The Chartered Institute of Taxation

Advanced Technical

Taxation of Larger Companies and Groups

May 2024

Suggested answers

Answer to Question 1

1)

Argon plc's business consists partly of making investments in foreign subsidiaries. It is therefore a "company with investment business". It may deduct expenses of managing its investment business from its total taxable profits unless they are capital in nature.

The expression "expenses of management" (EOM) is not further defined in legislation, and has therefore been interpreted by the courts in case law.

The ongoing monitoring and appraisal costs are directly incurred in managing Argon plc's investments in foreign subsidiaries and should therefore be deductible as EOM.

The investment bank fees should be EOM provided they were incurred in decision-making and not on the mechanics of implementing a decision to sell that has already been made (which is not management). However, even if they are EOM, they were incurred after an in-principle decision to sell, and applying the Centrica case they should be disallowed as capital.

The legal fees were directly incurred in selling the Neon BV shares. They are therefore capital, and no EOM deduction is allowed.

The disallowed fees may be deducted in the chargeable gain computation for the Neon BV shares.

The HR expenses are not EOM of Argon plc's investment business. They directly benefit Argon SA's business, and not Argon plc's, and should therefore be disallowed by Argon plc. In the future Argon plc should consider re-charging such expenses to Argon SA, which might then obtain a Ruritanian tax deduction.

The total disallowance is £16m (= £12m + £3m + £1m).

2)

Where a transaction between connected parties could produce a UK tax advantage, the transfer pricing (TP) rules adjust its terms for tax purposes to reflect those that would be agreed between independent parties acting at arm's length. Argon plc is participating in the management, control, or capital of Argon Pte Ltd and TP therefore applies to the £400m loan.

An arm's length lender would have charged interest, so Argon plc's interest income should be adjusted upwards. The imputed rate of interest should be based on comparable transactions between independent parties. Banks would lend to Argon group companies at 7.5% per annum, so the imputed interest income is 7.5% x £400m = £30m.

Aggregate net tax interest expense (ANTIE) is the excess of a group's tax interest expense over its tax interest income. Argon plc is the only UK company in the group, so no other companies need to be considered.

Interest on the Argon SA loan is subject to withholding tax (WHT). Argon plc may credit that WHT against its UK tax liability, which effectively means a portion of its UK interest income is not subject to UK tax. In calculating ANTIE Argon plc must reduce its tax-interest income to account for this (W1).

Argon plc's ANTIE is £161m (W2). Because this exceeds the £2m annual interest allowance, the corporate interest restriction (CIR) applies.

The CIR has two main rules:

- The fixed ratio method (FRM), which limits a group's UK net interest deductions for a period to the lower of 30% of its UK tax-EBITDA and its adjusted net group interest expense (ANGIE).

- The group ratio method (GRM), which limits a group's UK net interest deductions for a period to the lower of:
  a) A percentage (the 'group ratio') of its tax-EBITDA corresponding to the ratio of its qualifying net group-interest expense (QNGIE) to its worldwide group-EBITDA; and
  b) QNGIE.

The FRM applies by default, but groups may elect to use the GRM instead.

FRM

Tax-EBITDA is a group's UK taxable earnings before deductions for interest, capital allowances or amortisation for intangibles.

Argon plc's tax-EBITDA is £616m (W3), 30% of which is £185m. This is lower than the group's ANGIE of £200m, so the FRM cap is £185m.

GRM

Group-EBITDA is a group's worldwide earnings before interest, taxes, depreciation, and amortisation. QNGIE is ANGIE but also excluding interest expense due to related parties. The group ratio is 16.7% (W4). This is lower than the 30% fixed ratio. Argon plc should not therefore make the GRM election.

Argon plc's interest capacity is therefore £185m. This exceeds ANTIE of £161m, so the group may deduct all its current year interest. It may also 'reactivate' a further £24m of the interest disallowed in prior years to fully use its interest capacity.

