Practical Tax People

Association of Taxation Technicians

May 2015 Examination

PAPER 1

Personal Taxation

Part II Suggested Solutions

1.

1)

York & Co
Address

May 2015

Client Address (Format – 1 mark)

Dear Edward

Employee Shareholder Status shares

Further to your recent meeting with George, I have set out below a brief summary of how the ESS scheme operates.

ESS took effect from 1 September 2013 (1/2). In exchange for giving up certain employment rights (1/2) an employee can be given ESS shares (1/2). No consideration must be given for the shares other than entering into an ESS agreement giving up specific statutory employment rights (1/2).

The employment rights which are given up include:

- The right to receive statutory redundancy pay (1/2);
- The right to claim unfair dismissal (1/2); and
- Certain rights to request flexible working and training (1/2).

An additional notice period also has to be given in certain situations (1/2).

The market value of the ESS shares acquired must be at least £2,000 (1/2). The employee must obtain independent legal advice (1/2) on the ESS agreement. All costs of obtaining the advice must be met by the employer (1/2) and are not treated as a benefit in kind in respect of the employee (1/2).

(Max 6 marks)

2) **Income Tax implications**

The employee is deemed to have paid £2,000 (1/2) for the ESS shares. Therefore the first £2,000 of value is exempt from Income Tax (1/2). To the extent that the market value of the shares exceeds £2,000 the employee will be subject to Income Tax on the excess (1/2). The Income Tax relief is only available on the first occasion that ESS shares are acquired by that employee (1/2). The £2,000 exemption is not available if the employee holds a material interest in the company (1/2) that is at least 25% of the voting rights in the company (1/2).

(3 marks)

3) **Capital Gains Tax implications**

Providing the initial value of the ESS shares acquired did not exceed £50,000 (1/2) any growth in value of the shares on disposal will be exempt from Capital Gains Tax (1/2).

(1 mark)

Please feel free to contact me with any further questions.

Yours sincerely

Tax Consultant

(10 marks)

2.

	Non-savings £	Savings £	Dividends £	Total £
Termination payment (W1)	nil			
Salary from Aragon Ltd (W2)	3,500			
Salary from Tudor Tyrant Ltd (W3)	71,250			
Medical insurance (W4)	435			
Car benefit (W5)	8,138			
Fuel benefit (W6)	5,045			
Interest free loan (W7)	609			
Share option gain (W8)	37,500			
Bank interest (W9)		75		
3 ½% War loan (interest paid gross) (1/2)		1,550		
Dividends (W10)			2,222	
	126,477	1,625	2,222	130,324
Less: personal allowance (W11)	nil			
Taxable income	126,477	1,625	2,222	130,324
£31,865 @ 20% (1/2)	6,373			6,373
£94,612/£1,625 @ 40% (1/2)	37,845	650		38,495
£2,222 @ 32.5% (1/2)			722	722
Less: VCT relief £35,000 @ 30% (1)				(10,500)
High income child benefit charge (W12)				1,066
Tax liability				36,156
Less: PAYE deducted at source (1/2)				(27,000)
Less: tax paid on bank interest (W13)				(15)
Less: tax credit on dividends (W14)				(222)
Tax payable				8,919

Workings

W1 The first £30,000 will automatically be exempt from tax (1/2). As Catherine carried out some of her duties outside the UK she may be entitled to the foreign service exemption in respect of some or all of her termination payment (1/2). If at least ¾ of the employment relates to overseas duties then the entire termination payment is exempt from tax in the UK (1/2).

Total years of employment - 15

Time spend outside UK

1 June 1999 – 31 May 2006 7 years
1 June 2009 – 31 May 2014 5 years
12 years (1/2)

12/15 = 80% therefore entire payment exempt (1/2)

W2 As Catherine is UK resident and domiciled, she will be taxed on her non-UK employment income on a receipts basis in the UK (1/2).

