Chartered Institute of Taxation
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The Chartered Tax Adviser Examination

May 2019

Taxation of Major Corporates

Suggested solutions

ANSWER 1

Tax Solutions LLP
12 Main Street
Northmoor

Colin Macintyre
Finance Director
Challenger plc
57 New Road
Northmoor

X May 2019

Dear Colin

Disposal of shares of Endeavour Ltd and PropCo Ltd

Thank you for your letter concerning the proposed disposal of the shares of Endeavour Ltd and PropCo Ltd. For tax purposes, this disposal will constitute a chargeable disposal. However when disposing of a substantial shareholding, the Substantial Shareholding Exemption (SSE) may apply which exempts gains and means that losses are not allowable.

The SSE has requirements relating to both the investing company and the company being sold.

Investing company conditions

The investing company must have held a substantial shareholding (in excess of 10%) throughout a 12-month period beginning no more than six years prior to the disposal. In both cases, the investing companies (Challenger plc and Voyager Ltd) have each held a substantial shareholding throughout the last twelve months.

Investee company conditions

The company being disposed of must also have been a trading company or the holding company of a trading subgroup in the 12 months ending on the date of disposal. A trading company is one carrying on trading activities that do not include non-trading activities to any substantial extent (undefined, but generally a 20% benchmark is used.) As Endeavour Ltd is a trading company it appears that it would meet this test.

PropCo Ltd requires further consideration. The holding of property for the purposes of generating rental income will not of itself qualify as a trading activity. In a group context, intra-group activities are disregarded for the purposes of assessing the trading status of the group. However, where a subgroup is being sold, activities between group companies (which are not in the subgroup) and the subgroup are not disregarded. As such, when considering the disposal only of the shares in PropCo Ltd, the trading company condition will not be satisfied and the SSE will not apply.

The gain would be:

PropCo Ltd			£'000
Proceeds			30,000
Cost	1 January 2009	210.1	(15,000)
Unindexed gain			15,000
Indexation	RPI capped at December 2017	278.1	(4,855)
Gain			10,145

Degrouping charges

When a company leaves a chargeable gains group holding chargeable assets transferred to it as part of an intra-group transfer within the last 6 years, the rules on degrouping charges must also be considered. A degrouping charge is calculated as though the chargeable asset had been sold and immediately reacquired for its market value at the time of the original transfer. The degrouping charge is treated as an adjustment to proceeds when calculating the gain or loss on the disposal of the shares in the company being sold. Where a degrouping charge arises on a share sale, if the sale of the shares qualifies for the SSE, the SSE rules also mitigate the degrouping charge.

Whilst the transfer from Atlantis Ltd took place more than 6 years before the proposed disposal of the shares, the transfer from Discovery Ltd took place in December 2013 and therefore a degrouping charge may arise if there is a share disposal before 31 December 2019.

Provided the sale of the Endeavour Ltd shares does indeed qualify for the SSE, no degrouping charge would arise on this sale as a result of the transfers in.

However, it is likely that a degrouping charge would arise on the transfer of the property from Discovery Ltd to PropCo Ltd on 31 December 2013. I will need details of the original cost of the property and the market value at 31 December 2013 to calculate the potential adjustment to be included in the calculation of the gain above.

Delaying the disposal until 6 years from the time of the original transfer may be worth considering if the degrouping charge would be significant.

Restructuring possibilities

If the disposal were of a subgroup containing both PropCo Ltd and Endeavour Ltd, the property rental activities would be disregarded, meaning that the SSE could potentially apply in full to the disposal, depending on how the alternative structure arose.

I would be happy to discuss the commercial possibilities and their tax consequences.

Please see attached an Appendix detailing the tax treatment of the property transactions within Challenger plc associated with the proposed transactions.

I trust that the above is useful.

Regards

Jason

Appendix – Tax treatment of property disposals

Manchester

This is the grant of a short lease (less than 50 years) from a long lease.

Part of the premium will be taxed as property income and part as a chargeable gain.