W1:

Reduction to tax-interest income = A/B where:

- A is the foreign tax credited against UK tax (i.e., £15m x 10% = £1.5m), and
- B is the corporation tax rate (i.e., 25%)

The reduction is therefore 1.5m / 25% = £6m

W2:

	£m
Interest on Argon SA loan (£200m x 7.5%)	15
TP adjustment on Argon Pte Ltd loan	30
WHT adjustment (W1)	(6)
Interest expense	(200)
ANTIE	**(161)**

W3:

	£m
Profit before tax	665
Add:	
Depreciation	100
Interest payable	200
Disallowed expenses	16
Less:	
Interest receivable	(15)
Dividends	(350)
Tax-EBITDA	**616**

W4

	£m
PBT	800
Add:	
Depreciation	200
Interest payable	200
Group-EBITDA	**1,200**

QNGIE = £200m

Group ratio = QNGIE/Group-EBITDA = 200m/1,200m = 16.7%

3)

To reactivate disallowed interest from prior periods Argon plc must (if it has not previously done so) appoint a reporting company (RC) and file a full interest restriction return (IRR). Argon plc is the sole UK group company and hence the only company eligible to be the RC.

The RC must be appointed within 12 months of the end of Argon plc's period of account.

The RC must file an IRR by the same date. A full IRR should:

- identify the UK group companies (and the ultimate parent if it is non-UK),
- contain any relevant elections, and
- include calculations of:
  - Argon plc's tax-EBITDA and net tax-interest expense or income,
  - either the fixed ratio debt cap or GRR percentage as appropriate, and
  - the interest allowance for the period.

The IRR should also report Argon plc's interest reactivation. Argon plc should then report a deduction for the reactivated interest in its company tax return for the period ended 31 March 2024. If that return has already been made it may be amended irrespective of any other time limits that may apply.

MARKING GUIDE

TOPIC	MARKS	SUB-TOTAL
<u>Management expenses</u>		
- Identify that Argon plc has an investment business in relation to its foreign subsidiaries	0.5	
- Explain basis on which expenses of management are deductible	1.0 0.5	
- Allow ongoing costs (EOM, revenue in nature)	0.5	
- Disallow legal fees (capital, directly connected to sale)	1.5	
- Reasoned discussion and conclusion re investment bank fees	1.0	5
- Expenses re employee claim are for Argon SA's business therefore disallow		
<u>Interest deductions</u>		
- Identify requirement for TP adjustment to interest free loan	1.0	
- Explain basis on which to impute interest to interest-free loan	1.0	
- Calculate net tax interest expense	0.5	
- Adjustment to tax interest income in respect of interest WHT	1.5	
- Interest expense exceeds £2m de minimis therefore CIR applies	0.5	
- Explain Fixed Ratio Method and Group Ratio Method, including debt caps	2.0	
- GRM is elective	0.5	
- Calculate tax-EBITDA, including deduction of dividends	1.0	
- Calculate interest allowance under FRM	0.5	
- Calculate group-EBITDA and the group ratio	1.0	
- Conclude GRM election not favourable	0.5	
- Conclude no CIR disallowance for year	0.5	11
- Ability to reactivate prior year interest up to interest capacity	0.5	
<u>CIR admin</u>		
- To obtain reactivations must appoint RC which must file full IRR	1.0 0.5	
- RC appointment deadline	0.5	
- IRR filing date	1.0	
- Contents of IRR	1.0	
- IRR to report reactivation; effect flows through into company tax return		4
TOTAL		**20**

Answer to Question 2

1)

		Main pool £	SR pool £	Allowances £	Notes
TWDV b/f		4,000,000	-	-	
SD expenditure					
Kitchen equipment	1,150,000	-	-	-	1
Transport and installation	20,000	-	-	-	2
Floor alterations	30,000	-	-	-	3
Subtotal	1,200,000				
7.4% uplift	88,800	-	-	-	4
Super-deduction	(1,288,800)	-	-	1,288,800	
FE expenditure					
Smart TVs	700,000	-	-	-	5
Paintings	800,000				6
Full expensing allowance	(1,500,000)	-	-	1,500,000	
SR expenditure					
Thermal insulation	300,000	-	-	-	
AIA	(300,000)	-	-	300,000	7
Cars	500,000	-	-	-	8
Pooled	(500,000)	-	500,000	-	
18% WDA	-	(720,000)	-	720,000	
6% WDA	-	-	(30,000)	30,000	
TWDV c/f	-	3,280,000	470,000	-	
Total allowances	-	-	-	3,838,800	

Notes

1. The kitchen equipment was new plant and machinery (P&M) purchased between 1 April 2021 and 31 March 2023, and therefore qualifies for the super-deduction.

