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# **Taxation I**

## **Northern Ireland**

1<sup>st</sup> Year Examination

**August 2011**

**Paper, Solutions & Examiner's Report**



### NOTES TO USERS ABOUT THESE SOLUTIONS

The solutions in this document are published by Accounting Technicians Ireland. They are intended to provide guidance to students and their teachers regarding possible answers to questions in our examinations.

Although they are published by us, we do not necessarily endorse these solutions or agree with the views expressed by their authors.

There are often many possible approaches to the solution of questions in professional examinations. It should not be assumed that the approach adopted in these solutions is the ideal or the one preferred by us. Alternative answers will be marked on their own merits.

This publication is intended to serve as an educational aid. For this reason, the published solutions will often be significantly longer than would be expected of a candidate in an examination. This will be particularly the case where discursive answers are involved.

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## **Accounting Technicians Ireland**

**1<sup>st</sup> Year Examination : Autumn 2011**

**Paper : TAXATION I (Northern Ireland)**

Thursday 18<sup>th</sup> August 2011 : 9.30 a.m. to 12.30 p.m.

### **INSTRUCTIONS TO CANDIDATES**

#### **PLEASE READ CAREFULLY**

**For candidates answering in accordance with the law and practice of Northern Ireland.**

**Candidates should answer the paper in accordance with the appropriate provisions up to and including the Finance Act 2010. The provisions of the Finance Act 2011 should be ignored.**

**Allowances and rates of taxation to be used by candidates are set out in a separate booklet supplied with the examination paper.**

**Answer ALL THREE QUESTIONS in Section A, and ANY TWO of the THREE questions in Section B. If more than TWO questions are answered in Section B, then only the first two questions, in the order filed, will be corrected.**

**Candidates should allocate their time carefully.**

**All workings should be shown.**

**All figures should be labelled as appropriate e.g. £s, units etc.**

**Answers should be illustrated with examples, where appropriate.**

**Question 1 begins on Page 2 overleaf.**

**The following insert is enclosed with the paper:**

- **Tax Reference Material**
- **Form P11 (3 copies) (QUESTION 5)**

**SECTION A****Answer ALL THREE questions in this Section****QUESTION 1** (*Compulsory*)

Manus owns and runs 'Flamin' Hot', a business specialising in natural gas heating appliances. Manus is registered for VAT and all figures included in his accounts are net of VAT unless where otherwise stated. He operates out of rented premises in Ballymena and lives in an apartment above his shop. The following is his profit & loss account for the year to 31<sup>st</sup> December 2010.

**Income**

	£	£
Sales		841,791
Building Society Interest Received (1).....	600	
Dividends Received (1).....	<u>1,388</u>	<u>1,988</u>
<b>Gross Profit</b>		<b>843,779</b>
<b>Less: Expenses</b>		
Salaries (2).....	228,824	
Rates & Insurance (3).....	4,222	
Light & Heat (4).....	2,420	
Telephone (5).....	1,079	
Depreciation.....	1,600	
Legal & Professional (6).....	3,742	
Car Expenses (7).....	7,164	
Repairs	8,437	
(8).....		
Loan Repayments (9).....	1,661	
Miscellaneous (10).....	5,251	
Bad Debts (11).....	522	
Rent	<u>18,000</u>	<u>(282,922)</u>
(12).....		
<b>Net Profit</b>		<b><u>560,857</u></b>

£

**QUESTION  
1 (Cont'd)**

Note

**1** The interest relates to amounts received on a joint account held by Manus and his wife Jayne.

The dividends are amounts of dividends received on holdings of UK & foreign shares in Manus' name only.

**2** **Salaries**

Management salary taken by Manus.....	63,500
Staff salaries.....	90,000
Staff wages.....	48,000
Staff related NIC & pension costs.....	27,324
	<u>228,824</u>

Salaries include a payment of £12,500 to his wife Jayne who works in an administrative capacity for Manus.

**3**

**Rates & Insurance**

Rates (whole of the property).....	2,203
Keyman insurance for Manus.....	950
Business related insurance.....	700
Private dwelling contents insurance.....	369
	<u>4,222</u>

Manus lives in an apartment above the shop and it has been agreed with HMRC that the flat makes up 30% of the whole property.

**4**

The **light & heat** expense is broken down as follows:

Electricity.....	895
Oil.....	<u>1,525</u>
	<u>2,420</u>

Manus uses the same boiler to heat the entire building and has only one electricity meter for the whole building.

