November 2023 Examination

PAPER 4

CORPORATE TAXATION

Part I Suggested Answers

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

PART I

1.

	FYA @130% £	AIA @100% £	General pool £	Special rate pool £	Allowances £	
WDV b/f			1,654,123	125,521		
Additions						
Manufacturing equipment	550,000					(½)
Car (65g/km)				32,000		(½)
Office equipment		15,000				(½)
Disposal						(½)
Manufacturing equipment			(50,000)			
	550,000	15,000	1,604,123	157,521		
Allowances						
FYA @ 130%	(715,000)				715,000	(½)
AIA @ 100%		(15,000)			15,000	(½)
WDA @18%			(288,742)		288,742	(½)
WDA @ 6%				(9,451)	9,451	(½)
WDV c/f		Nil	1,315,381	148,070		
Total allowances					1,028,193	

4 marks

2. The saw is a wasting chattel that is not exempt for chargeable gains purposes as it has been used in the company's trade and capital allowances have been claimed on it. (½) As the proceeds exceed £6,000 the gain is the lower of the gain calculated in the usual way compared with 5/3 x (gross proceeds - £6,000) (½)

Gain calculated in the normal way:

	£	
Proceeds	7,600	(½)
Less: cost	(2,200)	(½)
Unindexed gain	5,400	
Less: Indexation on cost		
(278.1-163.7)/163.7 = 0.699 x 2,200	(1,538)	(1)
Gain before indexation	3,862	

Compared with: 5/3 x (£7,600 - £6,000) = £2,667 (1)
Lower gain is therefore £2,667. (½)

Max 4 marks

3. Bones Ltd may claim rollover relief on the sale of the building, as both the original office building and the new building are qualifying assets (½). Rollover relief can be claimed as the new office building was bought in the period one year before the disposal of the original office building to 3 years afterwards. (½)

   The effect of the rollover relief claim is to defer the gain on the sale of the office building in February 2023 (½) reducing the base cost of the replacement building purchased in December 2022. (½) As the company did not spend all the sale proceeds, full relief is not available and instead a gain equal to the amount of cash retained (£250,000) is immediately chargeable to corporation tax. (½)

   A claim for rollover relief must be made within four years from the end of the accounting period in which the old office building was disposed of (31 December 2027) (½) or the accounting period in which the replacement asset was acquired (31 December 2026) (½), whichever is later, therefore 31 December 2027. (½)

   4 marks

4. The two types of shares that could be issued by Brenan Ltd to raise funds are ordinary shares (½) and preference shares (½). All companies will have ordinary share capital (½), but it is not necessary to have preference share capital. (½) Ordinary shareholders are effectively the owners of the company due to the voting rights that are usually attached to these shares. (½)The owners of preference shares have priority over the ordinary shares in the payment of dividends.(½) Dividends paid to preference shareholders are usually of a fixed amount.(½) If Brenan Ltd was wound up the preference shareholders would be repaid their capital before the ordinary shareholders. (½) Dividends from preference shares may be cumulative but dividends from ordinary shares are not. (½)

   Max 3 marks

5. Eleven months of the accounting period falls into FY2022 and one month falls into FY2023. Profits are apportioned as follows:

	Total	FY2022	FY2023	
		11/12	1/12	
	£	£	£	
TTP	120,000	110,000	10,000	(½)
Augmented profits	150,000	N/A	12,500	(½)

The Upper and lower limits are:

Upper limit = 250,000 x 1/12 = £20,833 (½)
Lower limit = 50,000 x 1/12 = £4,167 (½)

Corporation tax liability:

		£	
FY22			
110,000	@ 19%	20,900	(½)
FY23			
10,000	@ 25%	2,500	(½)
Less: Marginal Relief			
3/200 x (20,833-12,500) x 10,000/12,500		(100)	2 x (½)
Corporation tax liability		23,300	

4 marks

6. Ragwort Ltd could carry forward the trading loss at 31 December 2022 and this could be deducted from the total profits made in the following period provided the company continues that trade. (½)

   However, where there is a change of ownership (which would be the case when Marigold Ltd purchases all the shares in Ragwort Ltd) then the use of these losses may be restricted. (½)

   If, within a five year period, (½) beginning no more than three years before the change in ownership (½) of Ragwort Ltd, there is a major change in the nature or conduct of the trade carried on by Ragwort Ltd, (½) then anti avoidance provisions will apply.

