Professional Level – Options Module

# Advanced Taxation (United Kingdom)

Friday 7 June 2013

**Time allowed**
Reading and planning: 15 minutes
Writing: 3 hours

This paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – TWO questions ONLY to be attempted

**Tax rates and allowances are on pages 2–5**

**Do NOT open this paper until instructed by the supervisor.**
**During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.**
**This question paper must not be removed from the examination hall.**

**The Association of Chartered Certified Accountants**

Paper P6 (UK)

ACCA

**SUPPLEMENTARY INSTRUCTIONS**

1. You should assume that the tax rates and allowances for the tax year 2012/13 and for the financial year to 31 March 2013 will continue to apply for the foreseeable future unless you are instructed otherwise.
2. Calculations and workings need only be made to the nearest £.
3. All apportionments should be made to the nearest month.
4. All workings should be shown.

**TAX RATES AND ALLOWANCES**

**The following tax rates and allowances are to be used in answering the questions.**

**Income tax**

| | | Normal rates % | Dividend rates % |
|---|---|---|---|
| Basic rate | £1 – £34,370 | 20 | 10 |
| Higher rate | £34,371 to £150,000 | 40 | 32·5 |
| Additional rate | £150,001 and over | 50 | 42·5 |

A starting rate of 10% applies to savings income where it falls within the first £2,710 of taxable income.

**Personal allowances**

| | | £ |
|---|---|---|
| Personal allowance | Standard | 8,105 |
| | 65 – 74 | 10,500 |
| | 75 and over | 10,660 |
| Income limit for age related allowances | | 25,400 |
| Income limit for standard personal allowance | | 100,000 |

**Car benefit percentage**

The relevant base level of $CO_2$ emissions is 100 grams per kilometre.

The percentage rates applying to petrol cars with $CO_2$ emissions up to this level are:

| | % |
|---|---|
| 75 grams per kilometre or less | 5 |
| 76 grams to 99 grams per kilometre | 10 |
| 100 grams per kilometre | 11 |

**Car fuel benefit**

The base figure for calculating the car fuel benefit is £20,200.

**Individual savings accounts (ISAs)**

The overall investment limit is £11,280, of which £5,640 can be invested in a cash ISA.

**Pension scheme limits**

| | |
|---|---|
| Annual allowance | £50,000 |
| Lifetime allowance | £1,500,000 |
| Maximum contribution that can qualify for tax relief without evidence of earnings | £3,600 |

## Authorised mileage allowances: cars

| | |
|---|---|
| Up to 10,000 miles | 45p |
| Over 10,000 miles | 25p |

## Capital allowances: rates of allowance

| | % |
|---|---|
| **Plant and machinery** | |
| Main pool | 18 |
| Special rate pool | 8 |
| **Motor cars** | |
| New cars with $CO_2$ emissions up to 110 grams per kilometre | 100 |
| $CO_2$ emissions between 111 and 160 grams per kilometre | 18 |
| $CO_2$ emissions over 160 grams per kilometre | 8 |
| **Annual investment allowance** | |
| First £25,000 of expenditure | 100 |

## Corporation tax

| Financial year | 2010 | 2011 | 2012 |
|---|---|---|---|
| Small profits rate | 21% | 20% | 20% |
| Main rate | 28% | 26% | 24% |
| | £ | £ | £ |
| Lower limit | 300,000 | 300,000 | 300,000 |
| Upper limit | 1,500,000 | 1,500,000 | 1,500,000 |
| Standard fraction | 7/400 | 3/200 | 1/100 |

## Marginal Relief

Standard fraction x (U – A) x N/A

## Value added tax (VAT)

| | |
|---|---|
| Standard rate | 20% |
| Registration limit | £77,000 |
| Deregistration limit | £75,000 |

