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Date of examination

07	11	20 17

Taxation of Major Corporates

An Advisory paper developed as part of the Joint Programme with the ICAEW leading to the ACA and CTA

	Candidate to complete
Question Number	1

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Part 1

Trading income (w1)	546,964,443
TTP	546,964,443
~~Tax~~ Corporation tax	109,392,889
Instalments paid	(79,300,500)
	30,092,389

Note: as Law Grey is large, instalment payments will be due. (large ⇒ profits over £1.5m).

Instalments of 27348222 (109,392,889/4) will have be due on:

14th April 2017
14th July 2017
14th October 2017
14th January 2017.

Over and under payments of corporation tax will ~~be due~~ see interest due/payable arising from the date the ~~over pa~~ underpayment or overpayment was made until the tax is paid/received.

Interest up until 1 July 2018 (9m and 1 day after year end) will be at a preferential rate.

A penalty may also be payable

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if HMRC suspect deliberate ~~careless~~ action causing the underpayment. This is based on interest but rarely enforced in practice.

Part 2

Income from an overseas PE may be exempted from UK corporation tax by ~~At~~ the company making an election.

The exemption will begin from the start of the next accounting period ~~to~~ from which the election is made and will apply to all PEs of the company.

The election is irrevocable and will also prevent the use of the PE's losses as well as ~~disa~~ no longer all capital allowances.

Chargeable gains will also be exempt

Exemption ~~must be~~ will only apply from point where the losses of the PEs have been offset by profits.

Certain income such as that requiring deductions or relating to investments may not be exempted.

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W1) PBT 530,257,000
Depreciation 15,650,450 disallowed
Profit on FA (11,000) disallowed
Profits of branches –
Pension adjustment 440,000 (W2)
Capital allowances (1,111,287) (W3)
Bonus 2,075,000 (W4)
R&D qual exp (335,720) (W5)
546,964,443

W2) Pension spreading provisions apply. Any excess (over 110% of PY) must be spread. 200,000
110% (~~1,100,000~~) = 220,000
∴ Excess = 1,100,000 − 220,000
= 880,000
As this is between £500,000 and £1m, must be spread over 2 years i.e. 440,000 recognised this period and 440,000 next.

Total allowable deduction
440,000 + 220,000 = 660,000
Actual deduction: 1,100,000
⇒ Add back 440,000

Allowable as paid within year.

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(W3)	Main	SRP	FYA	CAs
TWDV	2,350,350	1,657,200		
Additions:				
Electrical System		105,000		
Boiler		8,500		
Machinery	1,024,360			
Thermal insulation		1,365,000		
Equipment for R&D			76,700	
Disposals				
Car			(1,750)	
P&M	(33,150)			
	3341560	3135700	74950	
AIA		(200,000)		200,000
WDA @ 18%	(601481)			601481
WDA @ 8%		(234856)		234856
FYA			(74950)	74950
				1,111287

Notes:

- Electrical system is integral feature so capital allowances at 8%.
- Boiler allowed FYA if on energy saving criteria list, as not specified included as an integral feature
- Suspended ceiling fails function vs. setting test and is listed as part of building in legislation (not plant).
- 8% capital allowances for thermal insulation as not for a dwelling

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- 100% FYAs available for equipment used for R&D.

200,000 AIA available for year. This has been used on special rate purchases in priority due to law rate of 8%.

W4) Bonus must be paid within 9m of year end so only 500,000 allowable
⇒ add back 2075000

W5) 100% deduction available on consumables and employee costs. 65% deduction on external workers and no deduction for management expenses for R&D. (as do not directly relate to R&D).

⇒ 280,510 + 32,070 + 0·65(35,600)
= 335,720

~~Assuming apply f~~
A further adjustment could also be made if elect into RDEC scheme.

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ABC plc - due diligence Report

Date: November 2017

CDE Ltd - residence

A company is required to pay UK corporation tax if it is considered resident in the UK.

CDE will be deemed resident in the UK if it is either incorporated in the UK or has its central management and control in the UK.