		£
Premium		250,000
Capital element	2% x 250,000- x (10-1)	(45,000)
Income element		205,000

The chargeable gain calculation is treated as a part disposal with the allowable cost calculated as follows:

a/(A+B) x acquisition cost

where a is the part of the premium treated as capital i.e. £45,000, A is the gross amount of the premium (£250,000) and B is the reversionary interest in the lease. It would therefore be necessary to determine the reversionary value in order to calculate the gain arising.

Yorkshire

This is the assignment of a short lease. As the lease is less than 50 years it is a wasting asset. A chargeable gain is calculated but the company cannot take a deduction for the whole of the acquisition cost.

The deductible base cost is the original acquisition cost multiplied by S/P where S and P are the 'lease depreciation' percentages for the years of the lease remaining at the dates of sale and purchase respectively.

Lease remaining on purchase – 15 years – lease percentage 61.617

Lease remaining on sale – 10 years 7 months – lease percentage 46.695+7/12x(50.038-46.695) = 48.645

The chargeable gain based on a disposal of 1 June 2019 would be

		RPI	£
Proceeds	1 June 2019	278.1	300,000
Adjusted cost (500,000 x 48.645/61.617			394,737
Indexation allowance cannot increase a loss.			
Capital loss			(94,737)

MARKING GUIDE

TOPIC	MARKS	
Share disposal		
Chargeable disposal, SSE possible	1	
>10%, 12 months,	0.5	
Investing company conditions satisfied for both	0.5	
investee condition, met by Endeavour	1	
Enterprise fails as group activities outside subgroup disregarded	1	
Gain calc	1	
Avoid by restructuring so leave group together	1	
		6
Degrouping charge		
Holding assets transferred intra group in last 6 years	1	
Fixed assets and intangibles	0.5	
Relevant to Discovery transfer, not Atlantis	1	
Added to proceeds	0.5	
Exempted if SSE so no impact on Endeavour	0.5	
Applicable to PropCo	0.5	
Need gain at 31 December 13 and add to proceeds	1	
Consider delaying	1	
		6
Leases		
Manchester short lease so part income, part gain	0.5	
Income £205,000	0.5	
Gain a/(A+B)	0.5	
a=45,000	0.5	
A=250,000	0.5	
B=value of reversionary interest – to be determined	0.5	
Yorkshire – assignment of short lease, wasting asset	1	
Calculation of deductible base cost (principle, use of %, precise answer)	1.5	
Loss - no indexation	0.5	
		6
Presentation and higher skills		2
TOTAL		**20**

ANSWER 2

	Alpha Ltd	Beta Ltd	Gamma Ltd	Delta Ltd
Year ended 31 March 2018	£m	£m	£m	£m
Trade profit	5.5	Nil	1.2	0.5
UK property business income	0.5	Nil	Nil	Nil
Non-trade loan relationship profit	1.2	0.3	Nil	0.1
Total profit	7.2	0.3	1.2	0.6
Current period trade loss		(0.3)		
Non-trade deficit (LR)			(0.9)	
Group relief	(7.2)		(0.3)	(0.6)
Total Taxable Profit	Nil	Nil	Nil	Nil
Year ended 31 March 2019	£m	£m	£m	£m
Trade profit	6.7	1.2	1.3	0.4
UK property business income	0.5	Nil	Nil	Nil
Non-trade loan relationship profit	0.8	0.3	Nil	0.1
Total profit	8.0	1.5	1.3	0.5
Non-trade deficit (LR)	Nil	Nil	(0.1)	Nil
Current period result	8.0	1.5	1.2	0.5
Brought forward trade loss	Nil	(1.5)	Nil	Nil
Group relief of brought forward losses	(5.75)	Nil	(0.6)	(0.25)
Total Taxable Profit	2.25	Nil	(0.6)	(0.25)
Deductions allowance used	3.5	1.5		

Loss memorandum	Beta Ltd – trade loss	Gamma Ltd – non trade deficit
	£'000	£'000
Arising in year ended 31 March 2018	21.5	0.9
Offset against total profit	(0.3)	(0.9)
Surrendered as group relief	(8.1)	Nil
Carried forward	13.1	Nil
Brought forward	13.1	
Arising in year ended 31 March 2019	Nil	0.1
Offset against total profit	(1.5)	(0.1)
Surrendered as group relief	(6.6)	Nil
Carried forward	5	Nil

Explanations:

- In most cases, unutilised losses arising post 1 April 2017 can be offset against the total taxable profits of a later period provided a claim is made.

