November 2022 Examination

PAPER 4

Corporate Taxation

Part I Suggested Answers

Candidates will be given credit for relevant points not on the mark scheme.

1.

	FYA @130% £	AIA @100% £	General pool £	Special rate pool £	Allowances £	
WDV b/f			7,325,000	312,000		
Additions						
Processing equipment	900,000					(½)
Air conditioning system		175,000				(½)
Computer equipment	15,000					(½)
Disposals:						
Equipment			(50,000)			(½)
	915,000	175,000	7,275,000	312,000		
Allowances						
FYA @ 130%	(1,189,500)				1,189,500	(½)
AIA @ 100%		(175,000)			175,000	(½)
WDA @18%			(1,309,500)		1,309,500	(½)
WDA @ 6%				(18,720)	18,720	(½)
WDV c/f		Nil	5,965,500	293,280		
Total allowances					2,692,720	

4 marks

2.

Actual cash received:

	£	
Dr Bank B/S (12,000 x 80%)	9,600	(½)
Cr Patent royalties received (income) P&L	9,600	(½)

Tax suffered at source:

Dr Income Tax control account B/S (£12,000 x 20%)	2,400	(½)
Cr Patent royalties received (income) P&L	2,400	(½)

2 marks

3. Heron Ltd must give written notice within three months of the start of the first accounting period which began on 1 January 2021 (½) when the company first gained a source of income. (½) Notification must be therefore be given by 1 April 2021. (½) Heron Ltd needs to produce two tax returns, (½) one for the three month period ended 31 March 2021 before the company started to trade (½) and the second for the year ended 31 March 2022 (½). These are both due for submission 12 months from the end of the period of account, eg 31 March 2023. (½)

Max 3 marks

4. Smith Ltd is a close company as it is controlled by five or fewer participators. (½)

   Where a close company makes a loan to a participator, as Smith Ltd has with Archie, S455 tax is payable on the normal corporation tax payment date, i.e. 9 months and one day after the year end. (½)

   Tax is calculated as 32.5% of the loan. (½) The amount of the loan is taken as the lower (½) of the amount outstanding on:

   - the last day of the accounting period; or (½)
   - the normal due date. (½)

   3 marks

5. Leon Ltd, Tiffany Ltd and Kay Ltd are connected parties (½) as Leon Ltd controls the other two companies. (½) If the transaction is not at arm's length (½)and a tax advantage occurs (½) then an adjustment must be made to the tax computation of the company gaining the tax advantage if it is tax resident in the United Kingdom.(½) Therefore there will be an adjustment made in Leon Ltd's tax computation (½) to increase its taxable income by ((£710-£340) x 2) £740. (½) As Tiffy Ltd is UK Resident it can claim a corresponding adjustment to increase its allowable expenditure by £370 (£710-£340) to reflect the same arm's length price. (½) As Kay Ltd is not UK Resident it cannot claim a corresponding adjustment. (½)

   Max 4 marks

6. Thorne Ltd may be eligible to claim SSE on disposal of the shares in Jesmond Ltd, (½) This is because Thorne Ltd has held 21% of the ordinary share capital (more than 10%) (½) of Jesmond Ltd throughout a 12-month period (½) in the last six years. (½) Jesmond Ltd must have been a trading company or the holding company of a trading group (½) in the last 12 months. (½) If these conditions are satisfied then any gain arising on the disposal is exempt (½) and any capital loss is not allowable. (½)

   4 marks

7. Bailey Ltd will need to account for basic rate income tax (currently 20%) on a quarterly basis (½) on a CT61 return (½) based on the amounts paid and received in each quarter. (½) The quarters are the normal calendar quarters (½) and in Bailey Ltd's case there will be two returns due, one for the quarter ended 31 March (½) and the other for the quarter ended 30 September. (½) The return and any tax is due 14 days after the end of the return period (i.e. 14 April for the return to 31 March). (½)

   Max 3 marks

8. Both the reimbursement of the home telephone bill and the supermarket voucher will be subject to Class 1 NIC (½) as both are classed as earnings. (½) The National Insurance due is paid over via PAYE on 22nd of each month where the payment is made electronically. (½)

   The Gym Membership will be subject to Class 1A NIC (½) which will need to be reported to HMRC via a P11D. (½) The due date for the payment of the Class 1A NIC is 22 July following the tax year where payment is made electronically. (½)

   3 marks

9.

