



Chartered  
Institute of  
Taxation  
Excellence in Taxation

# **The Chartered Tax Adviser Examination**

November 2020

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## **Taxation of Individuals**

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Suggested Solutions

## **ANSWER 1**

### **Mike**

As Mike is a UK tax resident and non-UK domiciled individual, who is electing for the remittance basis to apply in respect of his foreign gains, he is only taxed on gains on foreign assets to the extent that they are remitted to the UK.

Gains arising on UK shares would be subject to tax and losses on UK shares would be allowable. Mike would be taxed on the gain on the shares in Red Ltd, but relief would automatically apply for the loss of the shares in Blue Ltd.

As Mike claims the remittance basis, if he does not make any further elections, he would not be allowed to utilise any losses arising on any non-UK shares.

Mike will not be allowed to claim an annual exempt amount for 2019/20 as he is claiming the remittance basis.

Therefore, if Mike does not remit any of the sale proceeds of his non-UK shares to the UK and does not make any further elections, the capital gains tax due would be as follows:

|                                     | £               |
|-------------------------------------|-----------------|
| Proceeds on sale of Red Ltd shares  | 300,000         |
| Cost of Red Ltd shares              | (5,000)         |
| Gain                                | <u>295,000</u>  |
| <br>                                |                 |
| Proceeds on sale of Blue Ltd shares | 600,000         |
| Cost of Blue Ltd shares             | 650,000         |
| Loss                                | <u>(50,000)</u> |
| <br>                                |                 |
| Gain on Red Ltd shares              | 295,000         |
| Loss on Blue Ltd shares             | (50,000)        |
| Net gain                            | <u>245,000</u>  |
| Tax @ 20%                           | <u>49,000</u>   |

Mike can make an election which would allow relief in respect of losses made on non-UK assets. This would enable relief for the loss arising on the sale of the Black Ltd shares in 2017/18 to be claimed.

As a result of the election the statutory ordering provision would apply and both the UK capital loss arising on the Blue Ltd shares and the non-UK capital loss arising on the Black Ltd shares would be utilised in the following order:

- i. First against foreign gains remitted to the UK; then
- ii. Against unremitted foreign capital gains; then
- iii. Finally against UK capital gains.

As there are no foreign gains remitted to the UK, this means that the non-UK loss of £195,000 arising on the sale of the Black Ltd shares in 2017/18 would first be utilised against the non-UK gain of £45,000 arising on the Green Ltd shares in 2018/19.

The balance of the loss on the Black Ltd shares of £150,000 would be carried forward and the UK loss of Blue Ltd of £50,000 (i.e. a total of £200,000) would then be used against non-UK gain of the Yellow Ltd shares of £50,000 in 2019/20.

The balance of losses of £150,000 would be set against the gains arising on the shares in Red Ltd in 2019/20, which would mean that the taxable gain would be reduced to £145,000.

If Mike makes the election, the capital gains tax due for the 2019/20 tax year would be as follows:

|   | £              |
|---|----------------|
| Proceeds on sale of Red Ltd shares            | 300,000        |
| Cost of Red Ltd shares                        | (5,000)        |
| Gain  | <u>295,000</u> |
| Remainder of losses on Black Ltd and Blue Ltd | (150,000)      |
| Net gain                                      | <u>145,000</u> |
| Tax @ 20%                                     | <u>29,000</u>  |

Mike should therefore consider making the election as this would be favourable for the 2019/20 tax year.

However, he should be aware the election is irrevocable once made and cannot be unwound. Therefore, the statutory ordering rules also apply to foreign and UK losses made in subsequent years. This may not be beneficial for Mike in future years, as this may mean that UK losses have to be offset against future unremitted foreign gains rather than UK gains.

Mike would not benefit from the annual exempt amount to set against the foreign gains in the year of remitting these against which the loss is used, even if he does not claim the remittance basis in the year in which he makes that remittance.

In addition, Mike would have to disclose the gain in Yellow Ltd to HMRC, which is an additional reporting requirement on his tax return for the year, which would not otherwise be required.

If Mike were to make the foreign loss election, he would have to do so within four years after the end of the first year in which the remittance basis claim is made i.e. by 5 April 2022.

### **Anna**

Even though Anna is a non UK resident individual, she will still be subject to UK tax on the gain arising on the shares in Purple Ltd. This is due to the fact that:

- Purple Ltd derives 75% or more of its gross asset value from UK land
- Anna has a substantial indirect interest in that land, as she holds at least 25% of the shares in Purple Ltd.

Automatic rebasing as at 5 April 2019 applies:

|                      | £             |
|----------------------|---------------|
| Proceeds             | 50,000        |
| 5 April 2019 value   | (35,000)      |
| Gain                 | <u>15,000</u> |
| Annual exempt amount | (12,000)      |
| Taxable gain         | <u>3,000</u>  |
| Tax at 10%           | 300           |

Anna should have filed a NRCGT return and paid the tax within 30 days of the disposal (April 2020) so this should be completed as soon as possible if not already dealt with.

