



The Chartered Tax Adviser Examination

May 2020

Application and Professional Skills

Taxation of Individuals

TIME ALLOWED – 3 ¼ HOURS

- The first 15 minutes is designated as reading time. During this time you may read your question paper and legislation, annotate your question paper and use your calculator. You are not permitted to start writing your answer. The Presiding Officer will inform you when you can start writing.
- In order to secure a pass in this paper, you will be required to demonstrate competence in each of three skills.

You will be assessed across your answer as a whole for Structure. A pass or fail grade will be awarded.

You will be assessed for competence in a number of broad topics for the following skills:

- Identification and Application
- Relevant Advice and Substantiated Conclusions

For each topic for each of these two skills, a grade will be awarded. The grades for those topics will be weighted and averaged to produce a final grade for each skill of 0, 1, 2, 3 or 4. A grade of 3 or 4 is required to demonstrate competence.

- Write on one side of the paper only. Do not write in the margins.
- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should tick the appropriate box on the cover sheet.
- Unless otherwise indicated by the provision of additional information, you may assume that 2019/20 legislation (including rates and allowances) continues to apply for 2020/21 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.

You are a tax senior in a firm of Chartered Tax Advisers. Jason Sterling and his wife, Irene Sterling, have been clients of your firm for many years.

Irene's elderly parents are becoming increasingly frail, so it has been decided that they will move in with Jason and Irene. To discuss the changes associated with the move, Jason and Irene have attended a meeting with your manager, Susan Lamb. Susan has agreed to provide Jason and Irene with a report advising them on how best to proceed and she has asked you to prepare a draft for her review.

The following exhibits are provided to assist you:

EXHIBIT A: File note of a meeting between Susan Lamb and Jason and Irene Sterling

EXHIBIT B: Email from Irene Sterling

EXHIBIT C: Pre-seen information

Requirement:

Prepare a draft report advising Jason and Irene Sterling on how best they should proceed in relation to the issues they raised in the meeting with Susan Lamb.

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Continuation

EXHIBIT A

File note of a meeting between Susan Lamb and Jason and Irene Sterling

Meeting Date: 27 April 2020

Jason and Irene arranged the meeting to discuss changes to their family circumstances. Irene's parents are both very elderly and are unable to live without support. Currently Irene's parents live in their own home (which they rent from a housing association). Rather than going to a care home, it is intended that Irene's parents will move to Jason and Irene's house. This will affect Jason and Irene's finances in the following ways:

Care package

Jason and Irene will use an external care agency to help care for Irene's parents. They have been offered a choice of one of two care packages. The more extensive care package costs £20,000 per year, and the other costs £10,000 per year. Neither package involves any live-in care.

Irene's employment

Irene is going to reduce her working hours so that she can spend time looking after her parents. Going forward, her salary will be £10,000 per year. Her only other income is profit from the couple's rental properties.

Jason's employment

Jason has applied for a job closer to home with more flexible hours. If Jason is offered and accepts the job, Jason and Irene believe they will be able to provide much of the care for Irene's parents themselves, so will use the cheaper care package costing £10,000 per year. If Jason remains with his current employer, Absolute plc, the more extensive care package costing £20,000 will be needed.

They will provide more information on this once they know whether Jason will be offered the job he has applied for.

Plan to build an extension

Jason and Irene will adapt and extend their house so that Irene's parents can comfortably live with them. The extension to their main residence will include its own kitchen and bathroom so that Irene's parents can maintain some privacy and independence. Whilst the extension is being built, they will use Jason and Irene's lounge as a bedroom.

The cost of the extension will be £175,000. Jason and Irene have spoken to their Independent Financial Adviser and have identified two ways in which they can raise the funds:

- 1) Re-mortgage a property. They have been offered an interest-only mortgage of £175,000 on either:
 - (a) 65 Hilltop View, their main residence, at an interest rate of 4%; or
 - (b) 14 Railings Way, a rental property, at an interest rate of 4.5%.
- 2) Access funds from Jason's pension. Jason has always saved money into his pension in preference to other savings vehicles. As a result, the couple have no significant cash savings but Jason has accumulated a large pension fund, which he is considering accessing now that he is over 55.

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Rental Properties

The two rental properties owned by Jason and Irene were purchased with interest only mortgages covering 100% of the purchase price. No capital has been repaid (nor any additional capital borrowed). Jason and Irene plan to repay the mortgages when they sell the houses, which they intend to do in approximately five years' time.

Jason and Irene would like advice on how to structure their tax affairs going forward, taking the proposed changes into account.

