



Practical Tax People
Association of
Taxation Technicians

May 2017 Examination

PAPER 3

Business Compliance

Part II Suggested Answers

1.

Part 1

Simplified test one:

1 – Is the monthly average total input tax £625 or less? **(1/2 mark)**

Monthly average = $£31,430/12 = £2,619$. **(1/2 mark)**

Therefore, Loughman Ltd does not pass test one for the year. **(1/2 mark)**

Simplified test two:

1 – Is the monthly average of total input tax incurred less input tax directly attributable to taxable supplies £625 or less? **(1/2 mark)**

Monthly average = $£31,430 - £24,800 = £6,630 / 12 = £553$ **(1 mark)**

Part 1 is passed.

2 - Is the value of exempt supplies no more than 50% of the value of total supplies for the period? **(1/2 mark)**

$38,500/101,000 = 38\%$ **(1/2 mark)**

Part 2 is passed.

Therefore, Loughman Ltd has passed test two for the year as a whole **(1/2 mark)** and does not need to make an annual adjustment **(1/2 mark)** as all of the input tax of £31,430 remains recoverable. **(1/2 mark)**

Max 5 marks

Part 2

The value of the supply for VAT is the VAT exclusive cost of £855 ($£1,026 / 1.2$). **(1 mark)**

Part 3

A discount can be given:

- by an amendment on the wording of the invoice **(1/2 mark)** to say that the customer must ensure he has only recovered the VAT actually paid **(1/2 mark)**, or
- by issuing a credit note if VAT has been charged on the full price and the customer takes advantage of the discount. **(1 mark)**

As the prompt payment discount is received in this case the net value of the supply is $£1,200/1.2 = £1,000 - £30 = £970$. **(1 mark)**

Part 4

Letter format

Address

Date

(1 mark for presentation)

Dear Managing Director.

I set out the advice on two of the various VAT schemes below:

Cash Accounting

With the Cash Accounting Scheme a business:

- Pays VAT on sales when a customer pays
- Reclaims VAT on purchases when suppliers have been paid.

In order to join the scheme, a business must:

- Be up to date with its VAT returns
- Not have committed a VAT offence in the last 12 months
- Have taxable turnover of £1.35 million or less.

If turnover exceeds £1.6 million then a business must leave the scheme.

(1/2 mark each max 3 marks)

Flat rate scheme

With the Flat Rate Scheme:

- A business pays a fixed rate of VAT to HM Revenue & Customs
- A business keeps the difference between what it charges customers and pays to HM Revenue & Customs
- VAT cannot be reclaimed on purchases except for capital assets of more than £2,000.

In order to join the scheme VAT turnover must be £150,000 or less (excluding VAT), in the next 12 months.

A business cannot join the scheme if:

- A VAT offence has been committed in the last 12 months, e.g. VAT evasion
- The business joined or was eligible to join a VAT group in the last 24 months.

A business must leave the scheme if:

- On the anniversary of joining, its turnover in the last 12 months was more than £230,000 (including VAT); or
- Total income in the next 30 days alone is expected to be more than £230,000 (including VAT).

(1/2 mark each max 3 marks)

I hope that this provides you with a useful overview of the two schemes, please do not hesitate to contact me if you require any further information.

Kind regards

A Advisor

2.

Part 1

	£	£
Total earned		50,000
Less 5% deduction (1 mark)		<u>(2,500)</u>
		47,500
Less salary (1/2 mark)	20,000	
Employer's NIC (1/2 mark)	<u>1,640</u>	
		<u>(21,640)</u>
		25,860
Deemed employment income		<u>(22,724)</u>
£25,860 x 100/113.8 (1 mark)		
Employer's NIC due on deemed payment		<u>3,136</u>
Total NIC due:		
Employer's NIC - £3,136 + £1,640	(1/2 mark)	4,776
Employee's NIC:		
NIC due on salary - £20,000 - £8,060 * 12%	(1/2 mark)	1,433
NIC due on deemed payment £22,724 * 12%	(1/2 mark)	<u>2,727</u>
TOTAL	(1/2 mark)	8,936

