THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Taxation of Larger Companies & Groups

May 2023

TIME ALLOWED

3 HOURS 30 MINUTES

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- Scots law candidates may provide answers referring to Land and Buildings Transaction Tax rather than Stamp Duty Land Tax.
- Unless otherwise indicated by the provision of additional information in the question, you may assume that 2022/23 legislation (including rates and allowances) continues to apply for 2023/24 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.
- Additional marks may be awarded for presentation.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

1. The McRaney group specialise in the manufacture and sales of sports equipment. The main trading company is McRaney Ltd.

Extract from the Income Statement of McRaney Ltd for the year ended 31 December 2022

	Notes	£'000
Turnover		297,341
Cost of sales		(275,682)
Gross profit		21,659
Administration expenses	1)	(15,568)
Interest payable		(1,000)
Net profit		5,091

Notes

1) Administration expenses include:

	Notes	£'000
Depreciation		4,000
Loss on disposal of plant		250
Legal expenses:		
Factory build		250
Incidental costs of raising loan finance		150
Pension contributions	2)	5,000
Qualifying charitable deduction		100

2) Pension contributions

The company makes a regular annual contribution of £2 million to the group defined contribution pension scheme. In the year ended 31 December 2022, in recognition of a successful year's trading, the company made a one-off additional contribution of £3 million.

3) General Bad Debts Provision

McRaney Ltd has a policy of making a general bad debts provision in its accounts. The accounting entries in recent years include:

Year ended 31 December	Balance sheet	Income statement
	£m	£m
2000	7	-
2021	9	(2)
2022	6	3

4) New factory

Due to increased demand for sports equipment, McRaney Ltd constructed a new additional factory during the year ended 31 December 2022. The land was acquired in February 2022, construction began on 1 April 2022 and the factory was first brought into business use on 1 November 2022.

The total cost of the factory was £11 million, including the following:

	Costs
	£
Land	2,500,000
Integral features	1,000.000
Acquiring planning permission	200,000
Clearing site in preparation for construction	300,000

5) Capital allowances

On 1 January 2022, the tax written down value of the general pool was £7,243,000 and the special rate pool was £652,000.

In addition to the purchase of the land and construction of the factory, the company also purchased plant and machinery for £4 million, which was delivered and installed during the first week in October 2022 with the work being completed by 7 October 2022. The payment for this plant was required to be made in four equal instalments on 15 October 2022, 15 November 2022, 15 December 2022 and 15 January 2023. Of the expenditure, 50% qualified for the general pool and 50% for the special rate pool.

There was a disposal of plant during the accounting period. The net book value of this plant was £450,000 at the date of sale. This plant had been acquired on 1 June 2021 at the cost of £500,000.

The Annual Investment Allowance is fully available to McRaney Ltd.

Requirement:

Calculate, with explanations, the Corporation Tax payable by McRaney Ltd for the year ended 31 December 2022, assuming the most beneficial claims and elections are made. (20)

2. The Bonnerton group operates in the specialist and high-end car market. Bonnerton Ltd is the main UK tax resident trading subsidiary, which also operates in Ruritania and Utopia through permanent establishments.

The Ruritanian permanent establishment has had periods of profitability but made a loss in the year ended 31 December 2022.

After several years making losses, the Utopian permanent establishment made a profit in the year to 31 December 2022 and is forecast to continue making profits.

The loss relief regime in both Ruritania and Utopia operates in the same way as the UK.

Bonnerton Ltd's directors are concerned that the operations in Utopia are no longer tax efficient and are considering three options:

1) Continuing to operate the Utopian business through a non-exempt permanent establishment;

2) Making a permanent establishment exemption election; or

3) Incorporating the Utopian permanent establishment into a Utopian subsidiary.

The corporate tax rate in Utopia is 30%.

Should the Utopian permanent establishment be incorporated, it will be exempt from any controlled foreign companies apportionment in the UK as Utopia is an excluded territory and the company would meet the necessary conditions.

