

THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Taxation of Owner-Managed Businesses

May 2026

TIME ALLOWED

3 HOURS 30 MINUTES

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- Scots law candidates may provide answers referring to Land and Buildings Transaction Tax rather than Stamp Duty Land Tax.
- Unless otherwise indicated by the provision of additional information in the question, you may assume that 2025/26 legislation (including rates and allowances) continues to apply for 2026/27 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.
- Unless otherwise required by the question, candidates may answer the question using Scottish Income Tax rates or Income Tax rates applying elsewhere in the UK.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

1. Loralan Ltd is an agricultural contracting company, wholly owned by Alan Wilson, with no associated companies. The company previously prepared accounts to 31 December but, for administrative reasons, the most recent accounts cover the 15-month period ended 31 March 2026.

The draft Profit and Loss Account for the 15-month period ended 31 March 2026 is:

	<u>Notes</u>	£
Turnover		986,000
Cost of sales		<u>(188,500)</u>
Gross profit		797,500
Staff and subcontractor costs		(212,600)
Interest payable	1)	(47,300)
Premises costs		(36,000)
Depreciation		(86,600)
Office and administration costs		(16,100)
Sundry costs	2)	(9,500)
Interest income	3)	8,800
Profit on disposal	4)	7,200
Net profit		<u>£405,400</u>

Notes

- 1) Interest payable relates to the hire purchase agreements for plant and machinery, and the financing of short-term working capital.
- 2) Sundry costs include qualifying charitable donations of £750 per month. The first donation was paid on 1 August 2025.
- 3) Interest income relates to a high-interest fixed-rate bond which Loralan Ltd acquired on 1 December 2025. It pays interest of £2,200 per month.
- 4) The profit arises from the sale of a plough on 14 February 2026 for £7,200. It was originally purchased in 2021 for £5,000, and 100% annual investment allowance was claimed. It had been fully depreciated within the accounts.
- 5) During the period, Loralan Ltd purchased the following assets:

<u>Date</u>	<u>Description</u>	<u>Cost</u>
		£
2 February 2025	Tractor	76,000
31 August 2025	Double-cab pickup (190 g/km CO ₂)	52,000
14 September 2025	Portable on-site cabin	62,400
18 January 2026	Second-hand Combine Harvester	256,500

- 6) At 31 December 2024, the Tax Written Down Values were:
 - a) Main pool: £16,600.
 - b) Special rate pool: £nil.

Requirement:

Calculate, with explanations, the Corporation Tax liability for Loralan Ltd for the 15-month period ended 31 March 2026 and state the due date(s) for any Corporation Tax returns and payments, assuming all beneficial claims are made. (20)

2. Jet Away Ltd is an unlisted company that sells private jets. It currently has 170 full time employees and gross assets of £12 million. Jet Away Ltd is currently wholly owned by Louise.

Louise is keen to incentivise the company's long-term sales manager Tom, by granting him a 4% shareholding in Jet Away Ltd. Louise is considering two alternatives:

- 1) For Jet Away Ltd to grant Tom an EMI-qualifying option over 100 ordinary shares on 1 June 2026. The option may be exercised at any time after grant and Tom would be required to pay £7,000 for the shares on exercise.

If Tom is granted the EMI option, he will exercise his option in the event of any sale of the company. All the qualifying conditions for the EMI scheme are met.

- 2) For Jet Away Ltd to issue 100 ordinary shares to Tom on 1 June 2026 at par value. The par value of these shares is £1 per share.

The current market value of the shares is £150 per share.

Louise plans to sell the company in June 2029, by which time she anticipates the shares will be worth £350 each.

Requirement:

Explain the employment taxes and Corporation Tax implications of the two alternatives for Tom receiving shares in Jet Away Ltd. (15)

3. Marianne Kimball owns 50 £1 ordinary shares in Silverbrook Ltd (a property development company incorporated in 2010) and 50 £1 ordinary shares in Carolwood Ltd (an interior design company incorporated in 2017), representing the entire issued share capital in each company. She is a director of both companies and is UK tax resident.

She also owns a warehouse, acquired in 2012. 75% of the warehouse is rented to Carolwood Ltd for the market value rent of £45,000 per year, and the remaining 25% is rented to third parties for £15,000 per year.

In early 2026, Marianne decided to retire from active involvement in the companies. Her adult daughters, Aurelia and Oakley, already work in the companies.

A professional valuation shows the shares of Silverbrook Ltd being worth £1,130,000 and the warehouse being worth £500,000.

The shares of Carolwood Ltd have been professionally valued at £900,000. The company's Balance Sheet as at 31 March 2026 is shown below.

