

1. In the year to 30 September 2018, Whitman Ltd purchased the following assets:

|                         |         |
|-------------------------|---------|
|                         | £       |
| Ventilation system      | 227,500 |
| Energy saving equipment | 50,000  |
| Warehouse racking       | 35,650  |

The company also sold the following for the stated proceeds:

|   |        |
|---|--------|
|   | £      |
| Packing machine (original cost £40,000) | 22,000 |

The tax written down values at 1 October 2017 were:

|                   |         |
|-------------------|---------|
|                   | £       |
| General pool      | 435,650 |
| Special rate pool | 335,900 |

Whitman Ltd is not a member of any group of companies.

**Calculate the maximum capital allowances available to Whitman Ltd.** (4)

2. The shares in Horncastle Ltd have Enterprise Investment Scheme (EIS) status. The finance director wishes to encourage new investment in Horncastle Ltd by making potential investors aware that investing in EIS shares can enable chargeable gains arising on the disposal of other assets to be deferred.

**Describe the circumstances under which investing in shares in Horncastle Ltd will give a Capital Gains Tax deferral, the amount of the deferral obtained and when the deferred gain is crystallised.** (4)

3. Frederick, who owns a wedding photography company, has been advised that the company should use the VAT Flat Rate Scheme.

**Explain the circumstances under which the company can use the VAT Flat Rate Scheme and the administrative advantages for the company in using the scheme.** (3)

4. Kiln Ltd currently has 500,000 ordinary £1 shares in issue. It proposes to make a bonus issue of one new share for every two shares currently held. The balance sheet of the company is as follows:

|               |              |
|---------------|--------------|
|               | £'000        |
| Net Assets    | <u>1,000</u> |
| Share capital | 500          |
| Reserves      | <u>500</u>   |
|               | <u>1,000</u> |

**1) Show the accounting entries necessary to record the bonus issue.** (1)

**2) Show the balance sheet following the bonus issue.** (2)

5. **Explain the issues to be considered for group relief of current period trading losses when a company enters or leaves a group.** (4)

6. Your client PAM Ltd, a UK resident company, is considering expanding its business into another country.

**Explain the differences for UK Corporation Tax purposes of PAM Ltd operating as either an overseas branch or setting up an overseas limited company as a subsidiary.** (4)

7. Brigham Ltd has 50,000 ordinary £1 shares in issue. In September 2018 Maria (who is employed by Brigham Ltd as sales director) sold her entire holding of shares in Brigham Ltd; the proceeds of the sale were £250,000. This is the first time Maria has sold any shares or other business interest.

The shares were purchased as follows:

| <u>Date of Purchase</u> | <u>Cost of shares</u> | <u>Number of shares</u> |
|-------------------------|-----------------------|-------------------------|
| January 2010            | £12,000               | 2,000                   |
| March 2011              | £20,000               | 500                     |
| November 2012           | £40,000               | 1,000                   |

**Calculate the Capital Gains Tax payable by Maria, assuming she is a higher rate tax payer, giving a brief explanation of the Capital Gains Tax rate used. (4)**

8. **Explain the conditions that have to be fulfilled for rollover relief to be available on the disposal of assets by a company, and what relief is available. (4)**

9. Large companies are required to pay their Corporation Tax liability in instalments.

**Explain the criteria for determining if a company which is part of a group is required to make instalment payments. (2)**

10. Beacon Hill LLP is a limited liability partnership with both individual members and company members. It has property income and trading income.

**Explain how both types of members of Beacon Hill LLP will be taxed on the LLP's trading profits and the tax treatment of interest paid on borrowings to invest in Beacon Hill LLP. (2)**

11. The ordinary shares in Horsley Ltd are owned as follows:

| <u>Name</u>  | <u>Percentage of shares</u> |
|--|-----------------------------|
| Jeff Horsley   | 22%                         |
| Angela Horsley (wife of Jeff)                          | 15%                         |
| Annette Jones (Jeff's aunt)                            | 5%                          |
| Mark Davies (finance director of Horsley Ltd )         | 2%                          |
| Elise Martin (managing director of Horsley Ltd)        | 5%                          |
| Various minority investors (23 investors with 2% each) | 46%                         |
| David Richards (Angela Horsley's brother)              | 5%                          |

Annette Jones is not an employee or director of Horsley Ltd.

