

The Chartered Institute of Taxation

Advanced Technical

Taxation of Owner-Managed Businesses

May 2025

Suggested answers

Answer 1

Plant and machinery allowances available

Computation:

	Note	AIA £	Full expensing £	Main pool £	SRP £	Allowances £
TWDDV b/fwd				287,000	12,000	
Additions:						
Production machine	1	320,000				
Strengthening floor	2	12,000				
Lorry (2nd hand)	5	32,000				
Packing machine	5	636,000	79,000			
Disposals:						
Boiler	6				(15,000)	
Qualifying expenditure		1,000,000	79,000	287,000	(3,000)	
Balancing charge					3,000	(3,000)
AIA/Full expensing @ 100%		(1,000,000)	(79,000)			1,079,000
WDAs @ 18%				(51,660)		51,660
TWDDV c/fwd		Nil		235,340	nil	
Balancing charge on pressing machine	7					(32,000)
Total allowances						<u>1,095,660</u>

Notes:

1. The acquisition of the new production machine on hire purchase is treated as an addition in the accounting period in which it is brought into use i.e. the year ended 31 December 2024. The cash cost of the asset is the amount treated as eligible for capital allowances.
2. The cost of strengthening the floor was necessary for the installation of this new machine and therefore eligible for capital allowances. [s.25 CAA 2001]
3. Whilst capital allowances would ordinarily be available on air conditioning, lift and electrical works as integral features [s.33A CAA 2001], as these costs relate to fixtures within an acquired property, it would have been necessary for the seller to have added these costs to a capital allowances pool and an election under s.198 CAA 2001 to have been signed by the parties, agreeing what allowances can be claimed by Boxtransfer Ltd as purchaser. In the absence of either of these things, no capital allowances can be claimed.
4. Plant and machinery allowances are not available on fixed partitions as these are treated as part of the building. [item 13 of list C, s.23 CAA 2001]
5. As the lorry is second-hand it is not eligible for full expensing and should be included in the AIA in priority to the other new items of plant and machinery.

Full expensing is available for these new machines, but a balancing charge would arise when sold, equal to the proceeds realised. Therefore, it would be more tax efficient to allocate the additions to the annual investment allowance to its maximum value. As the total of the additions exceeds £1m in the year, the balance will be eligible for full expensing but only on the items which are brand new.

6. The general rule is that the lower of actual proceeds and original cost is taken into account on the disposal of each asset. As the acquisition of the boiler took place before 1 April 2021, no enhanced allowances would have been available when purchased. Therefore, the disposal proceeds are deducted from the relevant pool. The boiler is an integral feature hence the proceeds are deducted from the special rate pool.
7. Enhanced capital allowances were claimed on the acquisition of the pressing machine. As the accounting period of disposal starts after 31 March 2023, a balancing charge will arise at 100% on the disposal proceeds. No other entry is made in the capital allowance computation.

SBAs

The new building will be eligible for SBAs as it was first acquired after October 2018 by the previous owner.

The costs of the land, legal fees and SDLT would be ineligible for SBAs.

The price that Boxtransfer Ltd paid for the property is not relevant, as SBAs are based on the original qualifying cost for the first owner.

An allowance statement should have been prepared by the previous owner and sent to the company.

The previous owner should be contacted to request this statement so that the qualifying cost for SBAs can be obtained and the relevant SBAs claimed at 3% of this cost.

Allowances will only be available for the final five months of the accounting period as the building was not brought into use until 1 August 2024.

