Part A

Answer-to-Question-_1_

ED Plc - UK trading company, APE 31 March, GBP functional currency

31/03/2020 USD 50m borrowed from bank - assumed loan/liability is issued in USD. share acquired in US subsidiary and held as an investment.

at 31/03/20 USD 50m / 1.28FX rate = £39,062,500

1)

for 31 March 2020 APE ED PLC will shows a liability in its balance sheet of £39,062,500 to its bank, this is the first balance sheet date since the loan was granted. ED Plc will also show an investment in subsidiary of £39,062,500 (the same amount) as an asset on its balance sheet.

for 31 March 2021 APE the exchange rate has increased to 1.29 so the £50m liability is now £38,759,869 under fair value liability accounting (assuming no capital repayments have been made or interest rolled up in the balance). this change represents an exchange rate gain of £302,631 which will be accounted for through the P&L, impacting retained earnings. ED Plc's USD 50m investment in its US sub will remain recorded at book value (£39,062,500) in accounts.

For 31 March 2022 APE the exchange rate has increased to 1.37

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so the £50m liability is now a £36,496,350 liability in the balance sheet, a fx gain for the year of £2,263,519 which will be accounted for through the P&L and impacting retained earnings. again, ED Plc's USD 50m investment in its US sub will remain recorded at book value (£39,062,500) in accounts.

2)

for 2020 there has been no balance sheet movement in the FX values as this is the same year the loans were first recorded, as such there will be nothing to recognises for tax purposes.

for 2021 there has been an FX gain on the liability of £302,631,the loan was used for investment rather than trading purposes so this will be taxable in this year as a non trading loan relationship credit. Any interest paid on the loan in the year will be a non-trading loan relationship debit which cannot be set again trading profits, but can be set against the NTLR credit.

for 2022 there has been an fx gain of £2,263,519. this will be treated as a NTLR credit, as in 2021.

3)

in 2023 US sub writes of RD programme. the US sub is sold for $30m, the spot exchange rate is 1.40 so ED plc received £21,428,571, representing a chargeable loss of £17,633,929 against its £39,062,500 initial investment. this entire amount will be recognised as an investment (not trading) loss in this accounting period. assuming the repayment of the bank loan is at the same spot rate then there will be a further fx gain of

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£782,065, this will a taxable NTLR credit but the loss on sale of the investment can be set against this.

Answer-to-Question-_2_

MEMO:

this memo seeks to set out the advantages and disadvantages of the proposed capital issuances;

1) - Capital Adequacy:

redeemable 4% fixed rate preference shares - as these are preference shares they would not be treated as tier 1 capital for regulatory purposes. regulators require tier 1 capital to not have preferential rights over other types of shares,it is expected that they would absorb losses before other classes of inventors. I would therefore not recommend issuing these shares if Tier 1 status is essential to expanding the loan book.

convertible 4% perpetual fixed rate bonds - these are not share capital, but are convertible bonds and would therefore be treated as additional tier 1 for regulatory purposes. this therefore meet the requirements to be tier 1 cap

2) treatment of servicing costs:

redeemable 4% fixed rate preference shares - the cost of servicing preference shares would be a distribution to shareholders taken from retained earning for accounting purposes, this amount would not be deductible for tax purposes.

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convertible 4% perpetual fixed rate bonds - perpetual and long dated debt is treated as equity for tax purposes and therefore no tax deduction is avails on servicing the debt. this is unless the instrument qualifies as a hybrid capital instrument (under UK tax rules) and a valid election is made within 6 months of the instrument being issued, we do not have sufficient information to determine if this instrument would be eligible, it would need (among other things) for payments to be cancelable by the debtor (alpha bank).

3) treatment of returns by investors:

redeemable 4% fixed rate preference shares - investors would treat their returns as dividends which are franked investment income for tax purposes, they would therefore pay dividend tax on the receipts.

convertible 4% perpetual fixed rate bonds - returns on bonds are typical investment income in the hands of investors, however, where they have been treated as equity in the hands of the debtors i would expect for these to be treated as franked investment income to avoid economic double taxation.

4) consequences of preference share redemption:

the bank has issued the preferences share to fund expand the banks loan bond, which is part of its trade. on redemption of the preference shares the bank would be expect to recognise an chargeable gain or loss which be taxable/deductible as part of its trading income.

5)potential additional lending:

Regulators set the tier 1 requirements of a bank based on a ratio of their risk weight assets. any increase in the banks loan book would increase its risk weighted assets, this means that if there is not sufficient excess tier 1 above current regulatory requirements, further tier 1 will need to be issued before the loan book can be expanded. of the two proposal, only the convertible 4% perpetual fixed rate bonds meet the requirements of tier 1 capital, i would therefore recommend selecting this type of instrument.

Part B

Answer-to-Question-_3_

UM Plc borrows EUR 50m, 5 year terms, from MB.

interest is payable annually to MB UK branch

relevant DTA states interest is taxable in state of beneficial owner.

loan should be eurobond notes, but never issued as such.

1) UM plc - has received a loan in EUR so will have to account for the FX differences. it is likely to account for any FX movements on the loan at the average FX rate at Accoutring period end, interest is due annually on the APE date so will use the same rate.