**QUESTION 1 (Cont'd)**

- 5** Manus estimates that 80% of **telephone** calls are business related.
- 6** **Legal & Professional**
- |   |              |
|---|--------------|
| Accountancy (Including VAT, drawing up accounts).....                 | £<br>1,410   |
| Accountancy (Including VAT, preparation of tax return).....           | 376          |
| Legal advice re: rental agreement with landlord (whole building)..... | 528          |
| Legal advice re: debt collection.....                                 | 1,428        |
|   | <u>3,742</u> |
- 7** Starting November 2009, Manus leased a Ford Galaxy with an official CO<sub>2</sub> emissions rating of 174 grams/km. The car expense is broken down as follows.
- |                    |              |
|--------------------|--------------|
| Lease charges..... | £<br>3,264   |
| Fuel.....          | <u>3,900</u> |
|                    | <u>7,164</u> |
- Manus estimates that the car is used 75% for business purposes.
- 8** **Repairs** related to sundry equipment and repairing damage to the entire building after a plumbing leak which had caused extensive water damage. The expense is broken down as follows:
- |                                     |              |
|-------------------------------------|--------------|
| Repair to equipment before use..... | £<br>517     |
| Repairs to the building.....        | 6,850        |
| Sundry general repairs.....         | <u>1,070</u> |
|                                     | <u>8,437</u> |
- 9** **Loan repayments** relate to repayments on a loan Manus had taken out to buy some new equipment and are made up as per the following:
- |                         |              |
|-------------------------|--------------|
| Capital repayments..... | £<br>719     |
| Interest.....           | <u>942</u>   |
|                         | <u>1,661</u> |

<b>10</b>	<b>Miscellaneous</b> expenses are made up as follows:	£
	Entertainment (see note below).....	2,300
	Gifts (see note below).....	1,225
	Fines (parking fines).....	190
	Gym membership for Manus & Jayne.....	<u>1,536</u>
		<u>5,251</u>

The entertainment expense referred to above, is made up of customer entertainment of £475 with the balance being the cost of the Christmas staff party. Similarly, the expense of the gifts relate to gifts to customers (£700, carrying a prominent business logo), gifts to two different employees, one for long service (£40) and the other on the occasion of their marriage (£35) and the balance being gift aid payments by Manus to a local charity.

<b>11</b>	<b>Bad Debts</b>	£
	Increase in general provision.....	75
	Specific provision created.....	252
	Debt to employee written off.....	<u>195</u>
		<u>522</u>

**12** The rent expense relates to payments made by Manus to his landlord, from whom Manus had leased the entire building in September 2003. Manus is responsible for repairs under the terms of the lease and his rent for the building is at the rate of £1,500 per month. He had only made eleven payments to his landlord in the year to 31<sup>st</sup> December 2010. Manus accrued for the twelfth month in his accounts.

**Required**

Show the adjusted profits computation for Manus for the year ended 31<sup>st</sup> December 2010.

**Total 20 Marks**

**QUESTION 2 (Compulsory)**

Sean (70) and Aoife (68) are married and live in Belfast. They would always jokingly express the sentiment that they are looking forward to retirement as they manage to keep themselves very busy indeed.

In Sean's professional life he practised as an accountant and still maintains a portfolio of clients for whom he performs a range of accounting and tax related services. During 2010/11 his fee income from these clients and related expenses was as follows:

Billed	£19,479
Income.....	
Administrative Expenses (paper, toner, filing expenses).....	£317

Sean has a home broadband facility that he uses for online filing of client's tax returns and maintenance of email accounts for business purposes, as well as for general personal use. Sean's home broadband cost is £180 per annum and he estimates that 80% of this relates to private use.

Sean converted a room in his house for use as a home office and estimated that the office occupies approximately 25% of the physical space of their dwelling. Sean also keeps meticulous records of household expenditure which reveals the following expenditure:

Heating (Oil).....	£1,750
Electricity.....	£819
Rates.....	£1,950
Insurance.....	£380
Secure filing cabinet for office.....	£560
New Desk & assorted office furniture.....	£1,200

Sean keeps equally meticulous records relating to vehicle expenditure which shows the following:

Road tax.....	£180
Insurance.....	£420
Fuel.....	£2,450
Servicing.....	£520
Parts.....	£200

Sean estimates that 10% of the use of his vehicle is business related.

Sean's other income and relevant outgoings for 2010/11 consisted of the following

State	£4,680
pension.....	
Private	£11,489 Gross (PAYE deduction
pension.....	£1,239)
Bank interest	£608
received.....	
Dividends received from UK companies.....	£765
Gift aid payments	£5,652
(net).....	

**QUESTION 2** (Cont'd)

Aoife is a registered childminder and, while having slowed down in recent years, still looks after a few children each day, including their grandchildren on two days each week. The parents of these children often use the childcare voucher system in order to make payments directly to Aoife's bank account. During 2010/11 this income came to a total of £9,360. During the year Aoife estimated that she had spent the following sums relating to this activity:

Fee to childminding association.....	£400
Re-registration fee including insurance.....	£620
Sundry items of expenditure (food, disposables etc.)...	£215

Even though the childminding activity takes place in their home, Aoife elected not to claim a deduction against income for a percentage of household expenses. Aoife also owns a small investment portfolio bequeathed to her many years ago which produces the following income:

State pension.....	£4,680
Building society interest received.....	£240
Gross dividends in connection with ownership of shares in UK companies.....	£1,100
3 ½ % war loan.....	£180

**Required**

Calculate taxable income for both Sean & Aoife and complete income tax computations for both of Sean and Aoife, showing clearly the total tax liability and the balance of any income tax due, if any, for the tax year ended 5 April 2011.