From the information provided, it appears that CDE is incorporated in the Isle of Man and until recently ~~undertook~~ its central management and control was also there such that the company was not subject to UK corporation tax.

~~The start of~~ The board meetings that have been held in the UK since, however, may create a risk that CDE is deemed to have its central management and control in the UK and so be deemed resident.

When assessing where a company's central management and control is, HMRC will look at

↳ where the directors of the company

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exercise management and control;
- whether the directors actually do exercise management and control; and
- where this is not the case, where and by whom it is exercised.

Thus, to determine the extent of the risk further information will be required in relation to the actual power of the directors to make decisions (or whether the directors are little more than cyphers and there is another individual making decisions) as well as the proportion of board meetings held in the UK (if directors do have this power) versus elsewhere.

If CDE is deemed to be resident in the UK, it will be taxed on its worldwide profits.

Note that as no tie-breaker clause exists, CDE will also be taxed in the Isle of Man as a result of being incorporated there.

Double tax relief is likely to be available in accordance with the double tax treaty

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between the UK and the Isle of Man for the lower of the UK tax charged and tax charged in the Isle of Man.

CDE - share disposal
As the disposal is in shares ~~the~~ the gain should be calculated in the functional currency of CDE, i.e. the dollar.

	£00
Proceeds	97,500
Cost	(58,500)
	39,000 (ignoring IA).

If CDE is deemed resident in the UK, corporation tax will be charged on this at 20% and the gain will need to be translated at the average spot rate for the year.

Note that the substantial shareholding exemption will only be available if CDE is UK tax resident but even if so will not be available here as CDE does not hold a substantial shareholding (5% when need at least 10%).

CDE - loan
CDE is not a trading company, nor is the loan held for a trading purpose. As such, it will fall under the non-trading loan relationship rules.

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Where CDE is UK tax resident, a deduction will be allowed against of ~~£70~~ $65 million per year.

~~The company's accounts will be produced~~

This will then be translated at the average spot rate for the year when calculating UK self assessment for tax.

FGH

FGH is a controlled foreign company (CFC) due to being resident outside the UK but controlled by a UK company.

As such, it is necessary to check whether any of its profits need to be apportioned to CDE.

~~It will~~ ~~See~~ Looking at the entity level exemptions, ~~th~~ Switzerland is not an exempt territory, nor ~~as~~ does its tax rate (8%) satisfy the tax exemption which requires the local tax amount to be at least 75% of the corresponding UK tax). The low profit and low margin exemption will also not apply due to the size of FGH's taxable profits.

Thus, the income is subject to the gateway for trading income

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However, ~~ACA~~ it is unlikely that any of the profits will require apportioning as they are not in relation to UK activities.

~~The~~ A large proportion of the group's management and employees are working in Geneva, thus, unless the IP originates from the UK or FGH is funded from the UK it is unlikely the CFC rules will apply

IJK and LMN

As the group is large and intra-group activities are being carried out, it is necessary that such services are provided at an arm's length.

This does not currently appear to be the case as ~~it~~ any excess profit is being paid to FGH such that the profits generated are not being recognised in the country which is ~~sub~~ carrying out the relevant functions, employing the assets and holding the risks

Appropriate adjustments should be made and transfer pricing documentation kept in place to support pricing decisions

An advanced pricing agreement

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may be applied for and as the group has turnover over €750m it is likely that country by country reporting will be required.

OPQ

The payment of royalties from the UK will see an allowable deduction for OPQ.

This should be included gross even though withholding tax of 20% may be necessary.

~~As Switzerland is in the EU, however, it is likely a claim can be made to pay royalties gross under the~~

Switzerland is not in the EU so a claim to pay gross cannot be made under the EU and Royalties directive

However, as FGH is an EU-associated (>25%) company, a certificate can be applied for to pay the royalties gross.

An appropriate arm's length price for the purchase of drugs from OPQ will also be needed.

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An analysis should be carried out to check 2% is appropriate.

Tax returns

As a member of the group is large and pays via QIPs, the UK group can apply to use group payment arrangements.

