Institution **CIOT - ATT-CTA**
Course **CTA Adv Tech Owner-Managed Business**

Answer-to-Question-_1_

The definition of plant and machinery is found in CAA2001 and significant case law. The case of Yarmouth v France (1887) defines plant as:
"Whatever apparatus is used by a business man for carrying on his business - not his stock-in-trade which he buys of makes for sale; but all goods and chattels, fixed or moveable, live or dead, which he keeps for permanent empoyment in the business"

HMRC practise is to treat an asset that has an expected useful life of two years or more to be for "permanent employment" and therefore sufficiently durable to qualify as plant.

Business premises are not plant as they are not goods or chattels. The test of whether an item is apparatus used in carrying on a business is the "functionality test".

The cost of repairs is normally allowable expenditure for tax purposes, whereas the cost of replacing an asset or making a significant improvement to an asset is capital expenditure.

An expense is a repair where it restores an asset to its original condition. The use of new technology as a part of a repair foes not necessarily mean the repairs becomes an improvement.

Work on existing facilities

1) Grass pitches

This is replacing one type of pitch for a different, arguably more durable pitch which is likely to be deemed an upgrade. It is therefore likely that this will not qualify as a repair and will instead be a fixture under capital allowances.

2) Access Road

Repairs to an access road is an allowable expense, following the decison in G Pratt & Sons v HMRC Commissioners (2011). This will therefore qualify as a repair in the P&L.

3) Five touring caravans.

The four caravans that are to be let to holiday makers will form part of the plant and machinery for capital allowances purposes. As the fifth caravan is to be fixed in place, this will form a new structure and will therefore not qualify as a repair or for capital allowances.

Upgrade and development work

1) Preliminary costs

Preliminaries such as site maintenance and professinoal fees can be claimed for capital allowances purposes in line with JD Wetherspoon v HMRC. They are apportioned across the main pool/special rate pool/non-qualifying in proportion with the

relevant expenditure on each category.

2) Shop

The advertising sign will qualify for capital allowances under plant and machinery as it will have an enduring benefit.

The cost of the suspended ceiling will form part of the airconditioning and electrical systems and will therefore qualify for captial allowances in the special rate pool as an integral feature.

Moveable partitions will qualify for capital allowances in the main pool as plant and machinery. Even though some will be kept in place, they are still moveable and therefore allowable.

3) Derelict Barn

Artworks can receive relief for capital allowances via the main pool where the trade involves the creation of an attractive setting or atmosphere (IRC vs Scottish and Newcastle Breweries Ltd 1982).

Tiling for splashbacks to signks and toilets can claim capital allowances in the main pool as a result of JD Weatherspoon plc vs HMRC 2009.

The tiled floor will be fixed and will therefore not qualify for capital allowance purpsoes. As it is not a repair, it will not qualify as a revenue expense either. This would form part of the structures and buildings allowance

4) Houses for animals

Buildings for animal quarantine will not qualify for capital allowances, these would form part of the SBA as per HMRC vs Sayer 1992.

---------------ANSWER-1-ABOVE----------------

---------- ANSWER-2-BELOW ----------

Answer-to-Question-_2_

Part 1) Corporation tax issues that could arise & potential structures

Anti-avoidance legislation rules exist to prevent a company from carrying forward it's trading losses where there has been a change in it's ownership and the new owner has effectively bought the company because it wants to utilise the losses brought foward.

If, within a three year period a single person acquried more than 50% of the share capital of the company, then there has been a change in it's ownership. As Mike it looking to purcahse 100% of the share capital, this would be the case in this scenario.

The period under review will be a five year period beginnning no more than three years before teh change in ownership of the company. No major change in the nature or conduct of the trade carried on by the company must happen in that five year period.

s.673 CTA 2010 defines a major change as "a major change in the

type of property dealt in, or services or facilities provided in the trade, or a major change in customers, outlets and markets".

If a MCINOCOT is deemed to have taken place, a brick wall is put up at the date of the change of ownership which blocks trading losses from being carried foward after that date.