**Total 20 Marks**

**QUESTION 3** (*Compulsory*)

Michael, a close acquaintance of yours, has a son, Gerry, who is about to graduate with the expectation of receiving a very good degree. Gerry currently holds some job offers secured through the university 'milk-round' but has a desire to be self employed which is a realistic proposition with his father's financial backing.

The potential employment prospects are UK based and offer packages which consist of a mixture of salaries, potential bonuses & commissions and benefits such as company cars, training courses and financial help with relocation and, if necessary, the offer of company provided accommodation until Gerry finds somewhere to live.

**Required**

Outline for Gerry how the system of UK income tax would operate on such an employment package as outlined above and paying particular respect to:

- What is considered to be income from employment and what would it actually consist of?
- How all relevant income from employment would be taxed and when would the tax be paid?
- What class or classes of National Insurance Contributions would Gerry pay on employment earnings and how would this be collected?
- What (taxable) deductions would be available for Gerry from his income as an employee?
- How would Gerry's tax position and obligations differ if he were to go into business in his own right? Would he have any initial or ongoing administrative obligations? On what would his tax liabilities be based and when would any such liabilities be payable?
- Would Gerry have to worry about VAT if he were in business on his own right?

**Total 20 Marks**

**SECTION B****Answer ANY TWO of the three questions****QUESTION 4****(a)**

EDECOR Ltd. is a VAT registered business involved in construction. Despite the economic slowdown, they have managed to keep the business going by concentrating on public sector 'build & refit' capital projects which are now a much more significant part of the business than construction of new residential properties.

Through their widespread involvement with subcontractors, EDECOR Ltd. became involved in acting as a broker for insurance policies sold to their subcontractors and this has now become a significant, albeit relatively small, part of their business.

Results for the two most recent quarters, exclusive of VAT, are as follows:

<b>VAT Status of Supply</b>	<b>Supply</b>	<b>Q/E 30/9/10</b>	<b>Q/E 31/12/10</b>
Zero Rated	Value of sales of new residential properties	£785,000	£329,000
Standard Rated	Value of 'milestone' payments re: 'build & refit' capital projects	£4,800,500	£1,800,500
Exempt	Value of supply of insurance policies.	£246,000	£115,457

Input tax attributable to supplies for these quarters is given as follows:

<b>Re: supply of:</b>	<b>Q/E 30/9/10</b>	<b>Q/E 31/12/10</b>
Residential properties	£98,000	£38,000
Milestone payments	£363,929	£91,473
Insurance	£13,071	£513
Unattributable	£211,005	£21,020

**Required**

Calculate the total amount of recoverable input tax for EDECOR Ltd for both quarters ended 30/9/10 and 31/12/10 showing clearly all workings.

**10 Marks****(b)**

LOYAR Ltd is a VAT registered business (accounting for VAT on an invoice basis) and, in common with many businesses, is suffering as a consequence of the economic downturn and is very worried about cash-flow for the business. They are particularly worried about the effect that any cash-flow difficulties may have on their ability to make quarterly VAT payments on time. They have asked you to briefly outline the operation of the cash and annual accounting schemes for VAT.

**Required**

Write to LOYAR Ltd outlining the schemes as they have requested, noting how the schemes may be of benefit to them and making them aware of any other salient points with respect to their eligibility for such schemes.

**10 Marks**  
**Total 20 Marks**

**QUESTION 5**

Andy, Eoin & Nuala (managing director) are on the board of a small but profitable local company, FISCAL Ltd. They outsource many functions for the company and you have been awarded the contract to prepare their monthly executive payroll. For month 9 of 2010/11 you have been given the following information;

	<b>Andy</b>	<b>Eoin</b>	<b>Nuala</b>
Cumulative Salary to Month 9	£41,950	-	£83,996
Company Pension Contributions	5%	-	5%
Tax Code	578L	-	K452
Cumulative Tax Paid to Month 9	£8,388	-	£27,667
Salary Month 10	£4,675	£4,175	£8,215
Salary Month 11	£4,600	£4,205	£8,300

Eoin has just recently joined the company from a public sector body and you do not, at the time of preparation of the payroll for either month, have a copy of his most recent P45.

**Required**

Complete all relevant sections of form P11 for each of the directors for months 10 and 11 of 2010/11, showing all your workings.

**Total 20 Marks**

**QUESTION 6****(a)**

Hermione has been trading for many years, making up accounts to 31 December each year. Her recent adjusted profits have been:

<b>Year Ended</b>	<b>£</b>
31 December 2008	31,900
31 December 2009	51,000
31 December 2010	81,500

What are Hermione's assessable profits for 2010/11? Explain your answer.

