



The Association of Taxation Technicians

## MAY 2007 EXAMINATION

### EXAMINERS' REPORTS

#### Paper 1 - Personal Taxation

##### General Comments

Overall the candidates made a good attempt at Paper 1, although certain questions caused problems for most candidates. There also seemed to be some confusion as to why a law question appeared on the paper (several candidates noting that they were not sitting the law paper yet and so had not studied this).

##### Part I

A large number of candidates did not attempt every question; in summary the most common errors were:

1. Candidates spent time calculating tax liabilities, when only asked for the personal allowance figure.
2. A significant number of candidates either did not identify the chattels rule, or incorrectly applied the restriction to the gain less £6,000, instead of applying the formula to the proceeds.
3. Very few candidates identified that the indexation figure should not be rounded. Also, several candidates used indexation figures to the current date.
4. This question was generally well answered, although some candidates explained the type of penalties that would be due but did not state the amounts (or calculate interest).
5. This question was well answered by most candidates, although some candidates applied the 37% restriction to the wrong figure.
6. Only around half of the candidates identified that the percentage tables would be required here and those who did often applied incorrect percentages.
7. Candidates were confused by the information in respect of 2005/06 (to test the connected person loss rules). Some candidates simply stated that prior year information was not relevant. A number of candidates applied Gift Relief to the disposals.
8. This question was very well answered by most candidates. The most common error was not applying a March 1982 comparative, having misunderstood the reference to no election having been made.
9. Many candidates were not aware of the rules about short tax returns. Those that had learnt these did well on this question.
10. Most candidates answered this question correctly until the point at which half of the basic allowance is allocated to the spouse. At this point either (i) the allowance was shared before applying the restriction or (ii) half of the total allowance was allocated. Only a handful of candidates reached the correct final answer.

11. Many candidates did not apply the concessionary split year residency rules, although most correctly identified that the non-UK resident would not be chargeable to UK tax.
12. Many candidates explained the process of identification checks, rather than the Money Laundering offence itself. This was due to misreading the question. (One candidate did remark that 'money laundering is when accountants take money out of a bank account'.)
13. This was generally well answered; the most common error was stating that all were non taxable as they were state benefits.
14. Most candidates scored some marks on this question, although many did not give enough detail (such as identifying the limits for proceeds to be excluded). Some misread the question and discussed wasting assets etc.
15. It was apparent that many candidates had not studied this; candidates typically obtained either full marks or no marks.

## Part II

### Question 1

Generally a very popular and expected question.

(a) The main problem with Jeremy's income was in grossing up the trust income and dividends using the appropriate tax rates. Many candidates did not appreciate the restriction on double tax relief.

With Christine some candidates seemed to think that NSB interest was a net figure and that relief for the pension contribution was given by expanding the basic rate tax band.

(b) The majority of candidates realised that David's salary would be taxed under the PAYE system. However with regard to the interest there were two common misconceptions:

(i) that being a student was a tax exempt status!

(ii) that all interest from his father would be assessed on his father overlooking the £100 rule, and that interest from his grandmother would follow similar rules.

(c) Most candidates realised that splitting the income from property jointly was not beneficial. However, many could not suggest any remedies and/or failed to realise that any other method of splitting the income would require that there be a tenancy in common.

### Question 2

1) Most candidates appreciated that there would be an exemption, but generally did not realise it would be a complete exemption if tenants lived in as lodgers. Candidates often failed to mention the £40,000 letting exemption.

2) Own property - it was generally realised that rent-a-room relief was available, but many candidates then incorrectly deducted the actual expenses incurred as well.

Properties 1 and 2

Income and expenses correctly dealt with, but some candidates were unaware that the wear and tear allowance was restricted by Council Tax.

Property 3

Again income and expenses correctly dealt with. Some candidates were unsure as to whether the 2% calculation based on the premium received was a tax relief as many treated it as income. Very few scripts showed any knowledge of the treatment of the sublease.