## **MARKING GUIDE**

| <b>TOPIC</b>  | <b>MARKS</b> |
|---|--------------|
| <b>Mike:</b>  |              |
| Impact of Mike's non domiciled status on capital gains position: foreign gains only taxed if remitted, UK gains chargeable, UK losses allowable | 1            |
| Foreign losses not allowable unless an election made  | ½            |
| Calculation of CGT due if no election made, including loss relief on Blue shares  | 1            |
| Order in which loss is used if election made  | 1 ½          |
| Application to client scenario – if election made, part of Black Ltd loss must be used against Green Ltd  | ½            |
| Application to client scenario – if election made, part of Black Ltd and Blue Ltd loss must be used against Yellow Ltd                          | 1            |
| Application to client scenario – balance of losses to be used against Red Ltd   | ½            |
| Calculation of CGT due if election is made  | ½            |
| Beneficial to make the election as Red Ltd taxable gain is lower with the election  | ½            |
| Election irrevocable  | ½            |
| Has impact on future losses   | 1            |
| Loss of AEA in year of future remittance  | ½            |
| Notify HMRC of gain in Yellow Ltd   | 1            |
| Deadline for election   | ½            |
| <b>Anna:</b>  |              |
| Gain subject to CGT because Purple Ltd derives 75% or more of its gross asset value from UK   | 1            |
| Gain subject to CGT because Anna holds at least 25% interest in company   | 1            |
| Advising rebasing applies   | 1            |
| Calculating gain on rebased method  | 1            |
| Anna's due date for tax   | ½            |
| <b>TOTAL</b>  | <b>15</b>    |

## **ANSWER 2**

### **Part 1)**

|                          | Workings | Non-Savings<br>£ | Interest<br>£ | Dividends<br>£ |
|--------------------------|----------|------------------|---------------|----------------|
| Employment Income        |          |                  |               |                |
| Charity salary           |          | 42,000           |               |                |
| Redundancy payment       | 1        | 12,600           |               |                |
| Mechanic salary          |          | 20,600           |               |                |
| Self-Employment Income   |          |                  |               |                |
| Horse event              | 2        | 5,020            |               |                |
| Property Income          |          |                  |               |                |
| Holiday cottages         | 3        | 5,250            |               |                |
| Dividend Income          |          |                  |               |                |
| UK dividends             | 4        |                  |               | 10,000         |
| Foreign Income           |          |                  |               |                |
| Sunnyland bank interest  |          |                  | 1,000         |                |
| Sunnyland reporting fund | 5        |                  |               | 4,100          |
| Miscellaneous Income     |          |                  |               |                |
| Offshore Income Gain     | 6        | 500              |               |                |
|                          |          | -----            | -----         | -----          |
| Total Income             |          | 85,970           | 1,000         | 14,100         |
| Less: Personal Allowance | 7        | (12,015)         |               |                |
|                          |          | -----            | -----         | -----          |
| Taxable Income           |          | 73,955           | 1,000         | 14,100         |
|                          |          | =====            | =====         | =====          |
| <b>Non-saving</b>        |          |                  |               |                |
| 37,600 @ 20%             | 8        |                  |               | 7,520          |
| 36,525 @ 40%             |          |                  |               | 14,542         |
| 73,955                   |          |                  |               |                |
| <b>Savings</b>           |          |                  |               |                |
| 500 @ 0%                 | 9        |                  |               | Nil            |
| 500 @ 40%                |          |                  |               | 200            |
| 2,000 @ 0%               |          |                  |               | Nil            |
| <u>12,100 @ 32.5%</u>    |          |                  |               | 3,933          |
| 89,025                   |          |                  |               | -----          |
| <b>Tax Liability</b>     |          |                  |               | 26,195         |
| Less: PAYE               |          |                  |               | (20,000)       |
|                          |          |                  |               | (2,500)        |
| Foreign tax credit       |          |                  |               | (1,000)        |
| UK dividends             |          |                  |               | (750)          |
|                          |          |                  |               | -----          |
| <b>Tax Due</b>           |          |                  |               | <u>1,945</u>   |

Tax due by 31 January 2021

## Workings and explanations

### **Working 1**

The redundancy payment is split into two elements:

1. Post Employment Notice Pay (PENP)
2. Amounts subject to s.403 ITEPA.

$$\text{PENP} = (4,200 \times 3) / 1 - 0$$
$$\text{PENP} = 12,600$$

This amount is treated as general earnings.

The remaining amount of Rosie's redundancy payment of £12,400 is taxable under s.403 ITEPA and the first £30,000 is exempt.

### **Working 2**

$$\text{Profit} = 6,000 - 980 = 5,020$$

### **Working 3**

Expenses incurred by the property rental business are only deductible if they are revenue expenses rather than capital expenses.

The replacement of the windows is a revenue expense as HMRC allow replacement costs where the item is being replaced by a modern equivalent such as double glazing.

$$\text{Allowable expenses} = 1,500 + 200 + 2,300 = 4,000$$
$$\text{Profit} = 9,250 - 4,000 = 5,250$$

### **Working 4**

Rosie was left a specific legacy of the investment portfolio. The UK dividends are redirected to Rosie.

The executors will have paid income tax of 7.5% and the gross dividend of £10,000 is taxable. Rosie receives a credit for the tax paid by the executors.

### **Working 5**

Income from a UK reporting fund is taxed as dividend income. The net receipt of £3,000 is grossed up by the tax deducted at source and Rosie receives a credit for the lower of UK tax or foreign tax deducted at source. As Rosie is a higher rate taxpayer, the foreign tax deducted at source will be lower.

$$\text{Gross income} = 3,000 \times 100/75 = 4,000$$

Excess reported income is taxable on Rosie as dividend income.