Requirement:

Explain the UK Corporation Tax implications of each of the three options and recommend the most appropriate course of action. (15)

3. Huxsmith Ltd is a successful UK tax resident company involved in technology development.

The company has no subsidiaries and is owned by individuals, none of whom have a controlling interest. All shares carry equal rights to assets and to distributions from the company.

In the year ended 31 December 2022, it had a turnover of £100 million and taxable profits before tax, interest and capital allowances of £15 million.

Several years ago, a US corporation, Wolff Inc, provided £100 million of funding to Huxsmith Ltd through a loan from Eflow Ltd. Eflow Ltd is a subsidiary of Wolff Inc, and is tax resident in Bermuda. The interest on the loan is 6% per annum and it is repayable in 2025. The interest has always been paid annually as it accrues, and no impairments or revaluations have been made.

Wolff Inc has a turnover of US$2 billion, and has neither subsidiaries nor permanent establishments in the UK.

Huxsmith Ltd has no other financing costs.

Some of the current shareholders of Huxsmith Ltd are considering selling their shares to Wolff Inc. If all of these share sales take place, Wolff Inc would own 60% of Huxsmith Ltd.

Requirement:

Explain the UK tax issues in relation to the loan from Wolff Inc. You should NOT consider the tax position of the shareholders disposing of their shares. (15)

4. Blundell plc is the UK resident parent company of a group of UK and overseas trading companies, reporting under IFRS with a 31 December year-end.

One wholly owned UK resident subsidiary is Blundell Developments Ltd. Blundell Developments Ltd acquires and develops property sites before either selling them externally or transferring them to Blundell plc. The UK freehold properties that are transferred to Blundell plc are rented out to either group companies or third parties.

On 31 December 2021, Blundell plc's general pool had a balance of £500,000 and its special rate pool had a balance of £2.5 million.

The following transactions took place in the year ended 31 December 2022:

1) In January 2022, Blundell plc granted a 40-year lease over office premises in Dundee. A premium of £500,000 was received and legal fees of £2,000 were incurred. The freehold had been acquired from a third party by Blundell plc in 2018 for £3 million. The freehold reversion was valued at £3.5 million.

2) In July 2022, Blundell plc sold an office building in Peterborough to a third party for £7 million and an accounting profit of £3.5 million was recognised in the income and expenditure account for that year. Both parties jointly elected that £250,000 be attributed to fixtures within the office building.

   The office building had been designed and constructed by Blundell Developments Ltd. This company had acquired the land for £1 million in January 2002 and had incurred costs of £2.5 million in the design and construction. The office building was transferred to Blundell plc at its book value of £3.5 million in December 2002 when the market value was £4 million. Since its construction, the office building has been let to third party tenants.

3) In November 2022, Blundell plc sold a factory in Northumberland for £7.5 million to a third party. The factory had previously been leased to and used by one of the subsidiaries. An accounting profit of £4 million was recognised in the income and expenditure account for the year. Both parties jointly elected that £300,000 be attributed to fixtures within the factory.

   This factory had originally been purchased by Blundell plc from a third party in January 2000 for £3.5 million and initially used by Blundell plc to manufacture products. In August 2006, when the market value of the factory was £5 million, the group restructured and the manufacturing trade was hived down to a new subsidiary, Norman Ltd. Although Norman Ltd traded from the factory, Blundell plc retained ownership of the factory.

   In January 2007, Blundell plc fully refurbished the factory at the cost of £750,000. This included £400,000 of redecoration costs, which Blundell plc claimed as tax deductible expenditure. No tax relief was claimed for the balance of the expenditure.

   Norman Ltd continued to trade from the factory until January 2022 when Blundell plc purchased a replacement second hand factory (originally constructed in 2015) for £6.5 million for Norman Ltd's Northumberland trade. On the acquisition, both Blundell plc and the third-party vendor jointly elected that £150,000 be attributed to fixtures within the second-hand factory.

4) In November 2022, Blundell plc acquired an office building (originally constructed in 2012) from a third party for £4 million with an existing third-party tenant in situ. Blundell plc and the vendor jointly elected that £200,000 be attributed to fixtures within the office building.

