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

Answer-to-Question-_1_

Capital allowances on the new factory

	Super deduction	AIA /FYA	Plant pool	Special rate pool	SBAs	Capital allowances
TWDV b/f			109,278	23,000		
New factory (N1)	40,500	9,800		55,000	685,500	
Steel rolling machine (N2)	120,000					
Disposal of rolling machine (N3)			(80,000)			
Deposit for spring machine (N4)	35,000					
Total	195,500	9,800	29,278	78,000	685,500	
195,500 x 130%	(195,500)					254,150
9,800 x 100%		(9,800)				9,800
29,278 x 18%			(5,270)			5,270
78,000 x 6%				(4,680)		4,680
685,500 x 3% x (5/12)					(8,569)	8,569
Total capital allowances						282,469

claimed						

Notes

N1 - New factory

Structures and buildings allowance is available in respect of qualifying structural spend incurred after 29 October 2018, qualifying structural spend excludes the cost of land and legal fees for the acquisition of the land as well as stamp duty.

Items which would qualify for other capital allowances such as integral features are also not included in the SBA claim.

The planning cost of £30,000, the structural spend of £650,000, decoration of offices (£3,000) and suspended ceiling (£2,500) all qualify for SBAs

30,000 + 650,000 + 2,500 + 3,000 = 685,500

SBAs are claimed from the date that the asset is brought into use, i.e. 31 October 2021.

The factory sign (£5,000), other main pool expenditure (£25,000), kitchen installation (£5,500), office furniture (£3,000) and the carpet tiles (£2,000) will all qualify for plant pool allowances at 18%, as the spend is incurred between 1 April 2021 and 31 March 2023, the spend qualifies for the capital allowances super deduction at 130%.

The sign qualifies as it advertises the busines and the carpet tiles qualify as they are removable and not fixed to the building.

£40,500 qualifies for plant pool (5,000 + 25,000 + 5,500 3,000 + 2,000)

The heating system (£55,000) is an integral feature as it incorporated into the building and is a hot water system, this qualifies for special rate pool allowances at 6% per annum, as the spend is incurred in the period 1 April 2021 to 31 March 2023, the spend qualifies for the enhanced 50% first year allowance for special rate pool spend.

The electric vehicle charge points of £4,800 qualify for 100% first year allowances.

Further, the costs to remove and reinstall plant and machinery are eligible for plant pool allowances as they would be deductible if they were expensed to the P&L, as the assets are not new, they are not eligible for the super deduction, AIA is claimed - £5,000 (£3,000 + £2,000)

N2 - New steel rolling machine

Capital allowances are available on the cost incurred by the company in respect of qualifying assets.

As the company has received a grant, the qualifying spend is reduced by the grant.

£160,000 - £40,000 = £120,000 eligible for capital allowances.

As this is a new machine acquired between 1 April 2021 to 31 March 2023, it is eligible for the capital allowances super deduction.

N3 - Old steel rolling machine

Normally plant and machinery is not a capital asset for capital gains tax purposes.

The exception to this is where capital allowances are claimed in respect of the asset and the asset is sold for more than the original cost.

For capital allowance purposes, the disposal proceeds allocated to the general pool are restricted to the original cost (i.e. £80,000).

A capital gain of £20,000 (£100,000 - £80,000) arises on the disposal and will be liable to corporation tax at 19%.

This will be due for payment on 1 January 2023.

N4 - Spring forming machine

The normal rule for capital allowances is that expenditure is incurred on the date that the obligation to pay becomes unconditional, this is usually taken as the delivery date.

The asset has not been delivered by the year end.

There is a separate rule which allows capital allowances to be claimed where expenditure is incurred under a contract, which on performance, the company will or may become the owner of the asset, as this is such a contract, capital allowances can be claimed on the £35,000 in the current period, the balance of the spend will be eligible for capital allowances in the period to 31 March 2023.

<u>Chargeable gain or loss arising on disposal of the factory</u>

		£	
Proceeds 920,000		920,000	
Less legal fees to sell	(3,000)		
Base cost	(835,000)		
Enhancement expenditure	(150,000)		
Legal costs to acquire	(2,500)	(990,500)	
Capital loss		(70,502)	

The cost of fixtures integrated into the building is included in the base cost of the asset on disposal as are any proceeds allocated to the fixtures.

