



J03

THE CHARTERED INSURANCE INSTITUTE

THURSDAY 22 OCTOBER 2009

**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.**

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. Nelson, a sole trader, owns a wholesale business. Over the last few years he has provided a range of heavily discounted supplies to his younger brother. Nelson's firm has been declared bankrupt and he has asked your advice as he has heard that the trustee in bankruptcy can apply to the courts to make certain transactions voidable.
 - (a) Explain briefly to Nelson how the transactions with his brother could be dealt with by the court. (8)
 - (b) List any other transactions made by Nelson which could be voidable by the court on the application of the trustee in bankruptcy. (3)

2. James and David are in the process of drawing up a formal written partnership agreement. In addition to the written terms of the agreement, the solicitor advises that the partnership is a contract of the utmost good faith and that they will also owe a fiduciary duty to each other. Unknown to James, David plans to keep some of his existing clients separate from the new business and service them using the new business' equipment and premises.
 - (a) Explain to James and David what the solicitor means by a contract of utmost good faith. (4)
 - (b) Explain to David how his fiduciary duty to James will affect his plan to retain some of his existing clients. (6)

3. Mike owns 15% of the share capital in a small private company. John owns the remaining 85% and is the sole director of the company. Mike is becoming increasingly concerned with regard to the running of the business and has asked you for advice regarding his rights.
 - (a) Give **six** examples of what could constitute unfair prejudice by John against Mike. (6)
 - (b) List **two** sources of information you would consult when advising Mike of his specific rights. (2)

4.
 - (a) List the current liabilities of a business on its balance sheet. (5)
 - (b) Explain why the working capital ratio may be more useful than the current ratio for interpreting business accounts. (4)

5. List **three** key pieces of information contained in the accounts of a small limited company that you would require to advise on the establishment of a shareholder protection arrangement **and** where you would find them in the last three years accounts. (6)
6. Tim has just been promoted to a salaried partner in the firm of accountants where he works. Explain what it means to be a salaried partner. (5)
7. Sally, a sole trader, is considering taking out a business loan. She wants to use part of the loan to cover her business capital account, which is currently overdrawn.
- (a) State the eligibility criteria for Sally to obtain tax relief on the interest paid on the business loan and how the amount of the loan eligible for tax relief is determined. (5)
- (b) Explain how tax relief is determined if the interest paid on a loan is unusually high. (2)
8. Compare and contrast self-invested personal pensions (SIPPs) and small self-administered schemes (SSASs) with regards to a member using the pension to purchase shares in their sole employer's company. (5)
9. Jason started trading as a sole trader on 1 November 2000 and makes up accounts to 31 October. Jason has decided to move abroad and will stop trading on 30 December 2009. By the time he stops trading, he will have made the following profits:
- | | |
|-----------------------------|---------|
| Year ended 31 October 2001 | £37,500 |
| Year ended 31 October 2002 | £43,000 |
| Year ended 31 October 2009 | £39,500 |
| Profits to 30 December 2009 | £3,000 |
- (a) Explain to Jason how his business profits were taxed in the first two years of trading. (5)
- (b) Calculate, **showing all your workings**, the profit on which tax is paid in the last year of trading. (4)
- (c) Jason's brother Fred is considering starting up his own business. State **three** advantages and **three** disadvantages of using an accounting date of 30 April for Fred's new business. (6)

10. Laura left her employer on 5 April 2009 and set up a business as a freelance management consultant.

Given the fact that Laura is starting with one client, state the main factors that HM Revenue & Customs (HMRC) will consider in deciding if she is employed or self-employed for National Insurance and tax purposes. (7)

11. Sue and John have been business partners running a chain of upmarket clothes shops since June 1992. Prior to the end of the 2008/2009 tax year, John retired and sold his 50% holding in the business and thus realised a gain of £750,000 along with an additional gain of £500,000 at the same time on an associated disposal of premises which were rented up until the point of sale to the business.

Calculate, **showing all your workings**, John's Capital Gains Tax (CGT) liability after he has made a claim for entrepreneurs' relief. *Assume John has not utilised his CGT allowance for the 2008/2009 tax year and that there are no other gains or losses to be included from either 2008/2009 or the previous tax years and that this is John's first claim for entrepreneurs' relief.* (5)

12. Peter employs three full-time staff and up to fifteen part-time staff in his new business, all of whom are regarded as being a relevant employee.

(a) State the alternative arrangements Peter could put in place and the associated eligibility criteria for employees to join them, so as to be exempt from offering a Stakeholder Pension Scheme to his employees. (6)

(b) Peter wants to contribute 2% of basic pay to the pension arrangement for each employee, rising to 4% after five years service. State whether this will satisfy the stakeholder exemption rules, giving your reason. (2)

(c) State the pension reforms introduced in the Pensions Act 2008 that affect Peter's responsibilities to provide employee pensions in the future. (2)

13. List the public duties for which an employer must allow an employee time off work. (6)

14. (a) State the issues relating to a business that should be considered in trying to assess how much key person cover should be put in place on their managing director. (7)

(b) State the documents that may be requested by a financial underwriter to substantiate the level of cover applied for in a key person assurance application. (4)

- 15.** Des and John have been business partners for a number of years and wish to put in place arrangements to deal with the continuation of the business in the event of either of them contracting a critical illness or dying.
- (a) Explain how a cross option agreement works and how it would work alongside an own life policy on each of their lives written in trust and payable in the event of death. **(9)**
 - (b) State, giving your reasons, which type of agreement would be most suitable in the event of either partner contracting a critical illness if neither partner wishes to be forced to sell. **(4)**
 - (c) State the main disadvantage of the type of agreement that you have recommended in **(b)** above. **(2)**

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

	0-3	3-4	4-5	5-6	6-7
Years before death					
% 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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