MARKING GUIDE

TOPIC	MARKS
1) Plant & machinery allowances	
Computation	
Including additions	0.5
Including disposals	0.5
SRP balancing charge	1.0
AIA/WDAs	1.0
Balancing charge on machine	0.5
Total CAs	0.5
Additions	
Hire purchase	1.0
Strengthening floor	0.5
New site recognition of no allowances without s.198 election	1.0
Fixed partitions	0.5
Lorry	0.5
Packing machine	0.5
AIA v full expensing	1.5
Disposal	
General rule	0.5
Pressing machine	1.0
Integral feature	1.0
SUB TOTAL	12.0
2) SBAs	
New building qualifies	0.5
Ineligible costs	0.5
Based on original cost	0.5
Rate of SBAs	0.5
Allowance statement	0.5
From 1 August 2024	0.5
SUB TOTAL	3.0
TOTAL	15

Answer 2

Tax adjusted loss for 2024/25

	<u>Notes</u>	<u>£</u>	<u>£</u>
Loss per draft accounts			(129,807)
Add:			
Lease premium	1	54,000	
Pizza oven	2	21,000	
Dining tables and chairs	2	5,750	
Restaurant management software	2	2,000	
Laptop	3	<u>1,500</u>	84,850
Deduct:			
Allowable premises lease costs	1	2,160	
Class 1A NIC on benefits	4	138	
Capital allowances	5	<u>23,931</u>	(26,229)
Tax adjusted loss			<u><u>(71,786)</u></u>

Notes:

- 1) As the lease is a short lease, some of the premium is treated as property income for the landlord. The same amount is an allowable deduction for Harriet but spread over the term of the lease.

Premium	<u>£</u> 54,000
Less: $2\% \times 54,000 \times (15-1)$	<u>(15,120)</u>
Property income assessed on landlord	<u>38,880</u>

(OR $54,000 \times (50-14) \div 50 = 38,880$)

The deductible amount for Harriet is £2,160 ($(38,880 \div 15) \times 10/12$)

- 2) The pizza oven is capital expenditure (plant and machinery) and therefore is added back. Capital allowances are available. The pizza oven qualifies for AIA.

The software is capital expenditure and is specifically treated as plant and machinery for capital allowances (CAA01 s71)

The dining tables and chairs are capital expenditure. As they were purchased from a connected person, no AIA is available.

- 3) Harriet's laptop is capital expenditure and is therefore added back.

As the laptop was used for another purpose before being brought in to use for the business, no AIA is available. The asset is also brought into the business at its market value at the time, rather than its original cost. The small pools limit does not apply to single asset pools.

- 4) Medical insurance costs attract a Class 1A NIC liability at 13.8% $\text{£}1,000 \times 13.8\% = \text{£}138$

5) Capital allowances.

	<u>AIA</u> £	<u>Main pool</u> £	<u>Laptop</u> £	<u>BU</u> %	<u>Allowances</u> £
Additions					
Pizza oven	21,000				21,000
Software	2,000				2,000
Dining tables and chairs		5,750			
Laptop			600		
		<u>5,750</u>	<u>600</u>		
WDA at 18% (5,750 x 18% x 10/12)		(863)			863
WDA at 18% (600 x 18% x 10/12)			(90)	75%	68
TWDV c/fwd		<u>4,887</u>	<u>510</u>		
Allowances					<u>23,931</u>

The qualifying assets were purchased before trading commenced. Under CAA 2001 s.12, this expenditure is therefore treated as incurred on the first day of trading.

Loss relief available to Harriet

There are four options for utilising the loss:

- Early years loss relief claim;
- Current year loss relief claim;
- Prior year loss relief claim; and
- If no other relief is claimed, carry the loss forward.

These claims can be made in any order.

As Harriet's losses arose in the first four tax years of trading, she can claim early years loss relief. The losses can be carried back and offset against her net income of the previous three tax years. The losses are offset against the earliest year first.

An early years loss relief claim is restricted to the greater of £50,000 and 25% of Harriet's adjusted total income for the year.

Harriet can carry back the losses arising in the 2024/25 tax year as follows:

	2021/22 £	2022/23 £	2023/24 £	2024/25 £
Net income	182,000	184,000	197,500	46,000
Trading losses	(50,000)	(21,786)	(0)	(0)
Revised net income	<u>132,000</u>	<u>162,214</u>	<u>197,500</u>	<u>46,000</u>

If an early years loss relief claim is made first, the tax repayment for 2021/22 will be £21,600 ((£32,000 x 45%) + (£18,000 x 40%)) and the tax repayment for 2022/23 will be £9,804 (£21,786 x 45%). A total repayment of £31,404.