3) The description of joint tenancy and tenancy in common was very well answered, probably as a result of appearing on the sample paper.

### Question 3

1) This question caused the biggest problems. The fact that cash received on a takeover would cause a gain to arise was not appreciated by many candidates.

The method of apportioning the original cost of the shares in Thomas Limited according to the market values of the shares/cash received from Excalibur plc was frequently not done correctly. In fact, the amount of shares and cash received was frequently miscalculated.

2) No problems in this section for those who calculated the correct number of preference shares received.

3) Again no real problems, other than the fact that many candidates deducted the personal allowance from £30,000 when it was actually stated that this sum was taxable income.

### Question 4

1) Generally well answered with many candidates scoring full marks. The most common errors arising were:

- Using the incorrect percentage for car benefits and not always restricting it on a time basis
- Job seekers allowance is assessable income
- The car received on redundancy does form part of Claude's redundancy package.

2) The description of summary and constructive dismissal was generally well answered, but many candidates got the two systems of dismissal the wrong way round.

## **Paper 2 - Business Taxation & Accounting Principles**

### Part 1

#### Question 1

This was the best answered question on the paper – the majority scoring well.

#### Question 2

Another well answered question, although there was some confusion by a minority of students over the term “drawing offices”.

#### Question 3

This was another straight-forward question which was reasonably well answered. Some students failed to make it clear that the payment on account figure was based on the previous year’s liability.

#### Question 4

Of the students that attempted, this few did well. The majority of the marks were on the calculation of interest on late payment and should have been obtained by the industrious student.

#### Question 5

Most answers detailed most of the main themes of a Letter of Engagement. A minority, however, didn’t appear to know what the letter was and answered the question on the basis that the sole trader was carrying out work for the tax adviser.

#### Question 6

This was a disappointing question. Too many candidates focused on taxation differences between sole traders and companies and not the more general legal differences.

#### Question 7

Well answered by most.

#### Question 8

A well answered question on the chattel rules.

#### Question 9

There were some good answers. However many failed to highlight the importance of a qualifying asset for rollover relief.

#### Question 10

Answers to this question were disappointing. Lots of candidates were confused as to the appropriate percentages needed to form the two different types of group.

#### Question 11

This was the first of the two VAT questions and, by far, the better answered. There was confusion over the “future” test for registration which led to many shedding marks.

#### Question 12

This was the second of the two VAT questions and was very poorly answered.

### Question 13

This was the final short form question for four easy marks. Many students obtained full-marks. However, a fairly large minority produced "T accounts" as an answer, when the question clearly asked for "journals".

## Part II

### Question 1

The majority of candidates did very well on this question. The most common error/omission being the calculation (or lack of) overlap relief for Henry in 2006/07. Presentation of the answers was generally poor as most candidates chose to show the profits for each partner separately and did not always make it clear the difference between their calculations of the profit share as per the accounts and that assessable for each tax year.

### Question 2

This question was generally fairly well answered although many candidates did not appear to understand the difference between the accounting changes and the adjustments for tax purposes, and therefore explained tax adjustments to part (1) instead of changes required to prepare a set of accounts. They then repeated the adjustments for part (2). In several cases, candidates did not bother to explain that first year and writing down allowances were available in their answer for part (3) and simply stated that capital allowances could be claimed.

### Question 3

There were many very good answers to this question, with the majority of candidates gaining high marks. The most common errors were in the calculation of the deposit interest; many candidates basing their answer on the amounts received in the period or apportioning the total based on the number of months in each period. Part (4) explaining the action required to change accounting date was often poorly answered. Candidates stated the rules for being allowed to change the accounting date, but in many cases appeared unclear over what action the company had to take. Many thought the company had to have permission from H M Revenue & Customs.

### Question 4

There was a wide range of answers to this question, some being very good but others appeared to have little knowledge of how to prepare accounts. The 'T' accounts gave many candidates problems, with entries being shown as debits rather than credits and many apparently not knowing which accounts to prepare and therefore showing 'T' accounts for every item which had a balance in the question. Several candidates deducted the drawings figure as an expense.