Currently, Safety Ltd provides safety training only. Besail Ltd predominately provides Yacht timeshares and social events, the training in first aid and fire safety is a minimal part of the business.

Mike is looking to change the focus of the company to attract a different type of customer from luxury yachts to more affordable ones and removing the provision of training by outsourcing it, presumably to his own company. It it likely that these would be deemed major changes in the trade and therefore the losses may be blocked from future use against profits.

If Mike were to purchase all of the shares himself, he is also taking on the entire history of the company and it's corporation tax filings in the past.

The first issue that may arise is that costs relating to social functions have been claimed for corporation tax relief purposes. Client entertaining is specifically blocked and should not have been deducted. If HMRC were to open an enquiry into this they can

levy penalties on the company for submission of incorrect returns.

The intangible asset of the bespoke booking system is also an issue as this has not been properly valued, nor has it been recorded correctly in the accounts. The previous owner has credited his own Director's loan account with the £100,000, meaning that as far as the accounts show, he is owed £100,000 from the company. This would still be "payable" to him if Mike acquired all the share capital.

Mike would also be taking on the legal issue regarding the death of a client on the Yacht. This could potentially result in a pay out of up to £1million which the company would be liable for. Whilst Mike has Limited liability by purchasing the company shares, he is still at risk of losing his £250,000 investment if this case is successful and the business goes into involuntary liquidation.

Another alternative structure that could be considered involves the use of a hive down.

This is an alternative way for a buyer to acquire a clean company with no history, but through a purchase of shares rather than a purchase of trade and assets. this method also allows the buyer to acquire just part of the target company.

A new company is set up by Besail Ltd called, for example NewCo

Ltd. Besail transfers it's trade and assets into NewCo Ltd - this is a normal transfer of trade and assets which would be a succession as 75% ownership is unchanged. The trade losses can be transferred with the trade.

Mike can then buy the NewCo Ltd shares from Besail Ltd. This is a normal sale of shares, but he has acquired a clean company.

Part 2) Tax issues of proposed loans

The loan of £100,000 from Safety Limited to Mike will be a "loan to a participator". Loans made to shareholders in a close company incur an additonal tax liability equivalent to 32.5% of the loan called s.455 tax. This arises when a loan is outstanding 9 months after the end of the accounting period in which the loan was originally made.

Therefore, if the loan is still outstanding at the corporation tax due date, a total of £32,500 of s.455 tax will be payable by Safety Ltd.
The company can seek a repayment of the s.455 tax when the loan is repaid to the company.

Where a close company makes a loan to a participator and either charges no interst or charges below the official rate, a taxable

beenefit is levied on the participator. However, as the loan is being made for a qualifying purpose (investing in a close company), the benefit is exempt.

The loan from the bank will charge interest at 7%. This is a loan that Mike would be taking out personally, rather than through a business. He will therefore not be able to claim any tax relief on the £7,000p/a interest he will be paying on the loan.

When Safety Ltd lends money to Besail Ltd this may be deemed a loan made in the ordinary course of business and will therefore be excluded from the S.455 charge.

---------- ANSWER-2-ABOVE ----------

----------ANSWER-3-BELOW----------

Answer-to-Question-_3_

Part 1) Calculate taxable profits for 2021/22 and 2022/23

		Total	Ross	Abby	Yousef	
1/2/20 - 31/1/21						
Total profits		150,000				
Salary		(24,000)		24,000		
Profit share(3:2)		126,000	75,600	50,400		
Total			75,600	74,600		
1/2/21 - 1/6/21						
Total profits(w1)		60,000				
Salary (w2)		(8,000)		8,000		
Profit share(3:2)		52,000	31,200	20,800		
Total			31,200	28,800		
1/6/21 - 31/5/22						
Total profits(w3)		180,000				
Salary		(36,000)		21,000	15,000	
Profit share(1:1)		144,000		72,000	72,000	
Total			0	93,000	87,000	