Current/prior year loss relief claim

Harriet could also make a current and/or previous year loss relief claim (s.64 ITA 2007) for her losses to be offset against her other income in 2024/25 and/or 2023/24, in any order. A current and/or previous year loss relief claim is also restricted to the greater of £50,000 and 25% of Harriet's adjusted total income for the year.

	2021/22	2022/23	2023/24	2024/25
	£	£	£	£
Net income	182,000	184,000	197,500	46,000
Trading losses	(21,786)	(0)	(50,000)	(0)
Revised net income	160,214	184,000	147,500	46,000

Making a claim against the previous tax year (2023/24) first will result in an income tax repayment of £22,500 (£50,000 x 45%) due to the additional rate tax band being £125,140 in 2023/24 as opposed to £150,000 in 2022/23.

A current year loss relief claim, at any time, saves income tax at a marginal rate of just 20%, so would not be beneficial in these circumstances.

Carry the loss forward

If Harriet doesn't make any loss relief claim, the losses will be carried forward and offset against future trading profits.

Conclusion

The most beneficial claim for Harriet is to first carry the loss back to the previous tax year and then claim early years loss relief for the remaining loss.

A claim to carry the loss back to the previous tax year (2023/24) would save tax at 45% (£22,500)

The remaining loss (£21,786) can then be carried back to 2021/22 under an early years loss relief claim which would generate an income tax repayment of £9,804 (£21,786 x 45%)

In this case, all tax is saved at 45% - a total income tax repayment of £32,304, which is £900 more than an early years loss relief claim on its own.

Harriet must make claims under s.64 ITA 2007 and s.72 ITA 2007 by 31 January 2027.

Harriet's national insurance liability for 2025/26

The profits for the purposes of Class 4 NIC are £62,000 but as the trading loss from 2024/25 has been utilised against non-trading income (and therefore has not attracted any Class 4 NIC relief) it is still available to carry forward to future years.

Therefore, no profits are subject to Class 4 NIC and there are losses for the purposes of Class 4 NIC to carry forward of £9,786 (£71,786 - £62,000).

MARKING GUIDE

TOPIC	MARKS
Requirement 1 - Tax adjusted loss for 2024/25	
Lease premium adjustments	2
Add back pizza oven, dining table/chairs and software cost	1
Laptop adjustment	1
Class 1A calculation and deducting from profits	1
AIA on pizza oven & software	1
No AIA on dining tables and chairs as from connected person and WDA calculation	1
Personal use adjustment to the laptop purchase and no small pools allowance claim	1
No AIA on the laptop as used for another purpose before brought in to use	1
Loss relief claim	
s.72 loss relief claim – oldest year first, restriction on loss, claim date	2.5
s.64 loss relief claim	2.5
s.83 loss relief claim	1
Recommendation – s.64 claim then s.79 claim	2.5
Deadline for claims	0.5
Requirement 2 - Tax calculation for 2025/26	
Adjustment to profits for Class 4 NIC	1
Losses available to carry forward for Class 4 NIC purposes	1
TOTAL	20

Answer 3

[Note – this answer is based on the factory disposal taking place on 5 April 2025 as per the note accompanying the question paper on the CIOT website]

Summary:

	BADR gains £	Non-BADR gains £
Shares	770,000	
Factory	94,379	152,621
	864,379	152,621
Excess over lifetime limit	(29,379)	29,379
	835,000	182,000
Less: annual exempt amount		(3,000)
Taxable gains	835,000	179,000
CGT rate	10%	20%
CGT payable	83,500	35,800

Total = £119,300

Gains arising on the two disposals:

	Shares £	Factory £
Sale proceeds	800,000	375,000
Less: costs	(30,000)	(128,000)
Gain	<u>770,000</u>	<u>247,000</u>