2. Transport and installation costs are expenditure on the provision of P&M and qualify for capital allowances on the same basis as the P&M to which they relate.

3. Expenditure on alterations to a building is deemed to be expenditure on P&M where the alterations are incidental to the installation of P&M. The floor strengthening costs therefore also qualify for the super-deduction.

4. Because Monck Ltd's accounting period ends after 31 March 2023, the rate of super-deduction must be reduced from the ordinary 130%. The rate is calculated as:

   100% + 30% x A/B

   where A is the number of days in the accounting period before 1 April 2023, and B is the total number of days in the accounting period. Here the rate is:

   100% + 30% x 90/365 = 107.4%

5. The Smart TVs were new P&M purchased between 1 April 2023 and 31 March 2026, and therefore qualify for the "full expensing" 100% first year allowance.

6. The paintings are decorative. While assets that form the setting in which a business takes place are not generally P&M, there is an exception for decorative assets in hospitality trades that create ambience for customers. The paintings are therefore eligible for full expensing.

7. Expenditure on thermal insulation is deemed to be qualifying expenditure on P&M. It is special rate (SR) expenditure, but may qualify for either a full expensing 50% first year allowance or the 100% Annual Investment Allowance (AIA), which is up to £1 million per annum. The AIA is most favourable.

8. The cars were purchased under a hire purchase contract that is accounted for as a finance lease. Monck Ltd is therefore treated as the owner of the cars for the duration of the contract, and entitled to claim capital allowances. It may claim allowances for all its capital expenditure under the contact, including the future instalments. Although the expenditure totals £550,000 (£150,000 + 40 x £10,000), only the £500,000 fair value is capital – the remainder is a finance cost and therefore revenue expenditure. Cars do not qualify for full expensing or AIA. Because Monck Ltd's cars have CO_2 emissions exceeding 50 g/km, the expenditure must be allocated to the SR pool.

9. The restoration is a repair to existing furniture that has become dilapidated. It does not enhance the furniture but returns it to its original state. The expenditure is therefore on revenue rather than capital account (and a trading deduction will be available).

2)

Monck Ltd receives tax deductions for its expenditure on vehicles at a slower rate than the expenditure is recognised in its income statement as depreciation. That is reflected in the difference between the vehicles' accounting NBV and their tax written-down value. The company should recognise a deferred tax asset (DTA) in respect of this deductible temporary difference provided it is probable that taxable profit will be available in the future against which the difference may be utilised. A corresponding deferred tax credit should be recognised in its income statement.

The deferred tax balances for the period ended 31 December 2023 are as follows:

	TWDV £s	NBV £s	Difference £s	DTA @ 25% £s
At 1 January 2023	0	0	0	0
At 31 December 2023	470,000	300,000	170,000	42,500
Movement				42,500

DTAs are measured at the tax rate expected to apply when the DTA is settled, based on the laws substantively enacted at the period end. Monck Ltd should therefore apply the main corporation tax rate of 25%.

Monck Ltd should recognise the following accounting entries:

DR	DTA (balance sheet)	£42,500
CR	Tax expense	£42,500

MARKING GUIDE

TOPIC	MARKS	SUB-TOTAL
Capital allowances		
- Kitchen equipment qualifies for super-deduction, including conditions	1.0	
- Correct treatment of transport and installation costs	0.5	
- Building alterations incidental to installation of P&M treated as P&M	0.5	
- Correct calculation of reduced super-deduction allowance	1.0	
- Smart TVs qualify for 100% FY full expensing, including conditions	1.0	
- Paintings are setting but regarded as P&M because create ambience	1.0	
- Thermal insulation is deemed SR expenditure	0.5	
- AIA available in respect of thermal insulation	0.5	
- Cars bought under hire purchase contract – Monck Ltd deemed owner, entitled to claim for all capital expenditure under the contract	1.5	
- Cars do not qualify for FE or AIA	0.5	
- Cars are SR expenditure because emissions >50 g/km	0.5	
- Restoration is revenue expenditure, with explanation	1.0	
- Main pool and SR pool WDA rates	0.5	
- Correct computation of overall allowances	1.0	
		11
Deferred tax		
- Deferred tax should be accounted for to reflect temporary differences between the tax base and accounting profits	1.0	
- DTA only recognised if future taxable profits are probable	0.5	
- Calculation of temporary differences at beginning and end of year	1.0	
- Calculate DTA at 25% tax rate	0.5	
- Correct accounting entries	1.0	
		4
TOTAL		**15**

Answer to Question 3

1)

Zutroy plc will realise a chargeable gain of £91.375m on the Rukim Ltd shares (W1).