## Inheritance tax: nil rate bands and tax rates

| | £ | |
|---|---|---|
| 6 April 2012 to 5 April 2013 | 325,000 | |
| 6 April 2011 to 5 April 2012 | 325,000 | |
| 6 April 2010 to 5 April 2011 | 325,000 | |
| 6 April 2009 to 5 April 2010 | 325,000 | |
| 6 April 2008 to 5 April 2009 | 312,000 | |
| 6 April 2007 to 5 April 2008 | 300,000 | |
| 6 April 2006 to 5 April 2007 | 285,000 | |
| 6 April 2005 to 5 April 2006 | 275,000 | |
| 6 April 2004 to 5 April 2005 | 263,000 | |
| 6 April 2003 to 5 April 2004 | 255,000 | |
| 6 April 2002 to 5 April 2003 | 250,000 | |
| 6 April 2001 to 5 April 2002 | 242,000 | |
| 6 April 2000 to 5 April 2001 | 234,000 | |
| 6 April 1999 to 5 April 2000 | 231,000 | |
| 6 April 1998 to 5 April 1999 | 223,000 | |
| Rate of tax on excess over nil rate band | – Lifetime rate | 20% |
| | – Death rate | 40% |

## Inheritance tax: taper relief

| Years before death: | % reduction |
|---|---|
| More than 3 but less than 4 years | 20 |
| More than 4 but less than 5 years | 40 |
| More than 5 but less than 6 years | 60 |
| More than 6 but less than 7 years | 80 |

## Capital gains tax

| | % |
|---|---|
| Rate of tax – Lower rate | 18 |
| – Higher rate | 28 |
| Annual exempt amount | £10,600 |
| Entrepreneurs' relief – Lifetime limit | £10,000,000 |
| – Rate of tax | 10% |

**National insurance contributions**
**(not contracted out rates)**

| | | | % |
|---|---|---|---|
| Class 1 | Employee | £1 – £7,605 per year | Nil |
| | | £7,606 – £42,475 per year | 12·0 |
| | | £42,476 and above per year | 2·0 |
| Class 1 | Employer | £1 – £7,488 per year | Nil |
| | | £7,489 and above per year | 13·8 |
| Class 1A | | | 13·8 |
| Class 2 | | £2·65 per week | |
| | | Small earnings exception limit – £5,595 | |
| Class 4 | | £1 – £7,605 per year | Nil |
| | | £7,606 – £42,475 per year | 9·0 |
| | | £42,476 and above per year | 2·0 |

**Rates of interest (assumed)**

| | |
|---|---|
| Official rate of interest | 4·0% |
| Rate of late payment interest | 3·0% |
| Rate of repayment interest | 0·5% |

**Stamp duty land tax**

| | % |
|---|---|
| £150,000 or less (1) | Nil |
| £150,001 – £250,000 | 1 |
| £250,001 – £500,000 | 3 |
| £500,001 – £1,000,000 | 4 |
| £1,000,001 – £2,000,000 (2) | 5 |
| £2,000,001 or more (2) | 7 |

(1) For residential property, the nil rate is restricted to £125,000.
(2) The 5% and 7% rates apply to residential properties only. The 4% rate applies to all non-residential properties where the consideration is in excess of £500,000.

**Stamp duty**

| | |
|---|---|
| Shares | 0·5% |

**Section A – BOTH questions are compulsory and MUST be attempted**

**1** Your manager has had a telephone conversation with Burt, the Group Finance Director of the Epon Ltd group of companies. Extracts from both a memorandum and an email from your manager are set out below.

**Extract from a memorandum from your manager**

On Thursday 6 June I spoke to Burt, the Group Finance Director of Epon Ltd. He is coming to the office on Monday to appoint us as tax advisers to the group, and possibly to the individual directors, and to discuss the group's affairs.

**The Epon Ltd group**

Epon Ltd is owned by a large number of unrelated individuals. Epon Ltd owns 100% of the ordinary share capital of Wahzah Ltd, Yoko Ltd and NewCo Ltd. All four companies are UK resident and prepare accounts to 30 June each year. It is the policy of the group to maximise the tax saved when relieving losses and only to carry losses forward if there is no alternative relief available.

| | **Epon Ltd** | **Wahzah Ltd** | **Yoko Ltd** | **NewCo Ltd** |
|---|---|---|---|---|
| Business activity | Manufacture of exercise equipment | Ownership and management of fitness clubs | Servicing of swimming pools | None |
| Budgeted results | | | | |
| Year ending 30 June 2014 | **£** | **£** | **£** | **£** |
| Tax adjusted trading profit/(loss) | 740,000 | 90,000 | (80,000) | Nil |
| Chargeable gains | 18,000 | Nil | 12,000 | Nil |
| Capital loss | Nil | (20,000) | Nil | Nil |
| Budgeted trading losses carried forward as at 30 June 2013 | Nil | Nil | (65,000) | Nil |

**The purchase of the Aquapower business**

NewCo Ltd is currently dormant. It was incorporated on 1 May 2013 in order to purchase the assets of the Aquapower business (Aquapower) from an unincorporated trader. It was intended that NewCo Ltd would purchase Aquapower on 1 July 2013. However, Burt has now decided that he would prefer the business to be purchased by Yoko Ltd, provided that this is not more expensive from a tax point of view. Under this option, Yoko Ltd would then be carrying on two separate trades.