	£	£
Fixed assets:		
Plant and machinery	42,500	
Motor vehicles	<u>72,500</u>	115,000
Stock and work in progress	86,000	
Debtors	18,740	
Cash at bank and in hand	650,000	
Prepayments	<u>3,475</u>	<u>758,215</u>
		873,215
Creditors (amounts falling due within one year)		(35,240)
Non-current liabilities:		
Bank loan		<u>(75,150)</u>
Net assets		<u>762,825</u>
Represented by:		
Share capital (50 £1 ordinary shares)		50
Retained earnings		<u>762,775</u>
		<u>762,825</u>

The following transactions have been proposed to take place on 30 June 2026:

- 1) Marianne will gift 35 of her shares in Carolwood Ltd, and the warehouse, to Oakley.
- 2) Carolwood Ltd will purchase Marianne's remaining 15 shares in the company for £270,000.
- 3) Marianne will gift her 50 shares in Silverbrook Ltd to Aurelia.

The company's cash balance has arisen from trading activities.

Requirement:

- 1) **Explain the Capital Gains Tax and Income Tax implications of the proposed transactions. Calculations are not required.** (12)
- 2) **Explain the extent to which the shares in Carolwood Ltd would qualify for Inheritance Tax business property relief in Oakley's estate following the gift by Marianne.** (3)

Total (15)

4. Norwood Kingswell Ltd is a company specialising in electric vehicles. It began trading on 1 April 2025 and has prepared its first set of accounts for the year ended 31 March 2026.

The company's two shareholders, Elias Norwood and Roy Kingswell, who are also its directors, set up the company to attempt to improve the efficiency of existing batteries for electric vehicles. This is the only activity the company has carried out to date. The company has obtained advance assurance from HMRC confirming that this project qualifies for enhanced tax relief for expenditure on research & development (R&D). None of the work undertaken is eligible for a patent.

The company's finance manager has provided the following information for the year ended 31 March 2026:

	<u>Notes</u>	£	£
Turnover			165,891
Costs:			
Staff costs	1)	121,370	
Sub-contractor costs	2)	428,248	
IT costs	3)	20,493	
Property costs	4)	85,076	
Other office administration costs		36,062	<u>(691,249)</u>
Net profit/(loss)			<u>(525,358)</u>

Notes

1) Staff costs

<u>Name</u>	<u>Salary</u>	<u>Company pension contributions</u>	<u>Employer's National Insurance*</u>	<u>Total per accounts</u>	<u>PAYE</u>	<u>Employee's National Insurance</u>
	£	£	£	£	£	£
Elias Norwood	12,570	6,000	535	19,105	-	-
Roy Kingswell	12,570	6,000	535	19,105	-	-
Miles Ryman	25,000	2,000	-	27,000	2,486	994
Agnes Lott	29,000	2,320	-	31,320	3,286	1,314
James Harper	23,000	1,840	-	<u>24,840</u>	2,086	834
				<u>121,370</u>		

*The liability has been reduced by the employment allowance: candidates do not need to consider this matter further.

The technical team consists of Elias, Roy, Agnes and James. Approximately 15% of their time is spent on administrative tasks. Miles is the company's finance manager.

2) Sub-contractor expenditure

The company contracted with Ravenscroft Ltd, an unconnected company, to carry out experiments to test different charging rates. Elias Norwood was able to specify exactly what work needed to be undertaken. The fee for the work undertaken was £371,524. Ravenscroft Ltd carried out 25% of the work outside of the UK, for cost reasons.

The company also contracted with Thornbridge Ltd, another unconnected company, to produce some of the battery testing equipment. Norwood Kingswell Ltd does not have the required expertise or equipment to design or produce the equipment to the required specifications. While undertaking the work, Thornbridge Ltd developed a new, more precise, product. The fee for the work undertaken was £56,724. Thornbridge Ltd carries out all the work in the UK.

3) IT costs

	£
Software for data analysis	10,187
Online data subscription	6,775
General IT costs	3,531
	<u>£20,493</u>

4) Property costs

	£
Rent	36,000
Rates and utilities	42,351
Repairs	6,725
	<u>£85,076</u>

Requirement:

Calculate, with explanations, the maximum cash repayment for the year ended 31 March 2026 as a result of the R&D tax relief claim, and any trading losses carried forward. (15)

5. Dee Johns is a self-employed garden designer and installer based in the south of England. She uses the default cash basis and has no other sources of income.

