THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Taxation of Major Corporates

November 2020

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, you may assume that 2019/20 legislation (including rates and allowances) continues to apply for 2020/21 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

1. You are a tax manager at a firm of Chartered Tax Advisers. Your client is Amarinette Ltd, a UK incorporated and tax resident furniture manufacturer that supplies furniture to third party retailers and also sells furniture through its website directly to the public.

Your firm has been engaged to prepare the Corporation Tax computation and Company Tax return for Amarinette Ltd for the year ended 31 March 2020. Denise Murray, the Finance Director, has requested that the computation is based on claiming any potential reliefs as early as possible.

Denise has provided you with the following information:

Extract from the Income Statement for the year ended 31 March 2020

	Note	£'000
Turnover		215,418
Cost of sales	1)	(198,745)
Gross profit		16,673
Administration expenses	2)	(8,425)
Interest payable	3)	(1,000)
Net profit		7,248

Notes

1) Cost of sales includes depreciation of £3.5 million.

2) Administration expenses include:

	Note	£'000
Gifts to customers	(a)	45
Write-off of loan to employee	(b)	30
Pension contributions	(c)	2,000
Charitable donation to NSPCC		25
Loss on disposal of plant	(d)	200

(a) The gifts to customers were bottles of vintage wine with the label 'Chateau Amarinette'. One bottle, at a cost of £40 to the company, was given to each customer who spent more than £500 on furniture during the month of December 2019.

(b) In the year ended 31 March 2019, the company made a loan to an employee to pay for medical treatment costs for her disabled daughter. In view of the company's successful period of trading, the directors have decided to write off the loan.

(c) The company makes a regular annual £2 million contribution to the pension scheme. In the year ended 31 March 2019, the company made a one-off additional payment, which resulted in an excess contribution of £3 million.

(d) Vans with a net book value of £800,000 were disposed of, generating a loss on disposal of £200,000.

3) The interest payable was incurred on two loans:

(a) £400,000 on a bank loan to purchase the shares in Cranwellion Ltd (see below); and

(b) £600,000 on a bank loan taken out to fund the purchase of new vans.

Continued

1. Continuation

In addition, you are aware of the following:

On 1 April 2019, the tax written down values of the general pool and special rate pool were £15,087,330 and £1,822,248, respectively. All capital expenditure was incurred and paid for during the accounting period.

The company purchased a workshop, originally constructed in 2010, on 1 June 2019 from a third party for £15 million. In the purchase contract, £10 million was designated as the purchase price of land and buildings and the balance to fixtures. The parties have made a joint election under s.198 CAA 2001 in respect of this allocation. The £5 million allocated to fixtures was based on the replacement value of the items; the original cost to the seller was £4 million. The seller has claimed capital allowances on these fixtures as part of its general pool.

Also, on 1 June 2019, the company purchased machinery for this workshop at a cost of £1 million. Alterations to the building, which took place in June and July 2019 at a cost of £250,000, were required to install this machinery. Unconnected to the machinery installation work, the company also installed lifts into the workshop at a cost of £750,000 in June 2019.

The following vehicles were acquired:

1) New vans with carbon dioxide emissions of 45g/km costing £1,250,000;
2) New cars with carbon dioxide emissions of 40g/km costing £500,000; and
3) A new car with carbon dioxide emissions of 160g/km costing £75,000, which is used privately by the managing director for 80% of the time and for business the remainder of the time.

Amarinette Ltd made a trading loss of £300,000 in the year to 31 March 2019, all of which was carried back and set against the trading profits of the previous period. It had a £400,000 non-trading loan relationship deficit in the year to 31 March 2019 to be brought forward at 1 April 2019.

Amarinette Ltd was not part of a group until it acquired all the shares in a competitor, Cranwellion Ltd, on 1 April 2018. Cranwellion Ltd had commenced trading in the UK as a furniture manufacturer on 1 April 2016 and has recorded the following results for tax purposes:

Year ended 31 March	Trading profits /(losses)	Non-trading loan relationship deficit
	£'000	£'000
2017	(1,000)	(500)
2018	(1,200)	(500)
2019	800	(400)
2020	(500)	(400)

Cranwellion Ltd did not incur any expenditure on plant and machinery in the year to 31 March 2020.

Requirement:

Calculate, with appropriate explanations:

1) **The taxable total profits of Amarinette Ltd for the year ended 31 March 2020; and** (17)
2) **Cranwellion Ltd's trading losses/non-trading loan deficit carried forward at 31 March 2020.** (3)

Total (20)

2. You are Lesley Walsh, a tax manager at Denton and Farley LLP, a firm of Chartered Tax Advisers. One of your clients is Girardson Ltd, a UK incorporated and tax resident property development company. It is part of a group of companies, some of which are not tax resident in the UK.