Business Asset Disposal Relief (BADR) availability

Shares

BADR is available if the following conditions are satisfied:

- The disposal is of shares in a personal trading company. HMRC's view of a trading company is one which has trading assets of at least 80% of the total asset value of the company, 80% of the income is generated from trading activities and 80% of the resources are employed in trading activities. The investment asset makes up only 15% of the total asset value and the non-trading revenue is only 12%. There is no information on the resources employed by the company in managing the investment assets but generally these do not take up much management time and is likely to be less than 20% of the total resources. Therefore, HMRC are likely to view this as a trading company.
- The fact Maxine spends 40% of her time managing personal investments is not relevant for the availability of business asset disposal relief.
- Maxine needs to own at least 5% of the ordinary share capital of the company for a consecutive period of two years prior to the disposal of the shares. As she had held 30% of the shares since 2002, this condition is met.
- Maxine needs to be an employee or officer of the company. As a director she was an officer of the company for at least two years prior to the disposal. There is no requirement for her to work full time in the company. She has therefore met this condition.

As all conditions have been met, the disposal of the shares qualifies as a material disposal for BADR.

Factory

BADR is available as an associated disposal provided that the property has been owned for at least three years and used by Maxine's personal trading company for at least two years prior to disposal. As there is gap between the sale of the shares and the factory, HMRC will treat the factory as an associated disposal provided that the sale of the factory takes place within three years of the sale of the shares and has not been used for any other purpose.

These conditions have been satisfied and the gain will qualify for business asset disposal relief.

Impact of rent

Where rent is charged by the owner of the associated asset to the company which uses it, the availability of BADR is restricted.

This restriction only applies from 6 April 2008 and no restriction applies before this date. BADR is therefore fully available for the first three years that the property was rented to the company.

The property was rented at 70% of market value and hence only 30% relief will be available between 6 April 2008 and 5 April 2022. For the final three and half years of ownership, 90% of the market rent was charged, hence only 10% relief will be available.

Relief available = $[(100\% \times 3) + (30\% \times 14) + (10\% \times 2.5)]/19.5 = 38.21\%$.

Therefore, BADR would only be available on £94,379 ($38.21\% \times £247,000$) of the gain

As Maxine has used up £165,000 of her lifetime business asset disposal limit of £1m, only £835,000 remains for these disposals.

BADR must be claimed by 31 January 2027.

MARKING GUIDE

TOPIC	MARKS
Gains summary	
Split factory gain	0.5
Transfer excess over lifetime limit	0.5
Deduct AEA from non-BADR gains	0.5
CGT payable	1.0
Election date	1.0
Gains arising	
Shares	0.5
Factory	0.5
Share disposal – BADR discussion	
Trading company discussion	1.5
Managing personal investments	0.5
5% ownership	0.5
Working condition	1.0
Conclude relief applies	0.5
Factory disposal – BADR discussion	
Conditions	2.0
Rent restriction	
Restrict relief	0.5
Only post April 2008	0.5
2008 to 2022	1.0
2022 to sale	0.5
Overall percentage	1.0
Eligible gain	0.5
BADR lifetime limit	0.5
TOTAL	15

Answer 4

PSA Agreement

A PAYE Settlement Agreement allows an employer to settle an employee's tax liability on certain benefits.

A benefit can be included in a PSA if it is:

- A minor benefit;
- Paid on an irregular basis; or
- Impractical to apply PAYE or apportion the value of a benefit shared by a number of employees.

Unless any exemptions are available, all of the items listed would give rise to a taxable benefit as they have been enjoyed by the staff at the expense of the company.

Taking each benefit in turn:

Relocation expense

Qualifying relocation costs are exempt, up to £8,000. This includes the costs of buying or selling a home and the associated moving costs. The excess of £2,000 would be suitable for inclusion in a PSA, as it is an irregular payment.

Wedding gift

This is a one-off (irregular) expense. It would therefore be suitable for inclusion on a PSA. VAT is included, whether or not this can be reclaimed by the employer and so the benefit to include in the PSA is £300 (£250 x 120%).

