Association of Taxation Technicians

Examination

November 2007

PAPER 2

BUSINESS TAXATION & ACCOUNTING PRINCIPLES

ANSWERS (without marks)

1. **Debtors**

Balance before adjustments	5,000	Bank (doubtful debt recovered)	400
		Bad debt	500
		Balance c/f	4,100
	5,000		5,000

Provision for doubtful debts

		Balance b/f	900
Provision c/f	600		
Change in provision – bad debts	300		
	900		900

Bad debts

Bad debt written off	500	Bad debt recovered	100
		Change in provision	300
		Profit and loss account	100
	500		500

Marking
1 mark each for correct treatment of the following:
- write off of debt previously provided
- bad debt recovery
- movement on bad debt provision
- amount posted to profit and loss account

2. Half a mark for a valid example of each type of supply.
Standard rates supplies – all input vat reclaimable
Zero rated supplies – all input vat reclaimable
Exempt supplies – no input vat reclaimable

3. The basic tax point arises when the goods are delivered or made available to the customer.

This can be overridden by the earliest of the following
- payment or invoice (if this takes place before delivery)
- invoice date (if within 14 days of delivery)

4. Proceeds

Proceeds			400,000
Cost	50,000		
Indexation			
$\frac{162.6 - 147.50}{147.50} = 0.102$	5,100		55,100
			344,900
Losses			44,900
			300,000
Taper – 25%			
Amount chargeable			£75,000

5. Sch D Case I

Sch D Case I		
Profits		50,000
Loan interest (2/3)		20,000
		£30,000
Sch A		
Rent		20,000
Loan interest		10,000
		10,000
Deficit b/f	20,000	
Set off (non-trading income only)	10,000	10,000
		£-

(Note that the current year non trade loan relationship deficit of £10,000 could also have been offset against the Schedule D Case I income leaving the £20,000 brought forward deficit to be offset against the Schedule A income in full. This would result in Schedule A income of nil, Schedule D Case I income of £20,000 and no losses to carry forward.)

6.

i. Must make a return (CT61) to Collector of Taxes of payments of interest to individuals, and the income tax for which it is accountable, and credits that it claims for income tax deducted from payments received.

ii. Returns must be made for return periods which end 31 March, 30 June, 30 September, 31 December and end of accounting period of company.

iii. Returns must be made within 14 days of end of period and must pay HMRC income tax deducted by that date.

7\.

Class 1 A due on:

Car benefit	5,000
Medical insurance	860
	5,860
@ 12.8 %	£750

Ignoring travel and telephone

8\. i. £3,000 should be deducted from income as the work has not yet been performed

ii. £5,000 should be added to income as the work was performed before 30 September

iii. £1,500 should be added to income as ¾ of work performed before 30 September

Net adjustment £3,500

9\.

Proceeds		400,000
Cost	200,000	
Indexation		
$\frac{196.6 - 168.4}{168.4} = 0.167$	33,400	233,400
		166,600
Rollover relief (166,600 less 50,000)		116,600
Chargeable		£50,000
Cost of new building		350,000
Rollover relief		116,600
Adjusted cost		£233,400

10\.

PCTCT £180,000 @ 30%	54,000

6 mth limit1,500,000 x 6/12
= 750,000 x ½ (1 associate) = 375,000

Marginal relief	
$(375{,}000 - 205{,}000) \times 11/400 \times \frac{180{,}000}{205{,}000}$	(4,105)
	£49,895

11. One mark for any four of the following:

(a) By effluxion of time, if the partnership was entered into for a fixed period of time.
(b) By termination of the venture, if the partnership was entered into for a single venture.
(c) By the death or bankruptcy of a partner or by notice given by a partner.
(d) By subsequent illegality, i.e. an event occurs which makes it unlawful to continue the partnership.
(e) By order of the court, e.g. on permanent incapacity of a partner, or on just and equitable grounds.

12. One mark for each of the following:

(a) Employers must give their employees a statement setting out the main terms and conditions of employment.
(b) An employer must take out employers' liability insurance, providing cover in the event of injury to the employee or to a third party as a result of the employee's actions.
(c) An employer is also responsible for collecting tax and national insurance correctly and dealing with statutory maternity pay, statutory sick pay and student loan deductions.

13. The minimum requirement for members of the Association is 45 hours per calendar year, of which 15 hours must be structured.

Structured training includes attending courses, etc that involve an active contribution by the member, preparation of lectures, writing articles, and other media so long as they involve active participation.

Unstructured training includes reading and any other form of learning that does not involve interaction with other individuals.

Answer 1
James' Income Tax and NIC computation

	£		
Profit per the accounts			47,799
Add back			
Depreciation			5,467
Goods for self			150
Legal costs			450
Subscriptions			100
			53,966
Less			
Bank interest			(47)
			53,919
Capital allowances			
Pool b/f		12,380	
WDA		(3,095)	(3,095)
		9,285	
Addition	560		
50% FYA (80% allowed)	(280)		(224)
		280	
WDV c/f		9,565	
Business profits			50,600
Interest from savings (gross) (47 x 100/80)			59
			50,659
Less personal allowance			(5,035)
			45,624
Tax liability			
10%	2,150		215
22%	31,471		6,924
(BR band extended for gift aid £321)			
40%	12,003		4,801
Class 4 NIC			
(33,540 – 5,035) = 28,505 x 8%			2,280
(50,600 – 33,540) = 17,060 x 1%			171
Liability for Tax and National Insurance			14,391
Less tax deducted at source			(12)
			14,379
Payments on account			(13,000)

Balancing payment due 31 January 2008	1,379
Payments on account due 31 January 2008 and 31 July 2008	
£14,379 x 50%	7,190