Girardson Ltd is considering bidding for contracts to construct, maintain and let several buildings for the education department of a local authority. If successful, the company will have a reliable source of income for many years to come but will need to fund the construction and maintenance cost with debt. The projected interest expense is £10 million per annum.

Mike Jackson, the Finance Director of Girardson Ltd, has expressed concern that the corporate interest restriction legislation will reduce the after-tax profits of the company and render the contract uneconomical although he has heard there are specific rules for infrastructure projects. Mike has requested advice from you on this matter including how the group should submit interest restriction returns to HMRC.

Requirement:

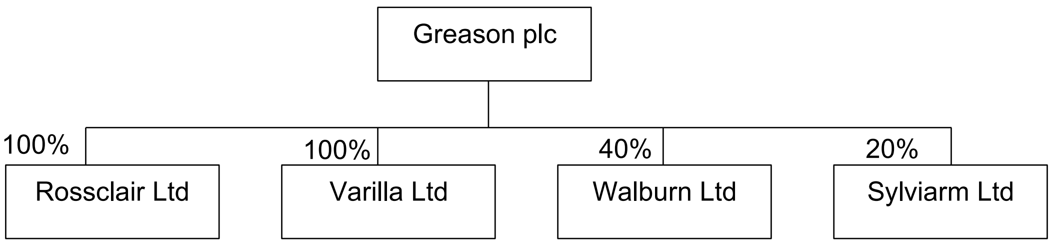
Prepare an email to Mike Jackson explaining:

1) How the corporate interest restriction legislation applies to Girardson Ltd; and (8)

2) The procedure for appointing a reporting company and filing interest restriction returns. (7)

Total (15)

3. The Greason group of companies manufactures and sells health supplements in the UK and overseas. On 1 April 2019, the group structure was as follows:



Zoe Willcox, the founder and Managing Director of the group owns 60% of the shares in Greason plc. Unrelated private equity investors hold the other 40%. At 1 April 2019, Greason plc had capital losses brought forward of £1,300,000; these arose from a transaction with a third party.

Rossclair Ltd is a manufacturing company.

Varilla Ltd trades as a wholesaler. At 1 April 2019, it had capital losses brought forward of £2.4 million; the loss arose from a previous transaction with Sylviarm Ltd which took place on 1 June 2017.

Walburn Ltd operates in the health supplement industry. The remaining 60% of its shares are held by unconnected persons.

Continued

3. Continuation

Sylviarm Ltd is an investment company. At 1 April 2019, Tim Willcox, who is Zoe Willcox's husband, owned 40% of the shares in Sylviarm Ltd. Mr Willcox does not hold shares in any of the other companies nor is he employed by any of the companies in the Greason group. Unrelated persons owned the other 40% of shares in Sylviarm Ltd.

All the shares in the Greason group companies carry equal voting rights.

All companies are tax resident in the UK and prepare accounts with a 31 March year-end.

During the year ended 31 March 2020, the following two transactions were undertaken:

1) Grant of Lease

On 1 November 2019, Rossclair Ltd granted a 20-year lease to Walburn Ltd for a premium of £2.5 million; Rossclair Ltd no longer required the building for trading purposes.

At the time of the grant of the lease, the reversionary interest was valued at £750,000. Rossclair Ltd had acquired the freehold of the building from a third party on 1 May 2011 for £1,750,000.

2) Disposal of Shareholding in Sylviarm Ltd

On 1 June 2019, Greason plc sold its 2,000 shares, representing a 20% shareholding, in Sylviarm Ltd to Tim Willcox for £1.5 million. At that date, the fair market value of a 20% shareholding in Sylviarm Ltd was £1,250 per share and a 60% shareholding was £2,000 per share.