Part 2

If the consultants are recruited as employees, employers' Class 1 National Insurance contributions at the rate of 13.8% are payable on their earnings in excess of £8,112 per year. **(1 mark)** An employment allowance of up to £3,000 can be set against this NIC. **(1/2 mark)**

If the consultants are recruited on a self employed basis, LO Ltd will have no National Insurance liability for them. **(1/2 mark)** The consultants will pay Class 2 and 4 National Insurance as they will be responsible for paying their own NIC. **(1/2 mark)**

Max 2 marks

Part 3

Any four from:

	Indicators of self employment	Indicators of employment
Mutuality of obligations	The individual is free to accept or turn down work if he desires. The engager is under no obligation to offer any work or further work.	The employer is obliged to offer work and the employee is obliged to do as the employer requests.
Right of control	Likely to be in control of most aspects of the work done.	An employer may control "what", "how", "where" and "when" work is done. However, a highly skilled employee may also exercise "what" and "how" as the employment demands.
Right of substitution	May sub-contract work or bring in assistance. Depending on the nature of the work, an individual may be engaged because of their personal reputation or skill and so no substitute will be acceptable.	It is rare for an employee to have the right to appoint a substitute.
Provision of own equipment	Will normally supply all small tools and bring in or hire in plant.	May sometimes supply own small tools or equipment. Employer will provide all plant and machinery.
Financial risk/ability to profit	Will quote on a job-by-job basis. Is able to make more profit by more efficient working, or may incur loss if overruns on time or if required to rectify defects in own time.	Paid whatever work is done. Benefits from the National Living / Minimum Wage and statutory holiday entitlement. An employee will bear little risk unless exceptionally work directly relates to a bonus or commission scheme. Or, if poor work affects appraisal for promotion or other benefits.
Opportunity to profit	Can profit if work is performed efficiently, or from re-charging and making a profit on materials.	May only profit under a bonus or incentive scheme. However, may benefit from tips or payments from third parties.
Length of engagement	Generally a fixed-term or short-term contract.	Contract will generally be open ended after probation period (if any).
Part and parcel of the organisation	May become "a fixture" in that his work brings him to the company regularly, but acquires no additional responsibilities or privileges as a result.	Is capable of being promoted or manages other staff. Part of works pension or SAYE scheme.

1 mark for each well explained point max of 4. All relevant points will be credited.

Part 4

Louis should ask new employees for a copy of their Form P45 which contains the tax code number operated by the previous employer. **(1 mark)**. Louis should operate this tax code until advised otherwise by HMRC. **(1 mark)**.

If the employee does not have a Form P45, Louis should complete a 'starter declaration' for the employee to determine the appropriate tax code. **(1 mark)**. This requires the employee to choose one of three options:

- If it is the employee's first job since 6 April, the personal allowance can be applied on a cumulative basis. **(1 mark)**
- If the employee has been in receipt of salary or taxable social security benefits since 6 April, the emergency code will be applied (i.e. the normal personal allowance on a month one basis). **(1 mark)**
- If the employee has another job or receives a pension, code BR will apply. **(1 mark)**

Max 4 marks

3.

Part 1

Payroll queries

A payroll report (known as a Full Payment Submission **(1/2 mark)** or FPS) needs to be submitted to HMRC on or before the time a payment is made to an employee **(1/2 mark)**.

Income Tax and employee NIC is deducted at the time the payment is made to the employee **(1/2 mark)**. Each tax month ends on the 5th of each month and the tax and NIC is due to HMRC on the 19th (22nd if paying electronically) of the month. **(1/2 mark)**.

The final payroll report in a tax year must indicate that it is the final report **(1/2 mark)** and should be sent on or before the last payday in the tax year **(1/2 mark)**.

A form P60 **(1/2 mark)** must be provided to all employees by 31 May following the end of the tax year **(1/2 mark)**. This reports the total amount paid to the employees in the year and the amounts of Income Tax and National Insurance contributions deducted **(1 mark)**.

Form P11D **(1/2 mark)** reporting the private medical insurance needs to be completed and provided to HMRC and employees **(1 mark)** by 6 July following the end of the tax year **(1/2 mark)**.