Any assets which are not "fixed to the building" are not included in the base cost, but it seems that all of these assets are fixed to the building and therefore form part of the building for capital gains tax purposes.

The company would also likely be able to claim indexation allowance up to 31 December 2017.

The capital loss of £70,502 can be partially offset against the capital gain on the steel rolling machine of £20,000, this leaves a capital loss of £70,502 to carry forward.

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

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

Answer-to-Question-_2_

		£	
Net profit		135,000	
Deposit (N1)	(3,500)		
Goods taken for own use (N2)	2,500		
Premises costs (N3)	22,267		
Hire purchase and private use of car (N4)	6,000		
Professional fees (N5)	2,000		
Bad and doubtful debts (N6)	10,200		
Less capital allowances (N7)	(32,160)		
Depreciation (N8)	14,000	21,305	
		156,305	

Notes

N1 - Turnover

Esther is not eligible to use the cash basis for tax purposes as her turnover exceeds £200,000 (£150,000 x 16/12), she is therefore using the accruals basis.

Under the accruals basis, income can only be taxed when it is earned.

She has not yet made the dress or sold it, therefore she has not "earned" the income and the deposit should not yet be taxed.

Deduct £3,500

N2 - Cost of sales

Goods taken for own use by the proprietor of a business are taxed at the market value of the goods rather than the cost to the business.

£175 + £200 = £375

£375/15% = £2,500 market value of goods taken

N3 - Premises cost

The amount liable to income tax as property income for the lessor is available to the lessee as a deduction in calculating the trading profit.

£25,000 x ((10-1) x 2%) = £4,500 capital element

£25,000 - £4,500 = £20,500 property income

£20,500/10 = £2,050 annual property income

£2,050 x (16/12) = £2,733 deductible in period to 30 April 2022

£25,000 - £2,733 = £22,267 addback

N4 - Motor and travel expenses

Esther can choose whether to claim capital allowances on her car (as it is under hire purchase) or she can claim HMRC approved mileage rates, we do not have details of her business mileage so capital allowances will be claimed.

Based on emissions over 50g/km, the car is a high emission car and is eligible for special rate pool allowances, as there is

private use, the car is allocated to a separate pool.

Addback hire purchase payments as they are capital in nature and relief is obtained via capital allowances- £5,400

Car running expenses, as there is 25% non business use, this need to be disallowed - £2,400 x 25% = £600

Van expenses are deductible.

N5 - Professional fees

The professional fees of negotiating/arranging a new lease are capital in nature as they provide an enduring benefit to the trade.

Addback £2,000

N6 - Bad and doubtful debts

The loan to a friend is not wholly and exclusively for the purposes of the trade and is therefore not tax deductible - addback £4,500

The loan to an employee is tax deductible and is treated like earnings for the employee.

The provision against a specific customer, assuming there is a good reason for it is tax deductible as a specific provision.

The general provision against 5% of all other customer debt is not allowable as there has to be a present obligation as a result of a past event and it has to be probable that there will be economic outflow to settle the obligation and the outflow has to be reliably measured for there to be an allowable provision.

The outflow is not reliably measured, this is not deductible - addback £5,700.

N7 - Capital allowances

	AIA/FYA	Plant pool	Special rate pool	Esther's car	Capital allowances	
Pre trading	26,000	4,000				

expenditure (A)						
Electric van (B)						
Computer software	2,500					
Esther's car (D)				45,000		
Total	28,500	4,000	-	45,000		
28,500 x 100%	(28,500)				28,500	
4,000 x 18% x (16/12)		(960)			960	
45,000 x 6% x (16/12) x (75%)				(3,600)	2,700	
Total capital allowances					32,160	

Notes

A - Pre trading expenditure is treated as incurred on the first day of the trade i.e. on 1 January 2021. The equipment costs qualify for AIA but the sewing machines do not as they were acquired from a connected party.

B - Electric van

There is no private use apportionment for a van. Electric vans qualify for 100% first year allowances

C - Computer design software

This is plant and machinery spend and eligible for AIA

D - Esther's car

As the car is acquired under hire purchase and is in use at the year end, the full spend is eligible for capital allowances.

