THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Taxation of Major Corporates

November 2021

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.
- Except as set out below or indicated by additional information in the question, you may assume that 2020/21 legislation (including rates and allowances) continues to apply for 2021/22 and future years.

  1) You MUST assume that the UK remains within the European Union.

  2) You MUST ignore all temporary Covid related legislation including furlough, grants, loans and the reductions in VAT and SDLT rates.

  Except in relation to points 1) and 2) above, 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. Derfel Ltd is a precision engineering company that has been consistently profitable for many years. The directors are seeking opportunities to expand, both organically by developing new products and by acquisitions.

Extract from the Income Statement for Derfel Ltd for the year ended 31 December 2020

	Note	£'000
Turnover		361,995
Estimated Research & Development Expenditure Credit		100
Cost of sales		(344,823)
Gross profit		17,272
Administration expenses	1)	(7,658)
Interest payable	2)	(750)
Net profit		8,864

Notes

1) Administration expenses include:

	£'000
Depreciation	5,000
Loss on disposal of cars	75
Legal expenses:	
Acquisition of Nimment Ltd	80
Incidental costs of raising loan finance	40

2) Interest expenses:

	£'000
Bank interest	600
Hire purchase interest	150
	750

Acquisition of Nimment Ltd

On 1 April 2020, Derfel Ltd acquired the entire share capital of Nimment Ltd for £15 million. The acquisition was funded out of a bank loan of £20 million, taken out by Derfel Ltd, at an interest rate of 4%. The remaining £5 million was used as working capital and to fund the acquisition of plant. All the bank interest incurred by the company relates to this loan.

Nimment Ltd specialises in new product innovation with several potentially lucrative projects underway. The company commenced trading on 1 January 2019 and prepared accounts to 30 June 2019 and then to 30 June 2020. In order to bring its accounting date in line with Derfel Ltd, it prepared accounts for the six months to 31 December 2020. Nimment Ltd's results are as follows:

	Profit/(loss) £'000
Six months ended 30 June 2019	(1,000)
Year ended 30 June 2020	(4,000)
Six months ended 31 December 2020	(1,500)

Nimment Ltd has agreed to surrender the maximum amount of losses to Derfel Ltd.

Research & Development

Derfel Ltd undertook research and development activity during the year ended 31 December 2020, although most of the personnel involved were provided by Nimment Ltd. Nimment Ltd first began providing the workers on 1 July 2019. A breakdown of the qualifying expenditure for the year ended 31 December 2020 is provided below; these costs accrued evenly over the year:

	£'000
In house qualifying expenditure	300
Externally provided workers (from Nimment Ltd)	1,200

Capital allowances

On 1 January 2020, the tax written down values of the general pool was £14,537,692 and the special rate pool was £850,361.

On 1 April 2020, Derfel Ltd acquired plant, with a capital cost of £3 million, under a hire purchase contract. The payment terms were £100,000 per month for 36 months. £1 million of the cost is qualifying capital expenditure for the purposes of Research and Development Expenditure Credit.

On 15 July 2020, Derfel Ltd signed a contract for an item of plant, which was to be constructed over a period of time. The total cost was £2.5 million and the work was completed and certified by an architect on the following dates, at which point the obligation to pay became unconditional:

Date work completed	Date work certified	Value of work £'000	Date payment due
5 November 2020	25 November 2020	1,500	9 December 2020
2 December 2020	5 January 2021	600	19 January 2021
22 December 2020	5 February 2021	400	19 February 2021

Derfel Ltd provides prestige cars to directors and other senior personnel. All the cars have CO_2 emissions of over 125g/km. In the year to 31 December 2020, Derfel Ltd purchased new cars costing £250,000. These replaced cars which had originally cost £225,000 and as at 1 January 2020 had a net book value of £175,000.

Requirement:

Calculate, with explanations, the Corporation Tax payable by Derfel Ltd for the year ended 31 December 2020, making the most beneficial claims and elections.

(20)

2. Denaustin Ltd was incorporated in England and Wales on 1 January 2012 and immediately commenced trading. The company manufactures and sells fitness equipment both to gyms and to home users in the UK. It also exports the equipment to third party retailers throughout Europe and to JHSE SL, its overseas subsidiary.