(w1) Profit
Feb - May = 4 months
£240,000 x 4/16 = 60,000

(w2) Salary
£24,000 x 4/12 = 8,000#

(w3) Profits
£240,000 x 12/16 = £180,000

Ross:

Ross' taxable profits for the 2021/22 tax year =
£31,200 - overlap relief of £30,000 = £1,200

Ross' taxable profits for the 2022/23 tax year = £nil

Abby:

Abby's taxable profits for the 2021/22 tax year =

Change of accounting date;
Year of change = 2021/22

Calculate taxable profits before the change - 12 months up to the old accounting date:
01/02/2020 - 31/01/2021:
£74,600

Calculate taxable profits after the change - 12 months up to the new accounting date
01/06/2021 - 31/05/2022:
£93,000

Gap = 01/02/2021 - 31/05/2021 = 4 months

8/12 x £93,000 = £62,000

Profit for 2021/22 = £93,000 + £62,000 = £155,000

Overlap profit b/fwd = £10,000
Add overlap profit = £62,000
Overlap profit c/fwd = £72,000 (10 months)

Abby's taxable profits for the 2022/23 tax year = £93,000

Yoursef:

Yousef's taxable profits for 2021/22:
01/06/2021 - 05/04/2022 = 10/12 x £87,000 = £72,500

Yousef's tacable profits for 2022/23:
01/06/2021 - 31/05/2022 = £87,000

Overlap relief c/fwd = £72,500 (10 months)

Part 2)

When a partner leaves a partnership, he is deemed to be making a disposal of his share in the property to the remaining partners. A Capital gain therefore arises on his share, which as at 01 June 2021

Ross's base cost:

01/02/2017 = £100,000 x (3:1) = £75,000

The asset was revalued on 31 January 2018, before the profit sharing ratios were changed, therefore he received (3:1) of the increase in value

31/01/2018 = £50,000 x (3:1) = £37,500

Therefore, his total base cost is = £112,500 as at 01 February 2018.

He then disposed of a portion of his share to Abby:
75% down to 60%

£112,500 x 15% = 16,875

This leaves him with a base cost of £95,625.

When he retires, he is disposing of his entire 60% share in the property with a market value of £300,000, therefore a gain arises as follows:

		£	
Proceeds (£300,000 x 60%)		180,000	
Less base cost		(95,625)	
Capital gain		84,375	
Less AEA		(12,300)	
Chargeable gain		72,075	

As this is the disposal of a business asset on the retirement from a partnership, Ross will qualify for business asset disposal relief on the gain of this property as he owned a share in the parntership for a period of more than 2 years. This gain will therefore be taxed at 10%:

£72,075 x 10% = £7,208.

Abby's base cost will be her initial acquisition base cost of: £100,000 x 25% = £25,000

Plus the additonal value she acquired on the change in the profit sharing ratio in 2018 = £16,875

Plus the additonal 10% she now acquires on Ross' disposal at MV: £300,000 x 10% = £30,000

This gives Abby a base cost of £71,875

Yousef is acquiring a 50% stake in the property. His base cost will be based on the current market value of £300,000;

£300,000 x 50% = £150,000.

----------ANSWER-3-ABOVE----------

----------ANSWER-4-BELOW----------

Answer-to-Question-_4_

Adjusted trading profits for 2021/22:

		£	£
Profit per accounts			97,930
ADD BACK:			
Depreciation (n1)		5,550	
Pension contributions (n3)		250	
General provisions (n4)		3,000	
Interest paid (n5)		0	
Sundry expenses		0	
			8,800
LESS:			
Interest rec'd (n2)		150	
Capital allowances (n7)		46,100	
			(46,250)
TATP			97,780

(n1) Depreciation is an accounting adjustment and should therefore be added back. Capital allowances are given in their place.

(n2) Interest received
Interest received is accounted for in the sole trader's self assessment return seperately from trading income.