This will require a nominated company to pay corporation tax on behalf of all the UK companies and an election must be made before the first instalment payment is due in the first period the group wishes it to apply.

This will see benefits both in terms of reducing interest payments and administration.

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Briefing Note
To: Jane Jenkins
From: Tax Manager
Subject: GAAR
Date: November 2017.

General

The purpose of the GAAR is to counteract tax advantages arising from arrangements that are considered abusive.

A tax advantage is considered to be:
↳ relief or increased relief from tax
↳ repayment or increased repayment of tax
↳ avoidance of possible assessment to tax
↳ deferral of payment of tax or advancement of repayment
↳ avoidance of obligation to deduct or account for tax.

Tax arrangements are considered abusive if, given all circumstances, it is reasonable to conclude that obtaining a tax advantage was the main purpose of the arrangement.

The GAAR applies to income tax, corporation tax, capital gains tax, petroleum revenue tax,

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diverted profits tax, SDLT and Annual tax on enveloped dwellings

Where a tax advantage as a result of an abusive arrangement is deemed to have occurred, HMRC can make an ~~count~~ adjustment as is just and reasonable to the company return by providing a counteraction notice.

A formal procedure must be carried out before this is provided however, where HMRC are concerned about a loss of tax, an advanced payment notice may be issued as well as a provisional counteraction notice.

The advanced payment notice will require the company to pay any tax due and this will be returned with interest if this turns out not to be the case.

A penalty of up to 60% of the counteracted advantage will also be ~~not~~ given if a counteraction notice is provided following assessment of the ~~tribunal~~ GAAR advisory panel

Hammersmith Group

The mismatches arising within

the group and the deductions being taken by one company when the corresponding income is not taxed is likely to fall under GAAR.

A UK tax advantage will be arising wherever tax deductions are taken in the UK but not taxed elsewhere since the deductions will be reducing the UK tax liability of the group. A counteraction notice and penalty is therefore likely.

The diverted profits rules and hybrid mismatch rules are also likely to appy here.

The group should have adjusted for such mismatches and by not doing so is likely to fall under the provisions for GAAR.

In order to reduce any exposure, adjustments should be made in the tax computations for the group, disallowing any deductions which do not see corresponding taxable income.

The group should also ensure that appropriate transfer pricing is in place and transactions between companies are at an arm's length.

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Appropriate documentation should also be kept in place to support the group's pricing

Appeals & others

The group will be informed if HMRC is considering to make a counteraction and will be able to make representations accordingly.

If HMRC has already seen a similar case before, a pooling notice or notice of binding may also be issued to the group.

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To: Michael Robins
From: Tax manager
Date: November 2017
Subject: Ramcourt plc - gains.

Building

The disposal of the building will result in a chargeable gain for Ramcourt on which corporation tax will be payable. at 20%

It may be possible to mitigate the gain using rollover relief (since the ~~ass~~ building is used for trade it would be a qualifying asset) or through the use of losses (see later)

In determining the consideration, both non contingent and contingent elements should be taken into account. ~~as well~~

The cash consideration of £4m will be included as will the additional £500,000 despite the fact the application has not been made yet

The contingent consideration of £1.5m if planning permission is granted will also be ~~payable~~ included.

If it later becomes the case that this is not payable

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due to the condition not being met, an adjustment can be made to the gains calculation at a later date.

The unknown contingent consideration should also be included at its expected value, i.e. £70,000. This is a chose in action and will be part of the proceeds here but also the base cost of a future gains calculation when the actual value of this part of the consideration is known. The actual value will be the proceeds here and a separate gain will arise)

Note that ~~any~~ if any part of the consideration is received more than 18 months after the first part, Courtfoods can apply to HMRC to pay any tax on the gain in instalments.

~~Then~~ The base cost of the building will be £1·75m. This will be indexed from 1 January 1999

The incidental costs of the purchase (professional fees and stamp duty) can be deducted from the proceeds.

The planning consultant fees will be allowable ~~if the planning~~ as ~~permission bid is successful~~. they have contributed to additional value.