Aquapower's business is the distribution of bottled drinks. The budgeted trading profit of Aquapower for the year ending 30 June 2014 is £60,000. None of the assets of the Aquapower business qualifies for rollover relief.

**The purchase of equipment from the country of Candara**

A new supplier of equipment for the fitness clubs has been identified in Candara. Wahzah Ltd intends to purchase equipment from this supplier in July 2013. The country of Candara is not a member of the European Union.

**The purchase of Kari's shares**

The planned changes to the Epon Ltd group have resulted in a dispute with Kari, the Group Sales Director. In order to resolve this, it has been proposed that Epon Ltd will carry out a purchase of its own shares on 31 July 2013 and acquire the whole of Kari's shareholding.

Kari subscribed £10,000 for 10,000 £1 ordinary shares in Epon Ltd on 1 December 2008. It has been agreed that Epon Ltd will purchase all of these shares on 31 July 2013 for £90,000. Kari has been advised that the money she will receive will be treated as a dividend. Kari's annual taxable employment income (before deducting her personal allowance) is £72,000. In the tax year 2013/14, she will not receive any other income or make any disposals for the purposes of capital gains tax.

Extract from an email from your manager

Please prepare a memorandum for the client file that addresses the following issues:

**(a) The purchase of the Aquapower business – corporation tax liabilities**

Calculations of the corporation tax liabilities of the four companies for the year ending 30 June 2014 on the assumption that Aquapower is purchased by:

**(i)** NewCo Ltd
**(ii)** Yoko Ltd.

You should assume that any claim(s) for loss relief will be made in accordance with group policy, as described in the memorandum. The **only** explanatory notes I need are in respect of the use of any losses.

**(b) The purchase of equipment from the country of Candara**

Explain the value added tax (VAT) implications for Wahzah Ltd of the purchase of the equipment from the country of Candara.

**(c) The purchase of Kari's shares**

I want you to:

**(i)** review each of the conditions for capital gains tax treatment in order to determine the reason(s) why the amount received will be treated as a dividend. I can confirm that Epon Ltd satisfies the condition of being an unquoted trading company.

**(ii)** calculate the increase in tax cost for Kari as a result of the sale of the shares being subject to income tax as opposed to capital gains tax. You should assume that entrepreneurs' relief would be available and would be claimed.

**(d) Appointment as tax advisers**

An explanation of whether or not it is acceptable for the firm to be appointed tax advisers to the companies' directors as well as to the Epon Ltd group of companies. On the assumption that it is acceptable, outline any safeguards that the firm should consider in relation to this joint appointment.

Tax manager

**Required:**

**Prepare the memorandum requested in the email from your manager. The following marks are available.**

**(a) The purchase of the Aquapower business – corporation tax liabilities.**

Note: For guidance, approximately 60% of the marks available in part (a) are for the calculations.
(13 marks)

**(b) The purchase of equipment from the country of Candara.** (2 marks)

**(c) The purchase of Kari's shares.**

**(i) Review of each of the conditions for capital gains tax treatment;** (5 marks)

**(ii) Calculation of the increase in tax cost for Kari.** (6 marks)

**(d) Appointment as tax advisers.** (5 marks)

**Professional marks will be awarded in question 1 for adopting a logical approach to problem solving, the clarity of the calculations, effectiveness with which the information is communicated, and the overall presentation of the memorandum.** (4 marks)

**(35 marks)**

**2** Your manager has had a meeting with Brad, a client of your firm. Extracts from your manager's meeting notes together with an email from your manager are set out below.

**Extracts from meeting notes**

**Personal details**

Brad is 69 years old. He is married to Laura and they have a daughter, Dani, who is 38 years old.

Brad had lived in the UK for the whole of his life until he moved with his wife to the country of Keirinia on 1 January 2010. He returned to live permanently in the UK on 30 April 2013. Whilst living in Keirinia, Brad was non-UK resident and non-ordinarily resident. He is now resident and ordinarily resident in the UK. He has always been domiciled in the UK. Brad has significant investment income and has been a higher rate taxpayer for many years.