- Losses carried forward from earlier periods can be surrendered as group relief.

- The claimant company should utilise its own losses first.

- The profit that can be relieved by brought forward losses is capped through a deductions allowance. The group deductions allowance is £5 million.

- The 'relevant maximum' is 50% of the relevant profits plus the deductions allowance. Hence with a group result for the year ended 31 March 2019 before offset of brought forward losses of £11.2 million, the total brought forward losses available for offset is £8.1 million ((11.2 + 5)/2).

- As Beta Ltd must use £1.5 million of losses before group relief the net Deductions Allowance available to other group members is £3.5 million which is allocated to Alpha Ltd, as explained below. The maximum group relief that can be claimed by the group companies is therefore £6.6 million.

- Given that there are no differential tax rates, the potential benefit in allocation of the maximum deductions allowance to Alpha Ltd arises on the timing of tax payments. As no group companies were tax paying in 2018, they will only be liable to pay tax on account in respect of the 2019 period if profits exceed £2.5 million (£10 million adjusted for the number of associated companies). Allocating the maximum group relief to Alpha Ltd means that no 'on account' payments are required in respect of the 2019 period although they will be required in respect of 2020.

- An allowance nomination must be made agreeing the allocation of the £5 million amongst the group members.

MARKING GUIDE

TOPIC	**MARKS**
2018 – current offset by all entities where available Group relief as far as possible	1 0.5
2019 – current offset Offset brought forward losses – with clam	0.5 1
Can group relieve, subject to restrictions	0.5
Loss offset restricted above £5m through deductions allowance	1
1.5m utilised by Beta, 3.5m remains	1
Group relief 6.6	0.5
Allocation due to payments	1
Allowance nomination required	1
Loss memoranda	1
Final result	1
TOTAL	**10**

ANSWER 3

Note on UK tax administration prepared for Larry Stevenson of Peter's Systems Ltd

Corporation Tax

Returns

Companies are liable to UK Corporation Tax if they are UK tax resident. This is usually the case if they are incorporated in the UK. They must file a company tax return with HM Revenue and Customs (HMRC) electronically within 12 months of the end of the accounting period. The filing must include the statutory accounts, a tax computation and return, all electronically tagged in Inline extensible Business Reporting Language (iXBRL).

HMRC may initiate an enquiry into a company tax return within 12 months from the due filing date (unless the returns are submitted late).

Within this return, or before the relevant deadlines, generally two years from the end of the accounting period, companies must claim deductions and reliefs including group relief (the sharing of losses between group companies), enhanced relief for Research & Development expenditure and capital allowances.

Corporate interest restriction

In addition to the company tax return, groups with more than £2 million of net interest expense and other financing costs may be required to submit an interest restriction return (IRR), which is a tax return at group level.

Since your UK subgroup appears to have a net interest expense of £4 million, which is above the £2 million de-minimis amount, the corporate interest restriction (CIR) rules will need to be considered. These rules differ from the rest of the Corporation Tax regime since the computational provisions operate mainly at group level.

If a group finds that some of its interest expense is restricted, the group can determine how the restriction will be allocated to the UK group companies. This is most effectively done in the IRR, which also allows the group to make certain elections.

The responsibility for filing the IRR falls upon the 'reporting company', which can be appointed by an eligible company within the group. If the group does not appoint a reporting company, HMRC may do so since the appointment of a reporting company triggers the need for an IRR to be submitted.

A group is not obliged to file an IRR or appoint a reporting company if it is not subject to an interest restriction. However, it may be beneficial for the group to file an abbreviated IRR if the group may be liable to a restriction in a later period. An abbreviated IRR may subsequently be replaced by a full IRR, which would allow the group to access unused interest allowances, although these expire after five years.