### **Working 6**

Rosie realised an offshore income gain when she sold units in a non-reporting fund. This is taxed as miscellaneous income and is non-savings.

|                      | £       |
|----------------------|---------|
| Sale proceeds        | 4,500   |
| Acquisition price    | (4,000) |
| Offshore income gain | 500     |

### Working 7

Personal allowance restriction:

|   | £       |
|---|---------|
| Net income                                  | 101,070 |
| Less: Gross gift aid donation (80 x 100/80) | (100)   |
| Adjusted net income                         | 100,970 |

Available personal allowance:

|   | £      |
|---|--------|
| Personal allowance                            | 12,500 |
| Less: Reduction $\frac{1}{2}$ (ANI – 100,000) | (485)  |
|   | 12,015 |

### Working 8

|  | £      |
|--|--------|
| Amount of income taxed at basic rate     | 37,500 |
| Add: Gross gift aid donation 80 x 100/80 | 100    |
|  | 37,600 |

### Working 9

Rosie's taxable income exceeds the basic rate band and therefore the savings allowance is £500. She is also entitled to the dividend allowance of £2,000.

#### Part 2)

Maximum contributions:

Test 1 applies when the taxpayer has more than one employment. SI 2001/1004 Reg 21.

|        |  | £   |
|--------|--|---|
| Step 1 | Calculate $53 \times (\text{UEL} - \text{PT})$ where: UEL is the weekly upper earnings limit for the year (£962 for 2019/20) PT is the weekly primary threshold (£166 for 2019/20) | 42,188  |
| Step 2 | Multiply the result of Step 1 by 12%   | 5,063   |
| Step 3 | For each of the employments, calculate the amount by which earnings exceed the primary threshold but do not exceed the upper earnings limit  | 50,000 – 8,632 = 41,368<br>20,600 – 8,632 = 11,968<br><u>53,336</u> |
| Step 4 | Figure found by Step 3<br>Less: Figure found by Step 1   | 11,148  |
| Step 5 | Step 4 figure $\times$ 2%. (If Step 4 is a negative number, this will be zero)   | 223   |
| Step 6 | For each of the employments, calculate the amount by which earnings exceed the upper earnings limit.   | (42,000 + 12,600) –<br>50,000 = 4,600                               |
| Step 7 | Step 6 figure $\times$ 2%.   | 92  |
| Step 8 | Figure found by Step 2   | 5,063   |
|        | Figure found by Step 5   | 223   |
|        | Figure found by Step 7   | 92  |
|        | Annual maximum   | 5,378   |

## **MARKING GUIDE**

| <b>TOPIC</b>  | <b>MARKS</b> |
|---|--------------|
| <b>Part 1):</b>   |              |
| Redundancy payment:   |              |
| An element of the PILON is taxable as it is split into two parts – PENP and income subject to s.403 | 1            |
| Correct PENP calculation  | 1            |
| s.403 ITEPA – first 30k exempt  | 1            |
| Horse event:  |              |
| Income taxable on Rose  | 1            |
| Property income:  |              |
| Allowable expenses  | 1            |
| UK dividends taxable on Rosie   | ½            |
| UK dividends grossed up   | ½            |
| Reporting fund taxed as dividend income   | ½            |
| Excess reported income  | ½            |
| Non-reporting fund sale is an offshore income gain, taxed to income tax                             | 1            |
| Gain calculation  | ½            |
| Offshore income gain is non savings income  | 1            |
| Personal allowance restriction (using adjusted net income)  | 2            |
| Taxable Income (PA deducted from NSI first)   | ½            |
| Gross up gift aid contribution  | ½            |
| Extend basic rate band  | ½            |
| Personal savings allowance restricted   | ½            |
| 7.5% tax credit on UK dividends   | 1            |
| Foreign tax deducted at source  | ½            |
| Correct rates used including dividend allowance   | ½            |
| Correct tax liability (deducting tax deducted at source to arrive at tax due amount)                | ½            |
| <b>Part 2):</b>   |              |
| Maxima calculation  | 3            |
| PENP subject to class 1 NIC   | 1            |
| <b>TOTAL</b>  | <b>20</b>    |



### **ANSWER 3**

Ms G Taylor  
1 High Street  
London NW1 2AB

Tax Adviser Partnership  
2 Central Avenue  
London S1 3YZ

November 2020

Dear Grace

#### **Capital Gains Tax Year Ended 5 April 2020**

As requested, I have set out below the Capital Gains Tax implications of the transactions we discussed.

The transfer of your share in Moor View House to Alex will give rise to a capital gain because as a result of your separation and divorce the usual rule that treats transfers between spouses as being at no gain no loss cannot apply. The gain will be based on the difference between your share of the market value of the property at November 2019 and your share of the original cost of the property.

Moor View House was worth £1,050,000 at the date of transfer. However, HMRC will accept that your half of the property is not worth as much as 50% of the value of the whole property. We can therefore reduce the market value accordingly. This is known as a tenanted deduction. I have used a deduction of 10% in my calculations, which are attached at Appendix A.

