

## 31 Paul and Palu Ltd (March/June 2021 amended)

18 mins

This scenario relates to one requirement.

You should assume that today's date is 15 March 2021.

Paul is the managing director of, and 100% shareholder in, Palu Ltd.

For the year ended 5 April 2022, Palu Ltd's tax adjusted trading profit, before taking account of director's remuneration, is forecast to be £175,000. Paul intends to extract all of Palu Ltd's profits (after allowing for corporation tax). This will be achieved by paying himself gross director's remuneration of £8,000 and dividends of £135,270.

Paul wants to know if it would be beneficial to cease trading via Palu Ltd on 5 April 2021, and instead run his business from 6 April 2021 onwards as a sole trader. His tax adjusted trading profit for the year ended 5 April 2022 would remain unchanged at £175,000.

Paul will not have any other income for the tax year 2021/22.

*Required*

Determine whether or not there will be an overall saving of tax and national insurance contributions (NICs) for the year ended 5 April 2022 if Palu Ltd's business is instead run by Paul as a sole trader from 6 April 2021. (10 marks)

### Notes

- 1 You are expected to calculate the income tax payable by Paul, any NICs payable by Paul and Palu Ltd, and the corporation tax liability of Palu Ltd for the year ended 5 April 2022 assuming that he continues to run the business via the company.
- 2 You should then compare this total amount with the income tax and NICs payable by Paul assuming that he runs the business as a sole trader.
- 3 You should assume that the rate of corporation tax remains unchanged.

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(Total = 10 marks)

## 32 Alfred and Amaia (March/June 2021 amended)

27 mins

This scenario relates to two requirements.

Alfred and Amaia are a married couple.

### Alfred

Alfred commenced trading as a sole trader on 1 September 2021. He prepared his first set of accounts for the seven month period ended 31 March 2022, and his draft tax adjusted trading profit before capital allowances was £63,000.

The draft tax adjusted trading profit is **before** adjusting for any deductions arising from the following:

- (1) £5,000 incurred during January and February 2021 on a marketing campaign for his business.
- (2) A premium of £30,000 paid on 1 September 2021 to acquire a ten-year lease on a workshop used for trade purposes.
- (3) Cost of a golf day on 31 March 2022 for a group of Alfred's largest clients totalling £1,000.
- (4) Expenditure of £116,000 on 1 September 2021 for plant and equipment.
- (5) The purchase of a motor car on 15 December 2021 for £24,000. The motor car has a CO<sub>2</sub> emissions rate of 24 grams per kilometre, and is used by Alfred's employee.

### Amaia

Amaia is employed by Argole Ltd and her remuneration package comprises:

- (1) A gross annual salary of £80,000.
- (2) From 1 January 2022, Argole Ltd provided Amaia with a petrol powered company motor car. The motor car had a list price of £25,000, although Argole Ltd received a discount and only paid £23,500. The motor car has a CO<sub>2</sub> emissions rate of 52 grams per kilometre. Argole Ltd did not provide any fuel for Amaia's private use.
- (3) Since 6 April 2019 Argole Ltd has provided Amaia with living accommodation which qualifies as job-related accommodation. The annual value of the property is £23,000 and Argole Ltd pays rent of £2,500 per month.

Argole Ltd deducted income tax under PAYE of £19,240 from Amaia's salary during the tax year 2021-22.

Since 6 April 2019 Amaia has let out her own house unfurnished at a rent of £1,200 per month. Amaia received 13 months' rent during the tax year 2021/22. Amaia has a mortgage which she took out to acquire the house, and in the tax year 2021/22 she made mortgage payments of £6,000, including interest of £2,600.

On 1 December 2020, Amaia paid an insurance premium of £800 for the house in respect of the year ended 31 December 2021. Then on 1 December 2021, she paid an insurance premium of £1,250 for the year ended 31 December 2022.

### Required

- (a) Calculate Alfred's revised tax adjusted trading profit or loss for the seven month period ended 31 March 2022. **(6 marks)**

### Notes

- 1 Your computation should commence with the draft tax adjusted trading profit of £63,000 and list all of the items referred to in notes (1) to (5), indicating with the use of zero (0) any items which do not require adjustment.
- 2 You should assume Alfred claims the maximum amount of capital allowances.

