May 2015 Examination

PAPER 2

Business Taxation & Accounting Principles

Part II Suggested Solutions

1.

	£	£	
Profit per accounts		350,000	
Add			
Depreciation	17,000		½
Loss on disposal of fixed assets	8,000		½
Provision for repairs	4,000		½
Legal costs re lease (allowed)	-		½
Legal costs re abortive property	2,000		½
Entertainment - customers	5,000		½
Entertainment – staff (allowed)	-		½
Penalty	1,350		½
Lease costs 15% x £2,400	360	37,710	½
		387,710	
Less			
Capital allowances		(21,220)	½
Taxable total profits		366,490	

Capital allowances	**Pool**	**Special rate**	**Allowances**	
WDV b/f	17,000			
Laminator	(3,000)			½
	14,000			
Additions				
Laminator	10,000			½
AIA	(10,000)		10,000	½
Heating system		7,500		½
AIA		(7,500)	7,500	½
Car – emissions >130g/km		15,000		½
WDA				
18% x 14,000	(2,520)		2,520	½
8% x 15,000		(1,200)	1,200	½
WDV c/f	11,480	13,800		
Total allowances			21,220	

	Total	**FY 2014**	**FY 2013**	
Limits	1,500,000	375,000	1,125,000	½
	300,000	75,000	225,000	
Profits	366,490	91,622	274,868	½
At 21%/23%		19,241	63,220	1
1/400 x (375,000 – 91,622)		(708)		½
3/400 x (1,125,000 – 274,868)			(6,376)	½
Corporation tax due	75,377	18,533	56,844	

(12)

2.

1)

All three partners will be able to claim relief for the loss against other income for 2014/15, the tax year in which the loss was incurred. ½ This is subject to the general cap on reliefs against general income, which applies from 2013/14 ½ onwards. Relief is limited to the greater of £50,000 or 25% of the individual's adjusted total income for the tax year.1 A claim can also be made to set the loss against total income of the previous tax year, i.e. 2013/14. ½ Claims can be made against either or both years ½ and the tax payer can decide which claim comes first. ½ Claims must be made by 31 January following the end of the tax year in which the loss arose: 31 January 2017. ½. The loss can also be extended to capital gains. ½

Robinson and Metcalfe, as partners in the continuing business, can offset the loss against the future trading profits of the catering school. ½ The carry forward is automatic, however a claim to establish the amount of loss to be carried forward must be made within four years from the end of the tax year in which the loss arose: 5 April 2019. ½

As a retiring partner, Noble can also make a terminal loss relief claim. A claim for the loss of the last twelve months of trading ½ can be can be made against the trading income ½ of the tax year in which he retires then the three ½ tax years prior to that tax year, based on the latest year first. ½ The loss will include any overlap relief to which Noble is entitled. ½ This means that Noble can make a claim against other income of 2014/15 and/or a terminal loss claim. He can decide which claim will be made first. ½ The time limit for a claim is four years from the end of the tax year in which the loss arose: 5 April 2019. ½

As a new partner, Metcalfe can make a claim to carry back losses incurred in his first four tax years ½ in the partnership against his general income ½ of the three previous tax years ½, setting the loss against the earliest year first. ½ The claim can be made alongside a current year claim ½ and the taxpayer decides which claim takes precedence ½. This claim too is subject to the cap on reliefs explained above ½. Claims must be made by 31 January following the end of the tax year in which the loss arose: 31 January 2017. ½

Note – candidates also received credit for commenting that as Metcalfe's basis period runs to 5 April 2015, it is possible that he will not have a loss for 2014/15.

Max (12)

2)

This situation represents a conflict of interest ½. The default position would be to cease to act for both parties ½. Both clients should be informed of the conflict ½ Any decision to continue to act for both clients must be taken with their full knowledge and agreement ½. With the agreement of the client, this may be effected by using separate teams ½. The decision may be taken to act for one client only, ½ in which case, this should be Robinson, as he made the first approach ½ and Noble should be advised of the decision as soon as possible ½.

Max (3)

3)

Partners who retire are still liable for any outstanding debts incurred while they were partners, ½ unless the creditor has agreed to release them from liability. ½

They are also liable for debts of the firm incurred after their retirement ½ if the creditor knew them to be partners (before retirement) ½ and has not had notice of their retirement. ½

Therefore, it is vital on retirement that partners give actual notice to all the creditors of the firm, ½ for example by having their names removed from the letterhead on which letters are written. ½ The retiring partners may have an indemnity from the remaining partners with respect to this issue. ½ Max (3)

Total (18)

3.