**2 Marks****(b)**

Harold, who has been trading for many years making up accounts to 31 January, ceased to trade on 30 September 2010. His recent results have been as follows:

<b>Accounting Period</b>	<b>Adjusted Profit (£)</b>
Year ended 31 January 2010	43,294
Period ended 30 September 2010	24,975

Harold has overlap profits carried forward from the commencement of his business of £7,397. What will be the assessment to income tax in respect of his income from self-employment in Harold's final year of assessment?

**2 Marks****(c)**

Jonathan has recently commenced business (1 October 2007) with following results:

<b>Accounting Period</b>	<b>Assessable Profits (£)</b>
Period ended 31 December 2008	27,510
Year Ended 31 December 2009	23,839
Year Ended 31 December 2010	31,734

Show Jonathan's assessments to income tax for all relevant years on the commencement of his business.

**5 Marks****(d)**

Miriam is self-employed and has earnings, adjusted for income tax purposes and net of capital allowances, of £51,820 for 2010/11.

Calculate Miriam's liability to Class 2 and Class 4 National Insurance Contributions for 2010/11 and state when these must be paid.

**4 Marks**

**QUESTION 6** (*Cont'd*)**(e)**

Jo, a self employed friend of yours, employs a number of staff, one of whom she provides with a Saab 9-3 TTiD with a list price of £21,995 and CO<sub>2</sub> emissions of 119 grams/km. Jo also provides this staff member with all fuel although she does require a contribution from them of £30 per week to go towards the cost of privately consumed diesel.

As an employer, calculate the class 1A NIC cost to Jo's business in connection with the supply of the above benefits.

**5 Marks****(f)**

Another self-employed friend of yours, Bill, is making a member of staff redundant. The staff member will receive £18,750 as a redundancy payment. How much Class 1 NIC (primary & secondary) will Bill have to deduct from this redundancy payment to the staff member?

**2 Marks****Total 20 Marks**

●

# 1st Year Examination: August 2011

## Taxation I NI

### Suggested Solutions

**Students please note:** These are suggested solutions only; alternative answers may also be deemed to be correct and will be marked on their own merits.

#### Suggested Solution 1

#### Adjusted Profits for Manus for Year Ended 31st December 2010

<b>Net Profits per Accounts</b>		£	560,857.00
<b>Add: Disallowed Expenses</b>			
Management Salary		£	63,500.00
Rates & Insurance	£2,203 x 30%	£	661.00
Keyman Insurance		£	950.00
Private Insurance		£	369.00
Light & Heat	£2,420 x 30%	£	726.00
Telephone	£1,079 x 20%	£	216.00
Depreciation		£	1,600.00
Accountancy - VAT element		£	210.00
Accountancy - prep tax return		£	376.00
Legal fees re private portion of lease (30%)		£	158.00
Car - lease	£3,264 x 15%	£	490.00
	£3,264 x 85% x		
Car - lease	25%	£	694.00
Car - fuel	£3,900 x 25%	£	975.00
Repair before use		£	517.00
Repairs to building	£6,850 x 30%	£	2,055.00
Capital element of loan repayments		£	719.00
Customer entertainment		£	475.00
Charitable donation		£	450.00
Parking Fines		£	190.00
Private club membership	Manus' half	£	768.00
Increase in general provision		£	75.00
Rent re: private dwelling	£18,000 x 30%	£	5,400.00
		£	81,574.00

#### Suggested Solution 1

*(Cont'd)*

**Less: Non-trading Income**

Building society Interest

£ 600.00

Dividends

£ 1,388.00

-£ 1,988.00

**Adjusted Profits**

£ 640,443.00

<b>W1</b>	<b>Sean's Income from self employment 2010/11</b>		
	<b>Billed Income</b>		£ 19,479.00
	<b>Less: Allowable Expenditure</b>		
	Administrative Expenses	£ 317.00	
	£180 x		
	Broadband	£ 36.00	
	Household		
	Expenses	£(1,750+819+1,950+380) x 25%	£ 1,225.00
	Car	£(180+420+2,450+520+200) x 10%	£ 377.00
			<u>-£ 1,955.00</u>
	<b>Net Income from self employment</b>		<u>£ 17,524.00</u>
<b>W2</b>	State Pension	£ 4,680.00	
	Private Pension	£ 11,489.00	
	Bank Interest	£608 x 100/80	£ 760.00
	Dividends	£765 x 100/90	<u>£ 850.00</u>
			<u>£ 17,779.00</u>
<b>W3</b>	Gift Aid	£5,652 x 100/80	£ 7,065.00
<b>W4</b>	Income from self employment (W1)	£ 17,524.00	
	Other Income		
	(W2)	£ 17,779.00	
	Gift aid Payments (W3)	<u>-£ 7,065.00</u>	
		£ 28,238.00	
	Earnings Threshold	<u>£ 22,900.00</u>	
	Excess	<u>£ 5,338.00</u>	
	1/2 Excess	<u>£ 2,669.00</u>	
<b>W5</b>	PAA (65-74)	£ 9,490.00	
	Less: Excess (W4)	<u>-£ 2,669.00</u>	
	PAA (restricted)	<u>£ 6,821.00</u>	