When an individual disposes of a property that has been used as their only or main residence for all or part of their period of ownership Principal Private Residence (PPR) Relief exempts from tax the gain that arises during their period of occupation and also during the final 18 months of ownership, even if they were no longer living in the property at that time. This claim would reduce your gain to £19,290.

As the property has been transferred as part of your divorce proceedings, and as Alex has continued to reside in the property as his PPR, you can make a claim to have the property treated as your PPR throughout your period of ownership, provided you have not nominated another property as your primary residence. This will result in a tax saving of £2,041 on Moor View House and allow your Annual Exempt Amount to be used elsewhere, saving a further £2,400 (£12,000 at 20%).

Please note that if you decide to make the claim for PPR in respect of Moor View House this will mean that 1 High Street will not be classed as your PPR for Capital Gains Tax purposes for the period from 1 February 2017 to 31 October 2019.

The sale of your Spanish bank shares will give rise to a gain of £10,252 as shown at Appendix B. I have assumed that you did not elect to treat the proceeds from the sale of rights in April 2018 as a part disposal, if this is not the case, please let me know.

The sale of the shop will give rise to a gain of £99,650 as shown at Appendix C. I have considered whether this gain will qualify for Entrepreneurs' Relief, which would reduce the tax rate from 20% to 10% but this disposal will not qualify as you are just selling an asset that is no longer required rather than disposing of a business. However, a relief called Rollover Relief exists, which a trader can claim when they sell one qualifying business asset and acquire another one within either 12 months before or 36 months after the date of sale. As you have used part of the proceeds from the shop to buy new fixed machinery for your business you can make a claim for this relief. A claim for rollover relief must be made within four years from the end of the tax year in which the gain is made or in which the new asset is acquired, whichever is the later. In your case this means that a claim must be made by 5 April 2025.

As a result of the claim, £22,650 of the gain will be frozen and will come back into charge on the earlier of:

1. The date the machinery is sold
2. The date you cease to use the machinery for the purposes of your business
3. Ten years after the machinery was acquired – 30 April 2030

Fixed plant and machinery is classed as a depreciating asset, which means that the treatment of the rolled over gain is as outlined above. However, if you were to purchase a non-depreciating asset for the purposes of your trade prior to the frozen gain coming back into charge, you could elect for the frozen gain to be rolled over against this new asset. This would have the effect of reducing the base cost of the new asset by £22,650.

If you decide to make the claims for full PPR Relief and for Rollover Relief, your total Capital Gains Tax liability for the year ended 5 April 2020 will be £15,051 as shown at Appendix D. This amount will be due for payment on 31 January 2021.

If you have any queries, please do not hesitate to contact me.

Yours sincerely

Tax Adviser

#### Appendix A

##### Transfer of 50% Share in Moor View House to Alex

|            |                          | £           |       |        |
|------------|--------------------------|-------------|-------|--------|
| 31/10/2019 | Market Value of 50%      | 525,000     |       |        |
|            | 10% "tenanted deduction" | (52,500)    |       |        |
| 01/11/1997 | Cost of 50%              | (133,000)   |       |        |
|            | Net Gain                 | 339,500     |       |        |
|            | PPR Relief               | (320,210)   | (W1)  |        |
|            | Gain After Relief        | 19,290      |       |        |
|            | Annual Exemption         | (12,000.00) |       |        |
|            | Taxable Gain             | 7,290       | x 28% | £2,041 |

##### Working One – Principal Private Residence Relief

|                            |            |    |            | Period of Residence (years) | Period of Ownership (years) |
|----------------------------|------------|----|------------|-----------------------------|-----------------------------|
| Living in the Property     | 01/11/1997 | To | 31/01/2017 | 19.25                       | 19.25                       |
| Absent                     | 01/02/2017 | to | 30/04/2018 |                             | 1.25                        |
| Deemed Period of Residence | 01/05/2018 | To | 31/10/2019 | 1.5                         | 1.5                         |
|                            |            |    |            | 20.75                       | 22                          |

Principal Private Residence Relief 20.75/22 x 339,500 = £320,210.

## Appendix B

### Sale of Spanish Bank Shares

|            |                        | £             |
|------------|------------------------|---------------|
| 26/02/2020 | Proceeds 4.26 x 11,575 | 49,310        |
|            | Cost (W1)              | (39,057)      |
|            | Net Gain               | <u>10,253</u> |

### Working One – Cost of Shares

|            |                                    | Number of<br>Shares | Cost<br>£     |          |
|------------|------------------------------------|---------------------|---------------|----------|
| 01/02/2017 | Share Option                       | 1,000               | 3,260         | (Note A) |
| 01/03/2017 | Purchase at £3.57 per share        | 12,000              | 42,840        |          |
| 15/04/2018 | Sale of rights (proceeds ≤ £3,000) |                     | (2,235)       |          |
|            |                                    | <u>13,000</u>       | <u>43,865</u> |          |
| 26/02/2020 | Sale: 11,575/13,000 x 40,605       | (11,575)            | (39,057)      |          |
|            | C/Fwd                              | <u>1,425</u>        | <u>4,808</u>  |          |

### Note A

The cost of the shares acquired under the option will be the amount paid for the shares £1.50 x 1,000 = £1,500, plus the amount that you were taxed on when you exercised the option (£3.26 - £1.50) x 1,000 = £1.76 i.e. a total of £3.26 per share

