Association of Taxation Technicians

Examination

May 2006

PAPER 1

PERSONAL TAXATION

SUGGESTED SOLUTIONS

THE ASSOCIATION OF TAXATION TECHNICIANS
PAPER 1 - MAY 2006 - PART I – SUGGESTED SOULTIONS

1.

Pension	4,250	4,250		
BSI	3,500		3,500	
Dividends	2,500			2,500
PA	(4,895)	(4,250)	(645)	
	5,355	_	2,855	2,500

Tax:		
2,090	@ 10%	290
765	@ 20%	153
2,500	@10%	250
		612
Tax credits (700 + 250)		(950)
Repayment		£(338)

2.

Pension	4,500
Interest	2,000
PA	(4,895)
	1,605
Tax @ 10%	£160
Tax due on gift aid payment £1,000 @ 22%	£220
Tax deducted Interest	400
Higher of above	220
Repay (restricted)	£180

3.

GRV			4,500
Cost	200,000		
Extension	50,000		
	250,000		
Less	75,000		
	175,000	@ 5%	8,750
			£13,250

4.

State pension		3,750
Employer pension		10,000
		13,750
PA		(7220)
		£6,530
2,090	@10%	209
4,440	@22%	977
MCA 5,975 @ 10%		(598)
		£588

5.

List price	£15,000			
@ 31% (15+ 16 (220-140=80x1/5))		4,650	x 6/12	£2,325

6.

Employment income		15,000
BSI		1,100
PA		(4,895)
		£11,205
2090	@ 10%	209
8,015	@ 22%	1,763
1,100	@ 20%	220
		£2,192

7.

WTC:	
Basic	1,620
Couple	1,595
30 Hour	660
CTC:	
Child (2 x 1690)	3,380
	7,255
Restriction	
23,000-5,220= 17,780@ 37%	(6,579)
	676
Family	1,090
	£1,766

8.

June 2005 MV 5,000 shares	50,000
Cost – 3.50p per share	17,500
	£32,500

9.

Date for P35 19 May 2006

Date for interest on PAYE 19 April 2006

10.

Telephone Calls	1,200
Less 75% business	(900)
	300
Rental	200
	£500

11.

90% of £20,000	£18,000

12.

Proceeds	350,000
Cost	320,000
	30,000
Loss relief	10,000
Chargeable	£20,000

13.

Painting 1			30,000
Cost		25,000	
Indexation $\frac{162.6-125.1}{125.1}$	.300	7,500	32,500
			nil
Painting 2			35,000
			25,000
			£10,000

14.

Value		15,000
Cost	30,000 x $\frac{15,000}{15,000 + 35,000}$	9,000
		£6,000

15.

Proceeds	100,000		
Less:	50,000		
	50,000		
Business use 2/4	25,000	taper 75%	6,250
Non-business use 2/4	25,000	taper 10%	22,500
			£28,750

16.

Premium bond win and gain on car exempt
Shares - gain £15,000 (3,000 @ £10 - £5 per share)

17.

Proceeds	10,000
Probate value	2,000
	£8,000
Excess proceeds over £6,000 = £4,000 x 5/3	£6,666

18.

Gift to daughter		2,000
AE 03/04		3,000
Unused		1,000
Gift to son		5,000
AE 04/05	3,000	
Balance 03/04	1,000	
		4,000
		£1,000

19. Value of building sold – part only proceeds re-invested therefore amount for IHT £250,000
Value of building retained – 100% business property relief.

20.

Gift to daughter on marriage	15,000	
Exemption	5,000	£10,000
Gift to niece	2,500	
Exemption	1,000	£1,500

Gifts to son and daughter in April covered by annual exemption

PART II - SUGGESTED SOLUTIONS

Question 1

i)	Salary –			45,000
	Bonus			10,000
				55,000
	Pension contributions (5%)			(2,750)
	Car benefit			
	35,000 @ 35%	10,500		
	Fuel 14,400 @35%	5,040		
		15,540 x 9/12		11,655
	Car for daughter			
	7,500 @ 15% = 1,125 x 7/12			656
	Trip (note 1)			795
	Ex – gratia redundancy	28,000		
	Loan written off	4,500		
		32,500		
	Less	30,000		2,500
				67,856
	Rental income (note 2)			6,750
	Chargeable event			4,000
	Dividends			15,000
				93,606
	Loss on unquoted shares			(10,000)
	Interest paid on loan to purchase shares			(5,000)
				78,606
	Personal allowance			(4,895)
				73,711
	Income tax	2,090	@ 10%	209
		30,310	@ 22%	6,668
		22,311	@40%	8,924
	Chargeable event	4,000	@ 40%	1,600
	Dividends	15,000	@ 32.5%	4 ,875
				22,276
ii)				
	Less:			
	PAYE		18,000	
	Tax re gain life policy		800	
	Dividend tax credit		1,500	20,300
	Payable 31.1.07			£1,976

