May 2022 Examination

PAPER 1

Personal Taxation

Part I Suggested Answers

Candidates will be given credit for relevant points not on the mark scheme.

1. **Harry**

Accrued income scheme

	£	
Interest received (30 June 2021)		
(£63,000 x 4% x 6/12)	1,260	1
Accrued income charge		
Levied on Harry as interest income		
From: 1 July 2021 (i.e. the day after the last interest payment)		
To: 30 November 2021 (i.e. the date of sale)		1
= 5 months interest.		
The charge is assessed in 2021/22		
(i.e. tax year of the next interest payment which is on 31 December 2021).		
(£63,000 x 4% x 5/12)	1,050	1
	———	
Interest income assessed on Harry in 2021/22	2,310	
	======	
Sale proceeds for capital gains tax purposes		
(£70,000 – £1,050)	68,950	1
	======	

Tutorial notes:

(a) *The sale of loan stock does not fall within the period 16 June – 30 June, nor 17 December – 31 December, therefore the sale is CUM DIV.*

(b) *The company loan stock may be exempt from CGT if a qualifying corporate bond, but may be chargeable.*

Harry's sale proceeds for capital gains tax purposes must be reduced by any accrued income taxed as interest income.

2. **Jawwad**

Property income – 2021/22

	£	£	
Rental income received (£860 x 8 months) (see Note)		6,880	1
Less: Allowable expenses			
Repairs	500		½
Replacement of dishwasher	330		½
Mileage allowance			1
(28 miles x 3 trips x 45p) (see Note)	38		
Toll charges			1
(£7 x 2 x 3 trips) (see Note)	42		
	———	(910)	
		———	
Property income		5,970	
		======	

Tutorial notes:

(a) *Property income is (by default) assessed on a cash basis.*

(b) *The flat rate for motor expenses are the ITEPA mileage rates.*

(c) *The flat rate covers the cost of buying, maintaining and running the car, but does not cover any costs associated with specific journeys. A separate claim can be made for these costs. Each trip to the bungalow will involve paying two tolls of £7.*

(d) *As the question states that no other election has been made in relation to the property, the £1,000 allowance has not been claimed.*

3. Marcus

	Liable to Class 1 NICs?	Explanation	
Gift of an iPad	No	Not cash earnings as cannot be surrendered for cash (see Note)	½
Gift of quoted shares	Yes	Cash earnings as quoted shares are readily convertible assets	1
Reimbursement of employment expenses	No	Not cash earnings	½
Termination payment	Depends	If ex gratia:	½
		£30,000 exempt from any NICs	½
		Excess over £30,000 is liable to Class 1A	
		If contractual: Treated as earnings	½

(Max 3 marks)

Tutorial notes:

(a) *The gift of an iPad will be subject to Class 1A NICs, but not Class 1 NICs.*

(b) *The reimbursement of genuine employment expenses are specifically excluded from the definition of cash earnings and are not liable to any NICs.*

4. Jacqueline

Investors' relief is only available on qualifying shares. Where the individual disposes of shares where only some are qualifying shares, only part of the gain arising will be eligible for investors' relief. **(½)**

Acquisition date	Number of shares acquired	Type of share	Reason	
25 October 2014	300	Excluded	Shares issued before 17 March 2016	½
14 July 2016	400	Qualifying	All conditions satisfied including	½
			ABC Ltd is an unlisted trading company	½
			Jacqueline has never been a relevant employee	½
30 December 2017	100	Excluded	Shares not subscribed for	½
6 August 2018	200	Potentially qualifying	All conditions satisfied except not held for the minimum holding period of 3 years	½

The portion of the gain qualifying for investors' relief is calculated as follows:

$$\frac{\text{number of qualifying shares}}{\text{number of shares disposed of}} \times \text{Gain on all shares disposed of} \quad ½$$

Accordingly, only 40% of the gain **(1)** will be eligible for investors' relief.