The most common errors in the profit and loss account were to ignore the amounts due from customers in the sales figure and that owed to suppliers in the purchases. Several candidates included both cars when calculating the depreciation charge. There were also several candidates who were not clear on how to layout the balance sheet, showing the cost of the car as a fixed asset but then deducting the depreciation charge as a current liability.

Very few candidates gave a good explanation in their answer to part (4) and in many cases just gave a simple statement that some items were not allowed for tax purposes.

## Paper 3 - Business Taxation: Higher Skills

### Short-form questions

Question 1 – A well answered question. The majority of candidates dealt with first year allowances correctly, identified the short accounting period and private use adjustment.

Question 2 – A reasonably answered question but many candidates failed to identify that STI for 2005/06 was covered by the personal allowance.

Question 3 – A reasonably answered question but many candidates failed to cope with basic double entry bookkeeping principles. Many candidates failed to deal with the payment in advance.

Question 4 – The majority of candidates could explain the tests to be considered for compulsory registration and give reasons for voluntary registration.

Question 5 – Answers varied greatly. Some candidates made a deduction for input VAT on the motor car when the question clearly stated the car expenditure was in addition to the standard rated expenditure.

Question 6 – A badly answered question. Many candidates failed to calculate the timing difference. Those that did failed to recognise the company should be taxed at the marginal rate.

Question 7 – A generally well answered question. Candidates recognised the share of profits between partners.

Question 8 – Most candidates could state the tax payable but without explaining how double tax relief was given.

Question 9 – A disappointing set of answers with a number of candidates failing to read the question properly e.g. candidates failing to state the effect of being UK resident for corporation tax purposes.

Question 10 – A well answered question with the majority of candidates calculating the tax liability correctly.

Question 11 – On the whole, a reasonable set of answers. Most candidates could state the when the instalments were due.

Question 12 – A reasonably answered question with most being able to identify the relevant conditions.

Questions 13 – A fairly disappointing set of answers. Candidates seemed intent on giving situations when an accounting period commenced which was not asked for in the question.

Question 14 – A fairly disappointing set of answers. Candidates failed to give concise answers showing a lack of knowledge in this area.

### Long-form questions

#### Question 1

##### Part A

This required candidates to calculate incorporation relief and the subsequent base cost of the shares in the limited company.

Most candidates relayed the rules in s162 TCGA without any problems and very detailed

answers were produced. The stronger students were able to correctly calculate the relief available on the gain and followed that through reflecting the correct base cost of shares.

The majority of candidates struggled on the calculations, but were awarded marks for method where the incorrect figure was picked up.

### Part B

Students displayed excellent knowledge in this part of the question and were able to produce extremely detailed answers, often gaining full marks. This part of the question was pretty straightforward and performance was in line with expectations. There were a lot of irrelevant comments and sometimes citation of company case law, which was not required in the question, but on the whole this was answered very well.

### Part C

A lot of candidates struggled with this part of the question. A lot did not even attempt it. Those that did tended to get the contents of the articles and memorandum mixed up. No students discussed how the articles could be changed by special resolution and only a few mentioned the use of Table A. Overall, the performance of students on this part was quite disappointing.

### Question 2

This question required candidates to calculate income tax payable for a sole trader. Some excellent answers were produced with a lot of candidates gaining full marks.

Candidates were very well prepared for this question and answers reflected this. The only area which caused some difficulty was the reduction of the capital allowance for private use of the car. All candidates restricted the allowance to £3,000 but often did not then go a step further.

The answers to this question were very well written and presented.

## **Paper 4 - IHT, Trusts & Estates**

### Short- Form Questions:

#### Question 1

Most of the three conditions were given correctly with good clear examples given.

#### Question 2

This question was answered very well. Most candidates gave all three conditions and gained full marks.