AIA cannot be claimed on a car, the car is a high emission car based on CO_2 emissions of 125g/km exceeding the limit of 50g/km and is eligible for special rate pool allowances

N8 - Depreciation is an accounting movement to do with a capital asset and is not tax deductible.

Assessable profit for 2020/21 and 2021/22

Tax year	Basis period		Assessable profit
2020/21	1 January 2021 - 5 April 2021	156,305 x (3/16)	29,307
2021/22	6 April 2021 - 5 April 2022	156,305 x (12/16)	117,229
2022/23	12 months to 30 April 2022	156,305 x (12/16)	117,229

Taxable income for 2020/21 and 2021/22

	2020/21	2021/22	
Assessable profit	29,307	117,229	
Salary (£12,000 x 9)	108,000		
Taxable income	137,307	117,229	

<u>Esthers liability to national insurance contributions on self employment income for 2020/21</u>

For 2020/21, Esther is both employed and self employed.

Employed individuals are required to pay class 1 employees national insurance (12%/2%) on their earnings and self employed individuals pay class 2 (£3.05 per week) and class 4 national

insuranace (9%/2%).

To prevent individuals who are both employed and self employed from paying too much national insurance, there is an annual maxima test, which works out the maximum national insurance they should pay, Esther should do this and may get a rebate of national insurance if too much is paid.

Contributions for 2021/22

		£	
Profits		117,229	
Class 2 (£3.05 x 53)	162		
Class 4			
(50,270 -9,568) x 9%	3,663		
117,229 - 50,270 x 2%	1,339		
Total class 2 and class 4 national insurance	5,164		

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

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

Answer-to-Question-_3_

As the company has fewer than 500 employees, turnover of less than 100m euros and net assets of less than 86m euros, the company is eligible for the small company enhanced R&D regime.

The small company R&D regime gives tax relief at 230% on qualifying costs.

As both projects have been confirmed to be to resolve an area of scientific or technological uncertainty and as HMRC have confirmed that they are eligible for R&D relief, the qualifying costs can obtain relief.

		P&L	130% enhancement	Total
Taxable profit before relief	225,000			
Staff costs		194,400	252,720	
Software		10,000	13,000	
Utilities		3,500	4,550	
Subcontractor - connected		40,000	52,000	
Unconnected subcontractor		16,250	21,125	
		264,150	343,395	607,545
Less 130% enhancement	(343,395)			
Tax adjusted loss	(118,395)			

<u>Tax relief for the losses</u>

Tax releif can either be given via a carryback of the losses against the prior year taxable profit of £735,000, this would give a corporation tax repayment of £22,495 (£118,395 x 19%).

Alternatively, the loss can be carried forward or surrendered for a payable credit of 14.5%.

For the payable credit, the surrenderable loss is the lower of the:

1. Qualifying R&D expenditure at 230% - £607,545

2. The unrelieved trade loss after any actual or potential current year loss relief claims or any actual carryback claims - £118,395 (if no carryback)

The payable credit would therefore be £0 as the loss carryback leaves the company with no unrelieved trade loss.

In any case a carryback would give relief at 19% rather than 14.5%.

The R&D claim must be made by 31 December 2023.

Staff costs

Staff costs are eligible for relief to the extent that their time is directly related to the R&D work.

The qualifying staff costs include salary and employers national insurance and pensions but exclude benefits in kind.

	Salary + employers NIC + pension	Percentage qualifying	Qualifying R&D cost
Fred McMurray (N1)	132,000	45%	59,400
Ruth Thompson	56,000	90%	50,400
Ken Anderson	44,000	90%	39,600
Mary Jones	25,000	90%	22,500
Tim Conway	25,000	90%	22,500
Total qualifying staff costs			194,400

Notes

N1 - Fred McMurray

The 40% of Fred's time spent meeting customers and viewing technology in operation is not directly related to resolving the scientific or technological uncertainty/ significant advancement and is therefore not qualifying.

The 15% discussing financing is also not directly related.

100% - 40% - 15% = 45% qualifying time

N2 - Admin time and training

As the training on VR software is directly related to the R&D project as it is to use the software which they are using in the project, this time qualifies, the admin time does not qualify.