Payments on account due – nil – less than 20% of total

iii)
Balance of tax can be collected through coding as less than £2,000
Return must be submitted by 30 September 2006 (post) or online by 31 December 2006

Note 1

Trip to Paris

Wife's train fare	120
Wife's hotel charge 6 x £75	450
Richard's hotel charge 3 x £75	225
	£795

Note 2

Rental income

Rent (includes deposit)		20,000
Agents fees	2,000	
Insurance	500	
Interest	4,000	
		6,500
		13,500 x ½ = £6,750

Question 2

Knowitall & Co
10 London Road
Newtown
Nearshire

Mr M Smith
9 Upper Vale
Middleton
Wayshire

May 2006

Dear Micheal

Letter to include following:

Responsibility as accountant -

1. Accountant who becomes aware that client is evading or seeking to evade tax should advise client to make full and proper disclosure to H M Revenue & Customs

2. Accountant cannot inform H M Revenue & Customs without client's consent – breach of duty of confidence owed to client

3. If client refuses permission to disclose the accountant must cease to act for them

(Note for Senior Partner)

4. *Must consider whether notification is required under money laundering regulations*

Enquiry Procedures

5. HMRC can open enquiry within one year from filing date unless there is fraudulent or negligent conduct in which case HMRC can go back 20 years.

6. Before an investigation is started, HMRC will look at the information in tax returns, accounts and statements and from other sources. They might also make enquiries of other people and organisations before they contact the taxpayer or their professional advisor in order to decide whether or not they need to proceed.

7. If they decide to investigate they will tell taxpayer and professional advisor in writing. They will normally tell you the reasons for starting the investigation although they are not obliged to do so. Sometimes they are unable to give reasons on grounds of confidentiality or if the investigation might be prejudiced.

8. They will ask for information and documents to assist the investigation giving a reasonable amount of time to provide any information. If they are informed that you have difficulty obtaining the information, or if you think the information is not relevant to their investigation they will discuss and try to agree the situation with you.

9. Parliament has given the Inland Revenue powers to obtain information. If they need to use these powers they will make sure that any representations you have made together with all the relevant facts are taken into consideration and put forward in any application they make before a Commissioner of Income Tax. The Commissioner is independent of the Inland Revenue.

10. You should ensure that any information you provide and any answers you give are correct. If you are unsure about any matter you should say so. It is important that you give all the relevant facts even if you are in doubt about the tax consequences of a particular matter. If, subsequently, you realise that something you have told HMRC or provided may have been wrong, you should tell them straightaway.

11. They will ask you to make a payment on account towards any additional liability they think is due pending the conclusion of the investigation. Making a payment on account will help to reduce any interest charges and will demonstrate your willingness to reach a money settlement.

12. They might make a provisional amendment to your Self Assessment (SA) before the end of the investigation if they think that you might not pay any additional tax due unless they act quickly. They could also make assessments for earlier years.

13. You have the right to appeal against such assessments or amendments and can ask to postpone payment. If they cannot agree, you can ask the Appeal Commissioners to decide how much tax you should pay.

14. If it is appropriate to seek a money settlement at the conclusion of the investigation they will try to reach an agreement with you covering the amount of tax and other duties, interest and penalties they believe are due.

15. If they cannot reach agreement they may formally determine the tax, interest and penalties they consider appropriate. You have the right to have any appeals you make heard by an independent appeal body.

16. Where there have been errors or omissions in your accounts or tax returns they will ask you to sign a Certificate of Full Disclosure confirming that you have now declared all your taxable income, gains and other duties. They will not ask for a certificate if the investigation showed nothing wrong. They will take a very serious view if you sign a Certificate of Full Disclosure you know to be false. You should consider the certificate very carefully before signing it. If you sign a certificate you know to be false, you may be liable to prosecution.

