Professional Level – Options Module

Advanced Taxation (United Kingdom)

March/June 2018 – Sample Questions

P6 UK ACCA

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – BOTH questions are compulsory and MUST be attempted

Tax rates and allowances are on pages 2–6

Do NOT open this question paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

Paper P6 (UK)

Think Ahead ACCA

The Association of Chartered Certified Accountants

SUPPLEMENTARY INSTRUCTIONS

1. You should assume that the tax rates and allowances for the tax year 2017/18 and for the financial year to 31 March 2018 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 – £33,500	20%	7·5%
Higher rate	£33,501 to £150,000	40%	32·5%
Additional rate	£150,001 and over	45%	38·1%

Savings income nil rate band – Basic rate taxpayers	£1,000
– Higher rate taxpayers	£500
Dividend nil rate band	£5,000

A starting rate of 0% applies to savings income where it falls within the first £5,000 of taxable income.

Personal allowance

Personal allowance	£11,500
Transferable amount	£1,150
Income limit	£100,000

Residence status

Days in UK	Previously resident	Not previously resident
Less than 16	Automatically not resident	Automatically not resident
16 to 45	Resident if 4 UK ties (or more)	Automatically not resident
46 to 90	Resident if 3 UK ties (or more)	Resident if 4 UK ties
91 to 120	Resident if 2 UK ties (or more)	Resident if 3 UK ties (or more)
121 to 182	Resident if 1 UK tie (or more)	Resident if 2 UK ties (or more)
183 or more	Automatically resident	Automatically resident

Remittance basis charge

UK resident for	
Seven out of the last nine years	£30,000
12 out of the last 14 years	£60,000
17 out of the last 20 years	£90,000

Child benefit income tax charge

Where income is between £50,000 and £60,000, the charge is 1% of the amount of child benefit received for every £100 of income over £50,000.

Car benefit percentage

The relevant base level of CO_2 emissions is 95 grams per kilometre.

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

50 grams per kilometre or less	9%
51 grams to 75 grams per kilometre	13%
76 grams to 94 grams per kilometre	17%
95 grams per kilometre	18%

Car fuel benefit

The base figure for calculating the car fuel benefit is £22,600.

Individual savings accounts (ISAs)

The overall investment limit is £20,000.

Property income

Basic rate restriction applies to 25% of finance costs.

Pension scheme limits

Annual allowance	£40,000
Minimum allowance	£10,000
Threshold income limit	£110,000
Income limit	£150,000
Lifetime allowance	£1,000,000

The maximum contribution that can qualify for tax relief without any earnings is £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 75 grams per kilometre	100%
CO_2 emissions between 76 and 130 grams per kilometre	18%
CO_2 emissions over 130 grams per kilometre	8%

Annual investment allowance

Rate of allowance	100%
Expenditure limit	£200,000

Cash basis accounting

Revenue limit	£150,000

Cap on income tax reliefs

Unless otherwise restricted, reliefs are capped at the higher of £50,000 or 25% of income.

Corporation tax

Rate of tax	– Financial year 2017	19%
Rate of tax	– Financial year 2016	20%
Rate of tax	– Financial year 2015	20%
Profit threshold		£1,500,000

Patent box – deduction from net patent profit

Net patent profit x ((main rate – 10%)/main rate)

Value added tax (VAT)

Standard rate	20%
Registration limit	£85,000
Deregistration limit	£83,000

Inheritance tax: nil rate bands and tax rates

Nil rate band

	£
6 April 2017 to 5 April 2018	325,000
6 April 2016 to 5 April 2017	325,000
6 April 2015 to 5 April 2016	325,000
6 April 2014 to 5 April 2015	325,000
6 April 2013 to 5 April 2014	325,000
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

Residence nil rate band		£100,000
Rate of tax on excess over nil rate band	– Lifetime rate	20%
	– Death rate	40%

Inheritance tax: taper relief

Years before death	Percentage 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

	Normal rates	Residential property
Lower rate	10%	18%
Higher rate	20%	28%

Annual exempt amount	£11,300
Entrepreneurs' relief – Lifetime limit	£10,000,000
– Rate of tax	10%

