



**Association of Taxation Technicians**

## **Examination**

November 2007

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**PAPER 1**

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**PERSONAL TAXATION**

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ANSWERS (without marks)

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1) Calculation of liability:

	Non Saving £	Saving £	Total £
Rent	16,000		16,000
Trust income (2,760 x 100/60)	4,600		4,600
Bank (780 x 100/80)		975	975
	20,600	975	21,575
Less: personal allowance	(5,035)		(5,035)
Taxable income	15,565	975	16,540
Tax charged thereon:			
2,150 @ 10%	215		
13,415 @ 22%	2,951		
975 @ 20%	195		
Income tax liability	3,361		
Less: tax suffered at source			
on trust income	(1,840)		
on bank interest	(195)		
Income tax payable	1,326		

2) Penalties and interest: None as all tax has been settled by 31 January 2008  
 HMRC deadline: 30 April 2009, 12 months after the end of the quarter  
 to 30 April 2008

- 3) 1) Scottish law (the proper law of the contract)  
 2) English law (the lex situs)  
 3) English law (the lex situs)

4) Entitlement is:

<u>Working tax credit</u>		<b>£</b>
Basic element		1,665
Couple's element		1,640
30 hour element		-
Childcare element	80% x 52 x £120	4,992
		8,297
Less: restriction for excess income	37% x (21,100-5,220)	(5,876)
		2,421
<u>Child tax credit</u>		
Family element		545
Child element	3 x £1,765	5,295
		5,840
Total credits		£ 8,261
<u>Income</u>		
Salary	Nick	18,000
	Heather	3,000
Interest	100	100
		21,100

The first £300 of the interest income is disregarded for calculating tax credits.

5) Calculation is:

	£	£	£	Total £
Proceeds		28,000		
Cost		(5,000)		
Indexation allowance (162.6 – 160.3/160.3)		(72)		
Gain before taper		22,928		
		<div style="display: flex; justify-content: space-around;"> <span>← <b>NBA</b></span> <span><b>BA</b> →</span> </div>		
		6/4/98 – 5/4/00 5,395	6/4/00 – 5/10/06 17,533	
NBATR (8 + 1 years)		(1,888)		
BATR (2+ years)			(13,150)	
Gain after taper	3,507		4,383	7,890

6) Tax reliefs available:

Income tax: tax reducer of £4,000 (20% of £20,000)

CGT: Holdover of £20,000 of the pre-taper gain from 2005/06

Revised gain for 2005/06:

	£
Original gain before taper (£16,000 tapered x 100/25)	64,000
Gain held-over against EIS investment	(20,000)
Remaining gain for 2005/06	44,000
Revised chargeable gain – after full BATR	11,000

Future sale:

- No gain on disposal of EIS shares themselves
- Held over £20,000 gain will crystallise with full BATR → £5,000 gain in 2010

7) The Phoenix Ltd shares need to be of negligible value:

- at the time the negligible value claim is made
- and at the earlier time at which the loss is claimed to arise

The claim needs to be made by 5 April 2008

8) He could set the capital loss against:

- the £60,000 gain.
- his income of 2005/06
- his income of 2006/07

Most tax efficient is to set against income of 2005/06 as:

- relief against income is achieved at 40% whilst relief against the capital gain is at 10% given availability of BATR.
- relief against the earlier year's income gives greater entitlement to repayment supplement.

9) Interest calculation:

Date		£
5 May 2006	$20,000 \times 5 \frac{3}{4}\% \times 6/12$	575
5 November 2006	$15,000 \times 5 \frac{3}{4}\% \times 6/12$	431
	$5,000 \times 5 \frac{3}{4}\% \times 4/12$	96
	(accrued income scheme charge)	1,102

10)

		£
Proceeds		120,000
Costs of disposal		(5,000)
Net proceeds		115,000
Cost of acquisition		(10,000)
Indexation allowance	$162.6 - 141.1/141.1 = 0.152$	(1,520)
Gain before taper relief		103,480
NBATR	8 + 1 years = 35% taper	(36,218)
Gain after taper	65%	67,262
Annual exemption		(8,800)
Chargeable gain		58,462

Tax thereon		£		
(33,300 – 22,965)	10,335 @ 20%	2,067		
(58,462 – 10,335)	48,127 @ 40%	19,251		
		21,318		

11) The properties must be:

- available for letting for at least 140 days in the year; and
- actually let for at least 70 days in the year; and
- not more than 155 days fall during periods of longer-term occupation
- a period of longer-term occupation is a continuous period of more than 31 days.

