



The Chartered Tax Adviser Examination

November 2019

Taxation of Owner-Managed Businesses

Advanced Technical Paper

Suggested solutions

QUESTION 1

MEMO

To: Angela Barton

From: A Tax Manager

Re: Re-Furb Ltd

Corporation tax / company liquidation

Re-Furb Ltd's normal corporation tax accounting period ended on 30 June 2019. It would then have an accounting period of five months from 1 July 2019 until the trade ceases on 30 November 2019.

A further accounting period will commence on 1 December and end on 6 January 2020 immediately before the appointment of a liquidator on 7 January 2020. The next accounting period begins on that date and ends on the earlier of completion of the liquidation or 12 months after the start of the accounting period.

For the year ended 30 June 2019, a trading loss arises as follows:

	£
Tax-adjusted trading loss before capital allowances	(250,000)
Capital allowances as below	<u>(45,000)</u>
Trading loss	<u>(295,000)</u>

Capital allowances:

Main pool written down value brought forward	250,000
Writing-down allowance at 18%	<u>(45,000)</u>
Written down value carried forward	<u>205,000</u>

The loss for the final period is calculated below. Payments made in order to close a business are not normally allowable (*CIR v Anglo Brewing Co UK Ltd* KB 1925, TC 12 803) but statutory redundancy is allowable under ss.76-77 CTA 2009 and if paid after cessation is treated as paid on the date of cessation. The write-off in respect of trade debts is allowable as a trading loan relationship debit. The liquidator's fees of £20,000 however are not an expense of the trade and no deduction is available.

The balance on the company's capital allowances pool at 30 September 2019 is £205,000. Under s.61(1) CAA 2001 a disposal value is required to be brought into account in various circumstances including the permanent discontinuance of the 'qualifying activity' (s.61(1)(f)). The disposal value will be the sale proceeds and as the anticipated sale proceeds are about £100,000, this will give rise to a balancing allowance based upon the actual sale proceeds.

Re-Furb Ltd's corporation tax computation for the period to 30 November 2019 is estimated as follows:

CTAP 01.07.2019 – 30.11.2019	£
Adjusted trading profit/(loss)	0
Statutory redundancy	(35,000)
Impairment adjustment re trade debts	(45,000)
Capital allowances balancing allowance	<u>(104,999)</u>
Adjusted trading loss	(184,999)
Chargeable gain	<u>300,000</u>
Corporation tax profit	<u>115,001</u>
Capital allowances:	
Main pool – written down value brought forward	205,000
Sale of fixtures	(1)
Estimated sale proceeds of plant and equipment	<u>(100,000)</u>
Balancing allowance	<u>104,999</u>

The loss for the year ended 30 June 2019 may first be carried back against the trading profit for the year ended 30 June 2018. The balance may be carried forward to the period to 30 November 2019 and may be offset against total profits under s.45A CTA 2010.

It would be preferable for the flat which Mr Banks wishes to retain to be purchased by him from the company prior to 30 November 2019 so that the gain may be relieved against the trading loss brought forward under s.45A. Any unused trading loss cannot be carried forward after cessation of the trade. Alternatively, the property could be distributed in specie by the liquidator but in that case the gain would be liable to corporation tax. I would suggest therefore that Mr Banks arrange temporary finance in order to purchase the property, which can be repaid out of cash distributions received during winding-up.

The corporation tax of £32,500 paid under s.455 CTA 2010 in respect of Mr Cotton's existing loan is repayable nine months after the end of the accounting period in which the debt is repaid. The liquidator would not be able to make a final distribution and complete the liquidation until then. It would be preferable therefore for Mr Cotton to repay the loan by 30 November 2019 so that the tax will be repayable on 1 September 2020. I would suggest therefore that Mr Cotton should also arrange temporary finance for this purpose, to be repaid out of cash distributions received during liquidation.

It would appear that no corporation tax profit arises for the period from 1 December 2019 to 6 January 2020.