   The anti-avoidance provision blocks the trading losses from being carried forward after the date of change in ownership. (½)

   The anti-avoidance rules will also apply where the company's trade was small or negligible (½) immediately before the change in its ownership and the trade undergoes a considerable revival in any period following the change of ownership. (½)

   Max 3 marks

7. Bailey Ltd and Scarlett Ltd are connected parties (½) as Bailey Ltd controls Scarlett Ltd (½), and the group is large for transfer pricing purposes. (½)

   As the transaction is not at arm's length, (½) and a UK tax advantage occurs, (½) an adjustment must be made to the tax computation of Bailey Ltd to increase its taxable income by £0.50 per item sold (£2.00 - £1.50 = £0.50). (½) As Scarlett Ltd is UK Resident it can claim a compensating adjustment to increase its allowable expenditure by £0.50 per item purchased to reflect the same arm's length price. (½)

   Max 3 marks

8.

	£	
Proceeds	1,215,000	(½)
Less: Costs of sale	(13,750)	(½)
Less: Cost 2,115,000 x (1,215,000/(1,215,000+1,425,000))	(973,381)	(1)
Less: Enhancement expenditure 255,000 x (1,215,000/(1,215,000+1,425,000))	(117,358)	(1)
Chargeable gain	110,511	

3 marks

9. Relief for foreign tax suffered is calculated on a source-by-source basis. (½)

   The relief available is the lower of: (½)

   i) UK corporation tax due on that source of income and. (½)
   ii) the foreign tax suffered. (½)

   In the case of the interest, the gross amount £159,500 (£125,000 + £34,500) at the UK corporation tax rate of 19% gives UK Corporation tax due of £30,305 as this is less than the £34,500 foreign tax suffered only £30,305 can be set against the UK corporation tax liability. (1)

   In the case of the overseas property income, the gross amount £105,000 (£100,000 + £5,000) at the UK corporation tax rate of 19% gives UK Corporation tax due of £19,950 as this is more than the £5,000 foreign tax suffered only £5,000 can be set against the UK corporation tax liability. (1)

   4 marks

10. The due date for filing a corporation tax return is generally 12 months from the end of the period of account, which was 30 April 2023 in this case. (½) As the return was not filed by this date a fixed rate penalty of £100 is due. (½) A further flat rate penalty of £100 will apply as the return was filed over three months late (½).

    There is also a tax geared penalty as the return was not filed within 18 months of the end of the period of account (½) which is calculated as a percentage of the corporation tax outstanding as at 18 months from the year end. (½) The tax geared penalty is 10% of the corporation tax unpaid at 31 October 2023 which is 10% x £225,000 = £22,500. (½)

    3 marks

11. Augmented profits for the year are calculated by adding taxable total profits (TTP) and dividends received from companies which Dandy Ltd owns less than 50%.(½) Dandy Ltd therefore has augmented profits of over £20 million (£18,500,000 + £2,500,000 = £21,000,000) (½) and therefore is a very large company. (½)

    Very large companies must make their instalment payments as follows:

    1. 14th day of month three from the start of the accounting period, 14 April 2022. (½)
    2. Subsequent payments are due in three months intervals after the previous instalment, 14 July 2022 (½) and 14 October 2022. (½)
    3. Final payment is due on 14th day of the final month of the accounting period, 14 January 2023. (½)

    Max 3 marks

12. The common period is 1.4.22 – 31.12.22 (½)

Common loss	9/12 x (£200,000) = £(150,000)	(½)
Common profit	9/12 x £150,000 = £112,500	(½)
Maximum claim is the lower ie	£112,500	(½)

    2 marks

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PAPER 4

CORPORATE TAXATION

Part II Suggested Answers

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

PART II

13.

1) Marchmain Ltd is a large company (½) for the purposes of obtaining research and development (R&D) tax relief. Relief is taken as an R&D expenditure credit (RDEC). (½)
   The RDEC is 13% of the qualifying expenditure incurred. (½). This amount is treated as a taxable receipt when calculating the total taxable profits of the company, (½) the qualifying expenditure having been taken as a deduction. (½) It is necessary to make a claim for the relief. (½)

   They type of costs which meet the definition of qualifying expenditure are:

   - Staff costs – if directly and actively related to the project. If staff only spend part of their time on the project, a proportion of their cost can be included.
   - Computer related costs – Software used directly in the research is included.
   - Consumables – only items used or consumed in the research are included – anything sold as part of the trade of Marchmain Ltd is not allowed.

