purposes (½).

If Landgrab Ltd is a property rich company, it is only the loss on the shares calculated from 5 April 2019 that would be allowable (½). The straight-line method is not available when calculating gains on the disposal of shares in a property rich company (½) while any loss calculated via the retrospective method is not relievably (½).

You will not be entitled to claim relief for the loss on the artwork (½).

(10 marks)

2. Reporting if you are UK tax resident

Within 60 days of completion (½), you will need to report the disposal of Foxglove Cottage (½) including a calculation of the chargeable gain and a computation of the tax due (½). The calculation of the tax due can take account of your Annual Exempt Amount (½) and the loss on the sale of your Landgrab plc shares (½). However, the loss on the artwork would not be taken into account (½) as the loss arose after completion of the sale of the Cottage (½). The disposal will also need to be reported, by 31 January 2027 (½), on your annual self-assessment tax return (½).

(Max 4 marks)

4.

(1) Benefits

Car	£	£		£
List price		35,000	(½)	
Accessories added:				
Alloy wheels	1,750		(½)	
LED headlight bulbs – excluded as provided after car first made available and costing < £100 (½)	-		(½)	
		1,750		
Revised list price		36,750		
Benefit percentage:				
Base		21%	(½)	
Addition	(145 – 75) / 5	14%	(1½)	
		35%		
Benefit	35% x 36,750 x 4/12	4,287	(1)	
Less: contribution	4 x 100	(400)	(½)	
Car benefit				3,887
Mileage				
Reimbursed	11,400 x 44p	5,016	(½)	
Less: tax-exempt limits				
10,000 x 45p		(4,500)	(½)	
1,400 x 25p		(350)	(½)	
				166
Accommodation				
Annual value		2,000	(½)	
Additional yearly rent				
Original cost	250,000		(½)	
- £475,000 value ignored as property was not bought more than six years before being made available to Rory (½)				
Conservatory	35,000		(½)	
Hot tub – excluded as not incurred before the start of the tax year (½)	-		(½)	
	285,000			
Less:	(75,000)		(½)	
	210,000			
	@ 3.75%	7,875	(½)	
		9,875		
Benefit for 2 months	2 / 12 x 9,875	(½)		1,645
Mobile phones				
Rory		-	(½)	
Wife		720	(½)	
				720
Subscriptions				

Institution of Structural Engineers	-	(½)	
Royal College of Psychiatrists	675	(½)	675
Christmas party		(½)	-
Golf club membership		(½)	4,000
Total benefits			11,093

(Max 14 marks)

(2) NICs

Class 1A NICs (½) will be payable on these benefits, aside from on the PSA where Class 1B NICs are payable (½). These NICs are payable by Masters Ltd (½) annually. The deadline for payment is 22 July following the end of the tax year ie 22 July 2026 for Class 1A NICs (½) and 22 October following the end of the tax year ie 22 October 2026 for Class 1B NICs (½). [These deadline marks will be given if the equivalent non-electronic payment deadlines are given – 19 July and 19 October respectively.]

[Tutorial note: Mileage payments in excess of 45p per mile are assessed to Class 1 Primary and Secondary contributions. As the mileage payments are only 44p per mile, there is no liability to Class 1 NICs.]

(Max 2 marks)

(3)

Possible actions:

- Include a clear notice or caveat in the information stating that the advice has been prepared for the client and that no liability is accepted to any third parties who choose to make use of the information. (½)
- Require, as a term of the engagement, that your clients seek your consent before information with which their own or their firm's name is associated, is released by them to third parties. (½)
- Require the third party and/or its advisers to undertake in writing that you will be excluded from liability or held harmless as a consequence of making the information available to them. (½)
- Communicate to the third party the terms upon which the information is released including limitations on scope, stating that the advice was prepared with only the client's interests in mind, may not apply in all circumstances, and confirmation that no responsibility is accepted. (½)
- Seek an indemnity from the client in respect of any possible claim against you by the third party. (½)
- Decline to provide the information. (½)

(3 marks)

5.

	Non-savings £	Interest £	Dividends £	
Employment income (N1)	62,450			(¹ / ₂)
REIT dividend (N2)	1,200			(¹ / ₂)
EIS dividend			350	(¹ / ₂)
VCT dividend (N3)			-	(¹ / ₂)
Rental income (W1)	1,350			
Bank interest		400		(¹ / ₂)
Net/total income	65,000	400	350	
Less: Personal allowance	(12,570)			(¹ / ₂)
Taxable income	52,430	400	350	
Income tax:				
	£		£	
Non-savings income (W2)	38,325	x 20%	7,665	(¹ / ₂)
Non-savings income	14,105	x 40%	5,642	(¹ / ₂)
Savings income	400	x 0%	0	(¹ / ₂)
Dividend income	350	x 0%	0	(¹ / ₂)
			13,307	
Plus: High income child benefit charge (W3)			787	(¹ / ₂)
			14,094	
Less: Tax deducted at source:				
PAYE			(12,500)	(¹ / ₂)
REIT dividend (£1,200 x 20%)			(240)	(¹ / ₂)
Income tax payable			1,354	

Notes

(N1) Employment income

Jack's employment income includes the private medical insurance, so his total employment income is.
 $£(61,000 + 1,450) = £62,450$. (¹/₂)

(N2) UK REIT

The dividend received is a 'qualifying REIT dividend' as it has been paid out of tax-exempt property income and gains of the REIT.