(Max 4 marks)

5. Morgan

Redemption of company loan stock

To qualify as qualifying corporate bonds (QCBs), the loan stock must:

- be issued after 13 March 1984 **(½)**
- represent a normal commercial loan **(½)**
- not carry any right to be converted into shares **(½)**
- be expressed in sterling at all times and there is no provision for redemption in, or conversion into, any other currency. **(½)**

The loan stock satisfies all the conditions except that there is a provision for redemption in another currency. **(½)** The fact that Morgan did not elect to be paid in Euros is not relevant, there was a provision for her to do so if she wished. **(½)**

Accordingly, the loan stock is not a QCB **(½)** and the gain on redemption is chargeable to capital gains tax in the same way as the disposal of shares in a company. **(1)**

(Max 3 marks)

6. Marion

	Explanation	£	
Late payment interest	Interest runs from: 31 January 2022 (i.e. the 31 January file date) (not from the actual filing date of the paper return).		½
	Interest runs to: 30 April 2022 (i.e. the date the tax is paid)		½
	(£4,650 x 2.6% x 3/12) (see Note)	30	**1**
Penalties	Unpaid 30 days after the payment due date of 31 January 2022		½
	(£4,650 x 5%)	232	½
Total interest and penalties due		262	
		=====	

Tutorial notes:

1. *Unless the question states otherwise, calculations in exams are performed:*
   - *on a monthly basis (not daily)*
   - *to the nearest £ (not pence).*
2. *HMRC will waive late payment penalties for 2020/21 Self Assessment taxpayers for one month provided the taxpayer pays the tax due in full (or sets up a 'Time to Pay' arrangement) by 1 April 2022. Marion pays on 30 April 2022. Accordingly the penalty will not be waived.*

7. **Simon**

Net chargeable gain/(allowable loss)

	£	£	
Jewellery (non-wasting chattel)			
Gross sale proceeds and cost < £6,000	Exempt	–	½
Car (specifically exempt)	Exempt	–	½
Painting (non-wasting chattel)			
Gross sale proceeds > £6,000, and cost < £6,000:			
Taxed on lower of normal gain or 5/3rds rule			
Normal gain			
Gross sale proceeds	6,900		
Less: Cost (including acquisition costs)			
(£4,000 + £500)	(4,500)		
Gain	2,400		½
	=======		
5/3 x (£6,900 – £6,000)	1,500	1,500	1
	=======		
Antique (non-wasting chattel)			
Gross sale proceeds and cost > £6,000:			
Normal gain/loss rules apply			
Gross sale proceeds	6,400		
Less: Incidental selling costs	(600)		
Net sale proceeds	5,800		1
Less: Cost (including acquisition costs)			
(£14,250 + £1,425)	(15,675)		½
Allowable loss		(9,875)	
Net allowable loss		(8,375)	
		======	

Tutorial note:

To determine which non-wasting chattel rule applies, the ***gross*** *sale proceeds are compared with £6,000 (NOT the net sale proceeds).*

8. **Charlie**

Income tax computation – 2021/22

		Total	Non-savings	Savings	
		£	£	£	
Employment income (£60,000 + £1,450)		61,450	61,450		½
Interest		1,300		1,300	½
		62,750			
Less: Personal allowance		(12,570)	(12,570)		½
Taxable income		50,180	48,880	1,300	
Income tax:					
Non-savings	Basic rate (see Note)	37,700	x 20%	7,540	½
Non-savings	Higher rate	11,180	x 40%	4,472	½
		48,880			
Interest	Nil rate band	500	x 0%	0	½
Interest	Higher rate	800	x 40%	320	½
		50,180			
Income tax liability				12,332	

Charlie's income tax liability would not be different if he were a Welsh taxpayer as the personal allowance, basic rate band and rates of income tax applicable are the same for all non-Scottish individuals in the United Kingdom. ½

9. Theresa

In Theresa's income tax computation:

- the income received must be grossed up at the appropriate rate **(½)**
  - for rental income and interest: multiply by 100/80 **(½)**
  - for dividend income: multiply by 100/92.5 **(½)**
- tax rental income as non-savings income, interest as savings income, and dividends as dividend income **(1)**
- deduct the appropriate tax credit from Theresa's income tax liability **(½)**
  - for rental income and interest:
    20% of gross amount in the computation (or 20/80 of net amount received) **(½)**
  - for dividend income:
    7.5% of the gross amount in the computation
    (or 7.5/92.5 of the net amount received) **(½)**

Tutorial note:

Income distributed from an interest in possession trust retains the nature of the source of income in the hands of the recipient. The income is deemed to be received net of the appropriate basic rate of tax for that source of income.