## Appendix C

### Sale of shop

|            |                  | £               |
|------------|------------------|-----------------|
| 15/03/2020 | Proceeds         | 155,000         |
| 27/08/1998 | Cost             | <u>(55,350)</u> |
|            |                  | 99,650          |
|            | Gain Rolled over | (22,650)        |
| Net Gain   | (155,000-78,000) | <u>77,000</u>   |

## Appendix D

### Capital Gains Tax Liability for the Year Ended 5 April 2020

|                      |                 | £             |
|----------------------|-----------------|---------------|
| Moor House           | nil             |               |
| Spanish Bank Shares  | 10,253          |               |
| Shop                 | 77,000          |               |
| Annual Exempt Amount | <u>(12,000)</u> |               |
| Taxable              | 75,254          | x 20% £15,051 |

## **MARKING GUIDE**

| <b>TOPIC</b>   | <b>MARKS</b> |
|--|--------------|
| Presentation and higher skills   | 2            |
| Explain that transfer of half share of Moor House to Alex will be at market value        | ½            |
| Explain tenanted deduction   | 1            |
| Explain PPR Relief available for period of occupation and final 18 months                | ½            |
| Explain s.225B TCGA 1992 claim and effect on tax liability                               | 1            |
| Explain effect of s.225B TCGA 1992 claim on 1 High Street                                | 1            |
| Explain treatment of sale of rights  | ½            |
| Consider availability of Entrepreneurs' Relief on the sale of the shop                   | ½            |
| Availability of rollover relief and required timing of acquisition of new asset          | 1            |
| Time limit for rollover relief claim   | ½            |
| Effect of rollover relief claim and explain when the frozen gain will crystallise        | 1            |
| Identify that fixed plant and machinery is a depreciating asset and implications of this | 1            |
| Explain ability to rollover frozen gain if purchases a non-depreciating asset            | ½            |
| Effect on base cost of non-depreciating asset  | ½            |
| Specify due date for tax payable   | ½            |
| Calculate gain on Moor View House  | 1            |
| Calculate PPR relief on Moor View House  | 1½           |
| Calculate tax saving if relief is claimed under s. 225B TCGA 1992                        | ½            |
| Explain claim under s.225B TCGA 1992 enables annual exemption to be used elsewhere       | ½            |
| Calculate the gain on the Spanish bank shares  | ½            |
| Calculate the cost of the Spanish bank shares  | 1½           |
| Calculate the gain on the shop & the amount to be rolled over                            | 1½           |
| Claim Annual exemption   | ½            |
| Calculate CGT liability  | ½            |
| <b>TOTAL</b>   | <b>20</b>    |

#### **ANSWER 4**

Chartered Tax Advisers  
1 High Street  
Anytown

Ms B Anderson  
1 Church Street  
Anytown

7 November 2020

Dear Bonnie

Thank you for your letter dated 5 May 2020.

Looking at each of the benefits offered:

1) If you accept the car allowance, this will be added to your salary and Income Tax (£3,200) and National Insurance (£160) will be deducted.

If you choose a company car, you will be liable to Income Tax, but not National Insurance, on the benefit. This is initially calculated as a percentage of the list price of the car when new. The percentage depends on the car's CO2 emissions, uplifted by 4% for a diesel car. This gives a taxable benefit of £7,680 (W1) and tax of £3,072.

However, because you have been offered a higher cash alternative, under the optional remuneration legislation, you will pay Income Tax on the £8,000 cash alternative foregone (£3,200). You will not have to pay National Insurance.

The tax payable on the fuel card will depend on whether you choose the car or the allowance. No National Insurance will be payable by you in either case.

If you choose the allowance, the cost of the fuel that you put onto the fuel card will be a taxable benefit. Based on your expected mileage this will be £2,520 (21,000 x 0.12p), resulting in tax of £1,008.

You can then claim tax relief on mileage as the company would not contribute towards your business mileage. This would result in a tax saving of £1,080 (W2).

If you choose the company car, you will be taxed on a fixed amount each tax year multiplied by the same percentage used to calculate the car benefit, which would be £7,712 (W3) tax at 40% would be £3,085. You will not be able to claim a deduction for business mileage.

If you reimburse your employer for private mileage, including commuting you could cancel the fuel benefit tax charge. To be effective, you must reimburse for every private mile. You expect to do 15,000 private miles. Reimbursing your employer at a rate of 12p per mile will cost you £1,800 which is considerably less than the tax on the fuel benefit.

Taking into account all of the above factors if you accept the car allowance you will be better off by £4,312 (W4: £5,000 - £688). However, as you will own the car yourself you will have to meet any maintenance costs for the car from this saving.

2) Although it would usually cost £750 to be a member of the gym, as Quality Gym Ltd will not have to pay a membership fee for you, you will be taxed only on the marginal cost of your membership to Quality Gym Ltd. This is likely to be very low or even zero, so probably a very low tax cost benefit for you. There will be no National Insurance liability.

3) Work related training provided an employer (training designed to improve knowledge or skills which are likely to prove useful to you in performing your duties or better qualify you to undertake the employment) is exempt from Income Tax and National Insurance. So if the company pays for your professional level qualification once you are an employee, this will be an exempt benefit.