National insurance contributions

Class 1	Employee	£1 – £8,164 per year	Nil
		£8,165 – £45,000 per year	12%
		£45,001 and above per year	2%
Class 1	Employer	£1 – £8,164 per year	Nil
		£8,165 and above per year	13·8%
		Employment allowance	£3,000
Class 1A			13·8%
Class 2		£2·85 per week	
		Small profits threshold	£6,025
Class 4		£1 – £8,164 per year	Nil
		£8,165 – £45,000 per year	9%
		£45,001 and above per year	2%

Rates of interest (assumed)

Official rate of interest	2·5%
Rate of interest on underpaid tax	2·75%
Rate of interest on overpaid tax	0·5%

Stamp duty land tax

Non-residential properties	
Up to £150,000	0%
£150,001 – £250,000	2%
£250,001 and above	5%
Residential properties (note)	
Up to £125,000	0%
£125,001 – £250,000	2%
£250,001 – £925,000	5%
£925,001 – £1,500,000	10%
£1,500,001 and above	12%

Note: These rates are increased by 3% in certain circumstances including the purchase of second homes and buy-to-let properties.

Stamp duty

Shares	0·5%

Section A – BOTH questions are compulsory and MUST be attempted

1 Your manager has had a meeting with Snowdon, a potential new client. Extracts from the memorandum prepared by your manager following the meeting, an inheritance tax computation prepared by Snowdon, and an email from your manager detailing the work you are required to do are set out below.

Extracts from the memorandum prepared by your manager – dated 6 June 2018

Snowdon is resident and domiciled in the UK. He requires advice in respect of a cottage he purchased from his sister, Coleen, and his unincorporated business, 'Siabod', which he started on 1 July 2009.

Purchase of the cottage from Coleen

Snowdon's sister, Coleen, died on 1 June 2018.

Coleen had sold a holiday cottage to Snowdon on 1 May 2014 for £225,000. At that time, the cottage was worth £260,000. Coleen had purchased the cottage for £165,000. The cottage qualified for capital gains tax gift relief and Snowdon and Coleen submitted a valid joint claim.

Coleen made a gift to a trust on 1 March 2010. This resulted in a gross chargeable transfer after all exemptions of £318,000.

Snowdon provided me with a computation he had prepared of the inheritance tax due as a result of Coleen's death in respect of the cottage. Snowdon is aware that he is not an expert when it comes to inheritance tax, such that this computation is unlikely to be totally accurate.

Siabod business

Budgeted figures relating to the unexpanded Siabod business for the year ending 30 June 2019 are:

	£
Turnover	255,000
Tax adjusted trading profit	85,000
Income tax on £85,000 using current rates	22,700
Class 4 national insurance contributions on £85,000 using current rates	4,115

The Siabod business is partially exempt for the purposes of value added tax (VAT). Snowdon's budgeted input tax for the unexpanded business for the year ending 30 June 2019 was £18,000. He would have been able to recover the whole of this amount because the business would have been below the *de minimis* limits.

Since the above figures were prepared, Snowdon has decided to expand the Siabod business and increase its budgeted turnover for the year ending 30 June 2019 from £255,000 to £435,000. In order to carry out this expansion, Snowdon will adopt either strategy A or strategy B. Whichever strategy is adopted, the partial exemption percentage of the business will continue to be 76% (recoverable).

Strategy A

Under this strategy Snowdon will recruit an additional employee with an annual salary of £48,000.

Strategy B

Under this strategy Snowdon will appoint a sub-contractor, Tor Ltd, which will carry out the work required for the expansion. Tor Ltd will charge fees of £90,000 plus VAT each year.

Budgeted costs of expanding the business

	Strategy A £	Strategy B £
Salary of additional employee	48,000	N/A
Other expenditure relating to the expansion, net of VAT at 20%:		
Overheads	38,000	N/A
Advertising	2,000	2,000
Fees payable to Tor Ltd, net of VAT at 20%	N/A	90,000

Extracts from the memorandum prepared by your manager – dated 6 June 2018 (continued)

Additional information

- Prior to the expansion of the Siabod business, Snowdon's liability to employer's class 1 national insurance contributions for the year exceeded £3,000.
- Apart from the profits of the Siabod business, Snowdon's only income is £740 of bank interest each year.

Inheritance tax computation prepared by Snowdon – dated 6 June 2018

Inheritance tax due in respect of the cottage

	£
Value of the cottage as at 1 May 2014 (no annual exemption on death)	260,000
Less: taper relief (£260,000 x 40%) (between four and five years)	(104,000)
	156,000
Nil rate band	325,000
Less: gifts in the seven years prior to death	nil
Available nil rate band	325,000
Inheritance tax (the gift is fully covered by the available nil rate band)	nil

Email from your manager – dated 7 June 2018

Please prepare a memorandum for Snowdon's client file covering the following:

(i) Purchase of the cottage from Coleen

- Identification and explanation of the errors in the inheritance tax (IHT) computation prepared by Snowdon, and a calculation of the correct amount of IHT due.