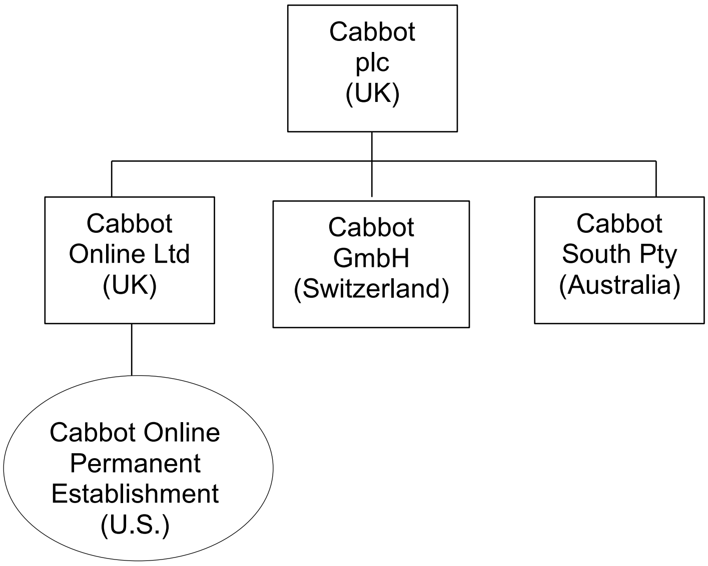
Greason plc had originally acquired 6,000 shares in Sylviarm Ltd, representing a 60% shareholding, for £4.5 million on 1 June 2010 from a third party. On 1 June 2016, it sold 4,000 of these shares to Tim Willcox for £3 million when the fair market value of a 40% shareholding in the company was £1,000 per share and a 60% shareholding was £1,500 per share.

Requirement:

Explain the Corporation Tax consequences of the transactions during the year ended 31 March 2020. (15)

4. Cabbot plc is a FTSE 250 listed UK incorporated and tax resident holding company of a software group with operations in the UK, Australia, Switzerland and the U.S.

The Cabbot group structure is set out below with the jurisdiction of incorporation and tax residency of each subsidiary company stated. All companies prepare accounts to 31 October annually. All subsidiaries are wholly owned and all shares are denominated in their local currency. As well as ordinary shares, Cabbot plc holds fixed rate redeemable preference shares in Cabbot Online Ltd.



Cabbot Online Ltd plans to set up a new wholly owned U.S. subsidiary, and transfer the assets and liabilities of the existing U.S. permanent establishment to this subsidiary.

The draft tax position for Cabbot plc for the year ended 31 October 2020 is as follows:

	£
Trading profits (note 1)	6,700,000
Expenses of management (note 2)	(1,750,000)
Non-trade deficit on loan relationship (note 3)	(3,100,000)
Chargeable gain (note 4)	12,320,300
Taxable profit (before group relief)	14,170,300

Notes

1) Included in trading profits is a £20 million royalty payable by Cabbot plc to Cabbot GmbH.

2) Expenses of management comprise:

	£
Bank fees related to re-financing	1,000,000
Due diligence fees re potential share acquisition (acquisition not approved by Board)	750,000
	1,750,000

Continued

4. Continuation

3) Loan relationship debits and credits comprise:

	£
Interest expense on Sterling external bank loan	(2,500,000)
Interest income on Sterling intra-group loan to Cabbot South Pty*	4,250,000
Interest expense on Australian Dollar bank loan taken out to acquire shares of Cabbot South Pty	(8,000,000)
Foreign exchange gain on Australian Dollar bank loan to acquire shares of Cabbot South Pty	3,150,000
	(3,100,000)

*Cabbot South Pty deducted 10% withholding tax (equivalent to £425,000) on the payment of the interest.

4) The chargeable gain includes a £5 million annual dividend from Cabbot Online Ltd on the fixed rate redeemable preference shares.

5) Cabbot Online Ltd has made a trading loss of £1,700,000 for the year ended 31 October 2020 and this is available for group relief to Cabbot plc.

6) Cabbot plc has losses brought forward as follows:

	£
Trading losses (pre-April 2017)	10,500,000
Trading losses (post-April 2017)	3,750,000
Non-trading loan relationship deficit (post-April 2017)	14,080,500

Requirement:

1) Explain any adjustments required to the taxable profits; (12)

2) Discuss the application of Diverted Profits Tax to the royalty payable by Cabbot plc to Cabbot GmbH; and (4)

3) Discuss the proposed incorporation of Cabbot Online Ltd's U.S. permanent establishment. (4)