The costs of the intermediate level training are pre-employment costs and unless there is a very strong and demonstrable link between the new employment and the costs, they will not be exempt. This is generally very difficult to prove, so the £1,000 contribution will be liable to Income Tax and National Insurance via payroll.

You will not be able to claim a deduction against your tax liability for the costs you incurred personally as you will not be able to show that the costs were incurred “wholly, exclusively and necessarily in the performance of your duties”, not least because you were not employed by Quality Gym Ltd when you started the course.

If you have any further questions, please do not hesitate to contact me.

Yours sincerely

Ben Thomson

Workings

W1 car benefit

$(23 + (120-95)/5) = 28\%$   
 Plus diesel uplift 4%

Total 32%

Car benefit £24,000 x 32% = £7,680

W2 mileage claim

|                     |                                  | £     |
|---------------------|----------------------------------|-------|
| Tax relief on 45ppm | $6,000 \times £0.45 \times 40\%$ | 1,080 |

W3 fuel benefit

$£24,100 \times 32\% = £7,712$

W4 comparison of options

|                                     | Car allowance costs (£) | Company car costs (£) |
|-------------------------------------|-------------------------|-----------------------|
| Cost of vehicle                     | 5,400                   | -                     |
| Car benefit tax/NI                  | 3,360                   | 3,200                 |
| Cash receipt                        | (8,000)                 | -                     |
| Tax relief on mileage claim         | (1,080)                 | -                     |
| Tax on fuel card 21,000 x 12p x 40% | 1,008                   | -                     |
| Reimbursement for fuel              | -                       | 1,800                 |
| Net cost                            | 688                     | 5000                  |

## **MARKING GUIDE**

| <b>TOPIC</b>  | <b>MARKS</b> |
|---|--------------|
| Presentation  | 1            |
| Car allowance taxed as salary – tax and NI both due                               | 1            |
| Car benefit – no NI   | ½            |
| Tax as a % of list price  | ½            |
| 4% uplift due to diesel   | ½            |
| Calculate correct benefit based on list price                                     | 1            |
| Cash alternative higher so taxable under optional remuneration rules              | 1            |
| Fuel card – no NI due   | ½            |
| Car allowance – taxed on actual cost on fuel card                                 | 1            |
| Business mileage claim  | 1            |
| Car benefit – fuel taxed due on deemed benefit                                    | 1            |
| Reimburse for private mileage would be beneficial if company car                  | 1            |
| Conclusion on which option to select  | 1            |
| Gym membership – taxable on marginal cost to employer                             | 1            |
| Work related training is exempt   | 1            |
| Contribution to pre-employment training will be taxable                           | 1            |
| Will not be able to claim a deduction for intermediate costs against personal tax | 1            |
| <b>TOTAL</b>  | <b>15</b>    |

## **ANSWER 5**

**To: Tax partner**

**Re: Jason Jones**

### **Position if no elections**

If Jason receives shares or securities from Generous Boss Ltd as a reward for services, there is a tax charge based on the value of the shares (s.62 ITEPA 2003).

However, as the shares are subject to a risk of forfeiture within five years, there should be no charge to tax at the time of issue (s.425 ITEPA 2003).

A charge will arise when the forfeiture restriction is lifted. The taxable amount is a percentage of the market value of the shares immediately after the forfeiture restriction is lifted (s.428 ITEPA 2003).

This percentage is equal to the initial unrestricted market value of the shares that was neither taxed nor paid for when the shares were originally acquired:

|                                   |            |
|-----------------------------------|------------|
|                                   | £          |
| Subscription price                | 1.00       |
| Initial unrestricted market value | 5.00       |
| 1.00/5.00                         | <u>0.2</u> |
|                                   | 20%        |
| 100% – 20%                        | <u>80%</u> |

This is reduced by any previously charged proportion (nil) and any “outstanding proportion”. Assuming forecasts are correct, the outstanding proportion will be 14%:

|  |             |
|--|-------------|
|  | £           |
| Restricted market value  | 6.00        |
| Unrestricted market value  | 7.00        |
| 6.00/7.00  | <u>0.86</u> |
|  | 86%         |
| 100% – 86%   | <u>14%</u>  |
| Percentage as above  | 80%         |
| Less previously charged proportion                               | (0%)        |
| Less outstanding proportion                                      | (14%)       |
| Chargeable proportion  | <u>66%</u>  |
| Chargeable proportion x unrestricted market value x 1,000 shares | 4,620       |



A charge will also arise when the disposal restriction is lifted. The taxable amount is a percentage of the market value immediately after the disposal restriction is lifted (s428 ITEPA 2003).

This percentage is equal to the initial unrestricted market value of the shares that was neither taxed nor paid for when the shares were originally acquired (i.e. 80% as above).

An adjustment is made for any previously charged proportion (i.e. 66%) and any "outstanding proportion" (nil). The amount brought into charge on the lifting of the restriction will therefore be 14% x £8 x 1,000 shares, i.e. £1,120.

However, two elections can be made for the exemption on acquisition not to apply.