- (b) Calculate the income tax payable by Amaia for the tax year 2021-22. **(9 marks)**

**Note:** Your computation should list all of the items referred to in the scenario, indicating with the use of zero (0) any items which are not taxable.

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(Total = 15 marks)

## 33 Mooncake Ltd (March/June 2021 amended) 27 mins

This scenario relates to four requirements.

Mooncake Ltd reported an operating loss of £93,820 in its statement of profit or loss for the year ended 31 March 2022 as follows:

	Note	£
Revenue		184,550
Operating expenses		
- Depreciation		(7,230)
- Leasing costs	1	(6,380)
- Other expenses	2	(264,760)
Operating loss		(93,820)

### Note 1 - Leasing costs

Leasing costs are as follows:

	£
Lease of office equipment	2,980
Lease of motor car with CO <sub>2</sub> emissions of 65 grams per kilometre	3,400
	6,380

### Note 2 – Other expenses

Other expenses are as follows:

	£
Entertaining staff (cost of £160 per head)	4,320
Entertaining overseas customers	8,720
Qualifying charitable donations	1,600
Balance of expenditure (all allowable)	250,120
	264,760

### Additional information

#### Plant and machinery

On 1 April 2021, the tax written down value of the main pool was £43,200.

The following vehicles were sold during the year ended 31 March 2022:

	Date of sale	Proceeds £	Original cost £
Delivery van	12 April 2021	11,800	14,700
Motor car [1]	13 August 2021	8,400	8,100
Motor car [2]	9 March 2022	5,300	12,200

The original cost of motor car [1] had previously been added to the main pool. The original cost of motor car [2] qualified for a 100% first year allowance.

#### Property business loss

Mooncake Ltd has a property business loss of £4,400 for the year ended 31 March 2022.

#### Profit on disposal of shares

Mooncake Ltd made a profit on disposal of shares of £3,700 in respect of a 1% shareholding which was sold on 8 November 2021. This profit on disposal is calculated as disposal proceeds of £34,200 less cost of £30,500. The indexation allowance is £6,700.

### Results for the year ended 31 March 2021

Mooncake Ltd's results for the year ended 31 March 2021 were:

	£
Trading profit	138,200
Property business income	23,700
Capital loss	(4,900)
Qualifying charitable donations	(1,400)

#### Required

- (a) State the factors which will influence a company's choice of loss relief claims. **(2 marks)**
- (b) Calculate Mooncake Ltd's tax adjusted trading loss for the year ended 31 March 2022. **(7 marks)**

#### Notes

- 1 Your computation should commence with the operating loss figure of £93,820, and should indicate by the use of zero (0) any items which do not require adjustment.
  - 2 You should assume that the company claims the maximum available capital allowances.
- (c) Assuming that Mooncake Ltd wishes to claim relief for its losses as early as possible:
- (i) Calculate the company's corporation tax liabilities for each of the years ended 31 March 2021 and 31 March 2022. **(4 marks)**
  - (ii) Calculate the amount of unused losses or payments which Mooncake Ltd can carry forward to be utilised in the year ending 31 March 2023. **(2 marks)**

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**(Total = 15 marks)**

## Section C

### 31 Paul and Palu Ltd (March/June 2021)

#### Marking scheme

	Marks
<b>Business run as limited company</b>	
(1) Trading profit	½
Director's remuneration	½
Corporation tax at 19%	½
(2) <b>Income tax</b>	
Director's remuneration	½
Dividend income	½
Personal allowance	½
Income tax at 20%	½
Income tax at 0% (dividend)	½
Income tax at 7.5%	½
Income tax at 32.5%	½
(3) No Class 1 NIC as below threshold	½
<b>Business run as a sole trader</b>	
(1) Taxable income	½
Income tax at 20%	½
Income tax at 40%	½
Income tax at 45%	½
(2) Class 2 NIC	½
(3) Class 4 NIC	1
Conclusion	1
	<u>10</u>

#### Business run as a limited company

- (1) Palu Ltd's corporation tax liability for the year ended 5 April 2022 will be:

	£
Trading profit	175,000
Director's remuneration	<u>(8,000)</u>
Taxable total profits	167,000

Corporation tax (167,000 at 19%)	31,730
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**Tutorial note:** Equivalent marks will be awarded if the corporation tax liability is alternatively calculated as  $175,000 - 8,000 - 135,270 = £31,730$ .