The requirement asks for the tax treatment in Theresa's income tax computation. Details of the treatment in the hands of the trustees is not required.

(Max 3 marks)

10. Sancho

Amount assessable to income tax

	£	
Premium received (A)	320,000	
Less: 2% x premium x (N – 1)		
2% x £320,000 x 29 years	(185,600)	
	———	
Income element of premium	134,400	1
	=======	

Tutorial note:

Alternative computation = P x (51 – N)/50 = £320,000 (51 – 30)/50 = £134,400

Amount assessable to capital gains tax: Grant of a short lease out of a long lease

	£	
Premium	320,000	
Less: Income element	(134,400)	
	———	
Capital element of premium received – 'a'	185,600	½
Less: Deemed cost		
$\frac{a}{(A + B)} = \frac{£185,600}{(£320,000 + £288,000)} \times £345,000$	(105,316)	1½
	———	
Amount assessable to capital gains tax	80,284	
	========	

Appropriate rates of tax

As Sancho is an additional rate taxpayer, he will be taxed on:

– the property income (non-savings income) at 45% ½
– the chargeable gain at 20% (see Note). ½

Tutorial note:

The property is a commercial investment property (i.e. not residential property and not eligible for business asset disposal relief) therefore the appropriate tax rate is 20%.

11. Sebastien

The chargeable part of the non-resident capital gain (NRCG) arising on the commercial (non-residential) property is calculated using the:

- Default method (Sale proceeds less **Value at 6 April 2019**) **(½)**.

However, if a lower gain would arise, **(½)** an election can be made, **(½)** for the:

- Retrospective method (Sale proceeds less Original Cost) **(½)** (see Note)

The chargeable part of the NRCG arising on the Welsh cottage (residential property) is calculated using the:

- Default method (Sale proceeds less **Value at 6 April 2015**) **(½)**.

However, if a lower gain would arise, **(½)** an election can be made, **(½)** for either the:

- Straight-line time apportionment method:
  Gain accruing after 6 April 2015 is chargeable **(½)**
  (Sale proceeds less Original cost) x (6½ years/10 years) **(½)**
- Retrospective method (unlikely as a gain is realised): **(½)**

The loss on the disposal of the antique furniture is not an allowable loss as Sebastien is non-UK resident. **(½)** (see Notes)

Tutorial notes:

(a) *There is no straight line time apportionment election available for disposals of non-residential property*

(b) *In general, non-UK resident individuals are not liable to CGT in the UK, not even on the disposals of assets situated in the UK – unless the individual is temporarily non-resident or disposes of interests in UK land.*

Accordingly, the disposal of antique furniture in the UK is ignored, whether the disposal gives rise to a gain or a loss.

(c) *Only allowable NRCG losses can be set against NRCG gains.*

(Max 4 marks)

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12.

Sally's Income Tax computation 2021/22

	Non-savings	Interest	Dividends	
	£	£	£	
Employment income	155,000			**(1/2)**
Private medical insurance (N1)	935			**(1/2)**
Company car benefit (W1)	14,912			
Equipment benefit (W2)	600			
Bank interest		900		**(1/2)**
Dividends			12,500	**(1/2)**
Net income (£184,847)	171,447	900	12,500	
Less:				
Personal allowance (N2)	(NIL)			**(1/2)**
Taxable income	171,447	900	12,500	

Tax on taxable income:

	£		£	
Non-savings income	37,700	x 20%	7,540	**(1/2)**
Non-savings income (higher rate)	112,300	x 40%	44,920	**(1/2)**
Non-savings income (additional rate)	21,447	x 45%	9,651	**(1/2)**
Savings income (N4)	900	x 45%	405	**(1/2)**
Dividend income (N5)	2,000	x 0%	0	**(1/2)**
Dividend income	10,500	x 38.1%	4,000	**(1/2)**
Income tax liability			**66,516**	**(1/2)**