An IRR (full or abbreviated) must be filed within 12 months of the period end and must contain the name of the ultimate parent of the group, together with details of all group companies within the charge to UK Corporation Tax, and a statement that the return is accurate. The abbreviated IRR must also contain a statement that there is no disallowance, whilst the full IRR should include the key numbers from group level calculations and the allocation of any disallowances or other amounts to group companies.

The CIR regime has its own enquiry procedures, which enable HMRC to open an enquiry into an IRR.

Payment

Although payment of Corporation Tax is normally due nine months after the end of the accounting period, larger UK companies fall within the quarterly payments regime. Given the size of the worldwide group, all companies will probably fall within this regime unless their Corporation Tax liability is less than £10,000. The first payment is due on the 14th day of month seven of the accounting period and subsequent payments due quarterly. Thus, for the year ended 28 February 2020, the payments will be due on 14 September 2019, 14 December 2019, 14 March 2020 and 14 June 2020. Each payment should be of such an amount that the cumulative total represents the appropriate proportion (25%, 50%, 75% and 100%) of the estimated liability for the period at the time that the payment is made, with any balance to be paid as soon as it is identified.

Records

All companies must maintain sufficient records to allow them to file a correct and complete tax return. These records must be preserved for a minimum of six years from the end of the period, and for longer if there is an ongoing enquiry into a tax return.

Senior Accounting Officer (SAO)

UK tax rules require the appointment of a SAO in larger businesses. Since the UK consolidated turnover exceeds £200 million, Peter's Systems Ltd will fall within the rules. As Finance Director you are likely to take on this role. The company must notify HMRC of the name of the SAO each financial year, no later than the accounts filing deadline.

The SAO is the officer of the company with overall responsibility for the company's financial accounting arrangements and must take reasonable steps to ensure that the company establishes and maintains appropriate tax accounting arrangements. An annual certificate must be provided to HMRC within 9 months stating whether the company has appropriate tax accounting arrangements and explaining aspects in which those arrangements are not satisfactory.

Country-By-Country (CBC) reporting and Tax strategy

Multinational groups are now required to file CBC reports. Provided one of the US group companies has filed a report which satisfies the UK reporting requirements, the UK companies only need to notify HMRC accordingly and do not need to file another report. However, the requirements for the publication of tax strategy will apply to the UK parent company. The turnover and gross assets limits are the same as those in the SAO rules.

The group must publish annually on the internet, accessible to the public free of charge, its tax strategy, including its approach to risk management, governance and tax planning in relation to UK taxation, the level of risk that the group is willing to accept and the group's approach to its dealings with the UK tax authorities.

MARKING GUIDE

TOPIC	MARKS
Corporation Tax Self Assessment	
CT if UK resident	0.5
Annual return within 12 months	1
Accounts, computation and return	0.5
iXBRL	0.5
Enquiry possibility/deadlines	1
Claims – within return/ separately Examples	1.5
Retain records for 6 years	1
Tax payments	
Quarterly unless <10k	1
Dates applied to group	1
Amounts	0.5
Corporate Interest Restriction	
Background and de minimis	1
Group return/rules	1
IRR, used for allocation and elections	1
Reporting Company	1
Abbreviated Return	1
Contents of return	1
Enquiry	0.5
Senior Accounting Officer	
Limits	0.5
Notification of ID required	0.5
Senior officer, appropriate records	1
Annual certificate, content	1
Country by Country reporting – notification re US filings should suffice	1
Tax strategy - must make appropriate content accessible	1
TOTAL	**20**

ANSWER 4

To	NTurner@dancongroup.com
From	Alex.Smith@XYZaccountants.com
Date	1 May 2019
Subject:	Symmel plc group – UK Corporation Tax matters

Natasha

Thank you for email regarding the recently acquired Symmel group.

Interest payments

The financing structure you have described takes advantage of differing tax treatments of entities between different tax jurisdictions. Lemmys Holdings Ltd is a "hybrid entity" because it is recognised as a taxable entity in its own right in the UK, but in the US, it is regarded as a branch of Symmel US Holdings Inc.

With effect from 1 January 2017, new UK tax legislation - Hybrids and other mismatches - was introduced to counter the tax advantage that can arise using such a group structure. There is no "purpose" test so the legislation can apply to structures put in place for wholly commercial reasons.