  I have already established that the cottage **did not** qualify for business property relief.
- The capital gains tax gift relief claimed by Coleen in respect of the cottage and Snowdon's base cost for the purposes of a future disposal by him.

(ii) Expansion of the Siabod business

- Calculations to show which of the two strategies is the most financially advantageous, i.e. the one which is expected to generate the most additional tax adjusted trading profit for the year ending 30 June 2019.
- A calculation of the additional budgeted post-tax income for the tax year 2019/20 which is expected to be generated by the most financially advantageous strategy.

(iii) Procedures we should follow before we agree to become Snowdon's tax advisers

A summary of the procedures we should follow before we agree to become Snowdon's tax advisers.

Tax manager

Required:

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

(i) Purchase of the cottage from Coleen. (9 marks)

(ii) Expansion of the Siabod business. (17 marks)

(iii) Procedures we should follow before we agree to become Snowdon's tax advisers. (5 marks)

Professional marks will be awarded for the approach taken to problem solving, the clarity of the explanations and calculations, the effectiveness with which the information is communicated, and the overall presentation and style of the memorandum. (4 marks)

(35 marks)

2 Your manager has forwarded an email to you from Ms Driver, the acting finance director of Set Ltd. Background information from your manager and the email from Ms Driver are set out below.

Background information from your manager – dated 7 June 2018

The finance director of the Set Ltd group of companies has become seriously ill and Ms Driver is standing in for him. I attach an email from Ms Driver requesting explanations of a number of matters.

Set Ltd has three wholly owned subsidiaries, Ghost Ltd, Steam Ltd and Wagon Ltd, and also owns shares in a number of other companies. Set Ltd and all of its wholly owned subsidiaries are resident in the UK.

You should assume that all of the UK resident companies in the Set Ltd group, including Ghost Ltd, pay corporation tax in instalments every year and will continue to do so, regardless of any loss relief planning entered into.

Please provide the explanations requested by Ms Driver in her email.

Thank you.

Tax manager

Email from Ms Driver– dated 7 June 2018

(a) Ghost Ltd – corporation tax payments

I'm working on the corporation tax instalment payments which Ghost Ltd will be required to pay in the period from now until 31 December 2018.

Set Ltd acquired the whole of the ordinary share capital of Ghost Ltd on 1 June 2018. Ghost Ltd had always prepared accounts to 30 April but following its acquisition has changed its year end to 31 December in line with all of the other companies in the Set Ltd group.

The finalised corporation tax liability of Ghost Ltd for the year ended 30 April 2018 was £597,500. I am now estimating the company's liability for the eight-month period ending 31 December 2018 so that I can determine the instalment payments required. As part of this work, I need to know if the company's corporation tax liability can be reduced in respect of the following:

– Steam Ltd will sell a building on 1 August 2018, which is expected to result in a loss.

– Wagon Ltd has a trading loss brought forward as at 1 January 2018 of £31,500. It is expected to make a further trading loss in the year ending 31 December 2018.

Please explain:

– how Ghost Ltd could make use of the losses of Steam Ltd and Wagon Ltd in the period ending 31 December 2018.

– the payments of corporation tax which will need to be made by Ghost Ltd in the period starting today, 7 June 2018, and ending on 31 December 2018. For the purpose of this explanation, please assume that Ghost Ltd's corporation tax liability for the eight-month period ending 31 December 2018 is £460,000.

(b) Wagon Ltd – value added tax (VAT)

Wagon Ltd intends to purchase manufacturing components from Line Co. Line Co is a company resident in the country of Terminusa, which is not a member of the European Union. There is no VAT in Terminusa.

Wagon Ltd is also planning to sell goods to Signal Co. Signal Co is resident in France, which is a member of the European Union. Signal Co is a small company which is not required to be registered for VAT in France.

Neither Line Co nor Signal Co has any links with the Set Ltd group.

Please explain the VAT implications of these transactions.