1)

Meera
Profit and Loss Account for the year ended 31 May 2014

	£	£	Format ½
Sales		100,000	
Purchases	60,000		
Closing stock	(10,000)	50,000	½
Gross profit		50,000	
Expenses			
Wages	14,500		
Rates and water (£3,000 - £833)	2,167		1
Light and heat	1,500		
Repairs	700		
Telephone	600		
Motor expenses (£1,800 + £450)	2,250		1
HP interest	400		½
Loan interest	10,000		
Accountancy	800		½
Depreciation	9,000		½
Use of home	120		½
		42,037	
Net profit		7,963	

Meera
Balance Sheet as at 31 May 2014

	Cost £	**Depn £**	Format **NBV £**	½
Fixed assets				
Shop	200,000	(4,000)	196,000	½
Equipment	12,000	(3,000)	9,000	½
Van	8,000	(2,000)	6,000	½
	220,000	(9,000)	211,000	
Current assets				
Stock		10,000		
Bank		3,500		
Prepayment		833		½
		14,333		
Current liabilities				
Accrual		(800)		½
Net current assets			13,533	
Long term liabilities				
HP creditor (£8,000 - £2,400 + £400)		(6,000)		1
Loan creditor		(125,000)		½
			(131,000)	
Net assets			93,533	

Capital introduced			
(£15,000 + £75,000 + £450 + £120)		90,570	1½
Drawings		(5,000)	½
Profit		7,963	½
		93,533	

Workings

	£	
Closing stock		
Sales value	20,000	
Mark-up (100/200 x 20,000)	10,000	
Cost price	10,000	1
Purchase of van		
HP repayments (£200 x 48)	9,600	½
Cost of van	8,000	½
HP interest	1,600	
Yearly (£1,600/4)	400	1
Prepayment		
Rates and water		
(£1,000 x 10/12)	833	½
Depreciation		
Shop – depreciation (2% x £200,000)	4,000	½
Equipment – depreciation (25% x £12,000)	3,000	½
Van – depreciation (25% x £8,000)	2,000	½
	9,000	
Use of car		
Capital introduced		
(1,000 miles at 45p)	450	½
Use of home		
Capital introduced		
(£10 per month for 12 months)	120	½

2)

Meera will pay Class 2 contributions calculated at a fixed weekly rate ½. She will also pay Class 4 contributions ½ based on her annual profits. Her employees will pay Class 1 primary contributions ½ and she will pay Class 1 secondary contributions in respect of their salaries ½. If she provides her employees with taxable benefits, Meera will also have to pay Class 1A. ½ Max 2

Total 20

4.

1)

Separate chargeable gains for both Elmer and his wife ½ would be calculated based on the difference between the sales proceeds and the cost of the shares ½. Both Elmer and his wife will be entitled to deduct any current year capital losses in full ½ and any losses brought forward to the extent that they do not exceed the annual exempt amount ½. They will then each be entitled to deduct an annual exempt amount ½ in arriving at a figure of taxable gain.

Max 2

2)

As Elmer is a director of the company ½ and controls more than 5% of the company's share capital ½ and has owned the shares for the year prior to disposal ½ the gain will be eligible for entrepreneurs' relief ½ .

He will not be entitled to entrepreneurs' relief on the disposal of the property ½ because a market value rent has been charged for the property ½.

His wife will not be eligible for entrepreneurs' relief ½ as she is not an employee or officer of the company ½.

Max 3

3)

As Elmer has already made a disposal qualifying for entrepreneurs' relief, the £10m lifetime limit must be reduced by the amount of relief already claimed. 1

1

4)

Elmer and his wife can both defer the gain on the disposal of their shares if they invest in shares in their son's company provided the new shares qualify as EIS shares. 1 Shares are not qualifying assets for the purpose of rollover relief. ½

Max 1

5)

In a sale of assets, the purchaser buys the assets from the company ½. In a share sale, the purchaser will be buying the shares of the company from Elmer and his wife ½.

In an asset sale, the purchaser decides which liabilities it wishes to take on. ½. In a share sale all the liabilities remain with the company ½.

Where a share sale takes place, then the purchaser will want to protect themselves from unforeseen liabilities by asking for a warranty from Elmer and his wife 1.

Max 3