



J03

THE CHARTERED INSURANCE INSTITUTE

THURSDAY 22 APRIL 2010

**DIPLOMA IN FINANCIAL PLANNING
J03 – THE TAX AND LEGAL ASPECTS OF BUSINESS**

SPECIAL NOTICES

- **All questions in this paper are based on English law and practice applicable in the tax year 2009/2010, unless stated otherwise and should be answered accordingly.**
- **Assume all individuals are domiciled, resident and ordinarily resident in the UK unless stated otherwise.**
- **Candidates should answer based on the legislative position immediately BEFORE the 2010 Budget.**

INSTRUCTIONS

- **Two hours are allowed for this paper.**
- **Read the instructions overleaf carefully before answering any questions.**
- **Fill in the information requested on the answer book and form B.**
- **If you bring a calculator into the examination room, it must be a silent battery or solar-powered non-programmable calculator. The use of electronic equipment capable of being programmed to hold alphabetic or numerical data and/or formulae is prohibited. You may use a financial or scientific calculator, provided it meets these requirements and you must enter the serial number, model and make on the form B.**
- **You are allowed to write on the inside pages of this question paper but you must **not** write your name, candidate number, PIN or any other identification **anywhere** on this question paper.**
- **The answer book and this question paper **must both be handed in personally by you** to the invigilator before you leave the examination room. **Failure to comply with this regulation will result in your paper not being marked and you may be prevented from entering this examination in the future.****

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J03 – The tax and legal aspects of business

CANDIDATE INSTRUCTIONS

READ THE INSTRUCTIONS BELOW BEFORE ANSWERING ANY QUESTIONS

Two hours are allowed for this paper.

The paper consists of 15 short answer questions and carries a total of 130 marks.

Read carefully the questions and information provided. You are strongly advised to attempt **all** questions to gain maximum possible marks. The number of marks allocated to each question part is given next to the question and you should spend your time in accordance with that allocation.

Any rough notes made in your answer book must be crossed through before you hand it in.

Tax tables are provided at the back of the paper.

Answer each question on a new page and leave six lines blank after each question part.

It is important to show all steps in a calculation, even if you have used a calculator.

Please ensure that you understand the Special Notices printed in the box on the front page.

Subject to providing sufficient detail, you are advised to be as brief and concise as possible, using note format and short sentences on separate lines wherever possible.

Attempt ALL questions

Time: 2 hours

1. Simon, Declan and Anthony are the partners in their firm of surveyors. They have recently converted the firm from a partnership into a Limited Liability Partnership (LLP).
 - (a) Explain the position of both the partners and the firm regarding their legal liability in the event of a claim made by a third party for negligent advice provided by one of the partners. *Assume both the negligent advice and the claim occurred after conversion to a LLP.* (4)
 - (b) Compare the position for both types of partnership in the event of the death of one of the partners. (6)

2. DPN Ltd was formed in August 2005 having adopted an unmodified Table A as its articles of association.
 - (a) List the main areas of the company's internal operations that would be dealt with in DPN's articles of association. (6)
 - (b) State whether the changes to company model articles introduced by the Companies (Model Articles) Regulations 2008, will affect DPN Ltd's existing articles of association. (2)

3. Matt Spencer and his friend Jonathan Marx are considering going into the retail clothing business together as partners trading as 'The National Style Council Outlet Store', which will entail opening a high street clothes shop under the same name.
 - (a) Explain to the two friends any effect the Business Names Act 1985 would have on their chosen name. (3)
 - (b) Explain why the alternative name of 'Marx & Spencer Outlet Store' would not be advisable. (3)

4. With regard to a sole trader's profit and loss account:
- (a) explain the difference between the gross profit figure and the profit before tax figure; (4)
 - (b) explain, giving examples where appropriate, why it will be necessary to make further adjustments to the profit before tax figure as part of the process of calculating the tax that a business will pay on their profits. (6)
5. PIF Ltd, a small company as defined by the Companies Act 2006, is 70% owned by John, with the remaining 30% owned in equal shares by Frank and James.
- (a) State the benefits of carrying out an audit on the company's accounts. (3)
 - (b) Outline the role of the Auditor when carrying out an audit of the company's accounts. (3)
 - (c) State **four** principal disclosures that would be included in the director's report. (4)
6. Joe has recently set up a new construction company which will initially employ 25 staff. List the steps that Joe should take to ensure that he is able to meet his legal responsibility to protect the health and safety of his staff. (11)
7. DAB Ltd has made a profit of £399,000 for the year ending 31 March 2010. The four shareholder directors have agreed that nearly all the money will be needed by the business to finance further expansion and are now deciding whether the best approach would be to retain the profit. Alternatively they could pay themselves a bonus to provide a net sum of £40,000 each and then lend it back to the company. Each shareholder director has already been paid a salary of £50,000 for the financial year.