90% qualifying time

I have assumed that Tim will be testing the product in the development phase and not in the production phase as this would not qualify for R&D relief

Software

The development and modelling software will qualify for R&D allowances and the payroll software will not as it is not directly related to the R&D project.

£10,000 qualifies

Property and other costs

The rent and rates and telephone costs do not qualify as they are not "consumed or transformed" in the course of R&D.

The heat, light and power costs will qualify as they are utility costs which are consumed in the R&D process.

£3,500 qualifies

Subcontractor costs

The subcontractor wholly owned by James Sullivan's son is a connected party.

Only 65% of subcontracted costs are eligible for R&D enhanced relief i.e. £32,500 (£50,000 x 65%).

It is possible and recommended that a joint claim is made with the subcontractor to treat the actual costs incurred as eligible for R&D, the claim needs to be made by 31 December 2023 and the costs of £40,000 would then qualify for R&D.

£40,000 qualifies.

The unconnected subcontractor, as the costs are not known , only 65% of the costs can be claimed i.e £16,250 (£25,000 x 65%)

£16,250 qualifies.

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

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

Answer-to-Question-_4_

30% discount for sales staff

The discount for staff is a taxable benefit, the value of the benefit is the cost to the business (i.e. the cost of the goods which are being acquired as opposed to the retail price).

As the benefit is widely offered to the sales staff and the amounts are small and irregular, the benfits could be included in a PAYE settlement agreement.

This would need to entered into before the due date for the P11Ds following the tax year.

Once a PSA is entered into, it does not need ot be renewed.

The amounts settled under a PSA are subject to class 1B national insurance, which is calculated based on the benefit grossed up for the income tax paid in respect of same.

No P11D is required where benefits are dealt with under a PSA.

Two week holiday

The provision of a holiday is a taxable benefit for the employee, the value of the benefit is the cost to the employer.

As the LLP does not own the property and as the senior partner did not charge the LLP for the use of the property, the cost will just be the contribution from the partnership for the bills for the two weeks it was used by the employee.

Sally Moss

Long service awards valued at up to £50 per year where the employee has served for 20 years or more are exempt benefits.

Sally has been employed for 15 years, none of the cost of the holiday is therefore covered by the long service award exemption.

As the holiday has been arranged by the employee, paid by the employee and reimbursed by the employer, it is treated as additional employment income and is liable to income tax and class 1 employees and employers national insurance.

If they wish to settle the tax for her, the LLP will have to enter into a PAYE settlement agreement ("PSA), which can be entered into before the due date for the P11Ds following the tax year.

The PSA can be entered into where there are minor irregular benefits on which it would be impractical to operate PAYE.

Once a PSA is entered into, it does not need ot be renewed.

The amounts settled under a PSA are subject to class 1B national insurance, which is calculated based on the benefit grossed up for the income tax paid in respect of same.

The P11D(b) and the tax due under the PSA need to be filed and paid by 19 October if filing on paper/not paying electronically and by 22 October if filing and paying electronically.

No P11D is required where benefits are dealt with under a PSA.

Colin Dean

A company van, if it has private use will be a taxable benefit of £3,500 and if fuel is provided, there will be a further benefit of £669 the van benefit and fuel benefit is liable to income tax and class 1A national insurance and must be reported on form P11D.

The vehicle allowance will cease when it was given up and a pro rata amount based on the period that he had the allowance should be included in the P11D.

Chloe knight

The roof rack, as it costs less than £100 and was added after the car was originally provided, is ignored.

The cost of the car for the purposes of the car benefit, is increased by the cost of the alloy wheels as they have been added after the car has been provided and they cost more than £100.

The contribution paid by Chloe, will be deducted from her taxable benefit from October, a total of £300 (£50 x 6 months) should be

deducted from the taxable benefit amount.

The car benefit is liable to income tax and class 1A national insurance and needs to be included on form P11D.

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

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

Answer-to-Question-_5_

Gift to daughter

For capital gains tax purposes, where there is a disposal of a capital asset, such as shares for below market value between connected persons, the deemed proceeds for the transfer are market value.

Aaron and his daughter are connected (connected persons includes husband, wife, children, ascendants, brothers and sisters and your spouses relatives) and therefore the disposal has deemed proceeds of market value.