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the FX rate across the period we have been provided shows a fall, which would result in an FX loss, and then a gain over and above that loss the following year.

it is likely that UK PLC sought to reply on the quoted euro bond exemption from deduction withholding tax on the interest payments but it has failed to issues the on the recognised stock exchange. this means UM PLC will have to deduct WHT from the payment, unless there is another domestic, or treaty provision, reliving it from this obligation.

2) MB UK branch - a key issue is where the interest is taxable under the UK/Netherlands treaty. we are told that this will be in the state the beneficial owner is resident.

we are told that the loan was "from Martindale Bank" wit a contract governed by English law and enforceable in English courts. from this we can not be certain whether the loan was issued by the UK branch or the HQ bank in Netherlands.

Looking at the OECD 2010 report on attribution of profits to a PE we know that it is important to carry out a thorough function and factual analysis when attributing functions assets and risk to a branch. in doing this should identify the significant people functions which in a bank are likely to comprise of key entrepreneurial risk taking (KERT)functions. in a bank KERT are likely to be concerned with work to create a financial asset, typically a loan, or the subsequent management of the risks associated with the loan. this distinction recognises that why a PE, such a MB UK branch, may have created an asset, but it is possible for that the subsequent management of the created risk

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is transferred and therefore so should the asset.

If it is determine, after following the OECD analysis that the loan is an asset of the PE it is therefore the beneficial owner for treaty purposes, it will be taxable in the UK on that interest. in calculating the profits of the PE MB will need to consider, among other things, the attribution of capital to the PE. the PE will need to have an appropriate amount of capital to support the assets it holds which may include the loan to UM plc. if the capital is in the form of debt, the PE will receive a tax deduction for interest on that debt which can be set again the interest receipt from UM plc. attribution of free capital (being capital in the whole enterprise that is none interest bearing) would also have to be attributed to prevent excess deductions in the PE and leaving all free capital sitting with the HQ bank. the 2nd part of the OECD 2010 report on PEs sets out a number of methods for attributions capital to a PE, including the BIS capital allocation approach, economic capital allocation approach, thin capitalisation approach and the safe harbour quasi thin cap/regulatory minimum approach.

3) MB - As a non-uk entity, if the interest is beneficially owned by MB it is possible, for the reasons discussed above, that WHT will have been deducted. if this is the case then MB will have make a claim in its Netherlands tax return for a credit or exemption method (?) under the treaty for the WHT deducted (assuming the treaty is based on the OECD MTC these would be in articles 23a and 23b). regardless of whether the loan is recognised in the PE or the HQ bank, MB would need to ensure it

has sufficient tier 1 capital to support the additional risk weights assets created by the loan under regulatory requirements. regulators look at the consolidated position of the group, so even if the loan was an asset of the PE, this would not change the regulatory position.

beneficial ownerships is generally a difficult subject and has to be considered in a number of context. for FATCA and CRS when determining benefical ownership we are asked to look to who ultimately has control of the asset.

Part C

Answer-to-Question-_5_

A loan note issuance programme will be organised by a bank on behalf of a business in order to raise additional funds. this type of arrangement will often be used by private equity funds on acquisition of a target business.

the bank will put together a prospectus for the issuance, setting out the terms of the notes, whether they are to be fixed or redeemable, the interest rate. the terms of the agreement will also set out provision for payments of interest,any collateral offered, and possibly for net settlement in the event of default.

the loan notes may be issued by the bank onto a regulated market, or could be offered "over the counter" directly to investor

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counter parties.

the bank may offer to act as market maker, guaranteeing a minimum price for the loan notes but it will charge Atlas Plc an additional fee for doing this.

loan notes will be accounted for as a liability by Atlas Plc.

the interest payments on the loan notes are unlikely to relate to the trade of Atlas Plc so they will likely be a non-trading loan relationship debit, which cannot be set against trading profits.

in the hands of the investor the treatment of the loan notes will depend whether they are a qualifying corporate bond, if they are then they will be exempt from chargeable gains.

Answer-to-Question-_6_

1) Basel III accord took effect from 2010 and built upon the Basel I and Basel II accords. Basel III sought to improve weaknesses in Basel II, in particular those that had been highlighted as a result of the 2007/2008 financial crisis. improvements included setting minimum liquidity requirements, seeking to prevent collapses of banks in a similar way to Lehman Brothers. Basel III also brought in addition requirements for the largest Globally Systemically Important Banks (GSIBS), acknowledge their role in the global financial system and the excess risk of contagion posed by their failure.

regulatory minimums are set by the Basel III accord but domestic

regulatory are free to apply additional requirements over and above those set by the accord.

2)

under the new regulatory requirements Omega has been set a regulatory minimum of 15% - this is a liquidity requirement to ensure the bank has sufficient Tier 1 and Tier 2 capital with view to preventing a run on the bank. Omegas current capital is £14bn(6+8) which is 14% of total risk weight assets.

in order to comply with this requirment Omega could issue additional tier 1 or tier 2 capital, so that its ratio hits 15%, or it could reduce its deposits.

Omega now needs a tier 1 ratio of 10%, currently omega's ratio is 6/100 = 6%. in order to meet this it could increase its tier 1 or reduce its deposits.

If Omega focus in increasing its tier 1 to meet the 10% requirment it would need an additional £4.4bn tier 1. in doing this it would increase its total capital to 17.6% and therefore meet both of its requirements.

Alternatively, in order to reduce deposits to a sufficient level to meet the 10% tier one ratio it would have to move £40bn deposits, this would again meet both requirement but is likely to be less appealing.