**Capital gains**

Whilst living in the country of Keirinia, Brad sold various assets as set out below. He has not made any other disposals since 5 April 2009.

| Asset | Date of sale | Proceeds | Date of purchase | Cost |
|---|---|---|---|---|
| | | £ | | £ |
| Quoted shares | 1 February 2010 | 18,900 | 1 October 2008 | 14,000 |
| Painting | 1 June 2012 | 36,000 | 1 May 2008 | 15,000 |
| Antique bed | 1 March 2013 | 9,400 | 1 March 2010 | 7,300 |
| Motor car | 1 April 2013 | 11,000 | 1 February 2009 | 8,500 |

I explained that, although Brad was non-UK resident and non-ordinarily resident whilst living in Keirinia, these disposals may still be subject to UK capital gains tax because he will be regarded as only temporarily non-UK resident. There is no capital gains tax in the country of Keirinia.

**Inheritance tax planning**

Brad's estate is worth approximately £5 million. He has not made any lifetime gifts and, in his will, he intends to leave half of his estate to his daughter, Dani, and the other half to his wife, Laura. I pointed out that it may be advantageous to make a lifetime gift to Dani. Brad agreed to consider giving Dani 1,500 of his shares in Omnium Ltd and has asked for a general summary of the inheritance tax advantages of making lifetime gifts to individuals.

Omnium Ltd is an unquoted manufacturing company which also owns a number of investment properties. Brad was given his shares in the company by his wife on 1 January 2009. The ownership of the share capital of Omnium Ltd is set out below.

| | Shares |
|---|---|
| Laura (Brad's wife) | 4,500 |
| Brad | 3,000 |
| Vic (Laura's brother) | 1,500 |
| Christine (friend of Laura) | 1,000 |
| | 10,000 |

The current estimated value of a share in Omnium Ltd is set out below.

| Shareholding | Value per share |
|---|---|
| | £ |
| Up to 25% | 190 |
| 26% to 50% | 205 |
| 51% to 60% | 240 |
| 61% to 74% | 255 |
| 75% to 80% | 290 |
| More than 80% | 300 |

Email from your manager

In preparation for my next meeting with Brad, please prepare the following:

**(a) Capital gains tax**

An explanation, with supporting calculations, of the UK capital gains tax liability in respect of the disposals made by Brad whilst living in the country of Keirinia. Your explanation should include the precise reasons for Brad being regarded as only temporarily non-UK resident and a statement of when the tax was/will be payable.

**(b) Inheritance tax**

**(i)** An explanation of the inheritance tax advantages of making lifetime gifts to individuals, in general.

**(ii)** In respect of the possible gift of 1,500 shares in Omnium Ltd to Dani:

- a calculation of the fall in value of Brad's estate which will result from the gift;
- a detailed explanation of whether or not business property relief would be available in respect of the gift and, on the assumption that it would be available, the manner in which it would be calculated;
- a **brief** statement of any other tax issues arising from the gift, which will need to be considered at a later date.

Tax manager

**Required:**

**Carry out the work required as requested in the email from your manager. The following marks are available.**

**(a) Capital gains tax.** (8 marks)

**(b) Inheritance tax.**

**(i) Explanation of the inheritance tax advantages of making lifetime gifts to individuals;** (7 marks)

**(ii) In respect of the possible gift of 1,500 shares in Omnium Ltd to Dani.** (10 marks)

**(25 marks)**

**Section B – TWO questions ONLY to be attempted**

**3** Your firm has been asked to provide advice to Shuttelle in connection with personal pension contributions and to three non-UK domiciled individuals in connection with the remittance basis of taxation for overseas income and gains.

**(a)** Personal pension contributions:
– Shuttelle has been the production director of Din Ltd since 1 February 2000.
– Shuttelle joined a registered personal pension scheme on 6 April 2010.

Shuttelle's tax position for the tax year 2012/13:
– Shuttelle's only source of income is her remuneration from Din Ltd.
– Shuttelle's annual salary is £204,000.
– Shuttelle lived in a house owned by Din Ltd for a period of time during the tax year 2012/13.

The house provided by Din Ltd for Shuttelle's use:
– Was purchased by Din Ltd on 1 January 2000 for £500,000 and has an annual value of £7,000.
– Shuttelle lived in the house from 1 February 2000 until 30 June 2012.
– The house had a market value of £870,000 on 6 April 2012.