	£	
Interest received on loan to subsidiary	4,000	(½)
Interest on a loan used to purchase an investment property	(12,250)	(½)
Interest on underpaid corporation tax	(500)	(½)
Interest on bank overdraft	-	(½)
Non-trade loan relationship deficit (½)	(8,750)	(½)

   3 marks

10. Broscombe Ltds augmented profits are:

	£	
Taxable total profits	1,200,000	
Dividends received from non 51% subsidiaries	75,000	
Augmented profits	1,275,000	(½)

   These are over the limit of £1.25m (£1.5m x 10/12) and below £16.7m (£20m x 10/12) (½). Broscombe Ltd was also large in the previous period(½). Therefore Broscombe Ltd is a large company for this purpose. (½)

   The corporation tax liability will be £1,200,000 x 19% = 228,000 and this will be due in the following instalments:

14 October 2021 (14th day of month seven) (½)	3/10 x 228,000 =68,400 (½)
14 January 2022 (three months later) (½)	68,400
14 April 2022 (three months later)	68,400
14 May 2022 (three months and 14 days from the end of the accounting period) (½)	1/10 x 228,000 =22,800 (½)

   Max 4 marks

11. For corporation tax purposes all of the payments will be deductible so long as paid in the period (or within 9 months in the case of the two redundancy payments). (1½)

    Income tax:

    - Statutory redundancy payment £12,000 is exempt from income tax (½) but uses up part of the £30,000 exemption. (½)
    - £18,000 of the ex gratia payment is exempt (½) as the £30,000 has be partially used up by the statutory redundancy payment. £15,000 (£33,000 - £18,000) is subject to income tax. (½)
    - The payment into Giles' occupational pension scheme is exempt. (½)

    4 marks

12. The due filing date of the corporation tax return is 12 months from the end of the period of account, which is 31 December 2021. (½) As the return was not filed until 7 August 2022 it is more than three months late (½), a flat rate late filing penalty applies of £200 (or £1,000 if this is the third consecutive late filing). (½)

    A tax geared penalty applies if the corporation tax return is not filed within 18 months of the end of the accounting period (by 30 June 2022) (½) and is calculated as a percentage of the tax outstanding at this point, 30 June 2022. (½) The penalty is calculated as 10% of the corporation tax unpaid at this point. (½)

    3 marks

November 2022 Examination

PAPER 4

Corporate Taxation

Part II Suggested Answers

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PART II

13.

1. The sale of shares in Fern Ltd and Box Tree Ltd will be a change in ownership as more than 50% of the company's share capital is acquired. (½) If there is a change of ownership in a loss-making company anti avoidance provisions may prevent the use of losses. (½)
   In the case of Box Tree Ltd there is likely to be a major change (½) in the nature or conduct of the trade, (½) for example the change in customer base. (½)
   The use of losses will be restricted if the major change occurs within a five-year period (½) beginning up to 3 years (½) before the change in ownership.

   Fern Ltd is to be sold after the trade has become small or negligible(½). If the trade is revived (½) the use of brought forward losses is also prevented. In this case the revival can be any time after the change in ownership (½)

   For both Box Tree Ltd and Fern Ltd no losses arising before the change in ownership will be carried forward (½) and used against profits arising after; also no losses arising after the change in ownership can be carried back (½) and used against profits arising before the change in ownership.

   This rule applies to trading losses only (½) and is not time limited. (½)

   Max (6)

2. Losses relieved to Redwood Ltd
   (The losses relievable will be restricted to the point at which arrangements came into force, being the date at which shareholder approval (½) was given – 31 October 2022.)