   The costs must be:

   - Be revenue in nature, and
   - Relevant to the trade

   (Max 1.5 for relevant points)

   Qualifying capital costs may qualify for a 100% First Year Allowance. (½)

   The relief is affected as a credit (½) against the claimant's tax liability equivalent to 13% of the qualifying expenditure. (½)

   The result is that the company's corporation tax liability is reduced by 10.53% (½) of the qualifying expenditure.

   If the company has insufficient tax liability to fully utilise the RDEC credit, a cash repayment will be made, subject to certain limits. (½) If there is a restriction on the cash payment, the credit may be carried forward to future periods. (½)

   Max (7)

2) It is necessary to determine the time of supply (½) of goods as this will determine when to account for output VAT. i.e. which VAT return this must be included on, and then the VAT must be paid. (½)
   The time of supply is known as the "tax point". (½)
   The basic tax point is when the goods are delivered to or collected(½) by the customer.

   However, there are two exceptions (½), being the earlier (½) of the following -

   - If payment is received before the basic tax point, the date of payment is the tax point (½)

- If the tax invoice is raised and dated before the basic tax point, the date of the invoice is the tax point(½)

If the basic tax point has not been overridden (½) (as above) and the tax invoice is issued in the 14-day period (½) after the basic tax point (½), then the invoice date becomes the actual tax point. (½)
If the customer pays in advance for the goods, then the payment date is the tax point(½). Similarly the tax point for a deposit is the payment date of that deposit. (½) The tax point for the final payment is determined by the normal rules. (½)

Max (6)

3) A charge is a way of securing a debt (½) and so gives the lender the right to recover money (½) due to it if the borrower does not repay it in line with the agreement between the parties. This could be for example by selling the company's property. (½)
The charge can either be fixed (½) or floating(½). A fixed charge is against the physical property of the company (½) and so that property cannot be sold (½) without the charge holders' permission. (½) A common example is land and buildings.
A company is obliged to register its charges at Companies House. (½)
A floating charge is a charge over a class of assets (½) and not a specific asset. (½) The assets can change (½) from time to time and the company can dispose of an asset (½) without recourse to the charge holder. (½)

Max (5)

Total (18)

14.
1)
Ridgeview House Ltd – year to 31 August 2023

	£	£
Trading profits less interest to buy equipment		
£750,000 - £12,500 (½)		737,500 (½)
Income from UK property (see working 1)		Nil (½)
Non-Trading loan relationships		
Impairment of loan to PMM Ltd (unconnected party) (½)	2,000	
Interest on overdue CT (½)	1,750	
Interest on loan to buy shares (½)	16,000	
Interest on loan from participator (working 2) (½)	7,000	
		(26,750) (½)
Total profits		710.750 (½)

Less B/f UK property loss (see below)		(9,875) (½)
Total Taxable profit		700,875

Working 1

	£
Property income	
Rent from Office Block B	35,000
Expenses	
Agent's fee (£35,000 x 12.5%)(½)	(4,375)
Insurance fee(½)	(500)
Income	30,125
Loss brought forward (½)	(30,125)
Taxable Income	nil
Loss b/f available for current year offset	
£40,000- £30,125	£9,875(½)
Loss carried forward	nil

Note – the cost of the replacement roof is not a revenue item(½) and is not allowable(½)

Working 2

Allowable in year	£
July 2023(½)	4,000
January 2024(½)	3,000
Allowable in year	7.000
Amount payable in September 2024 is not deductible as it is payable more than 12 months after the year end(½)	

Note – the impairment of the loan to RH Services Ltd is not deductible as it to a connected party. (½)

(10)

2)

Sale Proceeds per share - £1,000,000 / 50,000 = £20 per share

a. Shares sold within 9 days(½) of purchase –

	£
Proceeds	
8,000 shares x £20 per share(½)	160,000(½)

Cost	
8,000 shares x £8 per share	(64,000)
gain	96,000(½)

b. S 104 Pool –
cost of shares

	£
Purchase	
31 July 2014	
40,000 shares cost	60,000 (½)
Indexation	
(278.1 – 256.0) / 256.0 x £60,000(½)	
Indexation not rounded (½)	5180 (½)
Purchase rights issue	
40000/5 = 8,000 shares at £4 per share(½)	32,000
Cost of shares in the s104 pool	97180 (½)
Number of shares in pool – 48,000(½)	