Explain the tax consequences for both the directors and the company of:

- (a) retaining all of the profit; (3)
- (b) taking the net bonus of £40,000 each. (7)
- (c) (i) Explain to the directors the tax consequences for them on withdrawal, if they were to follow the course of action outlined in (a) above and then withdraw the retained profit from the business in the form of a dividend in a future year. (1)
- (ii) Explain to the directors the tax implications for them if, having followed the course of action outlined in (b) above, they then lent the net bonus back to the company. (2)

8. David, Peter and Lucy have a valid partnership agreement in place and the profit sharing ratio is 1:1:2 with Lucy having the largest share. Under the terms of the partnership agreement, it was also agreed that Lucy would be paid an annual salary of £10,000.

David provided partnership capital at outset of £25,000 on which interest is charged at a rate of 5%. The partnership net profits before tax for the current year are £150,000.

Calculate, **showing all your workings**, the share of the taxable profits for each partner in accordance with the agreed profit sharing ratio. (8)

9. CRM is an unquoted limited company. John owns 10% and Ian owns 80%. Pyxel PLC is a quoted company. John owns 25% and Ian owns 3%. John and Ian jointly own a warehouse that is let to CRM.

Identify the Inheritance Tax relief available to John and Ian, and state the level of relief applicable to **each** of the above holdings. (7)

10. State in what circumstances a trader must register for VAT. (5)

11. Railings Ltd are a small manufacturing company. They have recently purchased, in June 2009, new machinery at a cost of £65,000. They also purchased a new car in January 2009, wholly for business use, which cost £16,000. As at the financial year ending 31 October 2008, the general plant & machinery pool of written down capital allowances was £15,000.

Calculate, **showing all your workings**, the total capital allowances that will qualify for tax relief for the trading year to 31 October 2009. *Assume no other capital expenditure or any disposals.* (5)

12. Fred has worked for PDQ Ltd for 20 years but has recently decided to accept a voluntary severance package from his employer of £48,750.

Explain the Income Tax treatment on Fred for each of the following payments:

- (a) an ex-gratia payment of £25,000; (4)
- (b) contractual payment in lieu of notice of £13,500; (2)
- (c) a bonus payment of £10,250. (2)

13. Explain, in the context of employment law, the difference between direct discrimination and harassment. (6)

14. Frank and Kevin are the sole shareholder directors of a small publishing firm, owning 50% of the business each. They are concerned about how the business would be affected if either of them were to die and their reliance on Jane, their sales manager.

The company's profits for the year ending 31 December 2009 are £40,000. They have arranged term assurance policies to age 60 as detailed below:

Name	Age	Salary (£)	Sum Assured (£)
Frank	55	80,000	120,000
Kevin	45	100,000	150,000
Jane	55	50,000	1,000,000

- (a) State the **four** main conditions for the premiums on **each** policy to qualify for the tax relief. (4)
- (b) For Frank, Kevin and Jane, state, giving reasons, whether the company can claim tax relief for premiums paid for the above key person assurance policies on each of their lives. (6)
15. The directors of a small local business want to pass their share of the value of the business to their children if one of them were to die, without any Inheritance Tax (IHT) liability arising as a result of any arrangement put in place.
- (a) State the company document that should be obtained prior to making any recommendation and the reasons why it is important to do so. (3)
- (b) (i) State the **three** main alternative types of agreement that could potentially be put in place when setting up a shareholder protection arrangement. (3)
- (ii) State, giving your reasons, which of these alternative arrangements would not be suitable given the directors' requirements. (3)
- (c) Describe the main features of the type of arrangement identified in (b)(ii) above. (4)

The tax tables can be found on pages 9-13

TAX TABLES

INCOME TAX RATES

2009/2010		2008/2009	
Rate	Band	Rate	Band
%	£	%	£
10	1 - 2,440*	10	1 - 2,320*
20	1 - 37,400	20	1 - 34,800
40	Over 37,400	40	Over 34,800

* A new 10% starting rate is applied for savings income only from 06.04.2008. Only applicable where non-savings income after allowances is under £2,440 for 2009/2010.

