November 2017 Examination

PAPER 1

Personal Taxation

Part I Suggested Answers

1. Shannon

House:

	£	
Rent:		
(£1,400 x 12 months)	16,800	**(½)**
Less: expenses		
Fridge freezer	(465)	**(½)**
Profit/(loss)	16,335	

Flat:

	£	
Rent:		
(£6,000 / 6)	1,000	**(½)**
Less: expenses		
Repainting	(2,000)	**(½)**
Profit/(loss)	(1,000)	

Property income assessment for 2016/17: £16,335 - £1,000 = £15,335. **(½)**

The fridge freezer is an allowable cost under the replacement of domestic items relief **(½)** and the cost of disposing of the old one is incidental and therefore allowable. **(½)**

As the flat was habitable, the painting works are not capital in nature and therefore an allowable expense. **(½)**

2. Alice

If Alice's total qualifying care receipts in 2016/17 are lower than her individual limit in the year they will not be subject to tax. **(1)** The individual limit consists of a fixed amount of £10,000 p.a. **(½)** and a weekly amount based on the age of each individual placed with her. **(½)** She will not be able to deduct expenses incurred when calculating the total receipts for this purpose. **(1)**

If Alice's qualifying care receipts exceed her limit, she will be taxed on the gross receipts, less expenses and capital allowances as normal (the profit method). **(1)**

Alternatively, Alice can elect by 31 January 2019 to be taxed on the gross receipts, less her individual limit (the simplified method). **(1)**

(Max 4 marks)

3. Zara

The 1,000 free shares Zara was awarded in March 2009 are withdrawn more than 5 years **(½)** after the date of award and so there is no tax charge. **(½)**

For the free shares awarded in February 2013, as they are being withdrawn between 3 and 5 years **(½)** after being awarded, the employment income will be the lower of:

The initial value on receipt = 1,000 x £3.50 = £3,500 **(½)**

Market value at withdrawal = 1,000 x £4.50 = £4,500 **(½)**

For the free shares awarded in February 2015, as they have been withdrawn less than 3 years **(½)** after the date of award, the market value at withdrawal will count as employment income, i.e. 750 x £4.50 = £3,375. **(½)**

This gives total employment income of (£3,500 + £3,375 =) £6,875 **(½)** for 2016/17.

4. Salim

Salim can claim an income tax reducer of £25,000 x 30% = £7,500 in 2016/17. **(½)** This can reduce his tax liability to nil, **(½)** but it cannot itself create a tax repayment **(½)** if Salim's tax liability is lower than £7,500 for the year.

Alternatively, Salim can chose to carry back the income tax reducer one tax year to 2015/16. **(½)**

Salim can also defer capital gains made up to a maximum of £25,000. **(½)** The gain will remain frozen until there is a chargeable event, **(½)** such as the sale of the shares in Breen Ltd, when the frozen gain will crystallise. **(½)**

He can defer gains made in the period one year before he subscribed for the shares **(½)** and up to three years after he subscribed for the shares, **(½)** ie 5 October 2015 to 5 October 2019.

Salim does not have to claim the full capital gains deferral, but can select the amount he wishes to defer. **(½)** As such, he can leave £11,100 of gains in charge in 2016/17 that will be covered by the annual exempt amount for the year. **(½)**

(Max 4 marks)

5. Sean

	£	
Discretionary trust (£27,500 x 100/55)	50,000	**(½)**
Savings (£4,125 x 100/80)	5,156	**(½)**
Dividends (£2,200 x 100/92.5)	2,378	**(½)**
Less: Personal allowance	(11,000)	**(½)**
Taxable income	46,534	

6. Jess

Diamond ring

	£	
Proceeds (deemed)	6,000	(½)
Less: Costs of sale	(300)	(½)
Net proceeds	5,700	
Less: Cost (probate value)	(7,000)	(½)
Allowable loss	(1,300)	

Antique chest of drawers

	£	
Proceeds	7,500	
Less: Costs of sale	(300)	
Net proceeds	7,200	(½)
Less: Cost	(3,750)	(½)
Gain	3,450	

Check the 5/3 rule:
5/3 x (7,500 – 6,000) = £2,500. **(1)**
The lower gain of £2,500 is therefore chargeable. **(½)**

7. Flora

There are "annual maxima" rules in a tax year where an individual has two employments. **(½)**

As Flora has more than one employment, she can apply for deferment of Class 1 contributions. **(½)**
The National Insurance Contributions Office (NICO) will determine whether the deferment will apply to her job at Lender plc or the charity. **(½)**

For whichever employment the deferment is granted to, Flora will pay Class 1 primary contributions at the rate of 2% **(½)** on earnings above the primary threshold. **(½)**

(Max 2 marks)