**1) Explain whether Horsley Ltd is a close company. (2)**

**2) Explain the tax implications for the company of a loan made by Horsley Ltd to Annette Jones, assuming Horsley Ltd is a small company. (2)**

12. A company may be subject to the personal services companies' rules.

**Explain the National Insurance Contributions due by a company subject to these rules. (2)**



## November 2018 Examination

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### PAPER 4 PART II

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### Corporate Taxation

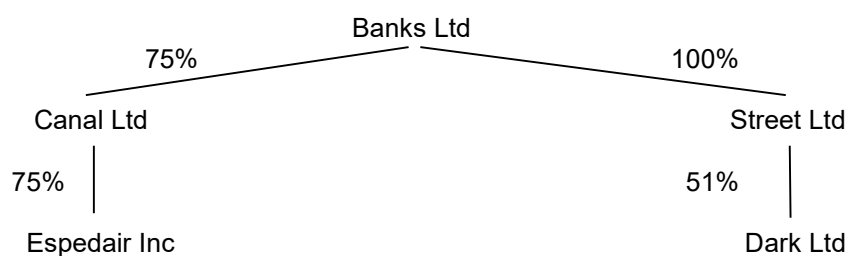
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TIME ALLOWED – 3 ¼ HOURS  
(for Part I and Part II)

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- The first 15 minutes of the three and a quarter hour exam is designated as reading time. You then have three hours to answer both the Part I and Part II questions.
- During the 15 minutes reading time, you may read and annotate your Part II question paper. You may also read the legislation and use your calculator.
- You are **NOT** permitted to open the Part I question and answer booklet until the Presiding Officer says the 15 minutes reading time is over.
- The Presiding Officer will inform you when you can start writing your answers.
- You are required to answer **all Part II** questions in the Part II answer booklet.
- Please start each answer on a fresh page and do not write in the margins.
- All workings should be shown and made to the nearest month and pound unless the question requires otherwise.

1. The following is the structure of the Banks Ltd group at 31 March 2017:



All of the companies are UK resident for tax purposes, apart from Espedair Inc which is a trading company tax resident in Earthsea, an overseas jurisdiction.

Canal Ltd has the following results for the year ended 31 March 2018:

|  | <u>Notes</u> | £       |
|--|--------------|---------|
| Adjusted trading profits before capital allowances             | 1            | 337,900 |
| Rental income receivable                                       | 2            | 50,000  |
| Bank interest receivable                                       |              | 8,450   |
| Interest payable   | 3            | 5,340   |
| Dividends from UK companies (no shareholding more than 4%)     |              | 3,800   |
| Chargeable gain  |              | 12,000  |
| Donations to a national charity                                |              | 1,500   |
| Capital loss brought forward from the year ended 31 March 2017 |              | 20,000  |

Notes:

1. The following information has been provided:

|   | £      |
|---|--------|
| TWDV b/f:   |        |
| Main pool   | 75,900 |
| Special rate pool                                 | 12,200 |
| There were no additions or disposals in the year. |        |

All adjustments, other than capital allowances, have been made in arriving at adjusted trading profits of £337,900.

2. Rental income is as follows:

|   | £             |
|---|---------------|
| Rental income from a property located in Earthsea. The amount is gross of withholding tax of 20% imposed by Earthsea. | 2,000         |
| UK rental income  | 48,000        |
|   | <u>50,000</u> |

3. Interest payable is as follows:

|   | £            |
|---|--------------|
| Overdraft interest payable  | 400          |
| Interest on overdue Corporation Tax   | 370          |
| Interest on a 5-year loan to purchase plant and machinery                           | 2,900        |
| Interest on a loan to purchase 5% of the shares in Dreams Ltd, a UK trading company | 1,670        |
|   | <u>5,340</u> |

Banks Ltd has a trading loss of £290,000 for the year ended 31 March 2018 and it has been decided that the maximum amount of loss will be surrendered to Canal Ltd.

*Continued*

Continuation

You are required to:

- 1) Calculate the Corporation Tax payable by Canal Ltd for the year ended 31 March 2018, including a calculation of the maximum group relief surrender from Banks Ltd. (13)
- 2) State the due date(s) for the payment of Corporation Tax by Canal Ltd for the year ended 31 March 2018, explaining how you have arrived at your answer. (2)

Total (15)

2. Ania Page is a photographer and set up an unincorporated business "ProSnaps" in January 2009. On 28 February 2018, Ania incorporated her business by transferring all of her assets to Snaps Ltd, a newly incorporated UK company, in exchange for 10,000 shares in Snaps Ltd and £30,000 on loan account.

Ania has been registered for VAT purposes since January 2009 and she prepares accounts to 31 December each year.

On cessation of trading on 28 February 2018, Ania transferred the following assets, except the cash, to Snaps Ltd:

|   | <u>Cost</u><br>£ | <u>Value</u><br>£ |
|---|------------------|-------------------|
| Freehold of photographic studio   | 120,000          | 140,000           |
| Photographic equipment (no single item with cost or value more than £6,000) | 24,000           | 19,000            |
| Cash  |                  | 7,000             |
|   |                  | <u>166,000</u>    |

Ania's adjusted trading profit after capital allowances for the period ended 28 February 2018 is £15,000. On 3 March 2018, she incurred legal fees of £2,400 in connection with the cessation of her business and has overlap profits from commencement of £3,900.