W3 £95,000 x 9/12 = £71,250 (1/2)

W4 £580 x 9/12 = £435 (1/2)

W5 The CO_2 emissions of Catherine's car are 190 g/km so the percentage to be applied is 12% + 1% for each 5g/km above 95 g/km i.e. 12% + 19% ((190 - 95)/5) = 31% (1)

The benefit is therefore £35,000 x 31% x 9/12 = £8,138 (1/2)

W6 £21,700 x 31% x 9/12 = £5,045 (1/2)

W7 £25,000 x 3.25% x 9/12 = £609 (1)

W8

Market value on exercise	£3.00 x 30,000 =	£90,000 (1/2)
Less: cost	£1.75 x 30,000 =	£52,500 (1/2)
Exercise gain		£37,500 (1/2)

W9 (£120 x 100/80)/2 = £75 (1)

W10 £2,000 x 100/90 = £2,222 (1/2)

W11 Taxable income exceeds £100,000 therefore personal allowance needs to be abated (1/2).
½ (£130,324 - £100,000) = £15,162 Exceeds personal allowance therefore fully abated. (1/2)

W12 As income exceeds £60,000 the high income child benefit charge will be equal to 100% of the child benefit claimed therefore:

Total child benefit claimed in 2014/15 £20.50 x 52 = £1,066 (1)

W13 Bank interest credit £75 - £60 = £15

W14 Dividend tax credit £2,222 - £2,000 = £222 (1/2 for bank interest and dividend credit)

(Maximum 15 marks)

2) All benefits included on the annual P11D return will be subject to class 1A National Insurance contributions (1/2). This amount is only payable by the employer (1/2).

(1 mark)

3) If Catherine files a paper tax return it must be submitted by 31 October 2015 (1/2). If Catherine files her tax return online it must be submitted by 31 January 2016 (1/2). For filing two days late, Catherine will incur an automatic penalty of £100. (1).

(2 marks)

4) Any 4 of the following (1/2 mark for each of the following):

- The names of the employer and employee.
- The date when employment began and the date on which the employee's period of 'continuous employment' began.
- Details of remuneration including the intervals at which it is paid.
- Terms and conditions relating to hours of work, holidays and holiday pay.
- Information on where rules on health and safety may be found.
- The length of notice required on either side to terminate the contract.
- The period of employment (if not indefinite).
- The job title or description of the work the employee is employed to undertake.
- The place of work.
- Any collective agreements that affect the terms of employment.
- Details of the currency in which remuneration will be paid, additional remuneration and any terms and conditions relating to return to the UK if the employee is required to work outside the UK for longer than one month.

(Maximum 2 marks)

Total 20 marks

3.

To: Margaret (Format – 1 mark)
From: Tax Consultant
Date: May 2015
Subject: Fire at Jasper Cottage

Dear Margaret

Further to your recent meeting with Edmund, I have set out below a brief summary of the information you requested.

1)

The destruction of an asset will be treated as a disposal for Capital Gains Tax purposes (1/2). Any compensation received i.e. insurance proceeds or compensation (1/2) will be treated as the sale proceeds for Capital Gains Tax purposes (1/2). If no compensation was received i.e. if the asset was uninsured (1/2) then the destruction will give rise to a capital loss (1/2). The date of disposal will be the date the insurance proceeds are received (1/2). Any scrap or residual value will be treated as part of the sales proceeds (1/2).

Rollover relief will be available if within 12 months (1/2) of receipt of the capital sum, Edmund replaces the assets (1/2). The capital gain on the loss of the original asset (1/2) can be rolled over against the base cost of the new asset. (1/2). The replacement asset does not have to be the same but has to be a chargeable asset (1/2). If Edmund retains any of the insurance proceeds, the amount of cash retained will be immediately chargeable (1/2).

The claim must be made within 4 years of the end of the tax year of disposal (1/2).

Note – candidates who discussed the chattels exemption were also awarded credit.

(Maximum 6 marks)

2)

If an asset is partly damaged it will be treated as a part disposal for Capital Gains Tax purposes (1/2). The allowable cost will be calculated as follows:

A/(A+B) x original cost

A = insurance proceeds received.
B = value of remaining asset. (1)

The date of disposal is the date the insurance proceeds are received (1/2). Any amount of money used to restore the asset will be treated as enhancement expenditure (1/2).