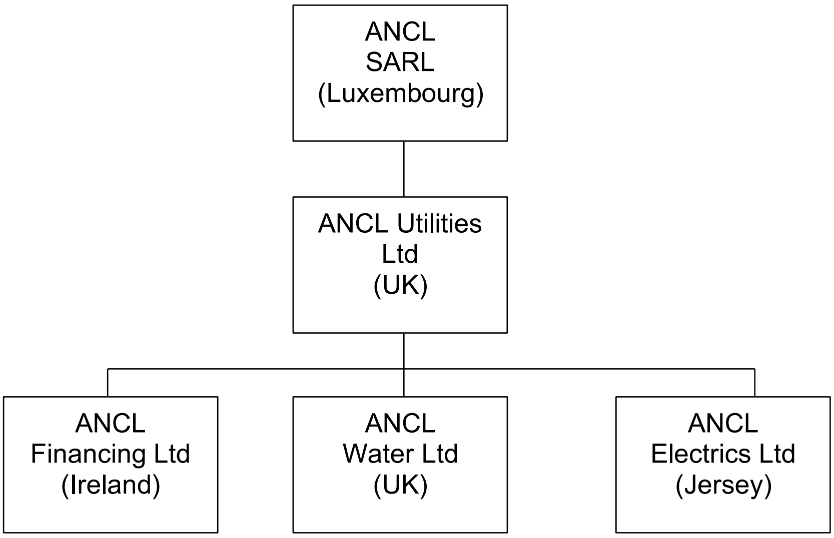
Total (20)

5. You are a senior tax manager in the Mergers and Acquisitions team at Kolter Knight Roberts LLP, a firm that advises large companies on the tax, legal and corporate finance issues relating to a broad range of transactions.

You recently met with Abdul Prince, the Chief Financial Officer of ANCL Utilities Ltd, an utility group preparing for an Initial Public Offering on the FTSE 250. You have been asked to explain the tax risks to your tax partner.

Following your meeting with Abdul, he has provided the information you requested:

The ANCL Utilities Ltd group structure is set out below with the jurisdiction of incorporation and tax residency of each subsidiary company stated. All the subsidiaries are wholly owned. ANCL SARL is owned by a private equity fund. All companies in the group prepare accounts to 30 September annually.



You have been provided with the following information about the group:

<u>Tax profile of companies</u>

1) ANCL Utilities Ltd has been loss making since its incorporation on 1 January 2016 due to an interest expense on the ANCL SARL loan (explained below under Financing). The company has not paid any Corporation Tax nor made any tax filings other than Company Tax Returns, VAT Returns and payroll returns which have all been filed on time.

2) ANCL Water Ltd operates a waterworks in London. It has been profitable and paid Corporation Tax each year. Its profits are reduced by group relief from ANCL Utilities Ltd. All tax filings have been made on time. The company owns a fully operational waterworks in the Isle of Man currently valued at £10 million; the property was acquired for £5 million on 30 June 2018. It also owns three patents, which have recently been registered in the UK.

3) ANCL Financing Ltd is not trading and does pay any tax in Ireland.

4) ANCL Electrics Ltd provides electricity to customers based in Jersey and pays corporate income tax on its profits at a rate of 20%.

Continued

5. Continuation

Financing

1) ANCL Financing Ltd was incorporated on 1 January 2016 and on that date ANCL Utilities Ltd subscribed for £400 million of ordinary shares. The proceeds from the share subscription were transferred to ANCL Water Ltd by way of a four-year interest-bearing loan with a fixed rate of interest of 5% per annum. The loan was repaid on 31 December 2019.

2) A quarter of the interest income of ANCL Financing Ltd was recognised as Controlled Foreign Companies income of ANCL Utilities Ltd and offset by tax losses each year. No other Controlled Foreign Companies disclosure has been included in the UK tax computations.

3) ANCL Utilities Ltd has a £200 million loan from ANCL SARL. The loan was advanced on 1 January 2015 and is repayable on demand with a maturity date of 31 December 2024. It has a fixed interest rate of 12% per annum. The terms are typical for this type of loan.

Management of companies

On 1 January 2019, Mr and Mrs de Groot, who are both directors of ANCL Water Ltd permanently emigrated to the Netherlands (from the UK) in advance of their planned retirement there and have since dialled into Board meetings from the Netherlands and not returned to the UK. The remaining director, Mr Patel, is tax resident in the UK and has attended all Board meetings in person here. The company has now recruited two UK based directors to replace Mr and Mrs de Groot, effective 1 January 2021 when they retire. Non-Dutch incorporated companies are considered tax resident in the Netherlands when managed and controlled there.

Requirement:

Prepare notes for a meeting with your tax partner to explain the UK tax risks based on the information provided. You should not consider the potential impact of the corporate interest restriction. (20)

6. You are a tax manager at a firm of Chartered Accountants and specialise in dealing with tax disputes. An accounting partner is meeting with a new client shortly and he has asked you to prepare an internal briefing note for him explaining the following:

1) The purpose of a HMRC Compliance Check and the procedure a company should follow for responding to this.

2) The circumstances in which HMRC can raise a Discovery Assessment.

3) The penalty regime applied by HMRC for inaccuracies in Company Tax returns.

Requirement:

Prepare the briefing note requested by the partner. (10)