The company's adjusted losses to cessation and their suggested optimum utilisation are as follows:

	£
<i>12 months to 30 June 2019</i>	Profit/(loss)
Trading loss as above	(295,000)
Carry-back to a.p. ended 30/6/2018 s.37(3)(b) CTA 2010	50,000
Carry forward	<u>(245,000)</u>
 <i>5 months to 30 November 2019</i>	
Corporation tax profit as above	115,001
Chargeable gain re flat	<u>100,000</u>
	215,001
Trading loss brought forward	<u>(245,000)</u>
Loss not utilised	<u><u>(29,999)</u></u>

MARKING GUIDE

TOPIC	MARKS
Identifying CT accounting periods	2.0
Adjusted loss to 30 June 2019 + CAs	1.0
Provisions for closure costs & whether allowable	2.0
Liquidators fees	0.5
Treatment of balance on CAs pool re s.61	2.0
Carry back of loss to 30/6/2018	0.5
Availability to carry forward against total profits s.45A	1.0
Apportionment of profits	0.5
Suggested sale of bungalow prior to cessation of trade v distribution in specie	1.5
Recovery of s.455 tax and suggestion to repay loan	1.5
Period 1/12/2019 – 6/1/2020	0.5
Optimum use of losses	2.0
TOTAL	15.0

QUESTION 2

To: Bella Cottrell
From: Examiner
Date: 6 November 2019
Subject: Tax advice re Hyperion Construction Limited

Dear Bella

Please find below my thoughts on the various issues we have discussed.

1) **Gift of shares**

Income Tax

Frank is being gifted shares in the company. As these are given to induce Frank to become an employee of the company, tax legislation and case law treats this as being in relation to his employment and there will therefore be a receipt of "money's worth" for the purposes of calculating Frank's employment income. This will therefore be taxable as earnings in the tax year that the shares are received – 2019/20.

As Frank's shares are worth £15 each on acquisition, he has therefore acquired shares with a value of £4,500, which will be the amount of his taxable income. However, PAYE and NIC will only apply if the shares are treated as Readily Convertible Assets ("RCAs") for tax purposes. For the shares to be RCAs, there would need to be a market, or arrangements in place, for their sale. As the company is a private company and is not in the process of a sale, the shares should not be treated as RCAs. As a result, PAYE and NIC (for either employee or employer) should not apply. The £4,500 will be reported on the online annual return for 2019/20 and the income will be included on Frank's own tax return.

Corporation Tax

Although the shares are gifted from your own holding, the company should be able to obtain a corporation tax deduction for the £4,500 which is charged to income tax. This should be included in the corporation tax computation covering the date of transfer of the shares.

Inheritance Tax ("IHT")

The transfer of the shares is a potentially exempt transfer which would only need to be considered if you were to die within 7 years of the date of the gift. However, it is likely that the transfer would be covered by Business Property Relief. If it were to be chargeable, the reduction in value of your estate is measured as the difference in the value of your shares before and after the transfer. Prior to the transfer, your 100% holding was worth £50,000. Following the transfer, your 70% holding was only worth £29,400 – a reduction in your estate of £20,600. The value of the shares received by Frank is not relevant for IHT purposes.

2) **Employer obligations**

As the company has now become an employer in need of a PAYE scheme, the company must register with HMRC as an employer to access the PAYE online service. It will be issued with a unique PAYE reference number for use in its employment tax dealings with HMRC.

The company will need to report the date on which the new employees start, along with their address and passport number (if known) on the submission to HMRC when the employee is first paid.

The company will also need to report a “starter declaration” for each employee and determine the tax code which should apply to each. If the employee has a P45 from a previous job in tax year 2019/20, this can be used to complete the starter declaration, and the tax code from the P45 should be used.

If the employee does not have a P45, or it is from an earlier tax year, the employee will need to be asked to make a “starter declaration” about their income in the year to date, to determine the tax code to be operated initially.

Payroll information must be submitted to HMRC when or before payments are made to employees. The submission is made electronically using a Full Payment Submission (“FPS”). This is generated by your payroll software and contains details of the pay and tax of the employees. If you do not pay your employees in a month, an Employer Payment Summary (“EPS”) must be submitted within 14 days of the end of the month.