(n3) Staff costs
Tax relief for pension contributions is strictly on a "paid" basis. Therefore, the employer contributions which were not paid until 4 April will need to be added back and accounted for in the next year.

(n4) Bad debts
Specific bad debts are an allowable expense, general provisions are not. Therefore the provision of £3,000 will need to be added back for tax purposes.

(n5) Interest payable
Interest payable on loans for business purposes is an allowable expense and therefore this does not need to be added back.

(n6) Sundry expenses
Staff entertaining is an allowable expense, but client entertaining is not.
Charitable donations are allowed for a sole trader as long as they are made wholly and exclusively for the purposes of trade and no gift aid declaration has been made. No adjustments are required to sundry expenses

(n7) Capital allowances

	FYA	Private	Main pool	Special	Total CAs
	£	£	£	£	£
TWDV b/f			20,000		
Additons					
New van			30,000		
Comp equp			12,500		
AIA			(42,500)		42,500
Total			20,000		
WDA @ 18%			(3,600)		3,600
TWDV c/f			16,400		
Total CAs					46,100

As both the van and computer equipment are new, they will qualify for AIA.

Income tax:

Profit for the 2021/22 tax year = £97,780
Less trading losses b/fwd = (£5,000)
Taxable trading profit = £92,780

	NSI	SI	DI
	£	£	£
Interest (n2)		100	
Profit	92,780		
Salary	18,000		
Total	110,780	100	
Less PA (w1)	(7,130)		
Taxable income	103,650	100	
SI £100 @ 0%		0	
NSI 37,700 @20%	7,540		
NSI 65,950 @40%	26,380		
Total	33,920		
Ded'd at source	(1,086)		
Tax payable	32,834		

(w1) Personal allowance is abated bvy £1 for every £2 earned over £100,000.

Total income = £110,880 -> £10,880 / 2 = £5,440 abatement
£12,570 - £5,440 = £7,130

The tax payable of £32,834 will be payable to HMRC by 31st January 2023.

National insurance;

As Alex has both employment and self employment income, he will be liable to pay Class 1 primary on his employment income as well as Class 2 and Clss 2 NICs on his sole trade profits.

The annual maxima rules apply where an individual is both employed and self employed to limit the amount of national insurance the individual pays;

Test 1 determines the maximum amount of Class 1 and Class 2 NICs due:

		£	£
Step 1) Calculate 53 x (UEL - PT)			41,499
Step 2) Multiply by 12%		4,980	
Step 3) Calculate the amount by which earnings exceed PT but do not exceed UEL (18k - 9,568)			8,432
Step 4) Step 3 - Step 1			0
Step 5) Step 4 x 2%		0	
Step 6) Calculate the amount by which earnings exceed UEL			0
Step 7) Step 6 x 2%		0	
Step 8) Step 2 + 5 + 7		4,980	
Annual max Class 1 & Class 2		4,980	

As Alex has only paid £1,011 of Class 1 and will pay £3.05 x 52 = £158.60 in Class 2, no refund of these NICs is due

Test 2 determines the amount of Class 4 NICs due:

		£	£
Step 1) UPL - LPL			40,702
Step 2) Multiply by 9%		3,663	
Step 3) Add 53 x Class 2 NIC		162	
Step 4) Less Class 1 NIC paid		(1,011)	
Less Class 2 NIC paid		(159)	
Total		2,655	

Comparative total

Class 4 NIC due:

£50,270 - £9,568 x 9% = £3,663
£92,780 - £50,270 x 2% = £850

Total = £4,513

Class 1 paid = £1,011
Class 2 paid = £159
Class 4 paid = £4,513
total = £5,683

As this exceeds the annual maxima, a Class 4 NIC refund will be due of £4,513 - £2,655 = £1,858

----------ANSWER-4-ABOVE----------

--------------ANSWER-5-BELOW---------------

Answer-to-Question-_5_

The first issue that arises is that Barput Ltd has failed to give notice to HRMC of coming within the charge to Corporation tax. Compaines are required to notify HMRC when their first accounting period begins. A company must give written notice to HMRC within three months of the start of the first accounting period. However, no penalty applies if notification is not given.