   Group relief

   Lower of(½)

   Aspen Ltd losses £300,000 (½) x 4/12 = £100,000

   and

   profits in Redwood Ltd

   £250,000 (½) x 4/12 = £83,333

   Losses relievable in Spring Ltd – from the date that Aspen Ltd joined the Spring group – 31 January 2023 (½)

   Lower of

   Losses surrendered by Aspen Ltd

   £300,000 x 5/12 = 125,000 (½)

   and

   Profits in Spring

   £450,000 x 5/12 = 187,500 (½)

   Loss memorandum

	£	
Loss in Aspen	300,000	
Surrendered to Redwood	(83,333)	
Surrendered to Spring	(125,000)	
Losses not surrendered in current year	91,667	(½)

(4)

3. It is possible for a sale of trade and assets to be a "transfer of a going concern" (½) (TOGC) if the following conditions are met –
   - Business transferred is a going concern; (½)
   - Assets are used to carry on the same business ; (½)
   - There is no significant break in the operation of the business; (½)
   - The purchaser is, or is to become, VAT registered (½)

   A TOGC is the outside the scope of VAT. (½) No VAT will be chargeable on the assets transferred. (½)

   If, however all of the conditions are not met output VAT of 20%(½) must be charged by the seller. (½)

   It is possible when a TOGC occurs to apply to HMRC to have the VAT number transferred (½)

   (5)

4. Each partner is an agent of the partnership for the purposes of carrying on the business (½) and each partner is a principal in that business. (½)
   All partners will be bound (½) by any contact made by another partner. (½)
   A partner's ability to enter into a contract is covered by the law of agency. (½) Therefore any partner may have –
   - Express authority; (½)
   - Implied authority; (½) or
   - Apparent authority. (½)

Therefore, if Redwood Ltd did not know that the partner didn't have express authority(½) they could assume he did have authority and the partners would be bound by the contract. (½)

(5)

Total (20)

14.

1.Calculation of total taxable profits

	£	£	
Non Trading profits (loan relationships)			
Interest received	72,800		
Interest paid	(35,000)		
		37,800	(½)
UK property income	2,650,750		
Less managing agent fee (amount recognised in the accounts under GAAP is deductible) (½)	(65,000)		
Net UK property income		2,585,750	(½)
Overseas property			
Norlandia	400,000		
Westlandia	(600,000)		
Overseas property loss carried forward (½)	(200,000)		
Gain on sale of property (see working 1)		nil	(½)
Management expenses :-			
Rent on office	44,000		(½)
Fees to managing director – only amount agreed as reasonable is allowed; excessive amount not deductible(½)	3,750		
Stockbroker commission	10,000		(½)
Deductible management expenses		(57,750)	(½)
Qualifying charitable donation		(2,000)	(½)
Total		2,563,800	(½)
Less excess management charges brought forward		(2,563,800)	(½)
Total Taxable profits		nil	(½)

Explanatory notes – UK dividend income is not taxable (½)

No capital allowances as computer not used for business purposes (½)

Release of loan not deductible as to a connected party (½)

Working 1

Gain on sale property

	£	

Proceeds	6,000,000	
Cost of property and related fees	(4,510,000)	
Indexation		
(278.1- 166.6)/166.6 (½)		
x £4,510,000	(1,490,000)	(½)
Note – restricted as IA cannot create a loss (½)		
Gain	Nil	

Excess management charges

	£	
Brought forward	4,600,000	
Current year offset	(2,563,800)	
Carry forward	2,036,200	(½)

(10)

2. When being asked to hand over papers relating to a client / former client, the following should be considered –

As the request has come from the new advisor and not from the client (½), ensure that written consent (½) has been obtain from the client before handing over the papers.

If there is a risk that the papers will be used in a claim against your firm, ensure that the firm's insurers are informed (½) and if necessary, take legal advice. (½)

Consider ownership of the papers, as some documents may belong to the client. (½) Your firm is required to hand these papers over. However other papers may belong to the firm (eg some working papers) – if ownership is disputed, legal advice should be sought. (½)

If the documents are originals, copies should be kept (½)

Your firm is still required to keep professional records of work done (½) even if the client requests they are destroyed. (½)

Your firm may have a right of lien (½) over the papers – ie a right to retain the papers – until any outstanding fees are paid. (½)

A reasonable fee can be charged for the handover work. (½)

Max (5)

Total (15)

15.