Contributions to Shuttelle's personal pension scheme:
– Shuttelle has made the following gross contributions:
6 April 2010 – £29,000
6 April 2011 – £48,000
6 April 2012 – £120,000.
– Din Ltd contributes £4,000 to the scheme in each tax year.

**Required:**

**(i) Calculate Shuttelle's income tax liability for the tax year 2012/13;** (8 marks)

**(ii) Calculate the amount of tax relief obtained by Shuttelle as a consequence of the gross personal pension contributions of £120,000 she made on 6 April 2012.** (3 marks)

**(b)** The remittance basis of taxation:
– Advice is to be provided to three non-UK domiciled individuals.
– Each of the three individuals is more than 18 years old.

Details of the three individuals:

| Name | Lin | Nan | Yu |
|---|---|---|---|
| Tax year in which the individual became UK resident | 2002/03 | 1997/98 | 2002/03 |
| Tax year in which the individual ceased to be UK resident | Still resident | 2011/12 | Still resident |
| Whether or not the individual is ordinarily resident in the UK | Yes | No | No |
| Overseas income and gains for the tax year 2012/13 | £39,200 | £68,300 | £130,700 |
| Overseas income and gains remitted to the UK for the tax year 2012/13 | £38,500 | Nil | £1,400 |

**Required:**

**(i) In respect of each of the three individuals for the tax year 2012/13:**

**(1) explain whether or not the remittance basis is available;**

**(2) on the assumption that the remittance basis is available to ALL three individuals, state, with reasons, the remittance basis charge (if any) that they would have to pay in order for their overseas income and gains to be taxed on the remittance basis.**

The following mark allocation is provided as guidance for this requirement:

(1) 3 marks
(2) 4 marks

(7 marks)

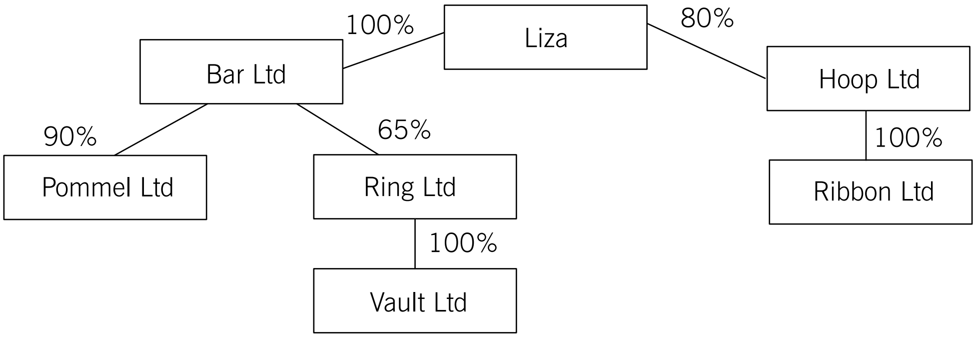
**(ii) Give TWO examples of actions that would be regarded as remittances other than simply bringing cash into the UK.** (2 marks)

**(20 marks)**

**4** Liza requires detailed advice on rollover relief, capital allowances and group registration for the purposes of value added tax (VAT).

**Liza's business interests:**

– Liza's business interests, which have not changed for many years, are set out below.




– All six companies are UK resident trading companies with a 31 March year end.
– All of the minority holdings are owned by individuals, none of whom is connected with Liza or with each other.

**A building ('Building I') sold by Bar Ltd:**

– Bar Ltd sold Building I on 31 May 2013 for £860,000.
– Bar Ltd had purchased the building on 1 June 2007 for £315,000 plus legal fees of £9,000.
– On 5 June 2007, Bar Ltd had carried out work on the building's roof at a cost of £38,000 in order to make the building fit for use.
– On 1 July 2012, Bar Ltd spent £14,000 repainting the building.
– Bar Ltd used Building I for trading purposes apart from the period from 1 January 2009 to 30 June 2010.
– It is intended that the chargeable gain on the sale will be rolled over to the extent that this is possible.

**A replacement building ('Building II') purchased by Bar Ltd:**

– Bar Ltd purchased Building II, new and unused, for £720,000 on 1 May 2013.
– Bar Ltd uses two thirds of this building for trading purposes; the remaining one-third is rented out.