The substantial shareholding exemption (SSE) will apply provided:

- Zutroy plc owned at least 10% of Rukim Ltd's ordinary share capital throughout a 12-month period within the six years before the sale; and

- During the 12 months before the sale, and immediately after, Rukim Ltd was trading and did not have substantial non-trading activities (typically judged according to whether 20% of a company's assets, income and staff resources relate to non-trading activities).

Zutroy plc owned 100% of Rukim Ltd's ordinary shares for 27 years and meets the first condition. Both ordinary and preference shares may qualify for SSE, but this condition is tested by reference to ordinary shares only.

Rukim Ltd is trading, and does not have non-trading activities (the office building is a trading asset). The second condition is met.

SSE therefore applies to Zutroy plc's gains.

A parent company forms a chargeable gains (CG) group with companies that are:

- its 75% subsidiaries, or a 75% subsidiary of such subsidiaries, etc., and
- effective 51% subsidiaries of the parent company.

Rukim Ltd is a wholly owned subsidiary of Zutroy plc and therefore part of Zutroy plc's CG group.

Transfers of capital assets within a CG group are deemed to happen for consideration that produces no gain or loss (NGNL) for the transferor. No chargeable gain therefore arose when Zutroy plc sold the office building.

However, if a transferee leaves a CG group within six years of receiving an NGNL transfer a "de-grouping charge" arises. The transferor is deemed to realise a gain equal to that which would have arisen had it sold the transferred asset for its market value (MV) at the transfer date.

Zutroy plc will incur a de-grouping charge. However, if the transferee leaves the group because of a share disposal then any de-grouping charge is added to the share disposal gain. Zutroy plc's charge is added to its gain on the Rukim Ltd shares. As SSE applies to that gain, SSE is also deemed to apply to the de-grouping charge.

Rukim Ltd's base cost for the building will be uplifted to its MV of £5m.

W1:

	£'000
Proceeds	100,000
Less:	
Cost - ordinary shares	(2,000)
Cost - preference shares	(1,000)
Indexation (W2)	(5,625)
Chargeable gain	**91,375**

W2:

Indexation factor = (278.1 – 96.73) / 96.73 = 1.875

Indexation allowance = £3m x 1.875 = £5.625m

2)

Rukim Ltd's £10m loss is a post-1 April 2017 trading loss, which may be carried forward and relieved against the company's total profits of later periods.

When Rukim Ltd becomes a wholly owned subsidiary of Pinchon plc the companies will be members of the same group relief group. From then, the loss may be group relieved against the total profits of UK companies in the Pinchon group.

However, because Rukim Ltd's ownership changed, group relief for brought forward losses is prohibited until five years after the end of Rukim Ltd's accounting period (AP) in which the change occurred, i.e., 30 September 2029.

The carried forward loss that may be relieved against the total profits of any company is limited to:

- the company's deductions allowance for the period, plus
- 50% of its total profits after deduction of the allowance.

The group has an annual deductions allowance of £5m, which may be freely allocated among group companies.

The loss will be ineligible for relief if, within a five-year period beginning no more than three years before Rukim Ltd's change in ownership there is a major change in the nature or conduct of the company's trade (including changes in its services provided, customers, outlets, or markets).

Whether Rukim Ltd has undergone a major change depends on all the facts. Changes to the company's service lines, referral channel and client base could indicate a major change, however further information is required to conclude.

3)

HMRC may enquire into Rukim Ltd's company tax return by giving notice within 12 months of the filing deadline.

If HMRC determines the loss is overstated, it may issue a closure notice stating its conclusions, and amending the return accordingly.