Whilst PAYE and NIC is applied at the time payment is made, it must be paid to HMRC on a monthly basis, by the 22nd of each month (or the 19th if not paid electronically).

At the end of the tax year, each employee will need to be given a P60 showing the total pay and tax details for the year. This must be given to the employee by 31 May following the end of the tax year.

The private medical insurance must be notified to HMRC on a P11D by 6 July after the end of the tax year. The value of the benefit in kind will be the £500 cost to the company, per employee. A copy must go to the employee by the same date. Class 1A NIC payable on the benefits in kind must be paid by 22nd July (or the 19th if not paid electronically).

3) **Purchase of assets**

Hire purchase

The assets are treated as acquired for capital allowances purposes, and allowances will be available on the full cost of the assets. The annual investment allowance of £200,000 should be available to provide 100% relief in the accounting year of acquisition.

Any finance interest charged will be expensed to the profit and loss account and should be tax deductible when it is included in the accounts.

Finance lease

In contrast, assets acquired under finance lease are not treated as acquired by the company for capital allowances purposes – although they are shown on the balance sheet as assets. As a result, no capital allowances will be available. However, the depreciation of the assets charged to the accounts will be deductible for tax purposes – the only time this is the case.

As above, interest charged to the profit and loss account should be tax deductible.

Recommendation

The HP option will allow immediate tax relief for the expenditure, using the AIA, as opposed to the finance lease, which will take a number of years to unwind. It is generally best to obtain tax relief at the earliest opportunity.

If you have any queries, please let me know.

Kind regards

MARKING GUIDE

TOPIC	MARKS
Part 1 – Gift of shares	
<i>Income tax</i>	
Earnings charge	1½
Valuation	½
RCAs	1½
P11D and inclusion on tax return	1
<i>Corporation tax</i>	
CT deduction	1
<i>Inheritance tax</i>	
Transfer PET, BPR	1
Reduction in estate calculation	1½
SUB TOTAL	8
Part 2 – Employer obligations	
Registration with HMRC	½
New starter obligations	2
Monthly payroll submissions	2
Payment date	½
P60 obligations	1
P11D obligations	2
SUB TOTAL	8
Part 3 – Purchase of assets	
Hire purchase	1½
Finance lease	2
Recommendation	½
SUB TOTAL	4
TOTAL	20

QUESTION 3

- 1) There are five capital disposals made by Donald in 2018/19 – two warehouses, the customer list and the two pieces of plant.

Entrepreneurs' Relief ("ER") may be available to reduce the rate of CGT to 10%. For ER to be available, as a sole trader, the disposal would need to constitute a "material disposal of business assets". This is where the trader disposes of the whole or part of their business or disposes of business assets within the three years after cessation, provided the trade has been owned for at least one year prior to disposal or cessation of trade, as detailed below. There is no entitlement to ER simply because business assets are sold.

Warehouse 1

This was sold on 30 April 2018 at a gain on £135,000. This will be charged to Capital Gains Tax as a disposal in 2018/19.

As Donald was continuing to trade when the warehouse was sold, ER would only be available on this disposal if it were "part of a business", as outlined above. For this to be the case, the part which has been sold must be capable of being operated as a business in its own right, if desired. Whilst the premises have been sold along with some stock, and the premises are not subsequently replaced by Donald, it is unlikely that HMRC will accept this as part of the sale of a "business" as opposed to the "scaling down" of the current trade. They are likely to contend that the purchase of a warehouse and some stock is not in itself a "business", nor could it be operated as one. This is despite the fact that the purchaser is using the assets as part of their own business. They would also point to the fact that Donald's trade continued largely unchanged until 30 September 2018.

On this basis, ER is unlikely to be available and the gain will be taxed at 20%, as Donald is a higher-rate taxpayer.

Customer list and plant

These assets are sold as part of the cessation of the business and there is therefore clear evidence of the sale of the whole of the remaining business at this point. ER should therefore apply to any gains made on the disposal of the assets at the date of cessation.

The sale of the customer list will give rise to a gain of £300,000. This is a capital disposal, as Donald is a sole-trader and therefore goodwill is always a capital asset.