8. Sonal

Redder Ltd share pool:

Date	No. of shares	Cost
		£
1 February 2010	3,000	8,000 **(½)**
15 October 2013	1,000	2,000 **(1)**
(1:3 rights issue at £2 per share)		
15 October 2014	1,000	Nil **(½)**
(1:4 bonus issue)		
Total	5,000	10,000

The total number of shares Sonal now holds in Bluer plc is (5,000 x 5) = 25,000 **(½)** and the base cost of these shares remains at £10,000. **(½)**

9. Fernando

Fernando:

	£	
Proceeds (market value)	78,000	**(½)**
Less: Cost	(38,000)	**(½)**
Gain	40,000	
Gift relief (balancing figure)	(23,000)	**(1)**
Chargeable gain (55,000 – 38,000)	17,000	**(1)**

Alain's base cost is therefore the market value of the shares, less the gift relief £(78,000 - 23,000) = £55,000. **(1)**

10. David

David can appeal the late penalty notice if he had a "reasonable excuse" for failing to submit the return on time. **(½)**

Whilst "reasonable excuse" is not defined in the legislation, **(½)** it does set out what is not a reasonable excuse, for example relying on a third party is not a reasonable excuse unless the taxpayer took reasonable care. **(½)**

As a close family member died around the time of the tax return deadline, David may well have valid grounds for appeal. **(½)**

He would need to appeal on the grounds the bereavement prevented him attending to his tax affairs in the proper time. **(½)**

(Max 2 marks)

11. Joy

As Joy is UK resident and domiciled, she is taxable on both her UK and foreign pension on the arising basis. **(1)**

However, where a foreign pension is taxed on the arising basis **(½)**, a 10% deduction is available. **(½)** This means Joy will only be taxable on £27,500 x 90% = £24,750. **(½)**

Her total taxable pension income in 2016/17 is therefore £(750 + 24,750) = £25,500. **(½)**

12. Sylvia

There is a Pre-Owned Assets (POA) charge where a taxpayer gives away an asset and they can continue to benefit from the asset, **(½)** but the gift is not covered by the "gift with reservation" rules. **(½)**

As Sylvia continues to enjoy the benefit of the vase by retaining it in her house, **(½)** the POA rules mean an income tax charge is levied on her. **(½)**

For a chattel, the benefit is calculated by taking the value of the chattel at the date when Sylvia first becomes liable to the income tax charge (6 April 2016) **(½)** and multiplying it by HMRC's official rate of interest. **(½)** This income amount is reduced by any rents paid by the donor for using the chattel **(½)**.

The notional income amount for 2016/17 is therefore £85,000 x 3% = £2,550. **(½)**

Where the annual value is less than £5,000, there is no POA charge in the year, **(½)** so Sylvia will have no income tax charge in 2016/17. **(½)**

(Max 4 marks)

November 2017 Examination

PAPER 1

Personal Taxation

Part II Suggested Answers

1. NEWT

1)

		Non-savings	Savings	Dividends	Termination payment
		£	£	£	£
Salary	½ x 44,000	22,000 ½			
Termination payment (W1)		15,000			26,125
Car (W2)		2,160			
Loan (W3)		143			
Interest			2,500 ½		
Dividend				7,000 ½	
Net income		39,303	2,500	7,000	26,125
Less: Personal allowance *			-	-	(11,000) ½
Taxable income		39,303	2,500	7,000	15,125
32,000	@ 20%	6,400	½		
7,303	@ 40%	2,921			
500	@ 0%	-	½		
2,000	@ 40%	800	½		
5,000	@ 0%	-	½		
2,000	@ 32.5%	650	½		
15,125	@ 40%	6,050			
Income Tax liability		16,821			
Less: PAYE		(12,000)	½		
Income Tax payable		4,821		Due for payment by 31 January 2018 ½	

* Allocating the personal allowance against the termination payment is the most beneficial to Newt. However, candidates who allocated it to non-savings income received equal credit.

(W1) Termination payment		£	£	
		Termination payment	Normal earnings	
Statutory redundancy		7,000		½
Payment to leave early (assumed contractual)*			5,000	½
Contracted amount			10,000	½
Ex-gratia payment		80,000		
Tax-free		(30,000) ½		
Taxable before foreign service relief		57,000		
Relief for foreign service relief	13/24 ½ x £57,000 ½	(30,875)		
Taxable		26,125	15,000	

* Candidates who assumed the payment to leave early was non-contractual received equal credit.