Where a notice to prepare a reutrn is not issued, a company is required to notify HMRC where it has taxable profits for an accounting period. It must make notificiation of chargeablility within 12 months of the end of the accounting period.

If notification of tax is not given, a penalty for failure to notify may be payable. The penalty will be based on the behaviour of the company and is a percentage of the "potential lost revenue" - i.e. the amount of corporation tax which is unpaid 12 months after the end of the accounting period.

The maximum and minimum penalties are as follows:

If the behaviour is deemed to be deliberate and concealed, the maximum penalty is 100% of the potential lost revenue (£16,750 in this case). The minimum penalty with umprompted disclosure is 30% and with prompted disclosure it is 50%.

If the behaviour is deemed deliberate but not concealed, the maximum penalty is 70%. The minimum penalty for umprompted disclosure is 20% and with prompted disclosure it is 35%.

For any other case, the the maximum penalty is 30%, with minimum penalties between nil and 20% for prompted and unprompted disclosure depending on whether it is within 12 months.

HMRC do not deem ignorance of the rules to be a genuine excuse, so it is likely in this case that if the directors made an umprompted disclosure of their mistakes, they would be deemed to have been deliberate, but not concealed and the penalty will range between 20% - 70%. The actual reduction in the penalty depends on the qualify of the elements of disclosure, including timing, nature and extent.

The next issue is that they did not submit their first corporation tax return within the deadline. For an accounting year ended 31 December 2020, the first CT return should have been submitted within 12 months of the year end (31 December 2021) and the tax should have been paid within 9 months and 1 day of the year end (01 October 2021). Neither of these deadlines were met and although draft accounts have been prepared, it does not appear as though any returns have been submitted and £16,750 of CT remains unpaid.

There are two types of penalty that may apply for late filing of coropration tax returns; a flat rate penalty and a tax geared penalty.

A flat rate penalty of £100 is levied automatically where the return is up to 3 months late. The penalty increases to £200 where the return is more than 3 months late. These penalties are increased to £500 and £1,000 for second and third offences.

A tax geared penalty of 10% applies if the return is not filed within 18 months of the end of the relevant accounting period.

The return is currently less than 3 months late, therefore, if it is submitted as soon as possible, only the £100 penalty will apply.

Interest will be charged on the late payment of corporation tax at the official rate of 3% from the date on which the tax was originally due (01 October 2022).

The directors have been taking a salary of £2,000 each per month for over two years without submitting a single PAYE sumbission or paying any tax or national insurance.

Monthly Full Payment Submissions (FPS) are required when running a payroll by the date on which the payroll is deemed to be run. A late filing penalty will be charged for a tax month were an FPS is submitted late. A penalty will not be charged in respect of the month in which the first late filing occurs within a tax year.

Where a penalty is charged, it is dependent on the number of employees. As there are only 2 directors, they will receive a £100 penalty for each late submission. Where the returns are three months late the penalty is 5% of the tax and NICs that

should have been shown on the return.

The penalties for incorrect FPS submissions are the same as the penalties for failure to notify of CT listed above.

The payments of PAYE will also now be late as each should have been paid over to HMRC by 22nd of the month following the end of the payroll period. Interest will be charged on the late payments.

Where an employer fails to operate PAYE correctly and this results in an udnerpayment of tax, HMRC can recover the tax from the employer or from the employee.

As the directors are both receiving company cars from the company, these should have been declared as "benefits in kind" to HMRC on a form P11d no later than 6th July following the end of the tax year. Both are high emissions vehicles which would have been subject to income tax at 37% of the list price.

The penalty for late submission of a Form P11d is £300 per late form.
A further penalty of £60 per day can be applied for each day that the faiture continues.

Where a director loans money to the business in return for interest to be paid quarterly, the company should be paying the interest to the director net of 20% income tax. The company must account for income tax on a quarterly basis using a CT61 quarterly return.