Answer 2

1) **Reconciliation of operating profit to net cash flow from operating activities**

	£000
Operating profit	3,546
Depreciation	900
Loss on disposal of fixed assets	44
Increase in stock	(1,115)
Increase in debtors	(463)
Increase in creditors	380
Net cash inflow from operating activities	3,292

Valentino Limited
Cash flow forecast
For the year ended 31 December 2006 ½

Net cash inflow from operating activities		3,292
Returns on investments and servicing of finance		
Interest paid		(186)
		3,106
Taxation paid		(1,959)
Capital expenditure		
Payments to acquire fixed assets	(2,975)	
Proceeds from sale of plant	168	
		(2,807)
Dividends paid		(663)
		(2,323)
Financing		
Issue of share capital	2,380	
Redemption of debentures	(851)	
		1,529
Movement in bank balance		(794)
Reconciliation of bank		
Cash balance b/f		478
Overdraft c/f		316

Movement	794

Workings

Depreciation

Fixed assets b/f	11,080
Additions	2,975
NBV of disposals	(195)
Scrapped	(17)
Total	13,843
Balance c/f	12,943
Depreciation	900

Loss on fixed assets

NBV of assets sold	195
NBV of assets scrapped	17
	212
Sales proceeds	(168)
Loss on sale	44

Taxation

Tax provision b/f	2,385
Tax charge in profit and loss	1,137
	3,522
Tax provision c/f	(1,563)
Tax paid	1,959

Dividends

Proposed dividends b/f	296
Dividends per profit and loss	750
	1,046
Proposed dividends c/f	383
Dividends paid	663

2)

Purchase of fixed assets
Increase in stock
Increase in debtors
Redemption of debentures
Taxation paid
Dividends paid

Marks will also be given for explaining that cash may not yet have been received in respect of credit sales.

Answer 3

i. New van – first year allowance of 40% (purchased in financial year 2005), balance of expenditure added to pool and writing down allowance of 25% on reducing balance claimed thereafter. Amount claimed in 2006 is 40% £12,000 = £4,800.

ii. Computer equipment – first year allowance of 50% (purchased in financial year 2006) = £5,000. Placed in short life asset pool provided election made by 31 December 2008. Balancing allowance then available on disposal within four years if sold for less than tax written down value (or balancing charge if proceeds exceed WDV). If still owned on anniversary of four years from end of chargeable period in which expenditure incurred, WDV transferred to pool.

iii. 100% FYA due on proportion of equipment certified to be energy saving. 50% FYA on balance. Allowances due on expenditure in year: 100% of £80,000 x 25% = £20,000 and 50% of £80,000 x 75% = £30,000. Balance of expenditure in pool for writing down allowances in future years.

iv. Industrial buildings allowance due on cost of factory and site preparation at 4% (£275,000 @ 4% = £11,000 per annum) for years in which building in use at end of year.

v. Industrial buildings allowance due on residue of expenditure after sale spread over remaining years (25 less number of years for which IBAs claimed by previous owner).

Cost to Duxford		700,000
IBAs 4% 28,000 x 9	252,000	
Period of disuse 28,000 x 5	140,000	392,000
Residue of expenditure		308,000
Proceeds		400,000
Balancing charge		92,000

Allowance for Royston: residue plus balancing charge = £400,000 /10years = £40,000 per annum.
Not in use at 31 December 2006, but period of temporary disuse so IBA due. Also IBA at 4% on renovation costs if incurred during period.

vi. 100% FYA is normally due on cars with CO2 emissions of not more then 120gm per km.
But to qualify the car must be purchased new; if used then it must be treated as a normal car and placed in a separate single asset pool.
Writing down allowances are due but restricted to £3,000 per annum.

4.

New & Home
Accountants
London
SW16 9BB

Ray Biggs
Old Court
London
SW16 7TT

November 2007

Dear Ray

There are three options available to you in respect of relief for the losses incurred in the year ended 6 April 2007.

1. If no claims are made then the losses will be carried forward automatically and set against the first available profits from the same trade.

   This would mean that your profits for the current year would be reduced to nil and the remaining losses of around £20,000 would be carried forward and set against profits in subsequent years.

   If you ceased trading without having utilised these losses against future trading income it is possible that relief will be lost.

   If the losses are set against profits for 2007/08 leaving a balance for 2008/09, it is likely that there will be no tax payable until 31 January 2010 as there will be no payments on account due for 2007/08 or 2008/09.

2. It is possible to claim to set losses against your other income for 2006/07 (year of loss) and/or 2005/06 (preceding year). There would be no benefit in claiming the loss against other income for 2006/07 as the only other source of income for that year was dividends and they do not have a repayable tax credit.

   If set against income for 2005/06, the relief would use losses of £11,000 (£10,000 plus £1,000 dividends) wasting the personal allowance and dividends (£4,895 plus £1,000).

3. It is possible to set losses incurred in the first four years of trading against income in the previous three years.
   Income of the earliest year is relieved first, so in your case income for 2003/04 and 2004/05 could be reduced to nil by the losses of 2006/07.

   It is not possible to restrict the loss claim to a particular year; the losses must be set against income of all three preceding years.

The losses used would be £31,000 for 2003/04 (£30,000 earnings plus £1,000 dividend) and the balance of £29,000 for 2004/05. A tax repayment together with repayment supplement would be due.

However, there would be no losses to cover the profits of the current year so it is likely that a substantial tax liability will be due for payment on 31 January 2009.

A claim to set losses against income of the same or preceding years must be made on or before the first anniversary of 31 January following the tax year in which the loss is sustained, which in your case means 31 January 2009.

Yours sincerely

A Hodge + 1 for presentation