**Income Tax computation for Sean 2010/11**

Income from self employment (W1)	£ 17,524.00		
State Pension (W2)	£ 4,680.00		
Private Pension (W2)	£ 11,489.00		
Bank Interest (W2)		<u>£ 760.00</u>	
Dividends (W2)		<u>£ 850.00</u>	
PAA (restricted W5)	<u>-£ 6,821.00</u>		
Taxable Income	<u>£ 26,872.00</u>	<u>£ 760.00</u>	<u>£ 850.00</u>

**Suggested Solution 2**



**Suggested Solution 3**

Answer to include the following points:

- Pay for income tax purposes includes wages, salaries, commissions, bonuses, tips, perquisites and 'benefits in kind' and less allowable expenses;
- To count as pay, earnings must be in the nature of a reward for services rendered, past, present or future;
- Largely, taxable benefits include use of car or van, provision of fuel, living accommodation, assets, medical insurance, access to loans at a beneficial rate, loans written off amongst other things;
- Allowable expenses are those incurred wholly, exclusively & necessarily in the performance of the duties of that employment although, in practice, this is quite limited;
- Commonly allowable expenses would include qualifying travelling expenses, relevant professional subscriptions, a percentage of household expenses if it is necessary for the employee to work at home, capital allowances & related interest expenses (if they employee is required to purchase equipment, possibly using loan finance)
- All income from employment is taxed through the 'pay as you earn' (PAYE) system, the object of which is to require employers to collect and account for income tax & NIC's on employment income;
- The employer is responsible for calculating & remitting tax and NIC on cash payments for each pay period (weekly, fortnightly, four-weekly or monthly);
- Each employee is issued with a tax code by HMRC and, when applied to the employees earnings, ensures the correct amount of tax is collected;
- PAYE is collected each time an employee is paid & is paid over by the employer to HMRC by 19<sup>th</sup> of the month following (smaller employers may pay on a quarterly basis);
- Gerry would have primary class 1 NIC deducted from his earnings and, as noted above, this would be collected from Gerry's earnings through the PAYE system;
- Pay for the purposes of NIC's is broadly the same as pay for income tax purposes although pension contributions & payroll giving deductions would not be deducted for NIC purposes;
- Should Gerry start his own business, he would be obliged to register for income tax, national insurance contributions and, possibly, VAT;
- Registration with HMRC on commencing self employment must be within three months of commencing self employment;
- Gerry would have to pay class 2 NIC at the rate of £2.40/week (monthly or quarterly payments), Class 4 NIC based on the adjusted profits of his business (see below) and income tax based on these same adjusted profits (not his drawings from the business);
- The adjusted profits are, broadly, the accounting profits of the business with adjustments made for disallowed expenditure (capital expenditure, private expenditure or other expenses specifically disallowed such fines, political or charitable donations etc);
- Class 4 NIC are paid at the rate of 8% on profits from £5,717 up to £43,875 and 1% above this amount;

**Suggested Solution 3** (*Cont'd*)

- Gerry would have to submit a tax return each year (31<sup>st</sup> October following the tax year for paper returns or 31<sup>st</sup> January following the tax year for electronic returns);
- Gerry would have to (probably) make payments on account based on the (estimated) liabilities for income tax and class 4 NIC on 31<sup>st</sup> January (before the end of the tax year) & 31<sup>st</sup> July following the end of the tax year with a balancing payment (if any) on 31<sup>st</sup> January following the tax year (with the electronic return);
- Gerry would have to register for VAT if the value of his annual taxable supplies exceeded £70,000 (from 1 April 2010) unless he could demonstrate that the value of his supplies would not exceed £68,000 in the next twelve months;
- Alternatively, Gerry would have to register for VAT (immediately) if he expected the value of his supplies to exceed £70,000 in the next 30 days;
- Failure to register for income tax, NIC or VAT can result in penalties.

**Suggested  
Solution 4**

(a)

**W1 Q/E 30/9/10**

$$\frac{\pounds(785,000+4,800,500)}{\pounds(785,000+4,800,500+246,000)} \times 100 = 95.78153134 = \text{Rounding up } 96\%$$

**W2 Q/E 31/12/10**

$$\frac{\pounds(329,000+1,800,500)}{\pounds(329,000+1,800,500+115,457)} \times 100 = 94.85705071 = \text{Rounding up } 95\%$$

**Q/E 30/9/10****Recoverable Input  
Tax****Recoverable**

		%	Recoverable amount
Re: taxable supplies	£ 98,000.00	100%	£ 98,000.00
	£ 363,929.00	100%	£ 363,929.00
	£ 211,005.00	96%	(W1) <u>£ 202,564.80</u>
			<u>£ 664,493.80</u>

