Answers

Section B *Marks*

1 (a) Garfield – Value added tax (VAT) return for the quarter ended 31 March 2015

	£	Marks
Output VAT		
Sales	22,500*	
Discounted sale (4,300 x 90% x 20%)	774	1
Equipment (12,400 x 20%)	2,480	1
Fuel scale charge	60*	
Input VAT		
Purchases	(11,200)*	
Motor car	0*	
Equipment	(2,480)	½
Impairment losses (1,400 x 20%)	(280)	1
Entertaining – UK customers	0*	
– Overseas customers (960 x 20/120)	(160)	1
Motor expenses (1,668 (1,008 + 660) x 20/120)	(278)	1½
VAT payable	11,416	
*Figures provided in question.		1
		7

Tutorial notes:

(1) *Relief for an impairment loss is only available if the claim is made more than six months from the time when payment was due. Therefore, relief can only be claimed in respect of the invoice due for payment on 29 August 2014.*

(2) *Input VAT on business entertainment is recoverable if it relates to the cost of entertaining overseas customers.*

(b) (1) Given Garfield's current annual turnover of £450,000, he can use the cash accounting scheme and the annual accounting scheme, but not the flat rate scheme. 1

(2) The cash accounting scheme would appear to be the most beneficial scheme for Garfield to use. ½

(3) The scheme will provide automatic VAT relief for the impairment losses which he is incurring. ½

(4) Where credit is given to customers, output VAT could be accounted for later than at present. ½

(5) The recovery of input VAT on most purchases and expenses will not be affected as Garfield pays for these on a cash basis. ½

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Tutorial notes:

(1) *The annual turnover limit for both the annual accounting scheme and the cash accounting scheme is £1,350,000, but for the flat rate scheme it is £150,000.*

(2) *Although the annual accounting scheme would mean only having to submit one VAT return each year (reducing the risk of late return penalties), payments on account are based on the VAT payable for the previous year. From a cash flow viewpoint, this is not beneficial where turnover is decreasing.*

2 (a) (1) The contract is for a relatively long period of time.

(2) George is required to do the work personally.

(3) Xpee plc exercises control over George via the weekly meetings and instructions.

(4) George will not incur any significant expenses in respect of the contract.

(5) George will only be working for Xpee plc.

(6) George is not taking any significant financial risk.

Four items only required; ½ mark per item subject to a maximum of: 2

Marks

(b) George – Income tax liability 2014–15

	£	
Income	40,000	½
Capital allowances (3,600 x 100%)	(3,600)	1
Trading profit	36,400	
Personal allowance	(10,000)	½
Taxable income	26,400	

Income tax

£		
26,400 at 20%	5,280	½
Income tax liability	5,280	

George – National insurance contributions 2014–15

(1) Class 2 national insurance contributions will be £143 (52 x 2·75). ½

(2) Class 4 national insurance contributions will be £2,560 (28,444 (36,400 – 7,956) at 9%). 1

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(c) (i) (1) If George is treated as employed in respect of his contract with Xpee plc, then the company will be required to deduct tax under PAYE every time that George is paid during 2014–15. 1

(2) If treated as self-employed, George's income tax liability for 2014–15 would not be payable until 31 January 2016. 1

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(ii) (1) If George is treated as employed in respect of his contract with Xpee plc, then his class 1 national insurance contributions for 2014–15 will be £3,845 (32,044 (40,000 – 7,956) at 12%). 1½

(2) The additional amount of national insurance contributions which he will suffer for 2014–15 is therefore £1,142 (3,845 – 143 – 2,560). ½

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Tutorial note: *For income tax purposes, capital allowances will reduce employment income in the same way that they are deducted in calculating the trading profit. However, there is no deduction for capital allowances when it comes to calculating class 1 national insurance contributions.*

3 (a) Jerome – Chargeable gains 2014–15

House

The gift of the house does not give rise to any gain or loss because it is a transfer between spouses. ½

Reward Ltd

	£	
Deemed proceeds	98,400	½
Cost	(39,000)	½
	59,400	
Gift relief (working)	(50,600)	W
Chargeable gain	8,800	

Working – Gift relief

Gift relief is restricted to £50,600 (59,400 x 460,000/540,000), being the proportion of chargeable business assets to chargeable assets. 1½

Marks

Antique bracelet

	£	
Disposal proceeds	12,200	½
Cost	(2,100)	½
Chargeable gain	10,100	

This is lower than the maximum gain of £10,333 (5/3 x (12,200 – 6,000)). 1

Land

	£	
Disposal proceeds	78,400	½
Cost	(26,460)	W
Chargeable gain	51,940	

Working – Cost

The cost relating to the nine acres of land gifted is £26,460 (37,800 x 78,400/(78,400 + 33,600)). 1½

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(b) (1) The house has a base cost of £112,800. 1

(2) The 12,000 £1 ordinary shares in Reward Ltd have a base cost of £47,800 (98,400 – 50,600). 1

(3) The bracelet has a base cost of £12,200. ½

(4) The nine acres of land have a base cost of £78,400. ½

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4 (a) James – Inheritance tax arising on death

Lifetime transfers within seven years of death

14 May 2013

	£	
Value transferred	420,000	
Annual exemptions 2013–14	(3,000)	½
2012–13	(3,000)	½
Potentially exempt transfer	414,000	
Inheritance tax liability 296,000 (working) at nil%	0	W
118,000 at 40%	47,200	½
	47,200	

James' daughter will be responsible for paying the inheritance tax of £47,200. ½

2 August 2013

	£	
Chargeable lifetime transfer	260,000	½
Inheritance tax liability 260,000 at 40%	104,000	½