Interest, surcharge & penalties

17. They will charge interest on any tax paid late. You could also have to pay a penalty and surcharge

18. Surcharge may be imposed in two stages, an initial surcharge on any tax outstanding more than 28 days after the due date and an additional surcharge on any tax outstanding more than six months after the due date. Both initial and further surcharge are charged at a rate of 5% of the outstanding tax.

19. They can charge you a penalty for an incorrect tax return if it was delivered fraudulently or negligently or if you find that it is incorrect and fail to correct the error within a reasonable time. You are responsible for the accuracy and completeness of your tax return even if a professional agent or advisor is acting on your behalf.

20. When calculating any penalty they will take into account the extent of any voluntary disclosure of irregularities you make, your co-operation with their investigation such as attending meetings and providing information and documents, and the seriousness of your errors or omissions.

21. The penalty figure will be a percentage of the tax underpaid or paid late. In law it could be 100% of that amount, but in practice it is always less than that in a negotiated settlement. They start with a penalty figure of 100% and reduce it by

    For disclosure – a reduction of up to 20% (30% for full voluntary disclosure where there was no fear of early discovery by HMRC).

    Co-operation - A reduction of up to 40%.

    Seriousness - A reduction of up to 40%. The less serious the offence, the bigger the reduction in the penalty.

Yours sincerely

A KNOWITALL

<u>Question 3</u>

Knowitall & Co
10 London Road
Newtown
Nearshire

Mr and Mrs D Smith
34 Tree Lane
Newtown
Wayshire

May 2006

Dear Dennis and Sarah

Letter to include following:

Income tax

1. Both will still be assessed to income tax separately on formal separation and subsequent divorce so there will be no change.

2. There is no tax relief on payments of maintenance and the receipt is not taxable

Capital gains tax

3. Assets can be transferred between spouses at no gain no loss.

4. In year of separation the above exemption still applies for whole year but is lost thereafter.

5. Assets transferred before separation allow the transfer of cost and indexation and period of ownership for taper relief. However, after separation, taper relief is given based on the period of ownership of the acquiring spouse.

6. On separation, the family home will cease to be Dennis's main residence for capital gains tax purposes.

7. His share of any gain on a subsequent sale will be chargeable in respect of period of non-residence

8. Last three years still qualifies even if he has another home.

9. Revenue concession D6 covers absences of more than three years flowing separation or divorce but only where property is eventually transferred to the spouse remaining in it as part of the financial settlement, and an election for a new qualifying residence has not been made by the spouse who moved out.

10. Qualifying business assets which are transferred between spouses after separation but before divorce need not be charged to tax if they jointly claim the business gifts relief.

11. Business assets transferred after divorce may not qualify if the transfer is considered as being for consideration. However, if transferred under a court order, gift relief is available.

12. They must be aware that a capital gains tax liability can arise on a deemed disposal (ie by way of gift to each other). Any transfers between spouses should be made at a time when they are still covered by any exemptions/reliefs/concessions mentioned above – if done at a later date there may be capital gains tax consequences although no proceeds are received.

13. Each spouse has their own annual exemption for CGT and will be assessed separately both before and after divorce.

Inheritance tax

14. For inheritance tax purposes, each spouse has their own estate and is tax individually.

15. Transfers between spouses are exempt for inheritance tax purposes. This exemption still applies on separation but is lost on divorce.

16. After divorce there is still exemption for inheritance tax purposes on transfers made to a former spouse for maintenance of the spouse or the couple's children.

17. Valuation of assets for inheritance tax purposes takes into account related property ie the value of property held by the couple jointly may be more than the value of their individual shares. Jointly owned assets will not be treated as related property after divorce.

18. Sarah's share of the business would still qualify for business property relief although she does not work in the business.

Child Tax Credit

19. Sarah and Dennis have a joint income as a couple which is in excess of the limit for claiming Child Tax Credit.

20. Sarah will be assessed as a single parent after separation for the purposes of claiming Child Tax Credit.

21. The maintenance payments will not be taken into account when assessing Sarah's income for CTC

Yours sincerely

A KNOWITALL

Question 4

Knowitall & Co
10 London Road
Newtown
Nearshire

Ms E Blanc
694 Sunnyside
Snowtown
Secondshire

May 2006

Dear Eva

Letter to include following

Residence and domicile

1. Must establish residence status if moving to UK

2. Regarded as UK resident if physically present in UK for more than six months (183 days), or if visits to UK average 91 days or more per tax year over a period of four years.