No gain arises on the disposal of the plant and stock is not a chargeable asset for CGT purposes.

Warehouse 2

The warehouse is sold after the cessation of the business. There are two key criteria for ER to be available on the disposal of assets used in the business after cessation – the asset must have been used in the business operated by the sole trader for one year prior to cessation, and the asset must have been sold within three years of cessation. ER should therefore be available on the disposal of the warehouse six months after the trade ceased. This is not affected by the building having been rented out in the interim – as this is not an associated disposal for ER purposes.

A capital gain of £225,000 will arise in 2018/19, based on the date of exchange of 12 March 2019. The date of completion is irrelevant for CGT purposes.

2) Donald's CGT liability for 2018/19 is as follows:

	ER gains £	Non-ER gains £
Warehouse 1		135,000
Customer list	300,000	
Warehouse 2	225,000	
Total gains	525,000	135,000
Annual exemption		(11,700)
	525,000	123,300
CGT at 10%	52,500	
CGT at 20%		24,660

His total CGT liability, payable on 31 January 2020 is therefore £77,160.

The annual exemption is allocated in priority to the gains which do not qualify for ER, as they are taxed at a higher rate.

3) Where a trade is continuing, redundancy payments are normally deductible in full, as these are paid to retain the support and motivation of the remainder of the staff.

However, as there is no longer a trade, the expense cannot be paid "wholly and exclusively" for the purposes of the trade. The legislation allows a deduction for statutory redundancy payments and additional relief for three times the statutory level of payment. Therefore a tax deduction will be given for only £16,000 of the £25,000 paid in this case. The remaining £9,000 will not attract tax relief.

As the employee has worked her notice period in full, no element of the termination payment can be said to relate to the notice period and therefore there is no post-employment notice pay. The payment is made on an "ex-gratia" basis and therefore, as the payment does not exceed £30,000, there is no employer's NIC due on the payment.

MARKING GUIDE

TOPIC	MARKS
Part 1 – Disposals and ER	
General conditions for ER to be available	1
No ER on simple sale of assets	½
<i>Warehouse 1</i>	
Only ER if disposal of part of business	½
Capable of separable operation	½
Analysis of situation and conclusion	2
<i>Customer list and plant</i>	
Cessation of whole of business	1
ER should apply	½
Goodwill as capital asset for individual	½
<i>Warehouse 2</i>	
Criteria for ER to apply	1
ER should apply	½
Not affected by rent	½
Relevant date is completion not exchange	½
Sub total	9
Part 2 – Calculation	
Correct annual exemption	½
Allocating AE to non-ER gains	1
Calculation of CGT at 10% (ER gain)	½
Calculation of CGT at 20%(Non-ER gain)	½
Date of payment	½
Sub total	3
Part 3 – Redundancy payment	
Normally deductible	½
Cannot now be wholly and exclusively	½
Restriction to four times statutory amount	½
Effect of restriction	½
No post-employment notice pay	½
No Class 1A NIC due	½
Sub total	3
TOTAL	15

QUESTION 4

1) Corporation tax computation

	£	Note
Profit/(loss) per accounts	(50,120)	
Add:		
Dilapidations provision	5,000	1
New building sign	1,500	2
Rugby sponsorship	2,500	3
Capital IT items	575	4
Website development	750	5
Client entertainment	1,500	6
Client gifts	400	7
Company formation costs	250	8
Lease transfer costs	500	9
Loan note interest	4,250	10
Depreciation	17,000	11
Less:		
Profit on sale of fixed assets	(6,500)	12
Profit/(loss) before capital allowances for 17 months to 31 March 2019	<u>£(22,395)</u>	

Notes:

- 1) This is a provision for capital expenditure on the building's structure, so is not deductible. No capital allowances are available as it will be structural expenditure.
- 2) This is capital expenditure on an asset. Capital allowances are available.
- 3) Whilst described as sponsorship, the entity sponsored is one with which Kate has a close involvement, which casts doubt on the "wholly and exclusively" nature of the payment. She also receives tickets in return which are used to entertain clients and therefore this is disallowable as entertaining.
- 4) These items are enduring assets which will qualify for capital allowances.
- 5) The creation of a website which is expected to generate future revenues in excess of its costs is capital expenditure on the creation of an asset. Capital allowances are available as it is plant.
- 6) Client entertainment is disallowed by statute.
- 7) Client gifts of food and drink are disallowed by statute. The diaries are deductible, as gifts of food and drink are not included in assessing the £50 annual limit per person and contain an advert for the company.
- 8) Company formation costs are capital expenditure on bringing the company into existence.
- 9) The transfer of the lease into the company is capital expenditure on the lease. Only renewal of an existing lease is deductible (by concession).

- 10) As Kate is a participator in a close company, the loan note interest is not deductible as it will not be paid within 12 months of the period end (not expected until summer 2020). Relief will be given when the amounts are actually paid.
- 11) Depreciation is a capital cost
- 12) Profit on sale of assets is an accounting adjustment.

Capital allowances

	AIA @ 100% £	Main pool £	Allowances £
<u>Y/e 31 October 2018</u>			
TWDV b/f	nil	nil	
Additions:			
New building sign	1,500		
IT items	575		
Website development	750		
Assets transferred on incorporation		60,000	
Flat top grill	1,000		
Office furniture	1,500		
Fridge freezer	400		
Dishes and bowls	275		
AIA @ 100%	(6,000)		6,000
WDA @ 18%		(10,800)	10,800
			<u>16,800</u>
TWDV c/f	<u>nil</u>	<u>49,200</u>	

5m/e 31 March 2019

TWDV b/f		49,200	
Additions:			
Food preparation unit	500		
Two-ring burner	750		
Disposals:			
Catering truck		(30,000)	
AIA @ 100%	(1,250)		1,250
WDA @ 18% x 5/12		(1,440)	1,440
			<u>2,690</u>
TWDV c/f	<u>nil</u>	<u>17,760</u>	

The amount removed from the capital allowances pool on disposal of the catering truck is restricted to its original cost of £30,000. A chargeable gain arises below as a result of the sale of qualifying plant in excess of cost.

	Year ended 31 October 2018	Period to 31 March 2019
	12 months	5 months
	£	£
Tax adjusted trading profit/(loss) before capital allowances	(15,808)	(6,587)
Capital allowances	(16,800)	(2,690)
Trade profit/(loss)	<u>(32,608)</u>	<u>(9,277)</u>
Chargeable gain		<u>10,000</u>
Total taxable profits	nil	723
Brought forward losses utilised		(723)
Trade losses carried forward	<u>32,608</u>	<u>31,885</u>

2) Kate's salary

As Kate transferred the business to the company in exchange for consideration comprising of at least 80% share capital (in this case, 83.9%), the trading losses of £26,450 from the sole trade carried forward at incorporation will be set against income received by Kate from the company. As a result, the salary of £15,000 will be set against these losses and will not be subject to income tax. The remaining losses of £11,450 will be set against the next available income received from the company (salary, loan note interest etc.).

If Kate has no other income for the year, her personal allowance may be lost as a result.

MARKING GUIDE

TOPIC	MARKS
Corporation tax computation	
Adjustments (inclusion and quantum) - ½ each	6
Associated explanations - ½ each	6
Splitting period into two for CAs	½
Inclusion of capital assets in revenue	½
Additions and disposals	1
No AIA on assets transferred in on incorporation	½
Restricting disposal proceeds where above cost	½
Claim AIA	½
Claim WDA in period 1	½
Reduced WDA in period 2	½
Allocation of profit after adjustments, before CAs	½
Deduction of CAs	½
Inclusion of chargeable gain	½
Sub total	18
Kate's salary	
Consideration of at least 80% in shares	1
Losses set against income from company	½
Potential loss of personal allowance	½
Sub total	2
Total	20

QUESTION 5

Bases of accounts preparation

Normally, a business (both a sole trader and a limited company) must prepare accounts under the 'going concern' accruals basis, as detailed in the accounting standards. This takes account of amounts paid and received, as well as future amounts payable and receivable by the business which relate to the current year.