#### Question 3

Marks were available for registered shares and bearer shares. Candidates still gained the marks if they stated that shares were located where they are registered. Most candidates gained the mark for stating that the bank account is located where the branch is.

#### Question 4

Most of the candidates who answered this question gained all three marks. Only a minority didn't know the answer and didn't make an attempt to answer the question.

#### Question 5

Again, this question was answered well and some good practical answers were given.

#### Question 6

Most candidates were able to calculate the unindexed gain. From this point, there was a mixture of mistakes. Some missed taper relief and some gave no annual exemption.

#### Question 7

Some attempts. Few candidates showed understanding of the difference between s165 and s260. Very few candidates mentioned the effect of the holdover and stated that taper and the annual exemption would be lost.

#### Question 8

Most candidates stated that no IHT would be due on the transfer out of the A & M trust, under the old rules, but very few gained the extra mark for stating that the beneficiary would need to be 18.

#### Question 9

Some good answers. Credit was given if the candidate showed rental income of £5,000 or £4,500 and all candidates who attempted this question showed all sources of income and made a deduction for the tax paid at source.

#### Question 10

Mixed answers. Few candidates mentioned the form IHT100. Many candidates stated the filing date incorrectly.

#### Question 11

The question asked for the value of the shares to be included in the estate for which there



were three marks. Whilst the calculations of the two methods were mainly correct, very few candidates calculated their share valuation price by the number of shares. (ie  $12,000 \times \text{£}9.90 = \text{£}118,800$ ). Therefore many didn't achieve the third mark.

#### Question 12

Mixed answers and many candidates did not attempt this question. Some tutorial bodies were concerned about the wording of this question and in view of this, credit was given where the candidate explained the concepts of PETs, GWROB, and Pre-Owned assets.

#### Question 13

A very well answered question with many correct answers. If a mistake was made in the calculations, follow through marks were given which meant that some good scores were obtained. The calculations were mainly well laid out and clear.

#### Question 14

Again, this was a well answered question with most candidates gaining at least 1 mark.

#### Long-Form Questions:

All (save one) candidates made an attempt at all three long form questions, and allocation of time to the questions posed seemed to be generally effective.

#### Question 1

The first three parts of the questions allowed well organised candidates to gain good marks based on methodical and clear workings. A disappointing minority either gave no BPR on the shop in Sussex or 100% relief.

Part 3 - candidates must remember that law forms an important part of the syllabus – a number seemed to be at a loss with a non-tax part of the question.

#### Question 2

This was generally well attempted, though there was a small minority who appeared to be unaware of the basic rules for taper relief on chargeable gains. Part 5 was not well tackled – candidates became confused as between advancement of capital and capital gains on the Trustees, and some got through their answer without mentioning IHT exit charges at all.

#### Question 3

The first part of the question was quite well tackled, though very few candidates noticed the "buy-sell" clause in the partnership agreement. A significant number considered, erroneously, that the property company shares would qualify for 100% BPR. As in Question 2, candidates must remember that much of IHT advice for this paper rests on straightforward planning – use of exemptions, normal expenditure out of income etc – and marks were awarded accordingly.

## Paper 5 - VAT

### General comments

In general I found that students did not read the questions properly. Indeed if there were two parts of the question a lot of students failed to answer one part. Students that were prepared for the exam seemed to score well - those that didn't scored badly. In general question around ethics and law were extremely poorly answered by all students.

### Short-form questions

#### Question 1

A lot of students failed to grasp the concept that the initial payment of £2,000 would have been treated as a gross value. Those that did, in general, answered the question well.

#### Question 2

In general this question was answered well.

#### Question 3

This question was poorly answered. Attempts were often minimal.

#### Question 4

In general this question was answered well. However, a surprising number of people did not seem to know the answer, despite the fact that it could be obtained from the legislation.

#### Question 5

Again, those students that attempted this question answered it well.

#### Question 6

This question was, in general, poorly answered.