Vouchers

As the cost of the voucher:

- does not exceed £50 per person;
- is not in recognition of service; and
- not cash or a cash voucher

the benefit will be considered trivial and, therefore, exempt. It does not need to be included in the PSA.

Christmas party

This is an annual event, but the exemption threshold of £150 per head is exceeded. There is therefore no exemption available. However, HMRC will accept that the cost of Christmas parties and similar entertainment which do not otherwise qualify for relief are 'impractical to apportion between staff', and therefore the full cost of the party can be included in the PSA.

Summer event

This is a one-off event and therefore does not qualify for the 'annual function' exemption. As with the Christmas party, the total cost can however be included on the PSA as HMRC accept it is impractical to apportion the cost between the employees.

HMRC must be contacted by 6 July 2025 if the business wants to have a PSA in place for the 2024/25 tax year. HMRC should be notified of the expenses that the PSA is proposed to cover.

Total amount payable

	Relocation	Gift	Christmas party	Summer event	Total	Tax
	£	£	£	£	£	£
Benefits (BR)		300	2,200	4,950	7,450	1,490
Benefits (HR)	2,000		1,800	4,050	7,850	3,140
Total					15,300	

	£
Grossed up tax (£1,490 x (100/80))	1,863
Grossed up tax (£3,140 x (100/60))	5,233
Total tax payable	7,096

Total on which Class 1B NIC payable (£15,300+ £7,096) = £22,396

Class 1B NIC @ 13.8% = £3,091

Total due (£7,096 + £3,091) = £10,187

Total amount due to HMRC for 2024/25 is £10,187. This tax is payable on or before 22 October 2025 (if paid electronically).

Both the employee's tax liabilities and Class 1B National Insurance Contributions are allowable deductions for corporation tax purposes.

Note: Alternative method

BR taxpayer benefits	£7,450	
Tax 7,450 x 20/80		£1,863
HR taxpayer benefits	£7,850	
Tax £7,850 x 40/60		£5,233
Totals	£15,300	£7,096

Benefits plus tax = £22,396

MARKING GUIDE

TOPIC	MARKS
Part 1 – Discuss eligibility of benefits and explain PSA process	8
General position	1
Discuss type of benefits a PSA can cover	1
Relocation expense exempt up to £8,000	1
Excess of £2,000 included on PSA	0.5
Wedding gift	1
Vouchers	1
Christmas party	1
Summer event	0.5
Registration process	1
Part 2 – Amount payable to HMRC	7
Quantify benefits for BR/HR taxpayers	1
Calculate tax on benefits	1
Quantify relocation benefit	0.5
Gross up HR/BR taxpayers	1
Calculate Class1B NIC due	1
Total amount due	1
Due date	0.5
Corporation tax	1
TOTAL	15

Answer 5

Implications of changes in share ownership and business operations

There are anti-avoidance rules in place when there is a change in ownership of a company that prevent the new owner utilising brought forward trading losses and there has been a major change in the nature or conduct of the trade.

For these purposes, a change in ownership occurs when either:

- Within a period of three years a single person acquires more than 50% of the share capital; OR
- Two or more persons acquire at least 5% of the share capital and taken together the shareholding exceeds 50%; OR
- A company acquires another company and becomes a member of the same group.

The gifting of shares does not constitute a change in ownership. Therefore, the existing shareholder's gift of shares to his daughter is not considered when looking at the anti-avoidance rules.

Lucy has acquired her shares within a three-year period, but her shareholding does not exceed 50% (as she holds 49%). This alone is not a change in ownership.

However, taken together, Russell and Lucy's shareholding is 54% and they both have a shareholding of at least 5%. This is therefore a change in ownership as at 1 June 2024.

It will then need to be determined whether there has been a major change in the nature or conduct of the trade.

The anti-avoidance rules state that there is a major change if there is a change in property dealt in, services or facilities provided in the trade, or a major change in customers, outlets or markets.