Requirement:

1) **Calculate, with explanations, the chargeable gains arising on the transactions including consideration of any opportunities to mitigate any tax liability arising.** (18)

2) **Calculate the capital allowances available in the year.** (2)

Total (20)

5. Donner plc is a UK resident listed company that manufactures and distributes household goods through third party retailers throughout the UK. Since 2000, it has had one wholly owned subsidiary, Dancer Ltd, which imports furniture for sale to retailers in the UK. Both companies have a 30 June year end.

Donner plc wants to expand its operations to sell products directly to consumers and plans to do so through a joint venture arrangement with a third party. It has received two offers: one from a German company, Blitzen GmbH; the other from a UK company, DP Ltd.

Under both offers, Donner plc will incorporate a new UK company, Vixen Ltd on 1 June 2023. It will then transfer an unused warehouse that it currently owns to Vixen Ltd.

The market value of the warehouse is currently £7.5 million. The warehouse was originally purchased by Dancer Ltd for £5 million in January 2005. A claim to rollover a chargeable gain of £250,000 on a business asset sold in May 2004 was made against the cost of the warehouse. The warehouse was transferred from Dancer Ltd to Donner plc in March 2009 for its book value of £4.5 million; on that date, the market value was £5.5 million.

Vixen Ltd will convert the warehouse and use it as retail premises. Vixen Ltd will start selling products in the UK on 1 July 2023. It will have a 30 June year end.

The two joint venture offers are:

Offer 1 – Blitzen GmbH

Donner plc will own 75% of the ordinary share capital of Vixen Ltd and Blitzen GmbH will own 25%. The consideration for the shares will be:

	£'000
Donner plc	
Warehouse	7,500
Cash	3,750
Blitzen GmbH	
Cash	3,750
Total	£15,000

Offer 2 – DP Ltd

Donner plc will own 65% of the ordinary share capital of Vixen Ltd and DP Ltd will own 35%. The consideration will for the shares will be:

	£'000
Donner plc	
Warehouse	7,500
Cash	2,250
DP Ltd	
Cash	5,250
Total	£15,000

The projected trading results for the year ended 30 June 2024 are:

	Donner plc	Dancer Ltd	Vixen Ltd
	£'000	£'000	£'000
Trading profit/(loss)	1,000	3,000	(1,500)

On 1 July 2023, Donner plc is expected to have total trading losses brought forward of £1.5 million from the years ended 30 June 2021 and 30 June 2022, and capital losses brought forward of £100,000.

Dancer Ltd has no tax losses brought forward.

Vixen Ltd is expected to start making trading profits in the year ended 30 June 2025.

Requirement:

Explain the Corporation Tax implications for Donner plc, Dancer Ltd and Vixen Ltd of the two offers and discuss the tax efficiency of each. (20)

6. Stevenson Investments plc is a UK resident non-trading company holding investments in UK and overseas subsidiary companies.

The directors are considering the acquisition of all of the shares of Target Ltd. The following expenses are expected to be incurred by Stevenson Investments plc and Target Ltd:

1) Initial due diligence work will be carried out on Target Ltd. It is expected that this will cost £25,000.

2) If no concerns are identified and Target Ltd is considered to align with the rest of the group, solicitors will be engaged to progress the acquisition and their fees are expected to be £100,000.

3) If the acquisition proceeds, it is anticipated that Stevenson Investments plc will pay £20 million for the entire share capital of Target Ltd. The acquisition will be financed by £10 million from reserves and £10 million from a loan from an external bank. An arrangement fee of 1% will be charged on the provision of the loan. Interest will be charged at 5% per annum with the full balance repayable in five years.

4) Compensation for loss of office of £125,000 will be paid by Target Ltd to the previous directors of Target Ltd.

5) A retention bonus will be payable to other key members of staff of Target Ltd, with a total of £100,000 payable at the time of the transaction and a further £100,000 payable in two years' time to staff members who remain in employment two years after the transaction. The full cost of £200,000 will be accrued in the accounts of Target Ltd at the time of the acquisition.

Requirement:

Explain the tax treatment of the expenses incurred by Stevenson Investments plc and Target Ltd associated with the acquisition of Target Ltd. (10)