#### Question 7

Few students were able to explain the Lennartz principle and how this would have impacted - a number of students failed to consider the VAT treatment of the purchase of the van at all.

#### Question 8

In general this question was answered well.

#### Question 9

In general this question was poorly answered - few candidates attempted to answer all parts.

#### Question 10

Candidates answered this question badly.

#### Questions 11, 12 and 13

Candidates seemed ill prepared for these questions on ethics - a number seemed to simply guess at the answers.

## Long-form questions

### Question 1

This question was attempted by most candidates with many answers scoring highly.

Part 1 – This was a straight forward question with most candidates picking up the majority of the marks available. A common error was a failure to mention that a late payment would incur the default surcharge and not the late return.

Part 2 – This part was also answered well by many candidates, but a failure to stipulate the relevant SLN extension dates was the most common cause of lost marks.

Part 3 – Very few candidates achieved full marks for this section with only very basic answers given in the majority of cases. However credit was given wherever possible for all relevant inclusions.

Part 4 – Most candidates attempted this part but the results were very mixed. Where the candidate knew about mis-declaration penalties, good answers were produced. However less well prepared candidates often produced lengthy answers of little value.

### Question 2

Many candidates did not seem to have a good grasp of the operation of the capital goods scheme. Most identified that adjustments were due over a five year period, but identifying the amount of the initial claim and of subsequent adjustments proved challenging. Particular difficulties arose from calculating the value of the final adjustments and recognising the restriction applicable to the final adjustment. Few candidates correctly identified the period in which the final adjustment should take place.

### Question 3

The best answers to this question were from candidates who methodically worked through the points in the letter and ensured that they had addressed them all. Although this is a difficult area of VAT legislation, much of the answer could be derived from identifying the exceptions set out in the legislation. There was little evidence that candidates had referred to the legislation which is surprising. Many candidates failed to identify that the 'donation' presented problems and answers to the different land scenarios were of varying quality. More candidates were aware of the benefits/pitfalls of waiving exemption and most identified the rules specific to new commercial buildings.

### Question 4

This question was attempted by most candidates but there was some evidence of time pressure in the quality and quantity of the answers given.

Part 1 – Most candidates stated the correct place of supply but a high number of answers missed the likely requirement to register in Germany for VAT/TVA.

Part 2 – Generally this part was not answered well by the majority of candidates, with a worrying lack of recognition of Sch5 services. Most missed the point that UK VAT registration would be a likely consequence.

Part 3 – Most candidates were aware of the 8<sup>th</sup> directive, producing reasonable answers and credit was given for all relevant inclusions.

Part 4 – This part caused confusion for a number of candidates with a significant number missing the import valuation point completely. Some merely stated that VAT should be charged on the goods on resale in the UK at the standard rate. The requirement for the addition of incidental expenses in the valuation calculation was also a common omission.

## **Paper 6 - Business Compliance**

### Short-form questions

The majority of the 14 candidates attempted all of the questions and scored highly, achieving 25-35 marks out of the possible 40.

In relation to the tax technical questions, the majority of candidates attempted all questions and answered them well. The number of candidates was not sufficient to draw a consistent picture of where marks were lost.

Candidates who scored less highly tended to be those who did not answer the law and ethics questions (Questions 9, 14 and 15) correctly. In most cases marks were lost because candidates either simply did not answer the question or gave answers which were far too brief for the marks allocated. Question 15 asked for the essential elements of a contract, candidates commonly listed the contents of an employment contract.

### Long-form questions

#### Question 1

Part 1 – Generally well answered – however too few candidates used a letter format.

Part 2 – No comment

Part 3 – Only one candidate correctly calculated the NI contributions with most not getting the correct director treatment for a partial year employment.

Part 4 – No comment

#### Question 2

Part 1 – Candidates made a fair attempt

Part 2 – No comment

Part 3 – Few candidates were able to provide a full answer

Part 4 – No comment

#### Question 3

A question well answered with most candidates gaining a good mark.