Workings

(W1) Car benefit (N6)

	£	
List price	26,000	
Add: Accessories	1,000	**(1/2)**
Less: Capital contribution (N6)	(5,000)	**(1)**
Revised list price	22,000	

	£	
Cash equivalent: £22,000 x 32%	7,040	
[(135 – 75) / 5 = 12 + 20] **(3 x 1/2)***		
Fuel benefit: £24,600 **(1/2)** x 32%	7,872	**(1/2)**
Taxable benefit	14,912	

(W2) Equipment benefit

Benefit for use:

	£	
£700 x 20% x 6/12	70	**(2 x 1/2)****

Transfer of equipment:

	£	£	
Higher of: **(1/2)**			
MV at transfer		550	**(1/2)**
Original MV	700		**(1/2)**
Less: Amount already charged	(70)		**(1/2)**
		630	

	£	
Use of asset	70	**(1/2)**
Transfer of asset	630	**(1/2)**
Less: Amount paid by Sally	(100)	**(1/2)**
Total taxable benefit	600	

Notes

(N1) Private medical insurance

Cost to Topsales Ltd is the taxable benefit.

(N2) Personal allowance

Income is greater than the £125,140 threshold, therefore she does not have any Personal allowance.

(N3) Company mobile phone

This is a tax exempt benefit **(1/2)** and it does not matter if Sally makes personal calls that Topsales Ltd pay for. **(1/2)**

(N4) Interest income

As an additional rate taxpayer, Sally is not entitled to a Personal Savings Allowance in 2021/22.

(N5) Dividend income

Sally is entitled to a dividend allowance of £2,000 for 2021/22, irrespective of whether she is a basic, higher or additional rate taxpayer.

(N6) Car benefit

No time apportionment reduction is made to the car benefit, as the period it was unavailable was less than 30 days. **(1/2)**

Marking notes

* ½ for rounding down 139g/km to 135g/km; ½ for taking away 75 and then dividing by 5; ½ for adding 20

** ½ for 20%; ½ for correct time apportionment

16 marks

2)

An employee can be dismissed by reason of redundancy **(1)** where the only, or main reason, for dismissal is that the employer intends to cease the business. **(1)**

An employee might have the right to claim for unfair dismissal if:

- the reason for dismissal was not fair **(1)** or,
- the procedure followed was not fair. **(1)**

13.

<u>Notes on PRR issues ahead of proposed sale of property by Salim Lao</u>

Salim's Bristol house is clearly his main residence based on fact. **(1/2)**

Salim did not occupy the property for the first year of ownership, therefore he has a period of 'absence' at the start. **(1/2)** The period of absence will be treated as a period of occupation for the purposes of PRR **(1/2)** as it is less than 24 months and there is a qualifying event. **(1/2)** The qualifying event in this case is the renovation and alteration of the house. **(1/2)**

PRR includes gardens and grounds, as long as it does not exceed half a hectare. **(1/2)** However, HMRC will permit a larger area to qualify for PRR relief **(1/2)** as long as it is satisfied the whole area of land **(1/2)** is required for the 'reasonable enjoyment' of the property. **(1/2)**

Full PRR relief will be available for 2015 to 2017. **(1/2)** There is no need for Salim to apportion the gain **(1/2)** and he will be treated as having lived in the whole of the property for PRR purposes **(1/2)** as his lodger did not have exclusive use of any of the house. **(1/2)**

The last nine months of the house will be always be exempt under PRR **(1/2)** as it has been Salim's PRR during his ownership. **(1/2)** As Salim has now purchased a second residence, he should sign a PRR election in favour of his flat **(1/2)** from the date he moved in. Salim is within the two-year window to make an election from the date he owned two residences **(1/2)** and he is using both as residences. **(1/2)**

By signing this election, as long as the sale of Salim's house is completed within nine months, **(1/2)** he can have PRR on two exempt residences for this period of time. **(1/2)**

10 marks

14.