12) Any six from:

- names of employer and employee

- date employment began and date on which employee's period of continuous employment began
- details of remuneration including intervals at which it is paid
- terms and conditions relating to hours of work
- terms and conditions relating to holidays, holiday pay, sickness leave, sick pay, pensions and pension schemes
- length of notice required on either side
- period of employment – if not indefinite
- job title or description of work to be undertaken
- place of work
- details of currency in which remuneration will be paid
- terms and conditions re return to UK if employee is required to work outside the UK

13) Information is regarded as made available if:

- it is contained in the return for the relevant year (or the two immediately preceding chargeable periods); or
- it is contained in any claim for the relevant year (or the two immediately preceding chargeable periods), or
- it is in any accounts, statements or documents accompanying the return or claim or produced in the course of an enquiry into the claim; or
- it is information the existence of which, and the relevance of which, could reasonably be expected to be inferred by the officer from the foregoing, or which is notified in writing to the officer

Answer 1

**John**

Foreign pension	£30,000	@ 90%	27,000
State pension			5,500
No winter fuel allowance (tax free)			
Foreign bank interest			550
Dividend income			3,000
REIT (taxed at 22%)			10,000
			-----
			46,050
PA (restricted to basic)			(5,035)
			-----
			41,015
			-----
Tax:			
	2,150	@ 10%	215
	31,150	@ 22%	6,853
	4,165	@ 40%	1,666
	550	@ 40%	220
	3,000	@ 32.5%	975
			-----
VCT	10,000	@ 30%	9,929 (3,000)
Tax credits: dividend			(300)
REIT			(2,200)
			-----
			£4,429
			-----

Answer 1 continued

**Sally**

Income from Estate of mother (4,000 x 100/80)	5,000
State pension	<u>2,200</u>
	7,200
PA	(7,280)
Tax due	nil
Tax repayment	<u>£1,000</u>

Pension contribution – qualifies as below £3,600 (gross) and Sally is less than 75 and resident in UK for previous three years – no effect on income tax liability – tax relief given at source

Rental income:

Rent		10,500
Expenses:		
Agency fees	1,575	
Water rates	200	
Electricity	200	
Council tax	1,500	
Interest on loan	7,000	
Capital allowances (£2,000 x 50% FYA)	<u>1,000</u>	11,475
		—

Loss (carried forward) £(975)

Capital Gains

Proceeds		150,000
Cost	300,000 x $\frac{150,000}{450,000 + 150,000}$	= 75,000
		—

Exempt 75,000  
(8,800)

66,200

CGT

2,150	10%	215
34,612*	20%	6,922
29,438	40%	11,775

£18,912

\*Basic rate band extended by gross pension contribution to £31,150 + (£2,700 x 100/78) = £34,612

Points in letter to Sally

1. Income from furnished holiday letting is treated as business income
2. Losses can be set against other sources of income for the current and previous tax year
3. Capital allowances can be claimed on the cost of furniture and equipment, instead of the wear and tear allowance
4. Income qualifies as net relevant earnings for personal pension purposes
5. Property qualifies as business asset for capital gains taper relief
6. Property also qualifies as business asset for capital gains rollover relief

Answer 2

**Harry Smith 2006/07**

<b>(a) Peaches plc</b>	No	Cost	
March 1990	1,000	3,000	
Index			
<u>149.9 – 121.4</u>		704	
121.4			
August 1995	<u>2,000</u>	<u>8,000</u>	
	3,000	11,704	
Index			
<u>162.6 – 149.9</u>		992	
149.9			
December 2004	2,000		
	—————	—————	
	5,000	12,696	
Sold	<u>(3,000)</u>	<u>(7,618)</u>	
Proceeds			30,000
Cost			(7,618)
			—————
Gain			22,382
			—————
Taper – non-business asset = 8 years + bonus year (9 years)			

**(b) VCT – exempt**

**(c) Employer company shares**

Proceeds	40,000
Cost	<u>10,000</u>
Gain	<u>30,000</u>

Held 1 year – 50% taper (business asset)

**(d) Painting**

Deemed proceeds	6,000
Cost	<u>(8,000)</u>
Loss	<u>(2,000)</u>

**Summary**

	<u>35%</u>	<u>50%</u>	
Peaches	22,382		
Employer		30,000	
Painting	(2,000)		
Losses b/f	(10,000)		
	—————	—————	
	10,382	30,000	
Taper relief 35%/50%	(3,634)	(15,000)	
	—————	—————	
Chargeable AE	6,748	15,000	21,748
			<u>(8,800)</u>
			£12,948
			—————
CGT @ 40%			<u>£5,179</u>



Answer 3.

i)