To : Jo, Finance director , Mildert Group

From A Tax advisor, Ant & Co LLP

Date

Subject – Group gains

Presentation 1

Jo

Thanks for your email. I can address the issues as follows -

1. If Elvert Parts Ltd and Dun Ltd are in a capital gains group (½) the transfer could be no gain/no loss. A capital gains group is one where there is a 75% direct (½) relationship and an over 50% indirect (½) relationship. Also, the transferor and transferee companies must be UK tax resident at the time of transfer (½) and the asset must be a chargeable asset. (½)

   This rule applies automatically and is compulsory. (½)

   Should these conditions be met, the tax consequences for Dun Ltd is that the base cost at which it acquires the asset is the cost to Elvert Parts Ltd plus indexation (if any) (½)

   (Max 3)

2. Gains can be rolled over if, within one year prior to the sale(½) and three years after, (½) all of the proceeds are reinvested into a qualifying asset. (½) The effect is to deduct the rolled over gain from the base cost of the new asset. (½). These rules apply to purchases made by any company which is in the gains group (½) at the time of the purchase of the new asset. (½) The company selling must be UK resident (½) or trading in the UK via a permanent establishment. (½) In this case Bede SA, is trading via a permanent establishment and has a UK liability to Corporation Tax on the sale of UK building and is therefore eligible for rollover relief. (½) Rollover relief is made by a joint election and must be made within 4 years (½) of the later of the disposal of the UK property or purchase of the new asset. (½)

   Max (5)

3. Chargeable gain on sale of Moatside Ltd.

   Degrouping charge (½)

	£	
Proceeds – MV at date of transfer	900,000	(½)
Cost to Mildert Group Holdings Ltd	(230,000)	(½)
Less indexation		

(278.1-213.4)/213.4 = 0.303 x £230,000(½)	(69,690)	(½)
Total	600,310	(½)

Disposal of shares in Moatside Ltd

	£	£	
Cash proceeds	1,635,000		(½)
Plus – degrouping charge	600,310		(½)
Total Proceeds		2,235,310	
Less cost		(450,000)	(½)
Less - indexation			
£450,000 x (278.1-178.4)/178.4(½)		(251,485)	(½)
Gain included in TTP		1,533,825	(½)

As Moatside Ltd is not a trading company at the point of disposal(½) (and has not traded in the past two years) it does not qualify for substantial shareholder exemption (½) and the gain will be chargeable.

(7)

Please let me know if you need any further assistance

Regards

A. Tax advisor

Total (15)

16.

1. During its ownership of Park House, Barnes Ltd can claim the following SBA –

Year to 31 December 2020

3% (½) x qualifying construction cost (£2.5m(½) less land (½) £200,000)

= £69,000 (½) x 2/12 (1 November to 31 December) (½) = £11,500

Year to 31 December 2021

Full year allowance of £69,000 (½)

Year to 31 December 2022

Annual Allowance of £69,000 plus allowance on renovation cost(½)

£100,000 (½) x 3% x 9/12 = £2,250

Total - £71,250

Year to 31 December 2023

Sale on 1 April 2023 - £72,000 (½) x 4/12 = £24,000 (½)

(5)

2. It is possible for Barnes Ltd to obtain tax relief if it is buying a so-called relevant asset - i.e. goodwill. (½) To obtain the tax relief the purchase must also be part of the acquisition of a business (½) in which Barnes Ltd must also acquire qualifying intellectual property. (½)

Qualifying Intellectual property includes patents, registered designs and copyrights(½) (together with patents and registered designs). However, there is a maximum to the cost of the goodwill. (½) The 'cost' is limited to six times (½) the value (½) of the qualifying IP (in this case copyrights) acquired. (½) The annual allowable deduction is 6.5% (½) of cost (for both the goodwill and other qualifying IP (½) , which is pro-rated for periods less than one year (½)

(Max 5)

Total (10)