Alternatively, if HMRC discovers Rukim Ltd's loss is overstated after the enquiry deadline, it may issue a discovery determination, but only if the overstatement:

- was careless or deliberate; or
- HMRC could not have been reasonably expected to be aware of it when the enquiry deadline passed.

Rukim Ltd may appeal either a closure notice or discovery assessment to the First Tier Tribunal.

MARKING GUIDE

TOPIC	**MARKS**	**SUB-TOTAL**
Gain on sale		
- Chargeable gain on sale	0.5	
- Indexation allowance	0.5	
- SSE: substantial shareholding condition	1.0	
- SSE: trading status of investee	1.0	
- SSE: preference shares qualify provided substantial shareholding condition met in respect of ordinary shares	0.5	
- Zutroy plc and Rukim Ltd in same CG group	0.5	
- Transfer of building was NGNL	0.5	
- De-grouping charge in respect of building	1.0	
- De-grouping charge may be added to share sale proceeds and benefit from SSE.	1.0	
- Building cost is re-based for Rukim Ltd	0.5	7
Losses		
- Post-1 April 2017 loss, carry forward against total profits	0.5	
- Rukim Ltd and Pinchon plc in the same group	0.5	
- Group relief to Pinchon companies	0.5	
- 5-year restriction post change of ownership	0.5	
- 50% loss restriction including deductions allowance	0.5	
- MCINOCOT restriction, including five-year test period	1.5	
- Reasoned discussion of MCINOCOT	1.0	5
Administration		
- Power to open enquiry	0.5	
- Enquiry deadline	0.5	
- Enquiry ends with issue of closure notice	0.5	
- Power to issue discovery assessment	1.0	
- Appeal to FTT	0.5	3
TOTAL		**15**

Answer to Question 4

There are two types of relief for expenditure on Research and Development (R&D) depending on whether a company is large, or a small and medium-sized enterprise (SME).

A company is large if it is not a SME.

A company is a SME if it has fewer than 500 employees and has either turnover of less than or equal to €100 million or assets of less than or equal to €86 million. These limits are aggregated for linked enterprises.

Hazdan UK Ltd clearly exceeds these amounts and therefore is a large company for R&D relief purposes.

Two enterprises are linked if one enterprise can exercise control over the affairs of the other. Hazdan UK Ltd owns 100% of the shares in Hazdan Innovations Ltd. They are linked and Hazdan Innovations Ltd will also be classified as large for R&D relief purposes.

Both companies may only therefore claim R&D expenditure credit (RDEC).

<u>Calculation of tax liability and RDEC for the year ended 31 March 2024</u>

		Hazdan UK Ltd		Hazdan Innovations Ltd	
	Notes	£'000	£'000	£'000	£'000
Turnover		150,000		10,000	
RDEC	1	200		1,800	
			150,200		11,800
Qualifying R&D expenditure		(1,000)		(9,000)	
Other expenditure		(147,000)		(3,000)	
			(148,000)		(12,000)
Taxable profits			2,200		nil
Tax at 25%			**550**		**nil**
RDEC		200		1,800	
Step 1: Corporation Tax	2	(200)	(200)	-	-
Step 2: Cap at net value	3	-	-	(1,350)	1,350
Carry forward, or		-	-	450	-
use as group relief		-	(350)	(350)	-
Carry forward to next period		-	-	**100**	-

Step 3: Possible cap	4	-	-	-	-
Steps 4, 5, 6: No other liabilities	5, 6, 7	-	-	-	-
Tax payable			**nil**		-
Tax credit repayable			-		**£1,350**

Notes:

1) RDEC equal to 20% of Qualifying R&D expenditure. The RDEC is a taxable receipt.

2) The tax credit must be used firstly to reduce the Corporation Tax liability for the period to which to relates.

3) Where the credit is not fully used against current period Corporation Tax liability, only the net value (that is net of the main rate of tax) can be utilised against other liabilities of the period or paid to the company. The excess can be surrendered to a group company or will be carried forward and offset against the Corporation Tax liabilities of the claimant company in subsequent periods. In this case £350,000, will be surrendered to Hazdan UK Ltd and the balance of £100,000 carried forward.

4) The credit can be further restricted should the net value calculated at step 2 exceed the PAYE and Class 1 NIC liability relating to the R&D staff. As that liability is £1.5 million, no further restriction is required.