**Election to disapply forfeiture exemption under s.425(3) ITEPA 2003**

The effect of one such election is to disapply the five-year exemption and crystallise an Income Tax charge on the restricted market value of the shares at acquisition. This means that an income tax charge would arise on the following amount:

|                                   | £     |
|-----------------------------------|-------|
| Restricted market value per share | 4.00  |
| Less: Subscription price          | 1.00  |
| Taxable amount per share          | 3.00  |
| x 1,000 shares                    | 3,000 |

The advantage of making this election is that because some of the initial value of the shares is taxed on acquisition, a lower percentage of the later value is then charged when the forfeiture restriction is lifted as shown below:

|   |       |
|---|-------|
|   | £     |
| Subscription price  | 1.00  |
| Amount taxed on acquisition   | 3.00  |
|   | 4.00  |
| Initial unrestricted market value                                     | 5.00  |
| Subscription price and taxed amount/initial unrestricted market value | 0.8   |
|   | 80%   |
| 100% – 80%  | 20%   |
| Less outstanding proportion (as above)                                | (14%) |
| Taxable percentage  | 6%    |
| Chargeable proportion x unrestricted market value x 1,000 shares      | £420  |

The election does not prevent a tax charge from applying on the lifting of the disposal restriction.

However, Jason will not be able to recover any Income Tax paid on the initial award if the shares are actually forfeited.

### **Election to disapply restricted securities regime under s.431 ITEPA 2003**

The effect of the other election is to apply an Income Tax charge on the unrestricted market value of the restricted securities when Jason acquires them (£5 per share).

The advantage of making this election is that there is no Income Tax charge when either of the restrictions are lifted.

Where this election is entered into, any future growth in the value of the shares should generally be subject only to Capital Gains Tax .

### **Both elections**

Either election must be made by Jason and Generous Boss Ltd jointly.

The elections must be made within 14 days following the award of the shares and are irrevocable.

There is no requirement to send the elections to HMRC, but they must be kept on file in case of an enquiry.

However, Jason should not make either election if it is expected that the shares will fall in value.

If he makes the election to disapply the forfeiture exemption, he will not be able to recover any Income Tax paid on the initial award of the shares if the market value of the shares is lower when the forfeiture restriction is lifted than when they were acquired.

If Jason makes the election to disapply the restricted securities regime and the shares fall in value, he is electing to be taxed on a higher amount (the unrestricted market value). This will be greater than the tax charge applying if the restricted securities regime applies. There would be no refund of Income Tax paid on the overpaid amount.

On the basis that the shares are not readily convertible assets, there would be no NIC arising on the award of the shares.

## **MARKING GUIDE**

| <b>TOPIC</b>   | <b>MARKS</b> |
|--|--------------|
| No tax charge arising on the acquisition due to forfeiture within 5 years      | 1            |
| Charge arises on the lifting of the forfeiture restriction                     | ½            |
| Explanation of how that charge is calculated                                   | 1            |
| Charge arises on the lifting of the disposal restriction                       | ½            |
| Explanation of how that charge is calculated                                   | 1            |
| Can elect to disapply the forfeiture exemption                                 | ½            |
| Effect of election: income tax charge on restricted value on acquisition       | 1            |
| Effect of election: lower percentage used on lifting of forfeiture restriction | 1            |
| Effect of election: still a charge on lifting on disposal restriction          | 1            |
| Can elect to disapply the restricted securities regime                         | ½            |
| Effect of election: income tax charge on unrestricted value on acquisition     | 1            |
| Effect of election: no income tax charge on lifting of restrictions            | 1            |
| Effect of election: future growth generally subject to CGT                     | ½            |
| Election is joint  | ½            |
| Deadline for making elections  | ½            |
| No requirement to submit to HMRC   | ½            |
| Irrevocable  | ½            |
| Should not make election if expected shares will fall in value                 | 1            |
| Will be no refund of overpaid tax  | 1            |
| No NIC arising as not readily convertible assets                               | ½            |
| <b>TOTAL</b>   | <b>15</b>    |

## ANSWER 6

|                                     | Non-Savings income | Tax     |
|-------------------------------------|--------------------|---------|
|                                     | £                  | £       |
| Pension income                      | 50,000             |         |
| Property income (W1)                | 2,275              |         |
|                                     | -----              |         |
| Total income                        | 52,275             |         |
| Less: personal allowance            | (12,500)           |         |
|                                     | -----              |         |
| Taxable income                      | 39,775             |         |
|                                     | =====              |         |
| Tax due at 20%                      | 37,500             | 7,500   |
| Tax due at 40%                      | 2,275              | 910     |
|                                     |                    | -----   |
|                                     |                    | 8,410   |
| Loan interest relief (W6)           |                    | (455)   |
| Tax deducted at source from pension |                    | (7,300) |
|                                     |                    | -----   |
| Tax due                             |                    | 655     |
|                                     |                    | =====   |

Tax will be payable by 31 January 2021, or Ted could ask for it to be coded through his 2021/22 tax code as long as the return is filed by 30 December 2020.