**Non-recoverable Input Tax**

Re: exempt supplies			£ 13,071.00
	£ 211,005.00	less	£ 202,564.80
			<u>£ 8,440.20</u>
			<u>£ 21,511.20</u>

Average non-recoverable input tax:  $\frac{\pounds 21,511.20}{3} = \pounds 7,170.40$

Since the non-recoverable input tax exceeds the de-minimus limit, the recoverable input tax stands at: **£ 664,493.80**

**Q/E 31/12/10****Recoverable Input  
Tax****Recoverable**

		%	Recoverable amount
Re: taxable supplies	£ 38,000.00	100%	£ 38,000.00
	£ 91,473.00	100%	£ 91,473.00
	£ 21,020.00	95%	(W2) <u>£ 19,969.00</u>
			<u>£ 149,442.00</u>

**Suggested Solution 4** (*Cont'd*)**Non-recoverable Input Tax**

Re: exempt supplies			£	513.00
	£ 21,020.00	less	£	19,969.00
			£	<u>1,051.00</u>
			£	<u>1,564.00</u>

		£1,564.00 / 3		
Average non-recoverable input tax:	=		£	<u>521.33</u>

Since the non-recoverable input tax is less than the de-minimus limit (£625 pm), and non-recoverable input tax is not more than 50% of the total, the recoverable input tax is now:

	£	149,442.00
	£	<u>1,564.00</u>
Total recoverable input tax:	£	<u><b>151,006.00</b></u>

(b)

Letter format, with marks awarded for making the following points:

**Cash Accounting Scheme**

- Businesses with a tax exclusive turnover of less than £1.35 million may use the cash accounting system;
- Business must be up to date with their VAT returns;
- Have paid all outstanding VAT (or made arrangements to do so);
- Tax (VAT) invoices still issued but output tax accounted for only when cash received;
- Input tax not recoverable until suppliers paid;
- Certain transactions (HP, advance supplies etc) are excluded from the scheme;
- Cash accounting scheme gives the registered business instant bad debt relief and mitigates all cash flow difficulties associated with making VAT payments;
- Business can leave the scheme voluntarily at the end of any tax period;
- Business must leave the cash accounting scheme if the value of taxable supplies exceeds £1.6 million in a one year period (unless caused by a large, 'one-off' transaction);
- Cash accounting scheme can be used in conjunction with the annual accounting scheme (see below)'

**Annual Accounting Scheme**

- Businesses with an annual tax-exclusive turnover of less than £1.35 million may apply to join the annual accounting scheme;
- Only one VAT return due for an annual period (rather than four – one for each quarter);
- The annual VAT return is due 2 months after the end of the annual period (compared to one month after the end of a normal VAT quarter);
- Businesses registered in this scheme make nine payments on account, equal to one tenth of the estimated liability, during the annual accounting period. When the annual return is made, a balancing payment (or refund claim) is made.
- Once in the annual accounting scheme, businesses must leave if their turnover reaches or exceeds £1.6 million.

**Suggested Solution 5****PAYE Tax Calculations**

	<b>Andy</b>	<b>Eoin</b>	<b>Nuala</b>
<b>Cumulative pay to M9</b>	£ 41,950.00		£ 83,996.00
Pension (5%)	<u>-£ 2,097.50</u>		<u>-£ 4,199.80</u>
	£ 39,852.50		£ 79,796.20
<b>Pay in M10</b>	£ 4,675.00	<u>£ 4,175.00</u>	£ 8,215.00
Pension (5%)	<u>-£ 233.75</u>		<u>-£ 410.75</u>
	£ 4,441.25	£ 4,175.00	£ 7,804.25
<b>Cumulative (net) salary to M10</b>	£ 44,293.75	£ 4,175.00	£ 87,600.45
<b>Free Pay</b>			
£5,789 x 10/12	<u>-£ 4,824.17</u>		
£6,475 x 1/12		<u>-£ 539.58</u>	
<b>Additional Pay</b>			
£4,529 x 10/12			<u>£ 3,774.17</u>
<b>Taxable Pay</b>	<u>£ 39,469.58</u>	<u>£ 3,635.42</u>	<u>£ 91,374.62</u>

**NIC Calculations**

	<b>Andy</b>	<b>Eoin</b>	<b>Nuala</b>
<b>Primary Contributions</b>			
<b>Pay in M10</b>	<u>£ 4,675.00</u>	<u>£ 4,175.00</u>	<u>£ 8,215.00</u>
£(3,656-476) x 11%	£ 349.80	£ 349.80	£ 349.80
£(4,675-3,656) x 1%	<u>£ 10.19</u>		
£(4,175-3,656) x 1%		<u>£ 5.19</u>	
£(8,215-3,656) x 1%			<u>£ 45.59</u>
<b>Total Class 1 Primary</b>	<u>£ 359.99</u>	<u>£ 354.99</u>	<u>£ 395.39</u>
<b>Secondary contributions</b>			
£(4,675-476) x 12.8%	<u>£ 537.47</u>		
£(4,175 - 476) x 12.8%		<u>£ 473.47</u>	
£(8,215 - 476) x 12.8%			<u>£ 990.59</u>
<b>Total Class 1 NIC M10</b>	<u>£ 897.46</u>	<u>£ 828.46</u>	<u>£ 1,385.98</u>