**The trading activities of the Bar Ltd and Hoop Ltd groups of companies:**

– The number of transactions between the Bar Ltd group and the Hoop Ltd group is increasing.
– Vault Ltd makes zero rated supplies; all of the other five companies make standard rated supplies.

**Required:**

**(a) (i) Calculate the chargeable gain on the sale of Building I, ignoring any potential claim for rollover relief;** (3 marks)

**(ii) In relation to claiming rollover relief in respect of the disposal of Building I, explain which of the companies in the Bar Ltd and Hoop Ltd groups are, and are not, able to purchase qualifying replacement assets, and state the period within which such assets must be acquired;** (4 marks)

**(iii) Explain, with the aid of supporting calculations, the additional amount that would need to be spent on qualifying assets in order for the maximum amount of the gain on Building I to be relieved by rollover relief.** (4 marks)

Notes:
1. You should ignore value added tax (VAT) when answering part (a) of this question.
2. The following figures from the Retail Prices Index should be used, where necessary.

| | |
|---|---|
| June 2007 | 207·3 |
| July 2012 | 242·1 (assumed) |
| May 2013 | 246·4 (assumed) |

**(b) Explain the capital allowances that are available in respect of the electrical, water and heating systems that were acquired as part of Building II.** (2 marks)

**(c) Explain which of the companies in the Bar Ltd and Hoop Ltd groups would be able to register as a single group for the purposes of value added tax (VAT) and discuss the potential advantages and disadvantages of registering them as a single VAT group.** (7 marks)

**(20 marks)**

**5** Spike requires advice on the loss relief available following the cessation of his business and on the tax implications of share options and a relocation payment provided by his new employer.

Spike:

– Ceased to trade and sold his unincorporated business to an unrelated individual on 30 September 2012.
– Sold his house, 'Sea View', on 1 March 2013 for £125,000 more than he had paid for it.
– Began working for Set Ltd on 1 May 2013.
– Has no income or capital gains other than the amounts referred to in the information below.

Spike's unincorporated business:

– There are overlap profits from the commencement of the business of £8,300.
– The sale of the business resulted in net capital gains of £78,000.
– The tax adjusted profits/(loss) of the business have been:

| | | £ |
|---|---|---|
| Year ended 31 December 2008 | Profit | 52,500 |
| Year ended 31 December 2009 | Profit | 68,000 |
| Year ended 31 December 2010 | Profit | 54,000 |
| Year ended 31 December 2011 | Profit | 22,500 |
| Nine months ending 30 September 2012 | Loss | (13,500) |

Remuneration from Set Ltd:

– Spike is being paid a salary of £65,000 per year.
– On 1 May 2013, Spike was granted an option to purchase ordinary shares in Set Ltd.
– On 1 July 2013, Set Ltd will pay Spike a relocation payment of £33,500.

The option to purchase ordinary shares in Set Ltd:

– Spike paid £3,500 for an option to purchase 7,000 ordinary shares, representing a 3·5% shareholding.
– The option is exercisable on 1 May 2017 at £4·00 per share.
– An ordinary share in Set Ltd was worth £5·00 on 1 May 2013 and is expected to be worth £8·00 on 1 May 2017.
– Set Ltd does not have any HM Revenue and Customs approved share option schemes.

The relocation payment of £33,500:

– Spike sold 'Sea View', and purchased a new house, in order to live near the premises of Set Ltd.
– £22,000 of the payment is to compensate Spike for having to sell his house at short notice at a low price.
– £11,500 of the payment is in respect of the costs incurred by Spike in relation to moving house.

**Required:**

**(a) (i) Calculate the trading loss for the tax year 2012/13, and the terminal loss, on the cessation of Spike's unincorporated business;** (4 marks)

**(ii) Explain the reliefs available in respect of the losses calculated in part (i) and quantify the potential tax savings for each of them.** (10 marks)

**(b) (i) Explain all of the income tax and capital gains tax liabilities arising on Spike in respect of the grant and the exercise of the share options and the eventual sale of the shares in Set Ltd;** (4 marks)

**(ii) Explain the income tax implications for Spike of the relocation payment.** (2 marks)

Notes:

1. You should assume that the tax rates and allowances for the tax year 2012/13 apply to all tax years.
2. Ignore national insurance contributions throughout this question.

**(20 marks)**

**End of Question Paper**