Absent the new hybrid mismatch rules, the tax position would be as follows:

Symmel plc would be taxable on the interest receipt from Symmel US Holdings Inc. Lemmys Holdings Ltd would be able to claim a deduction for the interest payment to Symmel US Holdings Inc. These are corresponding credits and debits, and the UK can be said to be "flat" for tax purposes.

However, in the US, Symmel US Holdings Inc would have a tax-deductible interest expense of $20 million on the loan from Symmel plc. But no interest income would arise from the interest flow between Symmel US Holdings Inc and Lemmys Holdings Ltd because they would be regarded as one entity for the purpose of US tax. As a result, there would be an overall net tax deduction of $20 million within the group.

Broadly in order for the new UK hybrid mismatch rules to apply, the following conditions must be met.

- The payments are made under, or in connection with, an arrangement. Here, a transaction took place resulting in a transfer of money (the interest payment) directly from Lemmys Holdings Ltd to Symmel US Holdings Inc.

- The payer is a hybrid entity. Lemmys Holdings Ltd is a hybrid entity.

- The hybrid payer or a payee is within the charge to corporation tax for a relevant payment period. Lemmys Holdings Ltd is within the charge to UK Corporation Tax.

- It is reasonable to suppose that there would be a hybrid payer deduction/non-inclusion mismatch in relation to this payment. As discussed above, this mismatch arises due to the different treatment of Lemmys Holdings Ltd for tax purposes in the UK and the US, so is directly attributable to the fact that Lemmys Holdings Ltd is a hybrid entity.

- The payer and payee are in the same control group. A control group is a group that prepares consolidated accounts.

As these conditions all appear to be met, the new legislation is likely to apply.

There are a range of possible adjustments under the new legislation, but in this instance, the relevant adjustment will be a restriction to the interest claimed by the hybrid payer i.e. Lemmys Holdings Ltd. This UK company is responsible for making the necessary adjustments in all tax returns that straddle the date that the new legislation commenced - 1 January 2017. An adjustment is required for any part of the accounting period that falls on or after 1 January 2017.

Controlled Foreign Companies (CFC)

The profits of a CFC are exempt from the CFC charge if any one of five entity-level exemptions applies.

The exemptions are:

- The exempt period exemption;
- The excluded territories exemption (ETE);
- The low profits exemption;
- The low profit margin exemption;
- The tax exemption.

It is possible that a number of these exemptions could apply to Symmel Pharma Inc but because only one is required, the most obvious one to consider is the ETE.

In addition to being resident in the excluded territory, there are normally other conditions that need to be met. However, the US is one of six countries to which the simplified ETE applies.

Under this exemption, provided all the income of the company is taxed in the US and the company does not have a permanent establishment outside the US, then the exemption applies.

Conclusion

The interest deductions in Lemmys Holdings Ltd for the period after 1 January 2017 should be disallowed within the relevant corporation tax computations.

Symmel Pharma Inc is very likely to be exempt for CFC purposes. Where a CFC satisfies the ETE rules, there is no requirement for the parent company to make a return in respect of the subsidiary.

Kind regards

Alex Smith

MARKING GUIDE

TOPIC	MARKS	
Hybrids and Other Mismatches		
Identification of Lemmys Holdings Ltd as a hybrid entity	1.0	
New legislation "Hybrids and other Mismatches" and effective date 1 January 2017	1.0	
Treatment absent the legislation		
UK Flat	1.0	
US deduction but no corresponding receipt	0.5	
Therefore D/NI applies	0.5	
The conditions and are they met?		
In connection with an arrangement	1.0	
Within UK CT Charge	1.0	
Is there a hybrid payer D/NI	1.0	
In same group	0.5	
No purpose test	0.5	
Counteraction	1.0	
Company's responsibility to identify and adjust	1.0	
		10.0
Controlled Foreign Companies		
CFC Exemptions	2.0	
Only one needed	1.0	
USA is ETE	1.0	
USA is simplified ETE	0.5	
No requirement to make return	0.5	
		5.0
TOTAL		**15.0**

ANSWER 5

Briefing note regarding migration of Stejar Ltd

The tax residence of Stejar Ltd is determined by its place of effective management. When the controlling directors transferred back to South Africa, it was no longer resident in the UK.