- (2) Paul's income tax liability for 2021/22 will be:

	Non savings income £	Dividend income £	£
Director's remuneration	<u>8,000</u>		8,000
Dividend income		<u>135,270</u>	<u>135,270</u>
Net income	8,000	135,270	143,270
Personal allowance (income > £125,140)			<u>0</u>
Taxable income			<u>143,270</u>

#### Income tax

£	
8,000 at 20%	1,600
2,000 at 0%	0
27,700 (37,700 – 8,000 – 2,000) at 7.5%	2,078
<u>105,570</u> (135,270 – 2,000 – 27,700) at 32.5%	<u>34,310</u>
<u>143,270</u>	
Income tax liability	<u>37,988</u>

- (3) There will be no class 1 NICs because the earnings of £8,000 are below the NIC lower thresholds.

#### Business run as a sole trader

- (1) Paul's income tax liability for 2021/22 will be:

	£
Trading profit	175,000
Personal allowance	<u>0</u>
Taxable income	<u>175,000</u>

#### Income tax

£	
37,700 at 20%	7,540
112,300 at 40%	44,920
<u>25,000</u> at 45%	<u>11,250</u>
<u>175,000</u>	
Income tax liability	<u>63,710</u>

- (2) Class 2 national insurance contributions (NICs) for 2021–22 will be £159 (52 × 3.05).  
 (3) Class 4 NICs for 2021/22 will be:

£	£
40,702 (50,270 – 9,568) at 9%	3,663
124,730 (175,000 – 50,270) at 2%	<u>2,495</u>
Class 4 NICs	6,158

## Conclusion

If Paul runs his business as a sole trader, then overall tax and NIC will be £309 more compared to running the business as a limited company:

	£
Limited company (31,730 + 37,988)	69,718
Sole trader (63,710 + 159 + 6,158)	<u>(70,027)</u>
Tax increase	<u>(309)</u>

## 32 Alfred and Amaia (March/June 2021)

### Marking scheme

		Marks
(a)	Pre-trading expenditure	½
	Client entertaining	½
	Lease premium	
	- Premium paid	½
	- Less £5,400	½
	- Deduction	1½
	Capital allowances	
	- Plant and machinery	½
	- AIA	½
	- Motor car	½
	- Motor car WDA	<u>1</u>
		6
(b)	Salary	½
	Motor car	1½
	Job related accommodation	1
	Personal allowance	½
	Income tax at 20%	½
	Income tax at 40%	½
	Interest relief	1
	PAYE	½
	Property income	
	- Rent received	1
	- Insurance	1
	- Mortgage interest	1
		<u>9</u>
		<u>15</u>

### (a) Alfred – Tax adjusted trading loss for the seven month period ended 31 March 2022

	£
Trading profit	63,000
Pre-trading expenditure	(5,000)
Deduction for lease premium (W1)	(1,435)
Client entertaining	0
Capital allowances (W2)	<u>(118,520)</u>
Trading loss	(61,955)

#### Working 1 - Deduction for lease premium

	£
Premium paid	30,000
Less: $30,000 \times 2\% \times (10 - 1)$	<u>(5,400)</u>
Amount taxable on landlord	<u>24,600</u>
Deduction $24,600/10 \times 7/12$	1,435

## Working 2 – Capital allowances

		Main pool	Allowances
	£	£	£
Addition qualifying for AIA			
Plant and machinery	116,000		
AIA - 100%	<u>(116,000)</u>		116,000
Motor car		24,000	
WDA - $18\% \times 7/12$		<u>(2,520)</u>	<u>2,520</u>
TWDV c/f		21,480	
Total allowances			<u>118,520</u>

### Tutorial notes

- 1 The cost of the marketing campaign is deductible because it was incurred in the seven years prior to the commencement of Alfred's trade and it would be deductible under general principles.
- 2 The motor car has CO<sub>2</sub> emissions between 1 and 50 grams per kilometre, and therefore qualifies for writing down allowances at the rate of 18%.