However, eligible sole traders can also elect to use the 'cash basis' to calculate their taxable trading profits. Limited companies may not use the cash basis.

Eligibility and making of election

Sole traders can elect to use the cash basis if their total business receipts for that tax year do not exceed £150,000. In a year in which your tax basis period is less than 12 months long e.g. the year in which you start to trade, this limit is proportionately reduced. If you therefore commence trading on 1 January, the limit will be reduced to £37,500 (being 3/12th of £150,000).

Once an election is made, it will apply for the tax year for which it is made and all subsequent tax years, until such times as the business receipts exceed £300,000 (unless these receipts will fall below £150,000 in the current year).

In order to make an election to use the cash basis, the relevant box must be ticked on the self-assessment return.

Effect of making the election

If an election is made for the cash basis to apply, it applies for income tax and Class 4 NIC purposes. The profits of the trade for an accounting period are then calculated simply as income actually received, less allowable expenses actually paid.

The tax treatment of costs is generally governed by the same rules as applying to those businesses not using the cash basis, however there are some exceptions.

- Capital allowances – the only assets which qualify for capital allowances are cars purchased by the business. All other plant and machinery is treated as deductible in full in the year it is paid, if used wholly for business purposes. Any private usage will reduce the allowances given. Sales proceeds will also be brought into the tax computation in full when received.
- Goods taken for own use – if goods are removed for your own use, the cost of the goods is disallowed in the tax computation, rather than making an adjustment to include the sales price of the goods.
- Interest costs – a maximum of £500 of loan/overdraft interest and related costs can be deducted each period for any loans obtained.
- Car leasing costs – all car leasing costs are deductible without any restriction based on emissions.

Finally, if the business makes losses, these losses may only be carried forward against future trading income. They cannot be used against other income in the same way as non-cash basis trading losses can be.

Illustrative calculations of tax liabilities

Sole trader

A sole trader earning taxable profits of £65,000 will suffer the following tax liabilities in 2018/19.

	£
Profits	65,000
Personal allowance	<u>(11,850)</u>
Taxable income	<u>53,150</u>
Tax thereon:	
£34,500 @ 20%	6,900
£18,650 @ 40%	7,460
Class 2 NICs (flat-rate) 153	
Class 4 NICs:	
£8,424 @ 0%	-
£37,926 @ 9%	3,413
£18,650 @ 2%	<u>373</u>
Total tax and NIC payable	<u>18,299</u>
Post tax income	<u>46,701</u>

Company director receiving salary and dividends

The director would withdraw a salary of £8,424, being the maximum amount payable without Class 1 NIC being payable by the company or the director.

	£
Profits	65,000
Salary	<u>(8,424)</u>
Taxable profits	56,576
Corporation Tax thereon:	
£56,576 @ 19%	<u>10,749</u>
Post tax profit paid as a dividend	<u>45,827</u>
Salary 8,424	
Dividend (calculated at right) 45,827	
Personal allowance	<u>(11,850)</u>
Taxable income	<u>42,401</u>
Tax thereon:	
£2,000 @ 0%	-
£32,500 @ 7.5%	2,438
£7,901 @ 32.5%	<u>2,568</u>
Total tax and NIC payable	<u>5,006</u>
Post tax income	<u>49,245</u>

Summary

At a profit level of £65,000, the individual would be £2,544 better off by operating through a limited company and withdrawing profits in full by a mixture of salary and dividend.

MARKING GUIDE

TOPIC	MARKS
Bases of accounts preparation	
Accruals basis is standard for both	1
Cash basis for sole-traders only	$\frac{1}{2}$
Threshold and reduction for short period	1
Basis continues until threshold reached	1
Claim required	$\frac{1}{2}$
Application to IT and C4 NIC	$\frac{1}{2}$
Basis of calculation	$\frac{1}{2}$
Capital allowances	1
Goods for own use	1
Interest	$\frac{1}{2}$
Leasing costs	$\frac{1}{2}$
Losses	1
Sub total	9
Illustrative calculations	
Sole trade – PA	$\frac{1}{2}$
Sole trade – calculation of IT	1
Sole trade – calculation of NICs	$1\frac{1}{2}$
Director – salary of £8,424	$\frac{1}{2}$
Director – calculation of CT payable	$\frac{1}{2}$
Director – calculation of dividend	$\frac{1}{2}$
Director – calculation of IT	1
Calculation of difference	$\frac{1}{2}$
Sub total	6
TOTAL	15

QUESTION 6

Although Victoria is a member of an LLP it is likely that her income will be caught by the “disguised employment” anti-avoidance legislation in s863A-G ITTOIA 2005

The provisions will apply where an LLP member’s income meets all three of the following tests.