#### Question 4

Most candidates were able to provide a sufficient answer but without depth to the answer.

## **Paper 7 - Practice Administration & Ethics**

### General

Many candidates did not properly read the questions, especially the long-form questions. Hence they tended to move away from the main thrust of the questions, concentrating on minor parts that scored very few marks. A considerable number of candidates did not follow the requirements of the questions that called for answers to be in the form of a letter or a memo and so failed to pick up easy marks.

Many of the candidates appeared well prepared to answer questions on administration, but less well prepared in other areas.

### Short-Form Questions

- 1) A straightforward question on VAT invoices, answered well by the majority of candidates.
- 2) Many candidates were unclear in their answers, omitting to mention the due date for payment for VAT liabilities, for example.
- 3) Candidates scored well in this simple question on CT penalties.
- 4) Although many candidates could advise on the rule for dates of enquiries, many were unable to apply that knowledge.
- 5) Most candidates made assumptions in this question, often without stating reasons why. For those who explained the different options, this question provided easy marks.
- 6) Many candidates were very unsure as to due dates. Few candidates recognised that the trustees of the trust were liable for some of the tax.
- 7) Answered generally well. Candidates lost marks by failing to explain the 'error or mistake' route.
- 8) Generally answered well, most candidates earning full marks.
- 9) This question was poorly answered, with only a dozen candidates obtaining full marks. Many candidates assumed the question concerned negligence and so listed out the requirements for the Tort of Negligence to be proved.
- 10) This question was answered very well with most candidates earning full marks.
- 11) Generally answered well, most candidates earning full marks. However, it was noticeable that a large number of candidates thought that tax avoidance only involved using formal avoidance schemes.
- 12) Generally answered well, most candidates earning full marks.
- 13) This question was not answered particularly well. Most candidates went to great length explaining 'clear desk' and 'lockable filing cabinet' procedures. However, they did not mention that client confidentiality also relates to the accountant using knowledge for his own personal purposes or for the benefit of other clients.
- 14) Generally answered well, most candidates earning full marks.

### Long-form questions

#### Question 1

This question was attempted fairly well, but candidates failed to earn marks by not giving sufficient explanation of basic points. For example, candidates mentioned that a letter of engagement was required, but failed to actually explain that the letter is a formal contract between adviser and client. Similarly, many candidates noted the requirement for a clearance letter, and they listed the information usually requested, but failed to explain the ethical purpose behind such a letter.

The most common error made by all but a dozen candidates was failing to realise that the

client was a company. Candidates mentioned the importance of identifying clients but only talked about taking copies of driving licences and passports, thereby losing a number of marks concerning checking the identity of companies.

Finally, a number of candidates simply gave the amendment deadline of 31 December 2007, without explaining how they reached that answer.

### Question 2

The majority of candidates poorly attempted this question. Many candidates stated that they were appalled by the conduct of the accountant, and listed his professional obligations, but failed to link the two areas together to show how the obligations had possibly been breached. Many candidates also lost marks because they were unaware of the complaints procedure in the PRPG. Most candidates stated that a complaint should be made against the accountant, simply stating that he should be expelled from the Association, completely ignoring the steps in the complaints procedure that lead up to this point.

The majority of candidates went to great length to explain the various methods of billing, but the question had already stated the billing method proposed by the accountant, and so wasted time going into too much irrelevant detail.

Finally, it should be noted that members falling foul of the complaints procedure are not “terminated”, neither are they “dismembered”.

### Question 3

This was a straightforward question in which many candidates scored very well. Presentation was poor in many cases, though, and many candidates did not answer the precise question which was to advise on the first three payments due. A significant minority of candidates failed to identify that there may have been a conflict of interest.

### Question 4

Many candidates answered the first part of the question well, although were often unable to comment on expenses that were reimbursed. The second part of the question exposed a large number of candidates who appeared ignorant of the Finance Act process; many considering that the whole Act was in force prior to the Budget and some considering that HMRC, rather than Parliament, debated the proposals!