The termination payment does not qualify for full exemption because:

- foreign service is not at least three quarters of total service; ½
- although total service has exceeded 10 years, the last 10 years of service was not spent abroad; 1
- although total service has exceeded 20 years, and at least half of total service was spent abroad, this did not include at least 10 of the last 20 years. 1

(W2) Car benefit		£	
List price			
When new		15,000	½
Leather seats		1,000	½
Leather steering wheel	Under £100	-	½
		16,000	
Applicable percentage			
Round down emissions		150 ½	
Less base emissions		(95) ½	
Excess		55	
Divide excess by 5 ½		11	
Add base percentage ½		16	
Applicable percentage		27	
Benefit	27% x £16,000	4,320	
Non-availability	6/12 x £4,320	(2,160)	½
		2,160	

(W3) Loan		
Average method		
Balance at start of year		12,000
Balance just prior to clearance		7,000
Average loan balance		9,500 ½
Benefit	9,500 x 3% ½ x 6/12 ½	143
Strict method		
6/4/16 – 5/9/16	5/12 x 12,000 x 3%	150 **1**
6/9/16 – 5/10/16	1/12 x 7,000 x 3%	17 **1**
		167

The average method of computation will apply as it is not beneficial for Newt to elect for the strict method and it is assumed that HMRC will not elect for the strict method either. ½

Max (18)

2)

To justify dismissal as fair dismissal, employers must show their principal reason relates to one or more of:

- The capability or qualifications of the employee for performing work of the kind which he was employed to do. ½
- The conduct of the employee. ½
- Redundancy. ½
- Legal prohibition or restriction by which the employee could not lawfully continue to work in the position which he held. ½
- Some other substantial reason which justifies dismissal. ½

Max (2)

2. JOHN

Our address

John's address

The date

(Top and tail as letter – 1)

Dear John

Venture Capital Trust (VCT) tax reliefs

Thank you for your letter.

I understand that you are interested in the tax reliefs that can accompany an investment in a VCT and when these might be withdrawn. Your interest is specifically in relation to a sum of £400,000 that you are looking to invest.

I am very happy to provide details of these tax reliefs but nothing I write should be taken by you to be investment advice ½, either recommending or discouraging you from making this or any other investment.

<u>Income Tax relief</u>

A 30% tax reducer ½ against your income tax liability is available on an annual subscription ½ of up to £200,000 ½. This tax reducer can reduce your liability to nil but cannot generate a repayment. ½

Dividends on up to £200,000 invested in a VCT in a tax year are exempt from Income Tax ½. For this relief it is not necessary that the shares are subscribed for – they can be acquired from another investor ½.

Income Tax relief will be withdrawn if the shares are sold or gifted away ½, other than to your wife ½, within 5 years ½. Where the shares are sold at arm's length, the tax reducer withdrawn is 30% ½ of the consideration received ½ albeit limited to the tax relief initially taken ½. Full withdrawal of relief ½ will occur if the disposal is not at arm's length or if the VCT loses its HM Revenue and Customs approved status ½.

<u>Capital Gains Tax relief</u>

Capital gains realised on the first £200,000 ½ of annual investment into a VCT are exempt ½ from Capital Gains Tax irrespective of the length of ownership ½; capital gains on any additional investment are subject to Capital Gains Tax in the normal way ½.

Similarly, capital losses realised on the first £200,000 of annual investment into a VCT are not relievable ½; capital losses on any additional investment are relievable against capital gains in the normal way ½ although such losses can never be relieved against income ½.

Please let me know if you have any queries.

Yours sincerely.

My name

Max (10)

3. SEBASTIAN HARRISON

1) DELEGATING WORK TO A JUNIOR

Delegating work to subordinate staff is permitted; **(½)** however, according to the Association of Taxation Technicians' Professional Rules and Practice Guidelines, the member will remain primarily responsible for any work carried out and advice given to a client. **(½)**

When work is delegated, the member should:

- be satisfied that the staff undertaking the tasks have been adequately trained **(½)** to carry out the work and have the necessary skills **(½)**
- exercise sufficient supervision to confirm that the work performed is adequate **(½)**
- remedy any defects in the work done if it is inadequate. **(½)**

Tutorial note:

This topic of delegating work is covered in syllabus area "Client Service" which is examinable in the Paper 1 syllabus and relates to the ATT's Professional Rules and Practice Guidelines section 5.

2) EMAIL RESPONSE

To:	Sebastian Harrison
From:	A. Supervisor
Date:	xxxxxxxxx
Re:	Capital Gains Tax liability – 2016/17 **(1 = layout as email)**

Dear Sebastian

Thank you for your recent email requesting an estimate of our professional fees and the after tax sale proceeds associated with the sale of your leasehold property in June 2016.