The dividend is deemed to have suffered basic rate income tax at source and therefore the gross amount is
 $£960 \times 100/80$ (¹/₂) = £1,200 which is taxed as non-savings income.

(N3) VCT dividend

As Jack invested less than £200,000 (¹/₂) in VCTs in 2020/21, the dividend is exempt from income tax.

Workings

(W1) Rental income

	<i>Normal calculation</i>	<i>Rent-a-room</i>
	£	£
Rent received: 50% x £10,200 <i>(1/2)</i>	5,100	5,100
Less expenses: 50% x £2,400 <i>(1/2)</i>	(1,200)	-
Less rent-a-room exemption: 50% x £7,500 <i>(1/2)</i>	-	(3,750)
	3,900	1,350

As the house is jointly-owned, half the rent-a-room exemption is given to each joint owner so Jack's exemption is £7,500/2 = £3,750.

Jack and Diane should make an election for rent-a-room relief to apply as it results in a lower taxable amount.

(W2) Gift aid donation

The gross gift aid donation is £500 x 100/80 = £625. *(1/2)*

This extends the basic rate band to £(37,700 + 625) = £38,325. *(1/2)*

(W3) High income child benefit charge

As Jack is the higher earner and his adjusted net income is over £60,000, he will have to pay the charge.

Jack's adjusted net income:

	£
Net income: £(65,000 + 400 + 350)	65,750 <i>(1 1/2)</i>
Less gross gift aid donation	<u>(625)</u> <i>(1/2)</i>
Adjusted net income	65,125
Less: Child benefit threshold	<u>(60,000)</u> <i>(1/2)</i>
Excess	<u>5,125</u>
5,125 / 200 <i>(1/2)</i> x 1% (round down) <i>(1/2)</i> = 25%	

Child benefit for three children is:

(£26.05 + (2 x £17.25)) <i>(1)</i>	£60.55 per week
£60.55 x 52	£3,149 <i>(1/2)</i>
Charge = £3,149 x 25%	£787 <i>(1/2)</i>

16 marks

2)

The due date for payment of Jack's Income tax payable is 31 January 2027. *(1/2)*

If payment is two months late, the interest charged by HMRC will be £1,354 *(1/2)* x 7% *(1/2)* x 2/12 *(1/2)* = £16.

2 marks

Total 20 marks

6.

1)

Takeover of ABC Ltd by LargerCo plc in June 2020

As a paper for paper transaction, no CGT arises at the date of the takeover. ^(1/2) The LargerCo plc shares 'stand in the shoes' ^(1/2) of the original shares in ABC Ltd. The base cost of the 2,000 LargerCo plc shares is therefore £10,000. ^(1/2)

Takeover of LargerCo plc by BiggerCo plc in May 2025

As Salim received different classes of shares and loan stock on the takeover, the base cost of the LargerCo plc shares must be apportioned with reference to the market value of the consideration received. ^(1/2)

Consideration:	MV £	Base cost £ (W1)
Ordinary shares: $2,000/1 \times 4 = 8,000$ shares at £5 per share ^(1/2)	40,000	6,250
Preference shares: 2,000 shares at £8 per share	16,000	2,500
QCBs $2,000 \times £4$	8,000	1,250
	64,000	10,000

Although this is a paper for paper transaction, as the loan stock part of the consideration received is qualifying corporate bonds (QCBs) ^(1/2), for CGT purposes the value of the QCBs is treated as cash, and therefore a gain arises on the QCB element of the consideration received ^(1/2) as follows:

	£	
Proceeds (value of QCBs received)	8,000	^(1/2)
Less apportioned cost (W1)	(1,250)	
Gain	6,750	^(1/2)

However, because Salim has not actually received cash, the gain on the QCB element is frozen ^(1/2) and will become chargeable on the eventual sale of the QCBs. ^(1/2)

Sale of 1,500 preference shares and QCBs on 1 February 2026

The gain on the sale of 1,500 BiggerCo plc preference shares is as follows:

	£	
Proceeds	30,000	
Less apportioned cost (W1)		
$1,500/2,000$ ^(1/2) $\times £2,500$	(1,875)	
Gain	28,125	^(1/2)

As Salim has sold the QCBs, the gain of £6,750 frozen on takeover becomes chargeable. ^(1/2) QCBs are exempt assets for CGT, therefore the loss of £200 (£7,800 – 8,000) is not allowable. ^(1/2)

Salim's chargeable gains for 2025/26 are therefore £34,875 ^(1/2) (£28,125 + 6,750).

(W1)

Ordinary shares: $40,000/64,000 \times £10,000 = £6,250$

Preference shares: $16,000/64,000 \times £10,000$ ⁽¹⁾ = £2,500

QCBs: $8,000/64,000 \times £10,000$ ⁽¹⁾ = £1,125

10 marks

2)

The loan stock will no longer be QCBs, ^(1/2) as one of the conditions for loan stock to satisfy the definition of a QCB is that it cannot be converted into another currency. ^(1/2)

Therefore, if the loan stock received on the takeover of LargerCo plc by BiggerCo plc was convertible into euros, then the gain of £6,750 would not be frozen on takeover ^(1/2) but would be chargeable in 2024/25. ^(1/2)

On the disposal of the loan stock on 1 February 2026, the loss of £200 would be allowable ^(1/2) and Salim's chargeable gains for 2025/26 would be £26,125 (£28,125 – 200). ^(1/2)

Salim will be able to use the annual exempt amounts of £3,000 for 2024/2025 and 2025/26 assuming they are not already used. ^(1/2)

Max 3 marks

Total 13 marks