### Workings

1. Rental profit
- 2.

|                               | working | £     | £      |
|-------------------------------|---------|-------|--------|
| Rental income                 | 2       |       | 12,000 |
| Less: expenditure             |         |       |        |
| Allowable costs               |         | 3,000 |        |
| Travel costs                  | 3       | 225   |        |
| Replacement of domestic items | 4       | 2,000 |        |
| Loan interest                 | 5       | 4,500 |        |
|                               |         | ----- |        |
|                               |         |       | 9,725  |
|                               |         |       | -----  |
| Taxable rental profit         |         |       | 2,275  |
|                               |         |       | =====  |

2. Rent received

|                      | £      |
|----------------------|--------|
| Residential rent     | 8,000  |
| Commercial rent      | 4,000  |
|                      | -----  |
| Total rents received | 12,000 |
|                      | =====  |

3. Travel costs

Ted can claim mileage at 45p per mile for miles travelled in connection with the rental business.

$$500 \times £0.45 = £225$$

#### 4. Replacement of domestic items

The new carpets can be claimed, as these are replacing old carpets. The cost of the washing machine is not deductible as this is a first time purchase and not a replacement.

#### 5. Loan interest

In 2019/20, 25% of the interest charge is deductible from the rental income for a residential property. The balance of the interest charge is deductible at 20% as a tax reducer against the tax liability.

Loan interest on a commercial property is allowable in full against the rental income.

For a mixed property, the loan interest should be split in a "just and reasonable basis". As rents received and also the value of the properties are in the ratio of 2:1, this split has been used.

(NB marks will be given for any reasonable split as long as it is justified)

|                                   | Residential | Commercial | Total |
|-----------------------------------|-------------|------------|-------|
|                                   | £           | £          | £     |
| Deductible from rental income     | 1,500       | 3,000      | 4,500 |
| Available at 20% as a tax reducer | 4,500       | 0          | 4,500 |
|                                   | -----       | -----      | ----- |
| Total interest                    | 6,000       | 3,000      | 9,000 |
|                                   | =====       | =====      | ===== |

#### 6. Tax reducer

The tax reducer is 20% of the lower of

Finance costs not eligible for full reduction as above £4,500

OR

Property income for the year after b/fwd losses £2,275

£2,275 at 20% =£455

2)

|  | £  | £       | £      |
|--|--|---------|--------|
| <b>Sale of house to Jessie – market value to be use as connected persons</b> |  |         |        |
| Sales proceeds   | deemed   | 300,000 |        |
| Allowable cost   | $210,000 \times \frac{300,000}{(300,000+150,000)}$ | 140,000 |        |
|  |  | -----   |        |
|  |  | 160,000 |        |
| Annual exempt amount   | Use against residential property                   | 12,000  |        |
|  |  | -----   |        |
| Taxable gain   |  | 148,000 |        |
|  |  | =====   |        |
| Capital Gains Tax at 28%   | Residential property rate                          |         | 41,440 |

The granting of the lease on the shop will result in both an income tax charge and a capital gain

| <b>Grant of short lease on the shop</b>     |   | £      | £             |
|---|---|--------|---------------|
| Capital element                             | $2\% \times (20-1) \times \text{£}60,000$ |        | 22,800        |
| Allowable cost                              |   |        |               |
| Remaining cost                              | 210,000 – 140,000                         | 70,000 |               |
| Allowable for lease                         | $22,800 / (60000 + 90000) \times 70000$   |        | 10,640        |
|   |   |        | -----         |
|   | Chargeable gain                           |        | <u>12,160</u> |
|   |   |        |               |
| Capital Gains Tax at 20%                    | Commercial property rate                  |        | 2,432         |
|   |   |        | -----         |
| Total CGT payable                           |   |        | <u>43,872</u> |
| Payable 31/1/2022                           |   |        |               |
|   |   |        |               |
| Premium chargeable to income tax in 2020/21 | $\text{£}60,000 - 22,800$                 |        | <u>37,200</u> |
|   | Income Tax payable at 40%                 |        | <u>14,880</u> |

As Jessie is a connected person, the market value of the property on the date of transfer will be used to calculate the gain.

Ted can allocate his annual exempt amount against the resulting gains in the most tax efficient manner, so assuming he has no other capital gains in the year he would allocate the annual exempt amount against the house first.

## **MARKING GUIDE**

| <b>TOPIC</b>   | <b>MARKS</b>     |
|--|------------------|
| Travel costs   | 1                |
| Replacement of domestic items- carpets allowable                   | 1                |
| Washing machine not allowable                                      | 1                |
| Split interest on just and reasonable basis                        | 1                |
| Calculate amount deductible from rent = residential part           | 1                |
| Calculate amount deductible from rent - commercial part            | 1                |
| Tax reducer lower of finance costs not relieved or property income | 1                |
| Correct tax due  | 1                |
| Due date   | ½                |
| or code out if submit return by 30/12/2020                         | ½                |
|  | --               |
| Sub total  | <u>9</u>         |
| <b>Sale of building</b>  |                  |
| Market value to be used as connected persons                       | 1                |
| Correct split of cost between the two properties                   | ½                |
| Allocate annual exempt amount against residential property         | ½                |
| Correct tax rates – residential property                           | ½                |
| Correct tax rates – commercial property                            | ½                |
| Calculate capital element of lease                                 | 1                |
| Allowable cost for short lease                                     | ½                |
| Correct capital gain   | ½                |
| Correct premium chargeable to income tax                           | ½                |
| Income tax payable   | ½                |
|  | --               |
| Sub total  | <u>6</u>         |
| <b>TOTAL</b>   | <b><u>15</u></b> |

If a candidate mentions that the CGT must be reported and is payable within 30 days after 5/4/20 they will get a bonus mark