Your Capital Gains Tax liability for 2016/17 will be £16,625 **(½)** assuming you have no other capital disposals in the tax year to 5 April 2017. **(½)** A copy of the computation is attached to this email. This liability will be payable by self-assessment by 31 January 2018. **(½)**

In the calculation of your Capital Gains Tax liability, it is important to point out to you that whilst the estate agent and solicitor's fees are allowable deductions in the calculation of your chargeable gain, professional tax advice is not allowable. **(1)** To be allowable for Capital Gains Tax purposes, incidental costs of acquisition or disposal must be incurred wholly and exclusively for the purposes of acquiring or disposing of the asset. **(1)**

With regard to our professional fees relating to this advice, our fee is £2,150. **(½)**

Accordingly, the amount of sales proceeds left for your retirement (after accounting for Capital Gains Tax and our professional fees) will be £265,753 (£290,800 – £6,272 – £16,625 – £2,150). **(1)**

If we can be of any further assistance, please do not hesitate to contact us.

Kind regards

A. Supervisor

ATTACHMENT TO EMAIL: Capital Gains Tax Liability – 2016/17

		£	
Sale proceeds		290,800	(½)
Less: Incidental costs of disposal		(6,272)	(½)
Net sale proceeds		284,528	
Less: Depreciated cost			
£240,600 (½) x $\frac{85.444\ (W)}{96.041\ (½)}$		(214,053)	(½)
Chargeable gain		70,475	
Less: Annual exempt amount		(11,100)	(½)
Taxable gain		59,375	
Capital Gains Tax (at 28%) (½)		16,625	

Tutorial note:

The rate of Capital Gains Tax in 2016/17 has reduced for higher rate taxpayers from 28% to 20%; however, the reduced rate does not apply to disposals of residential property.

Working: Appropriate lease percentages

Date of purchase	1.10.2003
Length of lease	41 years
Date of expiry of lease	1.10.2044
Date of disposal	1.6.2016

Lease remaining at date of disposal = 28 years and 4 months **(1)**

	%		%	
% for 29 year lease	86.226			
% for 28 year lease	(85.053)			
	1.173	x 4/12	0.391	(1)
% for 28 year lease			85.053	(½)
% for 28 year and 4 month lease			85.444	

4. JASMINE

1) SPLIT YEAR BASIS

The split year basis will automatically apply in 2016/17 as Jasmine:

- is automatically UK resident in the current tax year (2016/17) **(½)**
  (in UK ≥ 183 days in the tax year) **(½)**

- is returning to the UK after ceasing full-time employment abroad **(½)**
  (i.e. the situation falls within Case 6 FA2013,Sch 45 para 49).

Overseas part:	6.4.16 to 30.6.16	(3 months)	**(½)**
	The overseas part ends on the last day of overseas work.		
UK part:	1.7.16 to 5.4.17	(9 months)	**(½)**

Consequences:
Overseas part = taxed on UK income only, overseas income exempt **(1)**
UK part = taxed on worldwide income **(½)**

Tutorial note:
Statutory references are not required from candidates, but are provided for reference.

2) TAXABLE INCOME

	£	
Employment income		
• Abroad (exempt whilst abroad)	Nil	**(½)**
• UK (£84,000 x 9/12)	63,000	**(½)**
Rental income		
• UK home (£9,000 x 3/12) (rented until returns to UK)	2,250	**(1)**
• UK cottage	6,000	**(½)**
• New York apartment (£15,000 x 9/12) (exempt whilst abroad, taxable when back in UK)	11,250	**(1)**
UK interest income	1,800	**(½)**
Total income	84,300	
Less: Personal allowance (available in full as UK resident)	(11,000)	**(1)**
Taxable income	73,300	
	======	

3) CAPITAL GAINS TAX

An individual is temporarily non-UK resident if: *(FA2013, Sch 45 para 110)*

- an individual becomes non-UK resident immediately following a period of UK residence **(1)**
- immediately preceding the year of departure the individual was UK resident for at least 4 of the 7 tax years, and **(1)**
- the period of non-UK residence is 5 years or less. **(1)**

Jasmine's taxable gains

	£	
Jewellery (£20,600 – £7,250)	13,350	**(1)**
Car		
– exempt regardless of residence status	Nil	**(½)**
Quoted shares		
– exempt as bought and sold whilst abroad	Nil	**(1)**
Chargeable gains in 2016/17	13,350	
Less: Annual exempt amount (available as UK resident)	(11,100)	**(½)**
Taxable gains	2,250	
	======	

Tutorial notes:

Chargeable assets sold whilst temporarily non-UK resident are liable to UK CGT if they were owned at the date of departure.

They are taxed in the tax year of return (i.e. 2016/17), not the tax year of sale.

The car is not a chargeable asset.

The quoted shares were acquired and sold while temporarily non-UK resident.

The diamond necklace is disposed of in 2013/14 but is taxed in 2016/17.