The quarterly returns are due 14 days following the end of the return period.

If a company is constantly deemed to be non-compliant with filings for HMRC and Companies House, they can be struck off.

---------------ANSWER-5-ABOVE---------------

---------------ANSWER-6-BELOW---------------

Answer-to-Question-_6_

Whether an individual is deemed to be employed or self-employed is not a matter of choice, but a matter of the facts. It is important to make the correct determination as how an individual is taxed will vary siginificantly if they are treated as an employee rather than self-employed.

HMRC provide an online "status test" that can be used as a guide to determining an individuals employment status.

There is no single definitive test and you must look at all the facts for the particular case.

Where an individual is deemed to be an employee, the company will need to calculate a deemed direct payment which will be subject to PAYE and NICs. The amount of the deemed direct payment will be the amount paid to the intermediary, less and direct costs. Umber Printing is then responsible for deducting and accounting for PAYE/NIC and will need to provide the worker with a form P60 each year.

1) Small World Ltd

There are a number of key factors that can be looked at the determine whether or not the arrangement with Small World Ltd would be deemed to be inside the "off-payroll working" legislation:

1) Mutuality of obligation - is the employer required to provide work and is the worker obliged to accept it?

Umber Printing is providing work for Scott to do over a 12 month period. There is no guarantee of future work beyond that point and if there was, Scott would not be obliged to accept it. This points to him being self-employed

2) Substitution/personal service - employees must provide ehteir services personally but self-employed people are genereally able to provide a suitably qualified substitute.

Umder Printing is not allowing Scott to send a substitute in his place to undertake and of the work, this points to Scott being an employee

3) Control - the greater the degree of control exercised over the day to day work of the consultant, the closer this is to employment. Implementation of how, when and where objectives are achieved should be up to the consultant.

Scott will be working udner the control and supervision of Joyce. He does not appear to have much control in this case which points to him being and employee.

4) Own equipment - self-employed individuals will usually provide their won equipment.

Scott will be providing his own laptop and other computer equipment and this therefore points to self-employment

5) Number of engagements - self-employed workers are at liberty to undertake other contracts with third parties.

Scott will only work with Umber Printing 20 hours a week and spends the rest of his week working on a number of other clients. This points to him being self-employed.

There are a number of other factors including financial risk and opportunity for profit, intergration into the organisation and business operations. On balance, it appears as though Scott would be deemed to be self-employed through his personal service company.

This means that he can continue to invoice Umber Printing Limited and receive the money into his limited company. He can then extract the profits via salary and dividends. He will pay national insurance on any salary he takes out over the lower earnings limit, but no national insurane on the dividends. He will pay income tax on salary and dividends over his personal allowance.

Because the turnover of Umber Printing is more than £10.2 million and the balance sheet assets are more than £5.1million, Umber Printing is not deeemd to be a small company and therefore Umber Printing is responsible for determining if the services provided by Small World Ltd are such that he would be regarded as an employee if he were not undertaking the work through an intermediary.

Umber Printing must issue a status determination statement to Scott, setting out their asessment of his status and the reasons for it.
Primary responsibility to operate PAYE rests with the employer. Failure to do so where it would have been appropriate can result in sanctions and penalties being applies.

Cliff Edwards

Cliff's role as a non-executive director of the company is a employee role and therefore his salary of £12,000 per annum will be subject to PAYE and national insurance via the company payroll.

Non-executive directors can also provide consultancy services as self-employed, but as with Scott above, whether or not these particular services will fall within the scope of the off-payroll working legislation is a matter of looking at the facts.

It is not clear what level of control he will be under and whether this is one of many engagements he undetakes as a consultant, so more facts would be needed in this case to make a proper determination.

As Cliff is not looking to work through an intermediary limited company, he will pay income tax as well as class 2 and class 4 national insurance contributions on his income from the company if he is deemed to be self-employed rather than an employee whilst supplying these services.