5) Hazdan Innovations Ltd does not have any liabilities to pay to HMRC which may reduce the payable tax credit.

6) Hazdan UK Ltd has no further tax liabilities in the period.

7) Hazdan Innovations Ltd can make a claim for the remaining £1,350,000 tax credits to be paid to it in cash.

MARKING GUIDE

TOPIC	**MARKS**
Hazdan UK Ltd is large for R&D relief	1.0
Hazdan Innovation Ltd also large due to being linked	1.0
Calculate TTP for UK	0.5
RDEC for UK	0.5
TTP for Innovation	0.5
RDEC for Innovation	0.5
Step 1 for Hazdan UK Ltd	1.0
Step 2 for Hazdan Innovation Ltd cap	1.0
Step 2 surrender to Hazdan UK Ltd	1.0
Step 2 carry forward to subsequent periods	0.5
Step 3 No restrictions for PAYE/NIC	1.0
Steps 4-6 No restrictions	1.0
Step 7 Amount to be repaid	0.5
TOTAL	**10.0**

Answer to Question 5

Definition

A controlled foreign company (CFC) is a company which is not resident in the UK and is controlled by a UK resident person or persons.

Control is:

- the power to secure the affairs of the company are conducted as the persons wish,
- a shareholding of more than 50%, or
- one UK shareholding of 40% and non-UK holders have less than 55%.

All the non-resident companies apart from Tripletree (Deo) Ltd are controlled by UK persons as they are 100% owned by Tripletree (UK) Ltd. They are all therefore CFCs apart from Tripletree (Deo) Ltd.

When a company is a CFC, it is possible that the profits it makes will be taxable in UK. If the profits are taxable, they will be taxed at the main UK Corporation Tax rate, but the company should get credit for any foreign tax paid.

The profit can be apportioned to the company holding the shares based on its percentage interest in the CFC.

However, there are exemptions, and other tests commonly known as gateway tests, which may eliminate the CFC charge.

The CFC legislation does not specify an order between the exemptions and the gateways and companies can consider either method first.

Exemptions

1) Exempt period. This is a temporary exemption which can apply in the 12-month period when the company first becomes a CFC. As Tripletree (UK) Ltd has owned all the companies for more than five years this does not apply to any of the CFCs.

2) Excluded territories. Companies which are resident in certain territories can be exempt subject to meeting certain criteria. The criteria include that the company must carry on a business in the excluded territory and that the company must be liable to tax in the relevant territory. A list of the excluded territories is available online at gov.uk but none of the countries are on that list.

3) Low profits exemption. This applies if a company's accounting profits, or total taxable profits are less than £50,000. It also applies where accounting profits or total profits are less than £500,000 and not more than £50,000 is non-trading income. This exemption should apply to Tripletree (Ena) Ltd, and no CFC apportionment will be necessary for this company.

4) Low profit margin exemption. Where a company's profit margin is less than 10%, this exemption can apply. The operating expenditure brought into account in determining accounting profits for the relevant period is used as the basis of calculating the profit

margin for the purposes of this exemption This exemption should apply to Tripletree (Tesera) Ltd since it charges cost plus 7%.

5) Tax exemption. If the tax paid in the territory where the CFC is resident is more than 75% of the UK Corporation Tax that would be paid if the CFC were UK resident, this exemption may apply. As the rate of corporate taxes in Trialand is 22% then this exemption applies to Tripletree (Tria) Ltd.

None of the exemptions apply to Tripletree (Pendeland) Ltd. It is necessary to consider the gateway tests to identify if any profits need to be apportioned to Tripletree (UK) Ltd.

The five gateway tests

The above exemptions look at a CFC as an entity and therefore if they apply, all the company's profits will be exempt. The gateway tests can apply to some or possibly all of a non-exempt CFC's profits. For profits of a CFC to be apportioned to Tripletree (UK) Ltd, they must pass through at least one of five gateways. However, as Tripletree (Pende) Ltd only had profits from the provision of management and technology services to other group companies, the following four do not apply:

- non-trade finance profits,
- trade finance profits,
- captive Insurance, and
- solo consolidation.