It is possible for Edmund to make a claim so that the receipt of insurance proceeds is not treated as a part disposal, providing one of the following conditions is met (1/2):

- All the insurance proceeds are used to restore the asset (1/2).
- Any insurance proceeds retained are small (1/2), less than 5% of the proceeds or £3,000 (1/2).
- The insurance proceeds received are less than £3,000 or not more than 5% of the value of the asset (1).

The claim must be made within 4 years of the end of the tax year of disposal (1/2).

(6 marks)

3)

The Data Protection Act 1998 has two main aims. To give data subjects (1/2) rights to know what data is held by them on computer and in most paper records (1/2) and to ensure that data is handled properly by the data controllers (1).

(2 marks)

4)

Cold calling is not of itself unprofessional conduct (1/2). However, repeated cold calling may become offensive and lead to a complaint (1/2).

(1 mark)

Yours sincerely

Tax Consultant

(15 marks)

4.

1)

Chargeable gain on grant of lease on Flat 1

The term of the lease is in excess of 50 years and therefore is a long lease for tax purposes.

Allowable cost = £150,000/(£150,000 + £310,000) x £110,000 = £35,870 (1 1/2)

	£
Gross premium (1/2)	150,000
Less: cost	(35,870)
Gain	114,130

(2 marks)

Chargeable gain on grant of lease of Flat 2

The term of the lease is less than 50 years and therefore is a short lease for tax purposes. For tax purposes a lease expires on the first date on which the landlord can terminate the lease, so in this case 30 years.

Capital element of premium = 2% x (30 – 1) x £97,000 = £56,260 (1 1/2)

Allowable cost = £56,260/(£97,000 + £290,000) x £110,000 = £15,991 (2)

	£
Capital element of premium	56,260
Less: allowable cost	(15,991)
Gain (1/2)	40,269

(4 marks)

Chargeable gain on grant of sub-lease of the Gatehouse

This is the grant of a short sub-lease out of a short lease.

Capital element of premium = 2% x (20 – 1) x £35,000 = £13,300 (1 1/2)

Year of head-lease remaining at grant = 24 years 79.622% (1/2)
Year of head-lease remaining when sub-lease expires = 4 years 21.983% (1/2)
Year of head-lease remaining when head-lease acquired = 35 years 91.981% (1/2)

Allowable cost = £55,000 x (79.622 – 21.983)/91.981 = £34,465 (1)

	£
Premium received (1/2)	35,000
Less: allowable cost	(34,465)
	535
Less: income element of the premium received - restricted £(35,000 – 13,300) = £21,700 (1/2) Less; allowance for original premium paid 20/35 x (55,000 – 2% x 34 x 55,000 (1)	(535)
Gain (1/2)	Nil

Cannot reduce the gain below zero to produce a capital loss (1/2)

(Maximum 6 marks)

		£	£
Gains on Flat 1		114,130	
Gains on Flat 2		40,269	
Gains on Gatehouse		0	
Total chargeable gains for 2014/15			154,399
Less: Annual exempt amount	(1/2)		(11,000)
Taxable gain			143,399
£143,399 @ 28%	(1/2)		40,152
Capital Gains Tax payable			40,152

(1 mark)

(Maximum 13 marks)

2)

<u>Joint tenancy</u>

- The holders do not have separate identifiable shares but hold as one entity (1/2).
- On death the right of survivorship applies so that the interest of the deceased automatically accrues to the other (1/2).
- If a joint tenant wishes to dispose of the property all joint tenants must agree (1/2).

<u>Tenants in common</u>

- Each owner has title to his own share (1/2).
- On death the share of a tenant in common can pass under their will or intestacy (1/2).

(Maximum 2 marks)

Scots Law

<u>Joint property</u>

- *The holders do not have separate identifiable shares but hold as one entity (1/2).*
- *On death the interest of the joint owner accrues to the other (1/2)*
- *Anne and Euan cannot hold property in this way as it is generally only available to trustees or members of clubs (1/2)*

<u>Common property</u>

- *Each owner has title to his own share (1/2).*
- *On death the share of a common owner can pass under their will or intestacy (1/2).*

(Maximum 2 marks)

(15 marks)