Form P11D is not required where benefits have been included in the payroll. **(1/2 mark)** Instead, the benefits are included in the form P60. **(1/2 mark)** A description of the benefits and their cash equivalents must be provided to employees by 31 May following the end of the tax year. **(1/2 mark)**

Form P11D(b) **(1/2 mark)** reporting the Class 1A National Insurance is due to HMRC by 6 July following the end of the tax year **(1/2 mark)**.

Max 7 marks

Part 2

Training and membership costs

The soft skills training would be considered work related training, which is not taxable **(1/2 mark)**.

The cost of joining the professional body will be taxable **(1/2 mark)** as it is not necessary in order to practice the profession **(1/2 mark)**.

The annual subscription would not be taxable as it is paid to an HMRC approved body **(1/2 mark)**.

Part 3

Travel queries

The client site attended by Dan will not be considered a temporary workplace **(1/2 mark)** as he will be attending this workplace for a period of continuous work exceeding 24 months **(1/2 mark)**. Travel costs to the client site will therefore be subject to PAYE tax and NIC **(1/2 mark)**, which will be calculated and paid via payroll **(1/2 mark)**.

Laura is an 'area based' employee so travel from her home to the edge of the area **(1/2 mark)** is subject to Income Tax and NIC as ordinary commuting. **(1/2 mark)** Travel to clients within the North West area is business travel and can be paid free of tax and NIC. **(1/2 mark)**.

Max 3 marks

Part 4

New client acceptance

The objectives of communicating with the previous/existing adviser are to ensure that:

- The incoming adviser is fully aware of all factors that may be relevant to the acceptance of the appointment and the effective handling of the client's tax affairs **(1 mark)**.
- The incoming adviser is fully aware of all factors that may have a bearing on ensuring full disclosure of all relevant facts to HMRC **(1 mark)**.
- The client's affairs are properly dealt with, on a timely basis, and that no filing deadlines, time limits for claims, elections, notices of appeal and other similar matters are missed in the transitional period **(1 mark)**.

4.

Part 1

Termination payment

The statutory redundancy pay and compensation for loss of office fall within s401 ITEPA 2003. As together they do not exceed £30,000 they will not be subject to tax **(1 mark)**.

The payment made directly into David's approved pension scheme is exempt from tax **(1/2 mark)** and the payment to David's legal advisor is also exempt from tax **(1/2 mark)**.

The bonus payment of £10,000 is taxable and as it was paid after Form P45 was issued the tax code OT must be used on a month 1 basis **(1 mark)**. The tax due is calculated as follows:

BR band £32,000 / 12 = £2,667	
£2,667 x 20% =	£533 (1/2 mark)
£7,333 x 40% =	<u>£2,933</u> (1/2 mark)
	£3,466

Part 2

Ending a contract of employment

A contract of employment can terminate without breach in one of the following ways:

- By proper notice duly given (this may not be less than the statutory period, whatever the contract may specify)
- By the passing of time, when fixed term contracts expire without renewal
- By agreement, that is the parties to the contract agree to end their relationship at any time and upon any terms
- By frustration (which may arise on death, ill health, imprisonment or prolonged absence)
- By payment in lieu of notice, if there is a contractual right to terminate an employment on making a payment in lieu of notice.

1 mark for each to a maximum of 4 marks.

Part 3

Construction Industry Scheme invoice

The CIS deduction will be at 30% as the supplier cannot be matched in HMRC's systems **(1/2 mark)**

Item	CIS deduction
Labour – deduction applies to whole amount	£3,000 (1/2 mark)
Materials – deduction to be applied only to 10% mark-up	£150 (1 mark)
Scaffolding hire – no deduction as hired from third party	- (1/2 mark)
Wear and tear - deduction applies to whole amount	<u>£30</u> (1/2 mark)
Total deduction to be applied	£3,180

Part 4

CIS deductions

The CIS deductions can be offset against Gravel Ltd's monthly PAYE payments **(1 mark)**. If the CIS deductions are greater than the PAYE due that month, the excess is carried forward **(1 mark)**. If there is an excess at the end of the year, once all PAYE reports are filed, the excess deductions will be refunded or set against corporation tax due **(1 mark)**.