1) There is no tax charge on the grant of the EMI options. (½)

There is an income tax charge on the exercise of the options as they were granted at a discount (½) to the market value at the date of the grant.

The amount subject to income tax at exercise is 100,000 (½) x (£2.00 - £1.80) (½) = £20,000.

2) CGT computation:

			BADR (1) £	Non-BADR £
Disposal of Court Ltd shares				
Disposal proceeds	75,000 (½) x £6.50 (½)	487,500		
Base cost	75,000 x £2.00 (½)	(150,000)		
			337,500	
Disposal of land				
Disposal proceeds		2,000,000 (½)		
Base cost	(A / (A+B)) (½) x £125,000 A = 2,000,000 (½) B = 250,000 (½) 2,000,000/2,250,000 x £125,000 (1)	(111,111)		
	Planning fees	(50,000) (1)		
				1,838,889
Ring				
Proceeds	Insurance	150,000 (½)		
Cost		(25,000) (½)		
		125,000		
Gain deferred		(35,000) (½)		
Chargeable now	Insurance proceeds retained (½) (150,000 – 60,000)			90,000
			337,500	1,928,889
Annual exempt amount	(1)			(12,300)
			337,500	1,916,589
Chargeable gain				
BADR gain at 10%	£337,500 x 10% (½)	33,750		
Non-BADR gain at 20%	£1,916,589 x 20% (½)	383,318		
		417,068		

3) If Valerie refuses to make a suitable amendment to her tax return, you should:

- Check engagement letter to see if you have authority to disclose anyway (½)
- Cease to act (½) and advise Valerie of this in writing (½)
- Inform HMRC that you have ceased to act for Valerie (½)
- Consider withdrawing any reports you have signed (½)
- Consider whether a money laundering report should be made (½)
- Carefully consider your response to any ensuing professional clearance letter (½)

15.

Your address Our address

Date **(1 – format)**

Dear Clive

UK tax residence status for 2021/22

I understand that you would like some clarification as to your UK tax residence status for the 2021/22 tax year. As you know, this is assessed by reference to the tests included in the Statutory Residence Test (SRT).

Throughout the following tests, a day is a day of presence in the UK if you are physically in the UK at midnight at the end of the day **(½)**. A day is a workday if you do at least 3 hours work **(½)**.

Automatic non-resident tests

You already recognise that, due to your days of presence in the UK, you will not meet either of the first two automatic overseas tests. The remaining automatic overseas test is:

- Test 3 – You work full-time **(½)** overseas **(½)** and:
    - are present in the UK on fewer than 91 days **(½)**
    - work fewer than 31 days in the UK **(½)**
    - have no significant breaks from overseas work **(½)**

  You do not meet this test as your days in the UK exceed these limits **(½)** and you had a significant break from overseas work prior to taking up the employment in Germany **(½).**

Automatic UK resident tests

As you do not meet any of the automatic overseas tests, you need to consider the automatic UK tests.

- Test 1 – You have been present in the UK for more than 182 days **(½)**.

  You do not meet this test as your 130 days of UK presence prior to departure, together with the 16 days **(1)** you spent in the UK after departure, do not amount to more than 182 days **(½)**. After departure, each of your eight monthly visits to the UK represent 2 days of presence in the UK.

- Test 2 – All of your homes are in the UK **(½)**.

  You will meet this test **(½)** as there has been a period of at least 91 consecutive days **(½)**, 30 of which are in the 2021/22 tax year **(½)**, during which you:

    - had a UK home **(½)**, in which you spent at least 30 days during the tax year **(½)**, and
    - had no overseas home **(½)**.

- Test 3 – Over a period of 365 days **(½)** that includes a UK workday in 2021/22 **(½)**:
    - You work full-time in the UK **(½)**, and
    - Have no significant break from UK work **(½)**, and
    - More than 75% of your workdays are UK workdays **(½)**.

  You will meet this test **(½)** by reference to a 365-day period ending in the 2021/22 tax year prior to the cessation of your UK employment **(½)**.

  You will therefore be UK tax resident for the whole of the 2021/22 UK tax year **(½).**

  Please let me know if you have any queries.

  Kind regards,
  ATT Student