- Residence is defined as presence in UK for 183 days or more in tax year
- Per HMRC guidance, days of arrival and departure in the UK are normally ignored (IR20) but this rule may be disregarded and actual hours in the UK taken into account if HMRC consider that their published position is being abused.
- An individual leaving the UK is treated as still UK resident if visits to UK average 91 days or more per tax year (averaged over 4 years).
- As Elizabeth is leaving the UK to take up full time employment abroad for a period covering a complete tax year, her year of departure will by concession split into two periods. She will be treated as resident up to the date of her departure and non-resident thereafter.

ii)

- The property income will be liable to UK income tax irrespective of Elizabeth's residence status as it is UK income.
- Personal allowance are still available while non-resident if the individual is a UK citizen.
- Rental income based on rents accrued less expenses
- Expenses allowable include rates, insurance, property maintenance, agent's letting fees, professional fees
- If let furnished a claim can be made for renewal of furniture or an annual wear & tear allowance of 10% of gross rents less any payments which are the landlord's obligation
- Improvements to property not allowed against rental income – can be added to cost of property on disposal
- Interest on loan to purchase property allowed as an expense
- As Elizabeth will be a non-resident landlord, basic rate tax must be deducted by the agent from the net rents received (or by the tenant, if there is no agent). This can be avoided if:
  - tax returns are submitted and tax affairs are up to date (SI 1995/2902)
  - de minimis (if rent < £100 per week)

iii)

- CGT due on a gain on disposal of chargeable asset calculated as proceeds less acquisition cost, indexation allowance and taper relief
  - Costs include cost of improvements to property, agent's fees and legal fees of buying & selling
- Principal Private Residence Relief available –
  - must occupy house as PPR at some point during ownership
  - PPR is available for periods of actual occupation, and
  - last three years of ownership
  - Deemed occupation for PPR while working abroad, but
  - must reoccupy on return (unless required by terms of employment to reside elsewhere in UK).

- If PPR and then let as residential accommodation, can obtain further relief for the lowest of:
  - £40,000
  - amount equivalent to PPR relief
  - amount of gain accruing while let.
  
- iv)
  - CGT is only chargeable on disposals of assets owned before she left the UK if she returns to UK within five complete tax years of departure (s10A Taxation of Chargeable Gains Act 1992). Assuming this is the case:
    - Disposals made in the year of departure are taxable in the year of departure, irrespective of whether Elizabeth has obtained non-resident status at the time of the disposal
    - Disposals made in later years are taxable in the year of return.
  
- v)
  - Gains on assets acquired while abroad and disposed of before return to the UK will be exempt, any losses will not be available to carry forward
  - If Elizabeth disposes of the house abroad after she returns to the UK she will be assessed on her gain, but if she has sustained a loss, the loss will be available to set against other capital gains.

Answer 4.

Golden Hello			10,000
Salary		100,000	
Pension 5%		<u>(5,000)</u>	95,000
Bonus (voted 2007/08)			-
			105,000
Accommodation			
GAV		4,000	
Cost	500,000		
Less	<u>75,000</u>		
	425,000	@ 5%	21,250
Expenses:			
Council tax	3,500		
Water	500		
Electricity	750		
Cleaning	1,500		
	_____		6,250
Building insurance not included – liability of property owner			
Furniture & fittings	£20,000 @ 20%	4,000	
		_____	35,500
Interest free loan:			
5 July	50,000		
5 April	<u>30,000</u>		
Average balance	40,000		
@ 5% x 9/12		1,500	
50,000 @ 5% x 5/12	1,042		
30,000 @ 5% x 4/12	<u>500</u>	1,542	
Therefore use average method			1,500
Assuming HMRC does not opt for actual basis as difference minimal			
Laptop – one for private use			
£2,500 @ 20%			500
Moving expenses:			
Agent's fees	4,500		
Stamp duty	15,000		
Legal fees	2,500		
Removal costs	<u>2,500</u>		
	24,500		
Less exempt	<u>8,000</u>		16,500
			_____
			£159,000
			_____

Action re non-disclosure

1. Advise client in writing to make full disclosure to HMRC
2. Explain possibility of criminal prosecution where Revenue 'discover' fraud; voluntary disclosure normally results in lower scale of penalty
3. If he refuses to disclose, must cease to act for him – must write to client stating this
4. Inform HMRC that you have ceased to act, but give no reason
5. Cannot inform HMRC of omission without client's permission
6. If contacted by new accountant for professional clearance cannot give reason for non-longer acting, but should refer new accountant to correspondence between self and former client.
7. Consider whether Money Laundering Regulations apply.