The deemed proceeds are £300,000 (£15,000 x 20 shares) and the capital gain is £299,980 (£300,000 - £20).

As discussed below, Aaron's disposal of shares will qualify for BADR which will allow the gain to be taxed at 10% subject to his lifetime allowance of £1m (he has not made any other disposals), this is as compared to the normal rate of capital gains tax which applies to a disposal of shares, which is 20% for higher rate taxpayers.

BADR must be claimed by the anniversary of 31 January following the tax year of the gift.

Gift relief

An alternative is to claim gift relief as it is a disposal of business assets, a proportion of the capital gain could be deferred, this would be restricted by the the proportion of chargeable business assets to chargeable assets in the company so that some of the gain would be left immediately chargeable.

The investment property, as a chargeable assets, which is not a business asset would result in a partial restriction of gift relief.

The gain left chargeable would be eligible for BADR.

The gift relief claim is a joint claim which must be made within

4 years of the end of the tax year of the gift.

A gift relief claim would reduce the base cost of the shares in the hands of Crystal so that she would have a larger capital gain on a future disposal of the shares.

This is not advisable as Crystal does not work for the company and is therefore not likely to be eligible for BADR on a future disposal unless she takes a job with the company.

Income tax

There are no income tax implications of the gift for the daughter as she is not an employee of the company.

Gift to step son

The gift to the step son is a gift between connected persons and therefore takes place at market value.

The deemed proceeds are £150,000 (£1,500 x 10 shares) and the capital gain is £149,990 (£150,000 - £10).

BADR

The gain would be eligible for BADR and therefore could be taxed at 10% in the same way as the gift to Crystal.

Gift relief

Gift relief could again be jointly claimed by Aaron and Edward.

The gain deferred would be restricted as Edward has paid an undervalue sum for the shares, this is termed the excess proceeds.

The excess proceeds are £74,990 (£75,000 - £10) and they cannot be gift relieved and are immediately taxable.

The chargeable business assets/chargeable assets calculation will further restrict the amount eligible for gift relief.

BADR can be claimed on the amounts not eligible for gift relief.

The gift relief claimed will reduce the base cost (increasing the future capital gain on the sale of the shares) of Edwards shares, but as Edward works for the company he is likely to be able to claim BADR on a disposal of his shares.

Income tax

Whilst Edward is an employee, the gift to him is not in connection with his employment as he is Aaron's step son, the gift is as a result of a familial relationship.

Gift to Francois Gerald

The same applies to this gift, a capital gain of £149,990 arises, the same as it does for the gift to Edward.

The capital gain is eliglible for BADR and gift relief, there are no excess proceeds so the only restriction on the gift relief claim is the proportion worked out under chargeable business assets/chargeable assets.

If Francois becomes non-UK tax resident in the 6 years after the gift, the gain deferred under gift relief will become chargeable, if he doesn't pay the CGT within one year, Aaron could be pursused for the CGT.

Income tax

As Francois Gerald is an employee, the gift is in connection with his employment and he will be liable to income tax on the difference between the market value of the shares (£150,000) and the price paid (£nil).

He will have an income tax charge at 20%/40%/45% on same.

Business Asset Disposal Relief ("BADR")

BADR applies where an individual disposes of shares in a company and meets the conditions below:

1. They hold at least 5% of the shares

2. They work in the company

3. The company is a trading company

4. The above conditions have been met for the two years prior to the disposal.

Aaron holds 100% of the shares, works in the company and has done

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so from incorporation, conditions 1,2 and 4 are therefore met.

Trading company

The final condition, condition 3, the trading condition is that the company is not, to a substantial extent carrying on non-trade activities, substantial is considered to be more than 20% by reference to:

1. Turnover

2. Net assets

3. Management time

Based on the information, the company earns £15,000 from the investment property, compared with the company's turnover of £1.35m, this is 1.1% of the turnover and therefore the first test is not met.

The investment property represents 20.7% (£155,000/£750,000) of the net assets of the company. The company meets the net asset test.

The final condition is that 20% of managment time is spend on managing the property, given the level of income and the fact that it is let annually, it seems very unlikely that 20% of management time would be spent on managing this investment.

On balance of facts, whilst the balance sheet test appears to be met, the turnover and management time test are clearly not met and the company is clearly not, to a substantial extent, carrying on non-trade activities.