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Thus, the gain will be:

Proceeds:

Cash consideration	4,000,000
Additional consideration	500,000
Contingent consideration	1,500,000
Chose in action	70,000
Incidental costs	(60,000)
Cost of building	(1,750,000)
IA (1.75m × 0.665)	(1,163,750)
Planning fees	(12,000)
IA (12k × 0.010)	(120)
	30,84,130

Corporation tax payable on this is £616,826 (3084130 × 20%).

Plant and Machinery & Warehouse

The sale of the plant and machinery will see a ~~gain~~ loss of

Proceeds	75,000
Cost	(900,000)
	(825000)

Note that indexation cannot increase a loss. ~~However,~~

However, the loss will not be allowable since relief is already being obtained in the capital allowances computation

The proceeds of 75,000 will be deducted from the main pool

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which will have a balance in it relating to the plant of the original cost (900,000) less the capital allowances claimed (800,000), i.e. £100,000

Thus, the deduction of £75,000 will see ~~a balance~~ total relief, therefore, equal to the ~~allowable~~ loss balance of £25,000 and when allowances are finally given for this (main pool will continue) the total deductions allowed will be 825,000 (i.e the loss).

The purchase of the plant and machinery will have no tax implications. However, as it will be a qualifying asset, rollover relief will be available as a result of the purchase on other gains arising such as that on the building.

As the companies are in a capital gains group, it does not matter that the gain ~~arising~~ arises in Courtfoods and the purchase is by Court Packaging.

A ~~go~~ chargeable gains group ~~requires at least a a pn~~ includes a principal company plus its 75% subsidiaries and

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their 75% subsidiaries and so on. Any indirect holdings must be over 50%.

A company cannot be in more than one gains group.

For group rollover relief to apply it must be that the assets are used for the purposes of the trade and the acquisition of the replacement asset occurs in the period beginning one ~~month~~ year before and ending 3 years after the date of disposal.

A claim must also be submitted within 4 years of the later of the disposal and the acquisition

The plant and machinery has been purchased within the relevant period, as has the warehouse so either may be used to roll over the gain. (or both)

~~However, it is likely~~ However, the gain may only be rolled over as far as the proceeds from the sale of the building have been reinvested.

The proceeds were £6070000 and total amount reinvested is £2m. As such, £4070 000 of the gain will still remain chargeable

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(tax is £814,000) and roll over relief will be available on 1084130.

It is also likely that ~~both the fixed plant and~~ the warehouse bought will have useful economic ~~lives~~ life of over 60 years and so be depreciating asset~~s~~.

This will not see the base cost reduced (as will be the case for the plant) but the gain deferred will crystallise on the earlier of
↳ 10 years from the disposal
↳ when the warehouse is no longer used in trade
↳ when the warehouse is sold.

The gain rolled over into the plant will crystallise when this is eventually sold).

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Losses

As the companies are in the same capital gains group, current year capital losses and gains can be transferred.

A joint claim must be made within 2 years of the end of the accounting period in which the loss arose.

As the losses are all carried forward, the current year gain will need to be transferred by Courtfoods.

The losses in CourtPackaging are pre-entry losses (incurred before company joined group) and so these will not be available for use.

However, ~~tax~~ the remaining gain of 4070000 can be partly transferred to Court Manufacturing (1,475,000) and part transferred to Machines (690,000) such that the final gain left will be 1,905,000 and tax payable will be £381,000.

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A advisor
[address]

November 2017

Paul Smith
Group Tax Director
[address]

Dear Paul,

The transfer of shares in Jupiter to Venus will fall under the share for share rules. (if > 25% holding afterwards)

These will see the new shares issued take on the base cost of Jupiter's old shares and the old shares take on ~~the~~ a base cost equal to the market value of the shares on the date of transfer (£60m).

As ~~th~~ Jupiter and Mercury are in the same capital gains group (75% direct, >50% indirect), ~~&~~ the Substantial Shareholding exemption will not apply to the transfer.

However, the transfer will be at no gain, no loss as a result and the share for share rules will apply.

~~The is~~ As such, no gain will arise and no tax will be payable on the transfer of shares.