### (b) Amaia – Income tax payable for the tax year 2021/22

	£
Employment income	
Salary	80,000
Motor car ( $25,000 \times 14\% \times 3/12$ )	875
Job-related accommodation	0
Property income (working)	<u>14,350</u>
	95,225
Personal allowance	<u>(12,570)</u>
Taxable income	<u>82,655</u>
37,700 at 20%	7,540
44,955 ( $82,655 - 37,700$ ) at 40%	<u>17,982</u>
	25,522
Interest relief ( $2,600$ at 20%)	<u>(520)</u>
Income tax liability	25,002
PAYE	<u>(19,240)</u>
Income tax payable	<u>5,762</u>

### Working – Property income

	£
Rent received ( $1,200 \times 13$ )	15,600
Mortgage interest	0
Insurance	<u>(1,250)</u>
Property income	<u>14,350</u>

## 33 Mooncake Ltd

### Marking scheme

			Marks
(a)	(1) Timing	1	
	(2) Qualifying charitable donations	<u>1</u>	2
(b)	Depreciation	½	
	Lease of office equipment	½	
	Lease of motor car	1	
	Entertaining staff	½	
	Entertaining overseas customers	½	
	QCDs	½	
	Capital allowances		
	- WDV b/f	½	
	- Proceeds - van	½	
	- Proceeds - motor car	1	
	- Proceeds - motor car	1	
	- WDA	½	
			7
(c)	(i) Trading profit	½	
	Property business income	½	
	Chargeable gain	1	
	Trading loss	1	
	QCDs	½	
	Corporation tax	½	
			4
	(ii) Trading loss	½	
	Property business loss	½	
	Capital loss	½	
	QCDs	½	
			<u>2</u>
			<u>15</u>

- (a) (1) The timing and cash flow in relation to the relief obtained, with an earlier claim generally being preferable.
- (2) The extent to which relief for qualifying charitable donations will be lost.
- (b) **Mooncake Ltd – Trading loss for the year ended 31 March 2022**

	£
Operating loss	(93,820)
Depreciation	7,230
Lease of office equipment	0
Lease of motor car (3,400 × 15%)	510
Entertaining staff	0
Entertaining overseas customers	8,720
Qualifying charitable donations	1,600
Capital allowances (working)	<u>(3,240)</u>
Trading loss	<u>(79,000)</u>

### Working – Capital allowances

	Main pool	Allowances
	£	£
WDV b/f	43,200	
Proceeds		
- Delivery van	(11,800)	
- Motor car [1]	(8,100)	
- Motor car [2]	<u>(5,300)</u>	
	18,000	
WDA - 18%	<u>(3,240)</u>	<u>3,240</u>
WDV c/f	<u>14,760</u>	
Total allowances		<u>3,240</u>

(c) (i) **Corporation tax liabilities for the years ended 31 March 2021 and 2022**

	Year ended 31 March 2021	Year ended 31 March 2022
	£	£
Trading profit	138,200	0
Property business income	23,700	0
Chargeable gain	<u>0</u>	<u>0</u>
	161,900	0
Trading loss	(79,000)	0
Qualifying charitable donations	(1,400)	<u>0</u>
Taxable total profits	<u>81,500</u>	<u>0</u>
Corporation tax at 19%	<u>15,485</u>	<u>0</u>

**Tutorial note:** There is no chargeable gain for the year ended 31 March 2022 because the indexation allowance of £6,700 exceeds the gain of £3,700.

(ii) **Carry forward to the year ending 31 March 2023**

	£
Trading loss	0
Property business loss	4,400
Capital loss	4,900
Qualifying charitable donations	0

**Tutorial note:** Indexation allowance cannot be used to create a capital loss.