The fifth gateway is 'profits attributable to UK activities'. This gateway does not apply if any of the following conditions apply:

1) The motive test - there are no assets held or risks undertaken with the main purpose of reducing or eliminating UK tax?

2) The company has no assets managed from the UK or bear any UK risks?

3) Can the company operate effectively without any assistance from the UK?

4) Are the company's profits only from property or from non-trading loan relationships?

Significant people functions

Significant people functions are the key business and management functions relating to the control of assets and the management of risk. The significant people functions should be considered in the context of the business, and would involve functions that require active decision-making regarding the management of business risks and business asset. Any CFC profits for which the related significant people functions are undertaken outside the UK will not be subject to the CFC charge.

Safe harbour conditions

This gateway also does not apply if any one of the following 'safe harbour' conditions is met.

1. Business premises. The company must have a physical presence in the country of residence. This must be where its main activities are carried out and have a degree of permanence (usually more than twelve months).

2. The company must derive less than 20% of its total trading income from relevant trading income directly or indirectly from the UK.

3. The company must not incur costs of management in the UK which exceed 20% of its total costs of management expenses.

4. The company must not derive income from intellectual property which was transferred from the UK within the last six years.

5. The company must not derive more than 20% of its income from the export of goods from the UK.

All profits of Tripletree (Pende) Ltd are from management services carried out in Pendeland. There does not appear to be any significant people functions carried out in the UK and the company does not manage and control any UK assets or risks. The company has offices in Pendeland.

The profits of the company do not pass through any of the gateways and there will be no need to apportion any of those profits to Tripletree (UK) Ltd.

MARKING GUIDE

TOPIC	**MARKS**	
Definition of a CFC	1.0	
Meaning of control	1.0	
Identify the CFCs (all but Deo)	1.0	
Apportionment subject to exemption and gateway tests	1.0	
		4.0
Exempt period	0.5	
Excluded territories	1.0	
Low profits exemption Tripletree (Ena) Ltd	1.0	
Low profits margin exemption Tripletree (Tesera) Ltd	1.0	
Tax exemption (Tesera)	1.0	
No exemptions apply to Pende	0.5	
		5.0
The four gateway tests that do not apply to Pende	2.0	
		2.0
UK activities – four tests	1.0	
The four tests	2.0	
SPF define and explain	1.0	
Safe harbours	1.0	
Business premises	1.0	
Four other safe harbours	2.0	
		8.0
Conclusion		1.0
TOTAL		**20.0**

Answer to Question 6

Stepclive Finance Ltd: Corporation Tax computation for the year ended 31 December 2023

	Notes	£'000	£'000
Profit per accounts			2,500
Less:			
Change in bad debt	1)	3,000	
Pension spreading	2)	750	
Property income	3)	700	
			(4,450)
Add:			
Loan Interest	4)	4,000	4,000
Trading profit			**2,050**
Property income	3)		700
NTLR deficits	4)	4,000	
Trading profit		(2,050)	
Property income		(700)	
Available for group relief		**1,250**	
Surrender as group relief	5)		1,250
Total taxable profit			nil

Notes:

1) The transactions regarding the bad debts would not have been allowed or taxed in 2021 as the debt was to a connected person. The reversal of the write off is similarly not allowed or taxed in 2023.

2) For an excess pension contribution of £3 million, the period of spreading is four years. Therefore £750,000 is allowable in each of the years ending 31 December 2021, 31 December 2022, 31 December 2023, and 31 December 2024.

3) Property income and expenses are removed from the trading computation and taxed as a separate source of income.

4) Interest on the loan to invest in the equity of Stepclive Trading Ltd is not allowed as a trading deduction. Instead, it should be deducted from total taxable profits. The corporate interest restriction brought forward allowances covers this interest expense, therefore there will be no interest disallowance in this period.

5) The company surrenders its loss to Stepclive Trading Ltd to minimise the tax paid by the group for the period.