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The issue of corporate bonds will allow for a deduduction in Mercury equal to the interest payments.

As Mercury has no trade and the loan is not for trading purposes, this will fall under non-trading loan relationships.

If a deficit occurs, this may be used to offset total income in Mercury or be group relieved to any companies in the same loss relief group.

The loss relief group will include all companies but Saturn (due to only having a 50% holding) and any overseas companies may act as links but cannot partake in ~~the g~~ loss relief.

1) Body corporate with share capital.

If Venus is a company with issued share capital, resident in the US, it will not be subject to UK tax ~~and~~ as it is a legally separate entity.

As such, it will only be charged to tax in the US.

Capital allowances will not be available and local tax advice

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should be sought as to whether an alternative relief exists.

Venus will likely have to file its own tax return in the US.

Any dividend paid by Venus to its shareholders will be exempt as a result of the recipient having control of the payee.

Group relief is ~~unlikely to be~~ not available. As 100% owned, Venus will be included in the loss relief group, however, will not be able to partake as a result of not being resident in the UK

Whilst special conditions exist with regards to.

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3) Branch of Jupiter.

If Mercury is considered a branch of Jupiter its profits will be included in Jupiter's tax return for the purposes of calculating UK tax.

However, an election may be made to exempt profits

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To: chriswallace@omnicorp.plc
From: taxadvisor@whitecross.com
Date: November 2017
Subject: Utilisation of tax losses

A loss relief group exists where a parent company has at least 75% of the
- ordinary shares
- rights to distributable assets on a winding up
- rights to distributable profits

of a subsidiary and the shares are not held as trading stock.

Any indirect holding must also be at least 75% and companies may be in more than one loss group.

Thus, Omnicorp, OS Sarl, OmFraud, TeleIndex and Telesales are included in the loss relief group as all are wholly owned.

Usually, a company overseas cannot partake in a loss relief group, however, a special rule applies for a subsidiary in the EEA which is at least 75% owned and unable to utilise its losses elsewhere.

This appears to be the case for OS Sarl since its operations have been terminated. Thus, its losses, if unable to be used

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overseas will be available for use by the UK group.

Telenix ceased to trade on 30 June 2017. This will have ended its current accounting period and will restrict any trading losses from being carried forward as no continuing trade.

Terminal loss relief would be available such that Telenix could take its loss from the final 12 months back 36 months from the start of its final accounting period.

However, it is noted that profits in the prior period were nil so there may be nothing to offset.

The current year loss, can, however offset the £35m profit incurred in the previous period, reducing this to nil and seeing £15m available for group relief.

As the final year loss was only for the period 1 October 2016 to 30 June 2017, any profits this is to offset will need to be prorated for 9 months.

The transfer of know how will have been on a tax neutral basis

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since both companies are in the same capital gains group (75% direct, >50% indirect)

The annual royalty payment will represent income for Omnicorp and a deduction for Telesales which will ~~either~~ be a trading deduction if incurred for trade or a deficit on intangible fixed assets if otherwise.

The former can be group relieved fully but only excess from the latter may be group relieved after offsetting Telesales own income. Thus, £20m ~~to~~ will become nil and an excess of £5m can be group relieved.

It is assumed the royalty payments are made on an arm's length basis but where this is not the case a transfer pricing adjustment will first be needed.

Omnicorp's management expenses ~~must~~ and non-trading loan relationship deficits cannot be group relieved as these have been brought forward.

Thus, they can be used against Omnicorp's remaining income of £5m and the remainder carried forward into next period

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(£85m).

TeleIndex's remaining loss of £15m may be group relieved against 9/12 of Telesales's income for the year (£15m) and part of OS Sarl's loss can be claimed to cover the rest.

However, as OS Sarl's loss will otherwise be lost, it makes sense to use this fully where can.

Any claim for group relief should be made in the claimant company's tax return ~~one~~ within 2 years of the end of the accounting period to which the loss relates.

Where OS Sarl's loss is being claimed, it is also up to the claimant to prove that the loss cannot be used elsewhere, now or in future periods

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