JHSE SL is resident in Beavol, a state in Eastern Europe and a qualifying territory for UK transfer pricing purposes. JHSE SL was established by Juan Herrera and remained wholly owned by Juan until 15 January 2018. On that date, Denaustin Ltd issued new shares to Juan Herrera in exchange for 60% of his shares in JHSE SL. Following the issue of shares to Juan Herrera, he held 40% of the shares in Denaustin Ltd. Denaustin Ltd provides JHSE SL with a 10% discount on prices charged to the other retailers.

Prior to 1 January 2021, Denaustin Ltd's turnover did not exceed €40 million per annum, nor did its average number of employees exceed 200. Since mid-2020, there has been a significant increase in the demand for home gym equipment throughout Europe. By 31 December 2021, the company's average number of employees for the year will exceed 300 and the turnover for the year will exceed €75 million.

Requirement:

Explain how the UK transfer pricing legislation applies to Denaustin Ltd for the year ended 31 December 2021. (15)

3. Kukua Enterprises Inc is a US headed group with diversified interests including a number of UK subsidiary companies. One subsidiary is Kukua Homes SA, a non-UK resident company, which only has a substantial portfolio of property, all of which is located in the UK.

Kukua Homes SA has funded its property purchases by bank loans. The company claims capital allowances on plant and machinery used in the property business and its assets include goodwill. The company recently moved into profit but has carry forward Income Tax losses at 5 April 2020. It prepares accounts to 5 April each year.

On 6 June 2021, Kukua Homes SA sold a block of flats for £45 million to a third party. It had purchased the block for £30 million on 6 April 2012. Since then, the block of flats has been let to third parties and used for residential purposes. The value of the block of flats on 5 April 2015 was £35 million, and on 5 April 2019 it was £40 million.

Requirement:

1) **Explain how Kukua Homes SA is taxable in the UK for the year ended 5 April 2021.** (8)

2) **Calculate, with explanations, the chargeable gain arising from the disposal of the building by Kukua Homes SA on 6 June 2021.** (7)

Total (15)

4. Rummy Ltd is a UK incorporated and resident biscuit manufacturer, which makes up its accounts to 31 October each year. The company is a wholly owned subsidiary of a US manufacturing group.

Factory

Rummy Ltd purchased its factory in Sheffield in February 1990 for £400,000 and in addition, incurred legal fees of £7,000 and Stamp Duty of £4,000. In July 1990, it spent £25,000 on improvements to the factory; this amount did not qualify for capital allowances.

On 1 February 2021, Rummy Ltd granted an option for £500,000 to a third party property developer to purchase the Sheffield site for £5 million within the following 12 months. The developer exercised the option on 31 October 2021 and plans to demolish the factory and build residential houses on the site.

On 1 June 2021, Rummy Ltd bought a large building in Doncaster for £3 million, broken down as follows in the sale and purchase agreement:

	£
Freehold land	1,100,000
Building	1,400,000
Fixtures within building (original cost was £400,000)	500,000

The building was constructed in 2019 at a cost of £1.2 million. The vendor used the building for storage and claimed structures and buildings allowances as well as pooling the fixtures within its capital allowances computation, treating them as integral features.

Immediately upon acquiring the Doncaster site, Rummy Ltd started converting the building into a new factory in which to manufacture its biscuits. Some manufacturing began at the new factory on 1 September 2021 and the company gradually moved all manufacturing from the old Sheffield factory to the new Doncaster factory during the two-month period from 1 September to 31 October 2021.

Other assets

In January 2021, Rummy Ltd spent the following amounts on new equipment and vehicles for use in its biscuit manufacturing trade:

	£
Fixed plant and machinery (not qualifying as integral features)	1,050,000
Office furniture and IT equipment	158,000
Three lorries	150,000

Machinery costing £100,000 was scrapped on the move to the new factory

Capital allowance pool

Rummy Ltd's capital allowance pool brought forward at 1 November 2020 was £58,000. The original cost of the pool was £585,000.

Requirement:

1) Calculate, with explanations, the chargeable gain arising on the sale of the Sheffield factory, assuming all available reliefs are claimed by Rummy Ltd. (11)

2) Calculate, with explanations, the maximum capital allowances that Rummy Ltd can claim in the year ended 31 October 2021. (9)

Total (20)

5. Crecie plc is the holding company of a UK listed and headquartered mining group, with a year-end of 31 December, worldwide group revenues of over £3 billion per year and annual UK revenues of over £200 million. The Crecie group includes more than 70 subsidiary companies based in a number of different countries, including Crecie Australia Pty Ltd, a wholly owned company that is incorporated and tax resident in Australia.