The gift of shares will therefore qualify for BADR.

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

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

Answer-to-Question-_6_

	Raqeeb	Roman	Mason	Philip	Total	
	£	£	£	£	£	
Loss					(410,000)	
Interest on capital (400,000 x 10%)	40,000					
Annual salaries		50,000	5,000	50,000		
Profit share		(164,000)	(82,000)	(164,000)		
Total	40,000	(114,000)	(77,00)	(114,000)		
Reallocation of notional profit	(40,000)	16,000	8,000	16,000		
Total losses	-	98,000	69,000	98,000		

As the partnership has a loss overall (£410,000) and Raqeeb is left with a notional profit, there is reallocation of losses from the other partners in the same proportion as their profit share and this extinguishes Raqeeb's notional profit.

<u>Options for tax loss relief</u>

For partners in a partnership, loss relief can be claimed in the following ways:

Set against total profits in the current year

This is a s64 current year claim, it is an all or nothing claim and the trade losses set against total income are restricted to the higher of £50,000 and 25% of adjusted total income.

The claim needs to be made by 31 January 2024.

Set against total profits in the prior year

This is also a s64 claim and again, is all or nothing.

The claim can be done independently of a current year claim and again is subject to the higher of £50,000 or 25% of adjusted total income test.

The claim needs to be made by 31 January 2024.

Extended loss carryback

This is available where losses arise in a period ending between 1 April 2020 to 31 March 2022 and allows up to £2m of losses to be carried back up to 3 years, as the losses accrued in the period to 31 March 2022, this is an option.

The losses are offset on a LIFO basis and are subject to the £50,000/25% of adjusted total income test.

The claim needs to be made by 31 January 2024.

Early years loss relief

As Philip has just joined the partnership, he is treated as commencing to trade and losses accruing to him in the first four years of trade will be able to be carried back up to 3 years against his total income, subject to the £50k/25% of adjusted total income test.

The losses are offset on a FIFO basis.

The claim needs to be made by 31 January 2024.

Loss carry forward

The losses could be carried forward to set against profits in future tax years, notably 31 March 2023 (2022/23) profits.

Loss carryforward is not automatic and a claim needs to be made

by 31 January 2024.

Raqeeb

Raqeeb has not made a loss, however, as the partnership has been trading for more than 4 years and he has been a partner for more than 4 years and as he does not work in the partnership, he is a non active partner and his sideways loss relief from the partnership would be restricted to £25,000 per tax year.

Roman

Has no other income other than the partnership income, he could make a loss carryback claim, as this is all or nothing it would fully relieve Roman's partnership profits in the period to 31 March 2021 but the personal allowance would be wasted.

The balance of £28,000 could then be carried back via an extended loss carryback claim.

Under this option, tax would be saved at 20%/40% and the personal allowance in 2020/21 would be wasted.

If they are certain of the profits in 31 March 2023, the loss should be carried foward as it would save tax at 45% in that tax year and no personal allowance would be wasted.

Mason

Mason could make a current year claim, this would be restricted to £50,000 of his non-partnership income and £10,000 would then be allocated against his partnership income. The personal allowance would not be wasted (it would be used by his remaining non-partnership income) and he would save tax at 20%/40%.

The balance could then be carried back the year ended 31 March 2020, against his total income and tax would be saved at 40%.

Alternatively, the loss could be carried forward to 31 March 2023, where £50,000 would be set against his non-partnership income and the balance could be set against his partnership income, this would allow some of his personal allowance to be restored as he would have suffered abatement of his personal allowance in 2022/23 given his combined partnership and non-partnership income of £184,000.

Mason should carry his loss forward.

Philip

Philip could carry some losses back under a s72 claim against his capital gain, but this would save tax at 20% rather than 20%/40%/45% for income tax.

This is not recommended.

As Philip is in the early years of trade, he can do an early years loss carryback and set £50k against his income in each of the tax years 2018/19, 2019/20 and 2020/21, this would allow him to get a repayment sooner and would allow him to recover his personal allowance which will have been abated in each of those tax years, given his income of £120k.

The recovery of the personal allowance would mean that Philip would save tax at an effective rate of 60% with this claim.

This is what he should do.