NATIONAL INSURANCE CONTRIBUTIONS

2009/2010 Rates

Class 1 Employee	Weekly £	Monthly £	Yearly £
Lower Earnings Limit (LEL)	95	412	4,940
Upper Earnings Limit (UEL)	844	3,656	43,875
Upper Accruals Point	770	3,337	40,040

Class 1 Employee contributions 2009/2010

Total earnings £ per week	Contracted-in rate %	Contracted-out rate %
Up to 110.00*	Nil	Nil
110.01 - 770.00	11	9.4
770.01 - 844.00	11	11
Above 844.00	1	1

Class 1 Employer contributions 2009/2010

Total earnings £ per week	Contracted-in rate %	Contracted-out rate	
		Final salary %	Money purchase £
Below 110.00**	Nil	Nil	Nil
110.01 - 770.00	12.8	9.1	11.4
770.01 - 844.00	12.8	12.8	12.8
Excess over 844.00	12.8	12.8	12.8

* This is the primary threshold below which no NI contributions are payable. However, the lower earnings limit is £95 per week. This £95 to £110 band is a zero rate band introduced in order to protect lower earners' rights to contributory State benefits e.g. Basic State Pension.

** Secondary earnings threshold.

Class 2 (self-employed)	Flat rate per week £2.40 where earnings exceed £5,075 per annum.
Class 3 (voluntary)	Flat rate per week £12.05
Class 4 (self-employed)	8% on profits between £5,715 - £43,875 plus 1% on profits above £43,875

INCOME TAX RELIEFS

	2009/2010	2008/2009
	£	£
Personal (basic)	6,475	6,035
Personal (age 65-74)	9,490	9,030
Personal (aged 75 and over)	9,640	9,180
Married/civil partners (minimum) at 10% †	2,670	2,540
Married/civil partners (age under 75) at 10% †	N/A	6,535
Married/civil partners (age 75 and over) at 10%	6,965	6,625
Age-related relief reduced by 50% of income over	22,900	21,800
Child Tax Credit (CTC)		
family element	545	545
family element baby addition	545	545
CTC usually reduced by 6.67% of joint income over	50,000	50,000
Blind person's allowance	1,890	1,800
Enterprise Investment Scheme relief limit @ 20%	500,000	500,000
Venture Capital Trust relief limit @ 30%	200,000	200,000

† where at least one spouse/civil partner was born before 6 April 1935

PENSIONS

Lifetime Allowance		Annual Allowance	
2006/2007	£1.5 million	2006/2007	£215,000
2007/2008	£1.6 million	2007/2008	£225,000
2008/2009	£1.65 million	2008/2009	£235,000
2009/2010	£1.75 million	2009/2010	£245,000
2010/2011	£1.8 million	2010/2011	£255,000

Notional Earnings Cap

£123,600 – (For schemes that require post 1989 benefits to be still subject to a cap)

Annual allowance charge

40% member's tax charge on the amount of total pension input in excess of the annual allowance.

Lifetime allowance charge

55% of excess over lifetime allowance if taken as a lump sum.

25% of excess over lifetime allowance if taken in the form of income, which is subsequently taxed under PAYE.

CAR AND FUEL BENEFITS

The charge for company car benefits is based on the carbon dioxide (CO₂) emissions. There is no reduction for high business mileage users.

For 2009/2010:

The percentage charge is 15% of the car's list price for CO₂ emissions at or below the qualifying level of 135g/km.

The base percentage charge of 15% increases in 1% steps for every additional full 5g/km over the 135g/km threshold, up to a maximum of 35% of the car's list price.

A lower percentage charge of 10% of the car's list price applies for emissions at or below 120g/km.

If price of car exceeds £80,000 then its price for tax purposes will be fixed at £80,000.

There is an additional 3% supplement for diesel cars not meeting Euro IV emission standards or registered after 31 December 2005. However, the maximum charge remains 35% of the car's list price.

Car fuel The benefit is calculated as the CO₂ emissions % relevant to the car and that % applied to a set figure (£16,900 for 2009/2010) e.g. car emission 160g/km = 20% on car benefit scale. 20% of £16,900 = £3,380.