3. Days of arrival and departure are normally ignored when determining days spent in UK

4. Ordinarily residence denotes habitual residence.

5. Strictly residence applies by reference to whole tax year.

6. Concession - individual moving to UK to live for at least two years may claim to be resident from day of arrival.

7. Individual can only have one domicile at a time

8. Domicile of origin may be abandoned and a domicile of choice acquired but a high standard of proof is required eg obtaining citizenship

Income tax, capital gains tax, inheritance tax

9. As resident, Eva is subject to UK income tax on her worldwide income

10. She is entitled to full personal allowances for each tax year.

11. As non-domiciled she is charged on foreign income only to the extent it is remitted.

12. She will be taxed in full on any income arising in the UK eg rental income

13. Remittances are taxed at non-savings rate of tax although may be in respect of foreign savings income

14. She is liable to capital gains tax on gains on her worldwide assets but as non-domiciled only to the extent that gains arise in or are remitted to UK.

15. If she lives in the property she is considering buying it will be her main residence and will qualify for PPR on a subsequent sale in respect of the period of occupation and the last three years of ownership

16. If she has lived in the property and then rents it as residential accommodation there will be further relief of the lower of PPR or £40,000

17. If she returns to France permanently and then sells the property there will be no liability to CGT

18. Inheritance tax applies to world-wide property only if individual domiciled in UK.

19. Eva will only have an inheritance liability on any UK property she may acquire – her residence status does not change the application of IHT.

20. She will be entitled to nil rate band and usual exemptions and reliefs.

Yours sincerely

A KNOWITALL

Question 5

ABC plc shares

82 holding

	No	Cost	Indexed cost
June 1980	1,000	3,000	3,000
Indexation			
Aug 86 $\frac{97.82 - 79.44}{79.44}$ =.231			693
Rights	500	2,000	2,000
			5,693
April 98 $\frac{162.6 - 97.82}{97.82}$ =.662			3,769
Bonus	1,500		
	3,000	5,000	9,462

S104 holding

	No	Cost	Indexed cost
May 1984	500	1,750	1,750
April 85 $\frac{94.78 - 88.97}{88.97}$ =.065			114
			1,864
Aug 86 $\frac{97.82 - 94.78}{94.78}$ =.032			60
Rights	250	1,000	1,000
			2,924
April 98 $\frac{162.6 - 97.82}{97.82}$ =.662			1,936
Bonus	750		
	1,500	5,000	4,860

Post 98 shares

Dec 2000	1,000	5,000
Bonus	1,000	-
	2,000	5,000

Disposal - June 2005 – Identified with post 98 holding first

Post 98 holding 2,000 @ £10	20,000
Cost	5,000
	15,000

Taper – non-business asset – 90% chargeable

s104 holding 1,500 @ £10	15,000
Indexed cost	4,860
	10,140

Taper – non-business asset – 70% chargeable

82 holding 500 @ £10	5,000
Indexed cost 9,462/3,000 x 500	1,577
	3,423

Taper – non-business asset – 70% chargeable

QCB – exempt

Gift of building

Market value		300,000
Cost	50,000	
Indexation $\frac{162.6-149.8}{149.8}$ .085	4,250	54,250
		245,750
Qualifying for holdover 8/10		196,600
Holdover relief before taper relief		
		49,150

Taper –business asset 6.4.98 to 30.11.03 – £49,150 x 68/92 - 25% chargeable
Taper – non-business asset 1.12.03 to 30.11.05 – £49,150 x 24/92 - 70% chargeable

Summary

	Business 75%	Non-business 30%	10%	Total
ABC plc		13,563	15,000	
Building	36,328	12,822		
Losses		(15,000)	(15,000)	
		11,385		
Taper 75/30%	(27,246)	(3,415)		
	9,082	7,970		17,052
Annual exemption				(8,500)
				8,552

Tax Calculation:

8,552 @ 20%	£1,710

Due date for payment: 31 January 2007

Note:

Basic rate		32,400
Income	15,000	
PA	7,090	7,910
20%		24,490