The adjusted trading profit for ProSnaps for the year ended 31 December 2017 is £30,000.

You are required to:

- 1) Describe, with supporting calculations, the Income Tax and Capital Gains Tax consequences of the incorporation of Ania's business and the base cost of her shares in Snaps Ltd. Ignore Entrepreneurs' Relief. (10)
- 2) Explain the possible VAT consequences of the incorporation of Ania's business. (5)

Total (15)

3. Child Ltd is a UK trading company and owns 100% of the shares in Beck Ltd. Both companies prepare accounts to 30 June each year. The shares in Beck Ltd were purchased in January 2017 for £170,000.

On 4 April 2017, 15 Cook Road, a property in Birmingham, was transferred from Child Ltd to Beck Ltd when its market value was £280,000. The property had been purchased by Child Ltd on 7 August 2012 for £290,000. Beck Ltd had intended to use the property as its headquarters, but it was more lucrative to rent it out to a third party.

You advise Child Ltd and have just received the following email from Simone Franc, the new Finance Director of Child Ltd.

To: Adviser@co.uk

From: Simone@co.uk

Subject: Raising funds

I need some advice on proposals regarding Beck Ltd. Our shareholders are putting pressure on us to sell Beck Ltd as they do not agree with some of the sustainability policies with regard to this company. As a result I think we will have to either sell the shares of Beck Ltd or sell off its assets. Whatever we decide will happen in early 2019, so we might need to use some estimates when looking at the figures.

#### Option 1: Sale of shares

You already have on file the details with regard to the purchase of Beck Ltd shares. Please advise me of the potential gain on the sale of the shares for £310,000 and assume an indexation uplift of 10%. Also please look at the treatment of the gain both with and without the application of the substantial shareholding exemption. Are there any factors that may prevent the exemption applying in this situation?

#### Option 2: Sale of assets

As an alternative, we could sell the assets of Beck Ltd. Aside from some plant and machinery upon which we have claimed capital allowances and would be scrapped, the only other asset of value is 15 Cook Road. Please calculate the gain assuming disposal proceeds of £380,000. You may need to use some or all of the following indexation uplifts: for the period from August 2012 to final sale use 15%; from August 2012 to April 2017 use 8%; for the period from April 2017 to final sale use 7%.

#### Funds

If we decide on option 1, the sale of shares, which is looking increasingly likely, please provide a brief description of how the funds generated from the sale can be passed on to the individual shareholders of Child Ltd, none of whom are employees, and the tax consequences for both the company and its shareholders.

#### Share sale agreement

Were we to proceed with option 1, please explain the purpose and typical features of the heads of agreement, which I understand is prepared following initial negotiations.

#### Bonus to Stanley Streep

Stanley is the Managing Director of Child Ltd and we have agreed to pay him a bonus of £20,000 for the year ended 30 June 2018, but payment will be deferred until 30 May 2019. When you review the Corporation Tax computation for the year ended 30 June 2018, please note that this should be deducted. Obviously the delay in payment is just to minimise our tax and help cash flow.

Thanks

Simone

*Continued*

*Continuation*

**You are required to prepare an email responding to the queries raised by Simone Franc. Marks will be awarded as follows:**

- 1) Option 1: share sale (8)**
- 2) Option 2: asset sale (2)**
- 3) Distribution of funds (3)**
- 4) Heads of agreement (4)**
- 5) Bonus to Stanley (3)**

Total (20)

4. Spark Ltd, a UK trading company, owns a patent granted to it in the UK. As a result, Spark Ltd receives patent royalties from UK companies each year. The patent royalties receivable for the year ended 31 March 2018 are £300,500. Taxable trading profits for Spark Ltd for the year ended 31 March 2018 are £720,000.

Spark Ltd acquired goodwill from an unrelated party on 1 April 2018, which is amortised in its accounts. However, the new Financial Controller is uncertain as to how to treat the goodwill for Corporation Tax purposes in Spark Ltd's Corporation Tax return for the year ended 31 March 2019. In his previous job, he remembers that goodwill was allowable as a Corporation Tax deduction of 4% per year.

Spark Ltd filed its Corporation Tax return for the year ended 31 March 2017 on time, but there was an error within the return. An amount of rental income was carelessly omitted and as a result taxable total profits were stated as £630,000 when they should have been £670,000. Spark Ltd has yet to have any contact with HM Revenue & Customs regarding this error.

**You are required to:**

- 1) Explain the treatment of the patent royalties and calculate Spark Ltd's Corporation Tax payable for the year ended 31 March 2018. (5)**
- 2) Explain the Corporation Tax treatment of the goodwill acquired by Spark Ltd on 1 April 2018 and why this differs from the treatment described by the Financial Controller. (2)**
- 3) Explain the possible tax consequences of the error in Sparks Ltd's Corporation Tax return for the year ended 31 March 2017. (3)**

Total (10)