Notes:

1. **Accessories** are, in most cases, included in the list price on which the benefit is calculated.
2. **List price** is reduced for capital contributions made by the employee up to £5,000.
3. **Car benefit** is reduced by the amount of employee's contributions towards running costs.
4. **Fuel scale** is reduced only if the employee makes good **all** the fuel used for private journeys.
5. **All car and fuel benefits** are subject to employers National Insurance Contributions (Class 1A) of 12.8%.

PRIVATE VEHICLES USED FOR WORK

2009/2010 rates

Cars

On the first 10,000 business miles in tax year 40p per mile

Each business mile above 10,000 business miles 25p per mile

Motor Cycles 24p per mile

Bicycles 20p per mile

INHERITANCE TAX

	2009/2010	2008/2009
Nil-rate band*	£325,000	£312,000
Rate of tax on excess	40%	40%
Lifetime transfers to and from certain trusts	20%	20%
Overseas domiciled spouse/civil partner exemption	£55,000	£55,000

100% relief: businesses, unlisted/AIM companies, certain farmland/building

50% relief: certain other business assets

Reduced tax charge on gifts within 7 years of death

Years before death	0-3	3-4	4-5	5-6	6-7
% of death charge	100	80	60	40	20
Annual exempt gifts	£3,000 per donor			£250 per donee	

* From 8 October 2007 up to 100% of the unused proportion of a deceased spouse's/civil partner's nil-rate band can be claimed on the surviving spouse's/civil partner's death.

MAIN SOCIAL SECURITY BENEFITS

		From 06.04.09 £	From 06.04.08 £
Child Benefit	first child	20.00	20.00*
	subsequent children	13.20	13.20*
Incapacity Benefit	short-term lower rate**	67.75	63.75
	short-term higher rate**	80.15	75.40
	long-term rate	89.80	84.50
Attendance Allowance	lower rate	47.10	44.85
	higher rate	70.35	67.00
Retirement Pension	single	95.25	90.70
	married	152.30	145.05
Pension Credit	single person standard minimum guarantee	130.00	124.05
	married couple standard minimum guarantee	198.45	189.35
	maximum savings ignored in calculating income	6,000	
	increased from November 2009	10,000	
	Bereavement Benefit (lump sum)	2,000.00	2,000.00
Widowed Parent's allowance	95.25	90.70	
Jobseekers Allowance	64.30	60.50	

* From 5 January 2009

** Under State Pension Age

VALUE ADDED TAX

Standard rate	15%*/17.5%**
Annual registration limit - from 1 May 2009	£68,000

* Effective from 1 December 2008

** Effective from 1 January 2010

CORPORATION TAX

Financial Year	2009 to 31/3/10	2008 to 31/3/09
Full rate	28%	28%
Small companies rate	21%	21%
Small companies limit	£300,000	£300,000
Effective marginal rate	29.75%	29.75%
Upper marginal limit	£1,500,000	£1,500,000

CAPITAL ALLOWANCES

Plant & machinery 100% annual investment allowance (first year)	£50,000
Plant & machinery in excess of annual investment allowance (first year)	40%
Plant & machinery, patent rights, know-how (reducing balance) per annum	20%
Certain long-life assets, integral features of buildings (reducing balance) per annum	10%
Industrial & agricultural buildings (straight line)	2%
Energy & water-efficient investments	100%
Qualifying flat conversions & business premises renovations	100%
Motor cars: with emissions in excess of 160g/km	10%
generally	20%*
with CO2 emissions of 110g/km or less	100%
Research & Development: Capital expenditure	100%
Revenue expenditure - small/medium-size firms	175%
- large firms	130%

* Maximum £3,000

CAPITAL GAINS TAX

Exemptions	2009/2010	2008/2009
Individuals, estates etc	£10,100	£9,600
Trusts generally	£5,050	£4,800
Chattels proceeds (5/3 excess gain is taxable)	£6,000	£6,000
Rates		
Individuals	18%	18%
Trusts and estates	18%	18%

ENTREPRENEURS' RELIEF

Entrepreneur's Relief 2009/2010

4/9^{ths} of gain tax free. Lifetime limit eligible for relief: £1,000,000

For trading businesses and companies (minimum 5% employee shareholding) held for 1yr+

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