EXHIBIT B

Email from Irene Sterling

To: Susan Lamb
From: Irene Sterling
Date: 31 April 2020
Subject: Jason's Job Offer

Dear Susan

Further to our meeting, Jason has now been offered the new job, which is with a business called Relative plc. The salary offered is £90,000 per year, which is the same as Jason earns at Absolute plc. However, unlike Absolute plc, no employer pension contribution will be paid (beyond the legal minimum under auto-enrolment).

If Jason takes the job with Relative plc, he will save £7,000 in commuting costs each year. We will also save £10,000 a year with the cheaper care package.

However, Absolute plc are keen not to lose Jason. As he is at the top of his pay scale, they cannot increase his overall package but have offered to substitute the pension contribution of £20,000 they currently pay for an increase in his salary of £17,500 per year (and will then only pay the legal minimum pension contribution under auto-enrolment).

Kind regards

Irene Sterling

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Continuation

EXHIBIT C

Pre-seen information

Client Names:

Jason and Irene Sterling

	<u>Jason</u>	<u>Irene</u>
Date of birth:	5 April 1963	4 May 1975
Country of birth:	England	England
Domicile:	UK	UK
Tax Residence:	UK	UK
Scottish Taxpayer:	No	No
Employer:	Absolute plc	Magic Admin Ltd
Salary:	£90,000 per annum	£21,000 per annum
Benefits:	Employer pension contribution of £20,000 per annum	-

Date of marriage:

15 September 2000

Children:

Adam (age 8), Lily (age 6)

Jason and Irene Sterling – Asset Schedules at 1 May 2020

Jointly owned Assets

<u>Asset</u>	<u>Market Value on 1 May 2020</u> £	<u>Cost</u> £	<u>Notes</u>
65 Hilltop View	950,000	380,000	Main residence for entire period of ownership. Grounds do not exceed half a hectare
13 Lamppost Road	420,000	300,000	Rental property – let since purchase
14 Railings Way	380,000	120,000	Rental property – let since purchase

Assets owned solely by Jason Sterling

<u>Asset</u>	<u>Market Value on 1 May 2020</u> £	<u>Cost</u> £	<u>Notes</u>
5,000 shares in Absolute plc	4.20 per share (unrestricted market value)	4.50 per share	Restricted securities awarded by Absolute plc
Pension	940,000	Not applicable	Defined Contribution Plan

Assets owned solely by Irene Sterling

<u>Asset</u>	<u>Market Value on 1 May 2020</u> £	<u>Cost</u> £	<u>Notes</u>
Pension	14,200	Not applicable	Defined Contribution Plan

Continuation

Wills

Both Jason's and Irene's wills are written so that their entire estate is left to their spouse or to their children if the spouse dies first.

Jason Sterling – 2018/19 Tax Return

Disclosure

On 5 May 2018 I acquired 5,000 shares in Absolute plc, my employer, for 50 pence per share.

The unrestricted market value of the shares on this date was £4.50 per share.

If I leave my employment with Absolute plc before 5 May 2023 the shares will be returned to Absolute plc for 50 pence per share. I am prevented from disposing of these shares other than to Absolute plc before 5 May 2023. These restrictions reduced the market value of the shares to £1.00 per share at the date of acquisition.

On 5 May 2018 I made a joint election with my employer under s.431 ITEPA 2003 to treat the acquisition of the shares as if they were not subject to any restrictions. My employment income of £110,000 includes £20,000 relating to this acquisition.

Tax Calculation

	£
Pay from all employments	110,000
Profit from UK land and property	<u>11,675</u>
Total income received	<u>£121,675</u>
Income tax charged	41,365
Minus relief for finance costs	(765)
Minus tax deducted from all employments, UK pensions and state benefits	<u>(34,360)</u>
Total income tax due for 2018/19	<u>£6,240</u>

No payments on account are due.

Calculation of 2018/19 rental profit – Jason and Irene Sterling

	<u>13 Lamppost</u>	<u>14 Railings</u>	<u>Total</u>
	<u>Rd</u>	<u>Way</u>	
	£	£	£
Rents received	18,000	18,000	36,000
Professional fees, insurance and maintenance	(2,500)	(2,500)	(5,000)
Loan interest	(11,700)	(3,600)	(15,300)
Loan interest disallowed (50%)	<u>5,850</u>	<u>1,800</u>	<u>7,650</u>
Profit from land and property	<u>9,650</u>	<u>13,700</u>	<u>23,350</u>

Profit Allocation:

Jason	£11,675
Irene	£11,675