**Suggested Solution 5**  
(Cont'd)

**Taxed as per:**

£37,400 x 10/12 @ 20%	£ 6,233.33		
£(39,469.58 - 31,166.67) @ 40%	<u>£ 3,321.17</u>		
£37,400/12 @ 20%		£ 623.33	
£(3,426.67 - 3,116.67) @ 40%		<u>£ 207.50</u>	
£37,400 x 10/12 @ 20%			£ 6,233.33
£(91,374.62 - 31,166.67) @ 40%			<u>£ 24,083.18</u>
Cumulative Tax to M10	£ 9,554.50	£ 830.83	£ 30,316.51
Cumulative tax due M9	<u>£ 8,388.00</u>		<u>£ 27,667.00</u>
<b>Tax due M10</b>	<b><u>£ 1,166.50</u></b>	<b><u>£ 830.83</u></b>	<b><u>£ 2,649.51</u></b>

<b>Cumulative pay to M10</b>	£ 46,625.00		£ 92,211.00
Pension (5%)	<u>-£ 2,331.25</u>		<u>-£ 4,610.55</u>
	£ 44,293.75		£ 87,600.45

<b>Pay in M11</b>	£ 4,600.00	<u>£ 4,205.00</u>	£ 8,300.00
Pension (5%)	<u>-£ 230.00</u>		<u>-£ 415.00</u>
	£ 4,370.00	£ 4,205.00	£ 7,885.00

<b>Cumulative (net) salary to M11</b>	£ 48,663.75	£ 4,205.00	£ 95,485.45
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**Free Pay**

£5,789 x 11/12	<u>-£ 5,306.58</u>		
£6,475 x 1/12		<u>-£ 539.58</u>	

**Additional Pay**

£4,529 x 11/12			<u>£ 4,151.58</u>
<b>Taxable Pay</b>	<u>£ 43,357.17</u>	<u>£ 3,665.42</u>	<u>£ 99,637.03</u>

**Taxed as per:**

£37,400 x 11/12 @ 20%	£ 6,856.67		
£(43,357.17 - 34,283.33) @ 40%	£ 3,629.53		
£37,400/12 @ 20%		£ 623.33	
£(3,455.17 - 3,116.67) @ 40%		£ 219.50	
£37,400 x 11/12 @ 20%			£ 6,856.67
£(99,637.03 - 34,283.33) @ 40%			<u>£ 26,141.48</u>
Cumulative Tax to M11	£ 10,486.20	£ 842.83	£ 32,998.15
Cumulative tax due M10	<u>£ 9,554.50</u>		<u>£ 30,316.51</u>
<b>Tax due M11</b>	<b><u>£ 931.70</u></b>	<b><u>£ 842.83</u></b>	<b><u>£ 2,681.63</u></b>

**Suggested Solution 5** (Cont'd)**Primary Contributions**

<b>Pay in M11</b>	<u>£ 4,600.00</u>	<u>£ 4,205.00</u>	<u>£ 8,300.00</u>
£(3,656-476) x 11%	£ 349.80	£ 349.80	£ 349.80
£(4,675-3,656) x 1%	<u>£ 9.44</u>		
£(4,175-3,656) x 1%		<u>£ 5.49</u>	
£(8,215-3,656) x 1%			<u>£ 46.44</u>
<b>Total Class 1 Primary</b>	<u>£ 359.24</u>	<u>£ 355.29</u>	<u>£ 396.24</u>
<b>Secondary contributions</b>			
£(4,675-476) x 12.8%	<u>£ 527.87</u>		
£(4,175 - 476) x 12.8%		<u>£ 477.31</u>	
£(8,215 - 476) x 12.8%			<u>£ 1,001.47</u>
<b>Total Class 1 NIC M11</b>	<u>£ 887.11</u>	<u>£ 832.60</u>	<u>£ 1,397.71</u>

**Suggested Solution 6****(a)**

Current year basis of assessment:

Assessable profits are those arising Y/E 31/12/10 **£81,500****(b)****Year of cessation: 2010/11**

Profits unassessed to 2010/11 assessed in year of cessation:

P/E 31/9/10 **£24,975**Less: Overlap profits brought forward **-£7,397**Final assessable profits **£17,578****(c)**

	YOA	Period		Assessment
1st				
YOA	2007/08	1/10/07 - 5/4/08	6/15 x £27,510	£ 11,004.00
	2008/09	1/1/08 - 31/12/08	12/15 x £27,510	£ 22,008.00
	2009/10	Y/E 31/12/09		£ 23,839.00
	2010/11	Y/E 31/12/10		£ 31,374.00