Her draft Profit and Loss Account for the year ended 31 March 2026 is as follows:

	<u>Notes</u>	£
Payments received	1)	190,400
Cost of sales		<u>(51,200)</u>
		139,200
Employee salaries		(27,000)
Pension contributions	2)	(6,480)
Premises costs	3)	(13,600)
Travel and motor costs	4)	(7,900)
Legal and Professional fees	5)	(8,140)
Accountancy fees	6)	(1,600)
Equipment costs	7)	(4,800)
General overheads	8)	(6,350)
Proprietor's cash drawings		(55,000)
Rent received	3)	6,000
Bank interest received		1,100
Profit per accounts		<u>15,430</u>

Notes

- 1) Receipts include a one-off unsolicited gift of £200 made by a long standing client. This was in return for Dee feeding her cats whilst the client was in hospital.

- 2) Pension contributions comprise the following:

	£
Employee pension contributions paid	2,200
March 2026 contribution paid 14 April 2026	180
Contributions for Dee's personal scheme paid	<u>4,100</u>
Total charge	<u>6,480</u>

- 3) Premises costs:

	£
Rent paid	12,000
Office heating and lighting	<u>1,600</u>
Total charge	<u>13,600</u>

Dee rents a small office and storage facility. Dee meets all of the premises costs, but she shares the premises equally with a home jacuzzi business for which she receives a rent of £6,000 per year.

- 4) Travel and motor costs:

	£
Van running costs	3,800
Car running costs	<u>4,100</u>
Total charge	<u>7,900</u>

The van was purchased in 2023 and Dee elected to claim the flat rate motor expenses on this vehicle. The business mileage for the year was 13,400 miles.

The car was acquired in January 2024 for cash and is used 65% for business travel. Dee did not elect to claim the flat business mileage allowance for this vehicle.

- 5) Legal and professional fees:

	£
Business debt collection	540
Barrister costs	<u>7,600</u>
Total charge	<u>8,140</u>

The barrister was engaged to defend the business against a local authority prosecution for alleged use of banned weed killers. The defence was successful.

- 6) Accountancy fees include £560 for the preparation of Dee's 2024/25 self-assessment tax return. An analysis of time costs indicates that £180 of this relates to the completion of the self-employment supplementary pages.

- 7) Equipment costs consist of the following:

	£
Small tool replacements	170
Commercial lawn mower	<u>4,630</u>
Total charge	<u>4,800</u>

- 8) General overheads:

	£
Stationery	1,100
Telephone and computing	3,200
Training costs	400
Medical costs	650
Client gifts	840
Gift Aid donation to the British Heart Foundation	<u>160</u>
Total charge	<u>6,350</u>

The training costs arose when Dee and one of her employees attended a forklift driving course. Neither of them have done this before but it was felt that this could be a useful add-on for the business.

The medical costs are payments to a chiropractor engaged to treat Dee's long-standing back problems resulting from an earlier work-related injury.

The client gifts were Easter Eggs. The packaging included a prominent promotional for the business.

Continued

Continuation

During the year, Dee re-turfed her own garden using business materials reflected in the cost of sales figure above. The cost of the turf was £210 and the open market retail value was £470. She also provided free consultancy to her aunt on the design of her aunt's garden. She would have charged £1,800 if this had been for a client.

The Capital Allowances Tax Written Down Values at 1 April 2025 were:

	£
Main pool	nil
Car (165g/km purchased in 2024 – 65% business use)	14,000

Requirement:

1) Calculate, with explanations, Dee's taxable profits for 2025/26. (15)

2) Calculate Dee's Income Tax and Class 4 National Insurance liability for 2025/26. (5)

Total (20)

6. Summer Matthews, 42, was employed as a sales representative of Efficient Energy Ltd. Her gross salary was £132,000 per annum and she had been with the company for a number of years. Summer is not a Scottish taxpayer and was not a director of the company.

Due to a restructuring of the company, Summer's role was made redundant on 31 January 2026. Her contractual notice period was three months. The contract did not include a right for the employer to make a payment on lieu of notice but they agreed that she would leave the company immediately without working any of her notice. She is not entitled to any holiday pay.

Summer's contract entitled her to a bonus of £3,500 if her employment is terminated. Efficient Energy Ltd also offered her the following (paid on 31 March 2026):

	£
Statutory redundancy payment	6,000
Pension scheme contribution	4,000
Outplacement counselling	1,000
Ex-gratia redundancy payment	49,000
Write-off of employment related loan	7,500

Whilst Efficient Energy Ltd made a number of employees redundant as part of the restructuring, they agreed to provide outplacement counselling exclusively to Summer and no other employee.

Summer was issued with her Form P45 on 31 January 2026.

Requirement:

Explain the PAYE and National Insurance treatment of each element of the termination package and calculate the total PAYE and National Insurance due. (15)