Case law states that to be trigger a major change, the change must be "more than significant but not necessarily fundamental" (*Purchase v Tesco*).

Statement of Practice 10/91 provides guidance on the sort of changes a company can make that does not constitute a major change.

With reference to Statement of Practice 10/91, the changing of the existing menu by the business would be a change to rationalise the business by dropping unprofitable menu items. This would therefore not be a major change. Similarly, the redundancies would be considered an improvement in the efficiency of the company and so also not a major change.

However, the conversion of the property into a wine bar would be considered a major change in the services provided in the trade.

When the anti-avoidance rules apply, we must consider the 5-year period beginning no more than 3 years before the change in ownership. No major change can happen in that time.

The changes can be gradual and made over the course of time. If the cumulative changes are major then the rules apply.

In this instance, the major change has occurred within 6 months of the change in ownership. The anti-avoidance provisions will therefore apply.

Corporation tax payment due

As the anti-avoidance rules apply, there will be a block on the business carrying forward trading losses and offsetting them against future profits in Ginos Ltd.

This block will apply at the date of the change in ownership, being 1 June 2024. This means that losses can only be offset against profits in the period to 31 May 2024. The trading losses are blocked from being offset against any profits generated after 1 June 2024.

Corporation tax payable is therefore calculated as follows:

	Period from 1 April 2024 to 31 May 2024	Period from 1 June 2024 to 31 March 2025
	£	£
Taxable trading profits	15,000	130,000
Less:		
Losses c/f	(15,000)	
Revised taxable trading profits	<hr/> 0 <hr/>	<hr/> 130,000 <hr/>
Corporation tax	£130,000 @ 25%	32,500
	Less: Marginal relief $3/200 \times (£250,000 -$ $£130,000)$	<hr/> (1,800) <hr/>
	Corporation tax liability	<hr/> 30,700 <hr/>

Due date of corporation tax payment – 1 January 2026

Ginos Ltd will have blocked trading losses of £40,000 (£55,000 - £15,000). These will be blocked from being carried forward after 31 May 2024. There is no time limit on this and so losses are blocked forever.

MARKING GUIDE

TOPIC	MARKS
Part 1- Explain implications of change in ownership:	
Identify anti-avoidance rules	0.5
Explain circumstances when a change in ownership applies	1
Identify that gift to daughter is no a change in ownership	0.5
Identify shareholding as at 1 June 2024	0.5
Apply rules to Lucy and Russell's shares	1
Discussion of rules relating to major change	0.5
Reference legislation	1
Discuss SP/91 and what does not constitute a major change	1
Case law reference	0.5
Change of menu not a major change	0.5
Redundancies not a major change	0.5
Conversion to wine bar is a major change	0.5
Discussion of time period under review	1
Small changes over time can be major changes	0.5
No time limit/losses blocked forever	0.5
SUB TOTAL	10
Part 2 – Calculate post change profits	
Explain that if anti-avoidance rules apply that losses are blocked on post-change profits	0.5
Identify date of change in ownership	0.5
Split profits correctly between pre and post change of ownership	1
Offset losses against pre-change profits only	0.5
Calculate revised profit before tax	0.5
Calculation of CT	1
Due date	0.5
Calculation of blocked losses	0.5
SUB TOTAL	5
TOTAL	15

Answer 6

Limited company vs sole trader

Trading through a limited company

	Note	£
Accounting profits		80,000
Add:		
RDEC	1	7,000
Less:		
Salary		(12,570)
Employer's NIC on salary	2	(688)
Additional accountancy fees		(750)
Taxable profits		<u>72,992</u>
Corporation tax	3	<u>(9,217)</u>
Retained profits to distribute as a dividend		<u><u>63,775</u></u>

Workings:

1. RDEC

Qualifying expenditure

	Salary	Employer NIC (1)	Employer pension contributions	Total	%	Qualifying costs
	£	£	£	£		£
Peter	12,570	688	0	13,258	50	6,629
Ellen	47,600	5,522	3,620	56,742	50	<u>28,371</u>
						35,000

(1) $(£47,600 - (£9,100 \times 10/12)) \times 13.8\% = £5,522$. The employer NIC on Peter's salary is calculated below.