The trust will be responsible for paying the inheritance tax of £104,000. ½

Death estate

	£	
Chargeable estate	870,000	
Inheritance tax liability 870,000 at 40%	348,000	½

The personal representatives of James' estate will be responsible for paying the inheritance tax of £348,000. ½

			Marks
Working – Available nil rate band			
	£	£	
Nil rate band		325,000	½
Chargeable lifetime transfer 9 October 2007			
Value transferred	35,000		½
Annual exemptions 2007–08	(3,000)		
2006–07	(3,000)		½
Chargeable transfer		(29,000)	
		296,000	
			6

(b) Skipping a generation avoids a further charge to inheritance tax when the children die. Gifts will then only be taxed once before being inherited by the grandchildren, rather than twice. — 2

(c) (1) Even if the donor does not survive for seven years, taper relief will reduce the amount of IHT payable after three years. — ½

(2) The value of potentially exempt transfers and chargeable lifetime transfers are fixed at the time they are made. — ½

(3) James therefore saved inheritance tax of £20,000 ((310,000 – 260,000) at 40%) by making the lifetime gift of property. — 1

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5 Patience – Income tax computation 2014–15

		£	
Employment income			
Salary (3,750 x 9)		33,750	1
Pension contributions	– Patience (33,750 x 6%)	(2,025)	½
	– Employer	0	½
		31,725	
School place		540	1
Long-service award		0	½
Beneficial loan		0	½
Trading profit (working 1)		16,100	W1
Pensions (1,450 + 6,000 + 3,300)		10,750	1
Property business profit (working 3)		3,500	W3
		62,615	
Personal allowance		(10,000)	½
Taxable income		52,615	
£			
36,365 (working 4) at 20%		7,273	W4 ½
16,250 at 40%		6,500	½
52,615			
Income tax liability		13,773	

Tutorial notes:

(1) A non-cash long-service award is not a taxable benefit if it is for a period of service of at least 20 years, and the cost of the award does not exceed £50 per year of service.

(2) There is no taxable benefit if beneficial loans do not exceed £10,000 during the tax year.

			Marks

Working 1 – Trading profit

	£	£	
Year ended 31 July 2014		14,800	½
Period ended 31 December 2014	6,900		½
Balancing allowance (working 2)	(1,900)		W2
		5,000	
		19,800	
Relief for overlap profits		(3,700)	1
		16,100	

Working 2 – Capital allowances

	Main pool £	Allowances £	
WDV brought forward	2,200		½
Addition – Laptop computer	1,700		½
Proceeds (1,200 + 800)	(2,000)		1
Balancing allowance	(1,900)	1,900	½

Working 3 – Property business profit

	£	
Rent received (3,600 + 7,200)	10,800	½
Expenditure (4,700 + 2,600)	(7,300)	½
Property business profit	3,500	

Working 4 – Tax band

Patience's basic rate tax band is extended by £4,500 to £36,365 (31,865 + 4,500 (3,600 x 100/80) in respect of the personal pension contributions. 1

Patience – Capital gains tax computation 2014–15

		£	£	
Property one	– Disposal proceeds	122,000		
	– Cost	(81,400)		
			40,600	½
Property two	– Disposal proceeds	98,000		
	– Cost	(103,700)		
			(5,700)	½
			34,900	
Annual exempt amount			(11,000)	½
			23,900	
Capital gains tax: 23,900 at 28%			6,692	½
				15

			Marks
6	**(a)**	**Jump Ltd – Trading loss for the three-month period ended 31 March 2015**	

	£	
Operating loss	(144,700)	
Depreciation	8,100	½
Employee training courses	0	½
Employee pension contributions	0	½
Staff party	0	½
Lease of motor car (1,200 x 15%)	180	1
Accountancy	0	½
Legal fees – Issue of share capital	3,800	½
– Renewal of short lease	0	½
Entertaining UK customers	1,700	½
Entertaining overseas customers	790	½
Political donations	800	½
Balancing charge (working)	3,330	W ½
Trading loss	(126,000)	

Working – Capital allowances

	Main pool £	Special rate pool £	Allowances £	
WDV brought forward	12,100	5,700		½
Proceeds – Motor car [1]		(9,300)		1
– Motor car [2]	(6,100)			½
Balancing charge		3,600	(3,600)	½
	6,000			
WDA – 18% x 3/12	(270)		270	1
WDV carried forward	5,730			
Overall balancing charge			(3,330)	
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Tutorial note: *The proceeds for motor car [1] are restricted to the original cost figure of £9,300.*

(b) **(i)** The main factor which will influence Jump Ltd's choice of loss relief or group relief claims is the timing of the relief obtained, with an earlier claim generally being preferable. — 1

Tutorial note: *Other possible factors are the rate of corporation tax and the extent to which relief for qualifying charitable donations will be lost. However, neither of these are relevant given that all the companies pay tax at the same rate and Jump Ltd has not made any charitable donations.*

(ii) (1) The maximum loss relief claim for the seven-month period to 31 December 2014 is £42,400, being the total profits for this period. — ½

(2) The loss relief claim for the year ended 31 May 2014 is restricted to £33,250 ((78,600 + 1,200) x 5/12). — 1½

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(iii) (1) The maximum amount of trading loss which can be surrendered to Hop Ltd is £23,625, being the lower of £23,625 (63,000 x 3/8) and £126,000. — 1½

(2) Skip Ltd is not a 75% subsidiary of Jump Ltd, so no group relief claim is possible. — ½

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