Stepclive Trading Ltd: Corporation Tax computation for the year ended 31 December 2023

	Notes	£'000	£'000
Profit per accounts			9,337
Add:			
Depreciation	1)	2,000	
Change in bad debt	2)	3,000	
			5,000
Capital allowances	W1		(9,005)
Trading profit			**5,332**
Losses brought forward			(4,000)
Group relief	3)		(1,250)
Total taxable profit			**82**
			£
Taxable profits Jan to Mar			20,500
Taxable profits Apr to Dec			61,500
Jan to Mar @ 19%			3,895
Apr to Dec @ 25%			15,375
Marginal relief	4)		(484)
Tax liability			**£18,786**

Notes:

1) Depreciation is capital in nature and is not deductible for tax purposes.

2) The transactions regarding the bad debts would have not been allowed or taxed in 2021 as the debt was to connected person. The reversal of the write off is similarly not allowed or taxed in 2023.

3) Group relief is claimed from Stepclive Finance Ltd to minimise the tax paid by the group.

4) Marginal Relief applies where a company's profits for an accounting period are between the upper and lower limits of £250,000 and £50,000. The relief is calculated by applying the appropriate fraction to the difference between the upper limit and the taxable profit. The upper limit is reduced where the company has any associated companies. In this case there is one associated company therefore the upper limit is divided by two. The upper limit is also reduced where the accounting period straddles the date the relief was introduced on 1 April 2023.

Two companies for nine months	£	£
250,000/2 x 9/12	93,750	
Profit of £ 82,000 X 9/12	(61,500)	
Use fraction 3/200	32,250	484

Working 1 - Capital allowances

	Notes	Main Pool	Special Rate Pool	Allowances claimed
		£	£	£
Tax written down value at 1 January 2023		10,000,000	500,000	-
New plant and machinery	1) and 2	4,100,000		-
Full expense claim	1) and 2)	(4,100,000)		4,100,000
New vans	3)	1,075,000		
Full expense claim		(1,075,000)		1,075,000
Integral features			3,000,000	
AIA	4)		(1,000,000)	1,000,000
FYA 50%	5)		(1,000,000)	1,000,000
Writing down allowance (18% and 6%)		(1,800,000)	(30,000)	1,830,000
Tax written down value at 31 December 2023		8,200,000	1,470,000	-
Allowances claimed				**£9,005,000**

Notes:

1) The obligation to pay for plant that is constructed becomes unconditional when the work is certified. Therefore, the £2.5 million certified on 20 November 2023 is expenditure on main rate pool assets and the full expense can be claimed.

2) Additionally, work completed in the accounting period and certified within one month of the end of the accounting period is treated as incurred immediately before the end of the accounting period, therefore the £1.6 million certified on 17 January 2024 is also expenditure on main rate pool assets and the full expense can be claimed.

3) New vans are treated as plant and machinery and are eligible for full expensing.

4) Annual investment allowance for 31 December 2023.

			Annual amount	Pro rata amount
			£	£
01/01/2023	31/03/2023	3/12	1,000,000	250,000
01/04/2023	31/12/2023	9/12	1,000,000	750,000
Total				**1,000,000**

Annual investment allowance is used against the special rate expenditure because it provides a greater allowance for the year.

5) A first-year allowance of 50% can be deducted from the £3 million of the expenditure which qualifies for the special rate pool. However, £1 million of that expenditure has already subject to an AIA claim so the claim is limited to 50% of £2 million.

MARKING GUIDE

TOPIC	MARKS	
Trading company:		
Depreciation	0.5	
Bad debt	1.0	
		1.5
Capital allowances		
P&M general pool - new vans	0.5	
Constructed plant in period work certified	1.0	
Constructed plant in period work certified	1.0	
Integral features to special rate pool	1.0	
50% FYA special rate pool	1.0	
Allocate correct AIA against special rate pool	1.0	
Calculation of WDA each pool	1.0	
Calculation of total allowances	0.5	
		7.0
Total taxable profit	0.5	
Losses brought forward	1.0	
Group relief	1.0	
		2.5
Calculation of liability		
Straddle 19% 25%	0.5	
Marginal relief	1.5	
Tax due	0.5	
		2.5
Financial company:		
Bad debt	1.0	
Pension spreading	1.0	
Loan interest	0.5	
Property income	0.5	
		3.0
Trading income	0.5	
Property income	0.5	
NTLR debit No CIR	1.0	
Use NTLR as group relief (conditions)	0.5	
Use NTLR against Property income	0.5	
Use NTLR against Trading income	0.5	
		3.5
TOTAL		**20**