On 1 June 2021, Crecie plc purchased all of the shares of Preston Australia Pty Ltd from a third party for £250 million. Preston Australia Pty Ltd is incorporated and tax resident in Australia.

On 30 September 2021, to align group operations, Crecie plc transferred its shareholding in Crecie Australia Pty Ltd to Preston Australia Pty Ltd at its book value of £120 million satisfied by the issue of non-redeemable shares worth £120 million. The market value of Crecie Australia Pty Ltd was £200 million at the time of transfer.

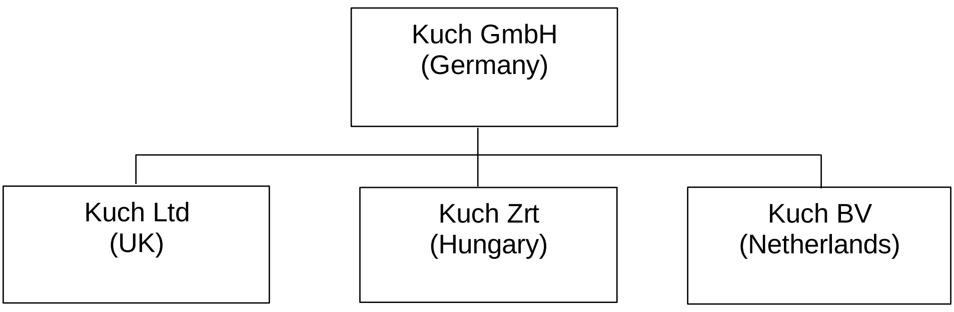
The Chief Financial Officer of Crecie plc and the Crecie group was Anthony Fieldhouse until 30 June 2021. On 1 July 2021, Crecie plc appointed a new Chief Financial Officer, Peter Denny. The Chief Financial Officer acts as the Senior Accounting Officer for the whole of the Crecie group.

Requirement:

Explain the relevance of the International Movement of Capital rules and Senior Accounting Officer rules for the Crecie group. (10)

6. Moy Ltd is a profitable UK incorporated and tax resident trading company that manufactures kitchen utensils in the UK. The annual turnover of Moy Ltd is currently in the region of £40 million and the company currently has no associated or subsidiary companies.

Moy Ltd is considering acquiring all of the share capital of Kuch GmbH for £15 million. Kuch GmbH is the parent company of a trading group that manufactures cutlery. Kuch GmbH has three wholly owned trading subsidiary companies that are incorporated and tax resident in the jurisdictions stated in the group structure chart below.



Kuch GmbH is a trading company with a cutlery manufacturing plant in Germany. The company is expected to make accounting and taxable profits of £1.5 million in each of 2021 and 2022 and plans to pay substantial dividends to Moy Ltd in future years. Kuch GmbH makes an operating margin of 45% and pays corporate tax in Germany on its taxable profits at a rate of 30%.

Kuch Ltd manufactures stainless steel cutlery at its UK factory. Quality problems at the factory during 2016, 2017, 2018 and 2019 resulted in the company making trading losses during those years. Kuch Ltd returned to profitability in 2020 and is expected to be profitable in 2021. At 1 January 2021 the company has brought forward trading tax losses of £750,000.

Kuch Zrt is a distribution company that buys cutlery from Kuch GmbH and sells it wholesale to third party companies in Southern and Eastern Europe. The company is expected to make accounting and taxable profits of £3.75 million in each of 2021 and 2022, based on revenue of £25 million and operating expenditure of £21.25 million. The company pays corporate tax in Hungary at a rate of 9%.

Kuch BV is a trading company with an office in Amsterdam and three Dutch employees. The company provides management services to the other Kuch companies. The company is expected to make accounting and taxable profits of £30,000 in each of 2021 and 2022. The company has an operating margin of 8% and pays corporate tax at a rate of 16.5%.

All inter-company transactions are carried out on arm's length terms.

All companies have a financial year-end of 31 December.

Requirement:

Explain the issues Moy Ltd should consider when preparing its Company Tax Return if it purchases the Kuch GmbH group. (20)