(2) The testing costs will not qualify for relief as the work could be carried out in the UK but is not.

RDEC – $20\% \times £35,000 = £7,000$

2. Employer's NIC – $(£12,570 - (£9,100 \times 10/12)) \times 13.8\% = £688$ (10/12 due to short period)

3. Corporation tax – $£72,992 \times 25\% - (((£250,000 \times 10/12) - £72,992) \times 3/200) - £7,000$ (RDEC) (10/12 due to short period)

	Non-Savings £	Dividends £	
Income	12,570	63,775	
Personal allowance	(12,570)		
Taxable income	<u>0</u>	<u>63,775</u>	
Tax:			
	£		£
Dividend allowance	500	0%	0
Dividends - basic rate	<u>37,200</u>	8.75%	<u>3,255</u>
	37,700		
Dividends - higher rate	<u>26,075</u>	33.75%	<u>8,800</u>
	<u>63,775</u>		<u>12,055</u>
Class 1 NIC:			
	£		£
Primary threshold (10/12 x £12,570)	10,475	0%	0
Main rate	<u>2,095</u>	8%	<u>168</u>
			<u>168</u>
	£		
Salary	12,570		
Dividends	63,775		
Less: income tax	(12,055)		
Less: Class 1 NIC	<u>(168)</u>		
After-tax position	<u>64,122</u>		

Trading as a sole trader

	Non-Savings £		
Income	80,000		
Personal allowance	<u>(12,570)</u>		
Taxable income	<u>67,430</u>		
Tax:			
	£		£
Basic rate	37,700	20%	7,540
Higher rate	<u>29,730</u>	40%	<u>11,892</u>
	<u>67,430</u>		<u>19,432</u>
Class 4 NIC:			
	£		£
Basic rate	37,700	6%	2,262
Higher rate	<u>29,730</u>	2%	<u>595</u>
	<u>67,430</u>		<u>2,857</u>
	£		
Accounting profits	80,000		
Less: income tax	(19,432)		
Less: Class 4 NIC	<u>(2,857)</u>		
After-tax position	<u>57,711</u>		

Operating as a limited company would provide the best after-tax position, by £6,411 (£64,122 - £57,711).

Benefits of operating via a limited company

Trading through a limited company offers protection from personal liability for Peter. A sole trader has unlimited liability for the debts of the business, whereas a shareholder generally only stands to lose the amount that they have invested in the company.

Limited companies generally pay corporation tax nine months and one day after the end of their accounting period. However, a sole trader is likely to have to make payments on account of each year's tax and Class 4 NIC liability on 31 January during the tax year and 31 July following the end of the tax year. This would be a cash flow disadvantage for Peter.

Profits can be extracted from limited companies efficiently for Peter's personal tax situation, whereas all of the profits of a sole trader are taxable on Peter in the year in which they are earned.

Enhanced tax relief for qualifying R&D expenditure is only available to companies. If Peter expects this to recur in future years, trading through a limited company is likely to produce a better after-tax result than being a sole trader, due to the availability of the relief.

Carrying on business through a limited company offers the opportunity to use the various risk capital schemes (EIS, SEIS), which are not available to sole traders, or simply to issue additional shares in the company.

MARKING GUIDE

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<i>Company:</i>	
Deduct salary and fees	0.5
RDEC	2.5
Calculate and deduct employer's NIC	1
Calculate and deduct corporation tax	2
Calculate amount available to distribute	0.5
Personal allowance	0.5
Income tax calculation	2.5
Primary Class 1 NIC calculation	1
After-tax position	0.5
<i>Sole trader:</i>	
Personal allowance	0.5
Income tax calculation	1.5
Class 4 NIC calculation	1.5
After-tax position	0.5
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Limited liability	0.5
Tax payment profile	1
Profit extraction	1
Availability of R&D tax relief	1
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