Shares sold out of s.104 pool – (50,000-8,000) = 42,000 shares

Gain in s104 pool

	£
Proceeds	
42,000 shares x £20 per share(½)	840,000 (½)
Cost	
42,000/48,000 shares x £97180 (½)	(85033) (½)
Gain	754,967

Total gain
£96,000 + £754,967 = £850,967 (½)

Max (7)

Total (17)

15

1)

- Clerk & Smith is a consortium company because-
    - It is not a 75% subsidiary of another company (½)
    - At least 75% of its shares are held by companies(½)
    - These companies hold at least 5% of the shares each (½)

In the case of Clerk & Smith Ltd the companies which hold at least 75% of the shares, holding at least 5% each are

- CS Investments Ltd (½)
- JFM Ltd (½)
- AMJ Ltd (½)
- UK Overseas Management Inc. (½)This is not a UK resident company but its shares are included when looking at the 75% test. (½)

Abdul Khan's shares are not included as he is an individual; (½) the shareholding of Acacia Road Holdings Ltd is not included as it is less than 5%. (½)

Max (4)

2)

The maximum losses available for offset are:

- CS Investments Ltd

    The lower (½) of

    the loss (½)in Clerk & Smith Ltd £2,000,500 x consortium member's lowest (½) interest – 43%(½)
    = £860,215(½)

    and

    CS Investments Ltd's profit - £900,000(½)

- JFM Ltd
    The lower of
    the loss in Clerk & Smith Ltd £2,000,500 x consortium member's lowest interest – 20%
    = £400,100(½)

    and

    JFM Ltd's profit - £3,000,000

- AMJ Ltd
    The lower of
    the loss in Clerk & Smith Ltd £2,000,500 x consortium member's lowest interest – 5%
    = £100,025

and

CS Investments Ltd's profit - £50,000(½)
Loss utilised

	£
Loss incurred	2,000,500
Offset – CS Investments	(860,215)
JFM Ltd	(400,100)
AMJ Ltd	(50,000)
Loss for carry forward	690,185 (½)

Max (4)

3)

The client should be advised as follows:

- The notice has been received (unless specifically precluded from doing so) (½)
- As the request is a valid formal request it overrides any duty of confidentiality (½) owed to the client
- Specialist advice may be required to support what should be disclosed to HMRC (½)
- In limited circumstances, there may be a right to appeal the notice (½)
- The firm is under a legal obligation (½) to comply with the notice (½)
- Failure to comply exposes the firm to civil(½) or criminal penalties (½)
- The firm will keep the client informed as to the progress of the notice (½)
- The firm will ensure that the no information other than that requested is disclosed to HMRC (½)

Marks will be given for other relevant points.

(5)

16

1) When determining if the relationship with Fred is one of employment or self-employment Andi should consider –
    - Is there mutuality of obligation(½) - i.e. does TVC Products Ltd have to give work to Fred and does Fred have to accept it? (½)
    - Does Fred have to personally do the work (½)or does he have the right of substitution? (½)
    - Will TVC Products Ltd have control over what Fred does and when? Or will Fred have control? (½)
    - Other factors should be considered, such as –
        - Is Fred taking any financial risk (e.g., does he have to rectify poor work in his own time/expense?) (½)
        - Could he be more productive and make more profit? (½)
        - Is he providing services to other different clients? (½)

    Max (3)

2) The net deemed Employment Income is

	£
Income from engagement	61,000
Less 5% deduction	(3050) (½)
Less NIC on pay (£20,000 - £9100) x 15.05%(½)	(1,640) (½)
	56,310
Less Pay	(20,000)
Gross payment	36,310
Less Employers NIC £36,310 x 15.05(½)/115.05(½)	(4,749)
Net deemed employment payment	31,561 (½)

The NIC employment allowance is not allowable (½) as Lucie is the worker and a director of Lucie Ltd and the only paid employee. (½)

(4)

3) If Hepworth & Moore Ltd established a subsidiary company overseas (½) (which is not UK tax resident) to undertake the work arising from the expansion, then any income arising will not be taxed in the UK. Income will be remitted back via dividends (½) which are generally not chargeable to UK corporation tax. (½)

If the overseas operations are conducted by way of a branch, (½) then the income arising will automatically form part of the UK taxable profits, whether or not they are remitted back to the UK. (½) It is possible for branch profits to be exempted by election from UK corporation tax. (½)

(3)

Total (10)