As a result of the migration, Stejar Ltd ceased to be within the charge to UK Corporation Tax (CT) on 31 January 2019. The accounting period ends on that date and there is a deemed cessation of trade.

All assets that do not remain within the charge to CT are treated as being disposed of at market value and trading or capital profits may arise. It may, however, be possible to defer the tax charge arising on these profits.

CT consequences of the migration

1) There will be a deemed gain of £5,811,000 in respect of the Spanish factory.

	£	£
Deemed consideration		13,000,000
Cost	5,000,000	
New workshop	500,000	
		(5,500,000)
Indexation allowance		
$\frac{278.1 - 209.8}{209.8} = 0.326 \times 5{,}000{,}000$	1,630,000	
$\frac{278.1 - 248.7}{248.7} = 0.118 \times 500{,}000$	59,000	
		(1,689,000)
Chargeable gain		£ 5,811,000

2) On migration plant and machinery in the above factory are treated as having been disposed of for capital allowances at market value, £500,000. A balancing charge of £100,000 arises.

   The items of plant should also be reviewed to identify whether any chargeable assets are included. However, even if that is the case, given the fall in value, it is unlikely that any gain arises. Any loss would be restricted by the amount of capital allowance claimed. This means that the company gets a trading deduction for the fall in value rather than a capital loss when the asset is sold.

3) The office block is not a trading asset and as a result of the migration will be outside the UK chargeable gains tax regime. There is a deemed gain of £706,000.

	£
Deemed consideration	3,000,000
Cost	(2,000,000)
Indexation allowance	
$\frac{278.1 - 242.4}{242.4} = 0.147 \times 2{,}000{,}000$	(294,000)
Chargeable gain	£706,000

4) The patent is an intangible asset and there is a deemed disposal of this asset. An income gain of £3,500,000 arises on the migration.

	£
Deemed proceeds	5,250,000
Tax written down value	(1,750,000)
Gain	£3,500,000

Deferment of the liability

Since Ryfe Ltd, a UK company, owns all the shares of Stejar Ltd, they can make a joint election within two years of the date of migration to postpone the tax charge associated with the foreign assets.

Foreign assets are those situated outside the UK and used in or for the purposes of a trade outside the UK. Should the election be made, any postponed tax becomes the liability of Ryfe Ltd.

Without this election, the tax in respect of the deemed disposal becomes payable nine months and one day after the date of the migration i.e. on 1 November 2019.

The amount of tax payable will not be affected by any subsequent disposal proceeds but subsequent transactions can result in the postponed tax becoming payable. This includes the disposal of an asset which contributed to the postponed gain within six years of the migration or the migrating company ceasing to be a 75% subsidiary of the UK parent.

1) As the factory is a trading asset, any liability can be deferred. Should the factory be disposed of before 31 January 2025, the gain will be charged in the accounting period of Ryfe Ltd in which the disposal takes place.

2) The investment property - it is not possible to defer the deemed chargeable gain on assets held as an investment and is situated in the UK. The tax is due on 1 November 2019.

3) It is not possible to defer the gain on a foreign intangible asset, such as the patent, to the extent that it relates to amounts for which a tax deduction has already been taken. As a result, £2,250,000 of the income relating to this asset will be taxable in the accounting period ending 31 January 2019. This relates to the amount of amortisation that has received tax relief. The profit in excess of the original cost, £1,250,000, can be deferred.

	£	£
Income gain (see note 4. above)		3,500,000
Original cost	4,000,000	
Tax written down value	(1,750,000)	
Chargeable to tax		(2,250,000)
Income gain available to be deferred		£1,250,000

Impact of future options

Sale of shares

If the proposed sale to Mr Jary goes ahead, Stejar Ltd will no longer be a 75% subsidiary of Ryfe Ltd. If the election mentioned above has been made, the liability in respect of the Spanish factory and the patent will become payable. The postponed amounts will be brought into account in the CT computations of Ryfe Ltd for the accounting period in which the sale takes place that is 30 June 2022.