1) Disguised salary:

More than 80% of the individual’s income is fixed or not linked or affected by overall profits
Victoria will meet this test as her fixed profit share in the year will be £54,000 whilst her variable share will be £4,500 i.e. 92.3% of her income is fixed. The value of any benefits in kind are not taken into account in this calculation

2) No significant influence:

The member has no significant impact on the running of the business

This test will also be met as the management of the LLP is undertaken by the two founder members

3) No significant investment:

The member’s funds at risk in the LLP is less than 25% of their profit share.

This test is applied to the level of fixed profit share. This is pro-rated to reflect the fact Victoria joined part way through the year. The pro-rated capital contribution is £7,500 and this is less than 25% of the fixed profit share of £54,000.

Where the above tests are all met then the LLP is required to treat the member’s profit allocation as ordinary remuneration and should deduct PAYE and primary and secondary Class 1 NIC and account for this on a monthly basis through the LLP’s Real Time Information returns. The payments will be treated as a tax deductible expense in the LLP rather than a profit allocation.

Benefits in kind provided to members falling within these provisions will be taxed in the same manner as those provided to employees and hence the LLP must complete a P11D and disclose the provision of a company car and account for class 1A NIC. Again these expenses will be treated as a tax deductible expense in the LLP rather than drawings.

Calculation of maximum primary Class 1 NIC

		£	£
Step 1	Upper Earnings limit (£3,863) less Primary Threshold (£702) x 12	37,932.00	
Step 2	X 12%		4,551.84
Step 3	LLP income:		
	between primary threshold (£702) and upper earnings limit (£3,863) x 12	37,932.00	
	Non executive income:		
	between primary threshold (£702) and actual income (£2,000) x 12	15,576.00	
	TOTAL	53,508.00	
Step 4	Figure in Step 3 less total in Step 1	15,576.00	
Step 5	x 2%		311.52
Step 6	LLP income (£58,500) in excess of upper earnings limit (£46,350)	12,150	
Step 7	Step 6 x 2%		243
Step 8	Annual maximum: Sum of Steps 2, 5 and 7		5,106.09

This figure is compared to the actual primary class 1 NIC paid during the year which is:

	£	£
LLP income		
£3,863 - £702 = £3,161 x 12% for 9 months	3,413.88	
£6,000 - £3,863 = £2,137 x 2% for 9 months	384.66	

		3,798.54
Non-Executive income		
£2,000 - £702 = £1,298 x 12% for 12 months		1,869.12
Total primary class 1 NIC paid		5,667.66

Victoria will be able to make a claim for repayment of £561.57 being the difference between the class 1 NIC paid and the annual maximum

MARKING GUIDE

TOPIC	MARKS
Disguised employment provisions will be relevant	1
All three tests must be met for the provisions to apply	½
More than 80% of income fixed	½
Application of the test to Victoria's income	½
Benefits in kind are not included in the test	½
Significant influence test	½
Application of the influence test to Victoria	½
Significant investment test	½
Test applied to the fixed profit element	½
The figure is pro-rated	½
LLP must treat the drawings as ordinary remuneration and apply PAYE/NIC	1
Tax deductible in the LLP	1
Benefits must be disclosed on form P11D	1
Subject to Class 1A NIC	1
Expenses tax deductible in the LLP	½
Marks allocated for applying the correct process	3
Calculate NIC on LLP income	½
Calculate NIC on non-executive income	½
The ability to reclaim the difference between the maximum NIC and the amount paid	1
TOTAL	15