Association of Taxation Technicians

Examination

November 2007

PAPER 2 – PART II

BUSINESS TAXATION & ACCOUNTING PRINCIPLES

TIME ALLOWED – 3 HOURS
(for Part I and Part II)

- You are required to answer **all** questions in Part I (printed separately) and Part II.
- The maximum number of marks for each question in Part II is shown in brackets.
- For Part II, start each answer on a new sheet of paper.
- All workings should be shown and made to the nearest month and pound unless the question requires otherwise.
- Marks are specifically allocated for good presentation.

1. James is self employed as a landscape gardener. You are provided with the following accounts for the year ended 31 March 2007.

Profit and Loss Account	£	£
Sales		80,000
Less: Purchases		(17,000)
Gross Profit		63,000
Expenses:		
Wages	5,000	
Use of home for business purposes	208	
Motor expenses	2,000	
Repairs and renewals	780	
Insurance	345	
Telephone	168	
Advertising	275	
Accountancy	375	
Legal costs	450	
Subscriptions	180	
Depreciation	5,467	
		(15,248)
		47,752
Bank interest received		47
Net Profit		£47,799

You have the following information:

The balance on the pool brought forward for capital allowance purposes was £12,380. During the year James purchased a lawnmower costing £560 which he used for both customers and his own garden. He estimated that the business use was 80%.

The bank interest represents the amount received in respect of James's bank account during the year, net of tax.

Subscriptions includes £100 in respect annual membership of a golf club, where James takes customers to entertain them.

Legal costs relate to the purchase of a workshop which had not been finalised by the year end.

During the year James used plants with a sales value of £150 for his own garden, these were included in purchases at £75.

James made a gift aid donation of £250 net.

In January and July 2007, James made payments on account totalling £13,000.

You are required to calculate the total liability of James for 2006/07 for Income Tax and Class 4 National Insurance, assuming no other income or outgoings during the year. Calculate the tax payments due in 2008 and state the due dates.

(12)

2. Valentino Ltd had the following profit and loss account and balance sheets in respect of the year ended 31 December 2006.

Profit and loss account	£000
Turnover	12,382
Cost of sales	(7,356)
Gross Profit	5,026
Distribution costs	(381)
Administrative expenses	(1,099)
Operating profit	3,546
Interest (paid)	(186)
Profit before tax	3,360
Taxation	(1,137)
Profit after tax	2,223
Dividends	(750)
Retained profit	£1,473

Balance sheets		31 December 2006 £000		31 December 2005 £000
Fixed assets		12,943		11,080
Current assets				
Stock	3,950		2,835	
Debtors	6,312		5,849	
Cash at bank	–		478	
	10,262		9,162	
Current liabilities				
Creditors	1,238		858	
Overdraft	316		–	
Taxation	1,563		2,385	
Proposed dividends	383		296	
	3,500		3,539	
Net current assets		6,762		5,623
		19,705		16,703
Creditors falling due after more than one year				
12% Debentures		(2,834)		(3,685)
		16,871		13,018
Financed by:				
Share Capital		3,563		1,183
Profit and loss account		13,308		11,835
		16,871		13,018

(Continued)

2. *(Continuation)*

You also have the following information:

Fixed assets purchased during the year totalled £2,975,000. During the year plant and equipment with a net book value of £195,000 was sold for £168,000. Plant and equipment with a net book value of £17,000 was scrapped with no sales proceeds.

A proportion of the 12% debentures were redeemed during the year.

You are required to:

1) Prepare a cash flow statement for the year ended 31 December 2006. (15)

2) Explain why, despite Valentino making a profit for the year, his bank position has worsened. (3)

Total (18)

3. Royston Ltd (qualifying as a small company under s.247 Companies Act 1985) has been trading for many years making up accounts to 31 December in each year.

For the year ended 31 December 2006 it has made the following purchases:

1) A new van was purchased on 25 February 2006 for £12,000.

2) New computer equipment was purchased in June 2006 for £10,000. It has an estimated useful life of three years after which it will be donated to a local charity.

3) In August 2006 a contract was signed for the purchase of a new heating system costing £100,000. The installation took place over several months and payments under the contract were made as each part of the contract was certified completed as follows: 40% on 30 September 2006, 40% on 31 December 2006 and 20% on 31 March 2007. The contract price included equipment representing 25% of the total cost which was certified as satisfying the criteria for energy saving.

4) In January 2006 it signed a contract for the purchase of land for £75,000 on which a warehouse and factory were constructed. The cost of site preparation was £50,000 and the cost of construction of the building was £225,000. The warehouse was in use by 30 November 2006.

5) In September 2006 it purchased a factory from Duxford Ltd for £500,000 which included £100,000 for the land. The factory and land had been purchased by Duxford Ltd unused from a developer in September 1991 for £750,000, of which £50,000 was for the land. Duxford Ltd also makes up its accounts to 31 December annually. It used the factory in its trade until September 2000 since when it has been empty. In the period to 31 December 2006, Royston Ltd spent £40,000 on renovating the factory. As soon as the renovations were complete, in January 2007, Royston Ltd started using it for trading purposes.

6) In December 2006 a car with CO_2 emissions of 110 gm per km was purchased for £14,000. The car was six months old having previously belonged to the managing director.

You are required to explain the capital allowance implications of the above purchases and to show clearly your calculations of the amounts which may be claimed for the year ended 31 December 2006. (18)

4. Ray Biggs commenced trading on 6 April 2005. For the year ended 5 April 2006 he had adjusted trading profits of £10,000. During the following year he borrowed a substantial sum of money to invest in the latest technology for use in the business. Due to high interest charges and capital allowances, he has an adjusted loss for 2006/07 of £60,000, but anticipates profits of £40,000 for 2007/08.

For the three years prior to the commencement of trading, he was employed earning £30,000 per annum. He also received dividend income of £900 (net) each year from UK company shares which he still holds.

Ray has been told by a friend that he can set his losses against his other income and receive a tax repayment. However, he had assumed that the losses would be set against this current year's income and therefore has not budgeted for paying any tax. He is now wondering whether he would be better off obtaining a tax repayment and has asked you to advise him on the options available to him.

You are required to draft a letter to Ray explaining the options available to him in respect of obtaining loss relief. You should consider the cash flow advantages/disadvantages of each option as well as the amount saved. (12)