	£
Chargeable gain	5,919,000
Non-trade IFA credit	1,250,000
Total	£7,169,000

Sale of factory

If the sale to the third party takes place, and an election has been made, then the gain will be charged in the accounting period of Ryfe Ltd in the year to 30 June 2020. The quantum of the gain is not affected by the subsequent sale price.

MARKING GUIDE

TOPIC	**MARKS**	
CT Consequences		
Ceases to be within charge to CT, AP ends, assets deemed to be disposed of at MV.	1.5	
Calculation of gain on Spanish factory.	1.5	
Calculation of gain on the office block and identify not within UK tax net.	1.0	
Identify that there is an income gain on the patent and correct amount	1.0	
Treatment of disposal proceeds Plant and cover possibility that CG might arise.	1.0	
		6.0
Deferment of the liability		
75% subsidiary therefore election available to defer payment, joint election within two years of the migration.	1.5	
No election then payable nine months and a day after migration	0.5	
If election made then parent becomes liable	0.5	
Subsequent transactions can crystallise liability i.e. disposal within six years or ceasing to be a 75% sub	1.0	
Office block gain cannot be deferred therefore due 1 November 2019	1.0	
Patent only gain over original cost can be deferred	1.0	
Patent difference between original cost and TWDV is not deferred	1.0	
If proposed share sale takes place no longer a 75% sub	1.0	
Gain on factory and patent will crystallise if sale to Mr Jary takes place in AP of transaction	1.0	
If factory sold gain charged in AP of transaction	0.5	
		9.0
TOTAL		**15.0**

ANSWER 6

	£	£
Loss per accounts		(5,163,000)
Add:		
Depreciation (2)	4054,000	
Entertaining (3)	12,545	
Loss on disposal (W1)	100,000	
Interest paid (W2)	596,000	
Adjustment to RDEC (W3)	37,400	
Legal expenses (4)	50,000	
Director' bonuses (5)	400,000	
Pension contributions (W6)	1,320,000	
Less		
Exempt dividends (1)	(310,000)	
Interest receivable (W2)	(272,000)	
		5,987,945
Adjusted trading profit before capital allowances		824,945
Capital allowances (W4)		(2,651,253)
Trading loss		£(1,826,308)
NTLR deficit (W2)		£(324,000)
RDEC payable (W3)		£121,014

Amounts available to surrender

Trading loss (W5)	£1,217,539
NTLR deficit (W5)	£216,000
RDEC (W3)	£18,924

Explanations and workings

1) UK dividends are exempt income.

2) Depreciation is capital in nature and is not allowable.

3) Business entertaining expenses are not allowable.

4) Legal expenses in connection with the sale of the shares are not wholly and exclusively for the purposes of the trade.

5) Bonuses not paid within nine months are not deductible therefore the payment on 1 February 2020 should be added back and relief claimed in the period of payment.

Workings

W1 - Calculation of disposal proceeds

	£
Net book value	250,000
Loss on disposal	(100,000)
Proceeds	£150,000

W2 - Interest

Bank interest received is treated as a non-trading loan relationship credit and not a trading receipt.

Although the loan to purchase the factory was taken out to fund the acquisition of a capital asset, the factory is used for trading purposes and the interest thereon is a trading expense. The interest paid on the loan to purchase the investment is a non-trade expense.

Non-trade loan relationships:

	£
Interest received	272,000
Interest paid	(596,000)
Non-trade loan relationships deficit	£(324,000)

W3 - Research & Development Expenditure Credit (RDEC)

This cannot be claimed in respect of overhead costs or subcontractor costs.

	£	£
Personnel costs	1,033,000	
Consumables	212,000	
	1,245,000	
Actual RDEC 1,245,000 @ 12%		149,400
RDEC in the draft accounts		(112,000)
		£37,400

This is an estimate, therefore an adjustment is required in the computations.