**(d)**

<b>Class 2 NIC</b>	£2.40 x 52 =		£ 124.80
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<b>Class 4 NIC</b>	£(43,875 - 5,715) x 8%	£	3,052.80
	£(51,820 - 43,875) x 1%	<u>£ 79.45</u>	£ 3,132.25

**Class 2 NIC** payable either **monthly** or **quarterly** in arrears.**Class 4 NIC** paid at the same time as the income tax liability (for Miriam this will be by **31/1/12**).**(e)**

Car benefit	£21,995	13%	£2,859.35
Fuel benefit	£18,000	13%	<u>£2,340.00</u>
			<b><u>£5,199.35</u></b>

Class 1A NIC due	£5,199.35	12.80%	<b><u>£665.52</u></b>
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**(f)****None** - an employee's earnings for NIC purposes does not include redundancy pay.

# 1st Year Examination: August 2011

## Taxation I NI

### Examiner's Report

#### General

Given that this was a re-sit session, where the standard of scripts can be poor, the overall standard at this sitting was very creditable indeed with a pass rate (68.3%) which was, effectively, identical to the summer sitting. The average mark achieved by candidates at this sitting (50.3%) was also similar to that at the summer session (52.5%) and these are heartening statistics.

Never-the-less, the number of candidates who present with what is, very obviously, a very unrounded understanding of the syllabus is worrying. Despite the fact that I picked up on this theme for the summer sitting results, I make no apology for the labouring the point again and I can't make this any clearer – it is unacceptable (and courting disaster) for a candidate to present for an examination not having familiarised themselves with all of the aspects of what is, after all, an introductory taxation syllabus with inherently limited scope. Perusal of the distribution of marks across the questions in this autumn paper will make this latter point obvious, indeed, it can be noted that the average mark achieved for exactly half the questions at this sitting was a 'failing' score for the question (ie. less than 50% of the marks achieved).

Note that the average marks for all candidates are given in brackets after the relevant question number.

#### Question 1 (12)

This was a very standard 'adjusted profits' style of question with which most candidates are relatively comfortable although this was only (marginally) the third best answered question at this sitting. Marks are invariably lost for simple lack of preparedness, relevant knowledge or carelessness. Some mistakes presented at this sitting included omitting an obvious add-back (getting the add-back for disallowed expenses and the deduction for non-trading income the wrong way around), getting confused with basic rules (allowing the capital element of loan repayments but disallowing interest) or, the omnipresent bug-bear – attempting to answer the question in a non-standard form by reconstructing the profit & loss account.

#### Question 2 (13.5)

This question required candidates to perform relatively basic income tax computations for an older couple with a straight-forward range of incomes. Prepared & grounded candidates invariably did well in this question (it was the best answered question at this sitting) although the mistakes by some of the poorer candidates were bewildering. For example:

- Assuming that Sean's deductible expenses against his self-employed income were in fact taxable benefits (despite it being very obvious that Sean was not an employee)
- Not restricting PAA for relevant income in excess of the earnings threshold
- Deducting a MCAA (despite neither Sean or Aoife being born on or before 5<sup>th</sup> April 1935)
- Adding gift aid to PAA
- Treating Sean's private pension as a payment into a scheme (despite it being clear that Sean was 70 years old) to be grossed up and used to extend his basic rate band
- Trying to make an issue that Aoife was a P11D employee!
- Apparently not having an understanding as to how to put an income tax computation together

### **Question 3 (8)**

Taking some heart in answers to this question, I can note that the narrative question was not at this sitting, as is usually the case, the worst answered question. Nevertheless, the general standard of answers was poor and the standard of written English often leaves much to be desired. Candidates must grasp the fact that they are studying taxation which often requires them to articulate their understanding of the subject matter and not just become automatons in repeatedly performing some routine computations!

### **Question 4 (2.2)**

This question was, by a very large margin, the least popular of the optional questions at this sitting. One need only consider the average score for this question to gain some understanding of the performance of candidates at this sitting who *had* attempted it. Not a single candidate realised that part (a) of the question was, in fact, an exercise in partial exemption and, while some candidates presented some relevant knowledge of the cash accounting scheme, no-one discussed the annual accounting scheme at all.

### **Question 5 (12.6)**

This was a well answered question, payroll calculations being one of the 'stock' questions on this examination. Where candidates lost marks, it invariably came from getting horribly confused in the calculations or not realising that Eoin should be taxed on a month 1 basis *for both months*. As long as candidates familiarise themselves with the performance of payroll calculations they will score well in questions of this nature.

### **Question 6 (8.9)**

Given that question 4 was so unpopular, it wasn't surprising that this question was chosen by the vast majority of candidates. It was surprising that this question wasn't very well answered given that it involved some very simple short-form questions or calculations. Under-pinning the apparent lack of rounded knowledge in poorer performing candidates, some answers displayed confusion with relevant knowledge in answering virtually all of parts (a)-(f). This examination will continue, as it must, to examine all aspects of the syllabus and to be successful, exam candidates must grasp this simple truth!