Calculation of amounts to be repaid, surrendered and carried forward:

RDEC for the period	149,400
Less CT rate 19% @ 149,400	(28,386)
Maximum amount payable	£121,014
Amount available to surrender or c/f (£149,400-£121,014)	£28,386
Only available to surrender for the overlap period 28,386 @ 6/9	£18,924
Balance c/f in respect of 9 months ended 31 December 2018	£9,462

W4 - Capital Allowances

	Note	Main Pool	Special rate pool	Allowances claim
		£	£	£
Tax written down value at 1 April 2018		11,247,326	248,562	
First year allowance				
R&D equipment				75,000
Cars		48,000		
New plant	a)	6,400,000		
Air conditioning	b)		170,000	
Disposal proceeds	(W1)	(150,000)		
Annual investment allowance	c)		(150,000)	150,000
		17,545,326	268,562	
Writing down allowance				
18% @ 9/12	d)	(2,368,619)		2,368,619
9% @ 9/12	d)		(16,114)	16,114
Tax written down value at 1 December 2018		15,176,707	252,448	
Allowances claimed				2,609,733

Notes

(a) £3,200,000 was payable more than four months after delivery. That amount is treated as having been incurred when it is required to be paid, which is 1 April 2019.

(b) Air conditioning systems are treated as integral features.

(c) Restricted due to the accounting period being nine months and allocated in the most effective manner.

(d) Restricted due to the accounting period being nine months.

W5 - Group relief calculations

Any losses incurred before the acquisition cannot be surrendered to Griffin Ltd for five years.

Trading loss £1,826,308 @ 6/9 £1,217,539

NTLR deficit £324,000 @ 6/9 £216,000

Griffin Ltd has profits of £8,350,524 @ 6/12 which is £4,175,262 which is sufficient for these losses to claimed.

W6 - Pensions

	£	£
Tax relief for pension contributions is on a paid basis rather than accruals.		
Contributions **paid** in nine months to 31 December 2018		
24 June	400,000	
14 July	1,900,000	
29 September	400,000	
		£2,700,000
Contribution paid in year ended 31 March 2018 (4 x £400,000)		1,600,000
Adjust for difference in length of chargeable period (1,600,000 @ 9/12)		1,200,000
Contributions in current period are 225% of contributions in previous period. As this exceeds 210% spreading of the relief is required		
Excess:		
Contributions **paid** in nine months to 31 December 2018	2,700,000	
Corresponding period (1,200,000) @ 110%	(1,320,000)	
		£1.380,000
Excess is greater than £500,000 and must therefore be spread. As it is between £1million and £2 million it is spread over three years (£460,000 relief per annum).		
Tax adjustment:		
Charged in income statement		3,100,000
Paid in period	2,700,000	
Less effect of spreading	(920,000)	
Allowable for tax		1,780,000
Therefore adjustment required		£1,320,000

MARKING GUIDE

TOPIC	MARKS	TOTAL
Adjustments to trading profit:		
Depreciation	0.5	
Exempt dividends	0.5	
Loss on Disposal	0.5	
Interest		
Received	0.5	
Payable	0.5	
RDEC		
Amount due	1.0	
Adjustment in comps	0.5	
Legal expenses	0.5	
Entertainment	0.5	
Directors bonuses	0.5	
Pension contributions		
Paid basis	1.0	
Spreading		
Amounts paid in each period	0.5	
Adjust chargeable periods to match	0.5	
Identify excess	0.5	8.5
Spread over three periods	0.5	
Capital Allowances:		
FYA		
Cars	0.5	
R&D equipment	0.5	
Calculation and treatment of disposal proceeds	1.0	
Restriction of general pool addition due to instalments	1.0	
Allocation of Aircon to special rate pool	1.0	
Restrict AIA due to short period	0.5	
Allocate AIA against SR Pool	1.0	
Calculation of WDA restricted to 9/12	0.5	
Calculation of total allowances	0.5	6.5
Calculation of liability:		
Trading loss	0.5	
NTLR deficit	0.5	
Group relief		
Trading losses	1.0	
NTLR	1.0	
RDEC		
Amount payable	1.0	
Amounts available to surrender and carry forward	1.0	5.0
TOTAL		**20.0**