Email from Ms Driver– dated 7 June 2018 (continued)

(c) Dee Co and En Co – controlled foreign company (CFC) charge

Set Ltd owns shares in two CFCs: Dee Co and En Co. Both of these companies have chargeable profits for the purposes of the CFC legislation. Estimates of the relevant financial information in respect of the year ending 31 December 2018 are as follows:

	Dee Co	En Co
Percentage of ordinary share capital owned by Set Ltd	21%	37%
	£	£
Non-trading income	nil	65,000
Operating expenditure	8,100,000	3,200,000
Accounting profit	1,100,000	280,000
Taxable total profit	1,300,000	350,000

I can see from my files that the only exemptions from a CFC charge requiring consideration are the low profits exemption and the low profit margin exemption.

Please explain whether Set Ltd will be subject to a CFC charge in respect of either Dee Co or En Co.

(d) Steam Ltd – Project Whistle

Steam Ltd will commence Project Whistle in 2019. As part of the project, Steam Ltd will engage in scientific research, some of which will qualify for the additional 130% tax deduction available in respect of qualifying research and development expenditure. Due to the significant costs involved, Steam Ltd is expected to make a trading loss in the year ending 31 December 2019.

Please explain:

– how any trading loss made by Steam Ltd in the year ending 31 December 2019 can be relieved.

– the factors to consider when choosing between the available reliefs.

Regards

Ms Driver

Required:

Provide the explanations requested in the email from Ms Driver. The following marks are available:

(a) Ghost Ltd – corporation tax payments. (9 marks)

(b) Wagon Ltd – value added tax (VAT). (5 marks)

(c) Dee Co and En Co – controlled foreign company (CFC) charge. (4 marks)

(d) Steam Ltd – Project Whistle. (7 marks)

(25 marks)

Section B – BOTH questions are compulsory and MUST be attempted

3 Max ceased trading two years ago, and is now about to move overseas. He would like advice on the capital gains tax (CGT) implications of the disposal of two assets previously used in his unincorporated business, and the inheritance tax (IHT) implications of gifting one of them.

Max:

– Has always been UK resident and domiciled.
– Is widowed and has one daughter, Fara.
– Is a higher-rate taxpayer.
– Makes disposals each year to use his annual exempt amount for capital gains tax.
– Has made one previous lifetime gift to Fara on 6 May 2015, which resulted in a gross chargeable transfer of £194,000.

Max – unincorporated business:

– Max operated as a sole trader for many years, but ceased trading on 31 May 2016.
– Max still owns office premises and a warehouse which had been used exclusively in his business until 31 May 2016.
– Max now wishes to dispose of these buildings prior to moving overseas.

Proposed gift of the office premises:

– Max is proposing to gift the office premises to Fara on 30 June 2018.
– Max acquired the premises on 1 April 2010.
– Since 1 June 2016, the premises have been let to an unconnected company.
– The market value of the premises in June 2018 is £168,000, which exceeds the original cost.

Max – move overseas:

– Max has decided to move overseas for a period of two and a half years commencing on 1 November 2018.
– Max does not intend to return to the UK at all during this period.
– Max will return to live permanently in the UK on 30 June 2021.
– Max is not entitled to use the split year treatment for determination of his residence status in any tax year.

Proposed sale of the warehouse:

– The warehouse was acquired on 1 August 2014 for a cost of £72,000.
– On 1 December 2013, Max had sold a small showroom for proceeds of £78,000, which gave rise to a chargeable gain of £16,000.
– Max made a claim to defer the gain against the acquisition of the warehouse.
– Max has received an offer of £84,000 for the immediate sale of the warehouse in June 2018.
– An alternative buyer has offered £90,000 for the warehouse, but will not be able to complete the purchase until June 2019.

Required:

(a) In respect of the proposed gift of the office premises to Fara on 30 June 2018:

(i) Advise Max whether or not capital gains tax (CGT) gift relief will be available, and if so, to what extent. (3 marks)

(ii) Advise Max of the maximum potential inheritance tax (IHT) liability, and the circumstances in which this would arise. (5 marks)

(b) Explain the effect of Max's period of living overseas on his UK residence status for all relevant tax years, and advise him of the CGT consequences of the sale of the warehouse (1) in June 2018, or alternatively (2) in June 2019.

Note: No calculations are required for this part. (6 marks)

(c) Explain whether or not entrepreneurs' relief will be available on the sale of the warehouse, and calculate the increase in Max's after-tax proceeds if he sells the warehouse in June 2019 rather than in June 2018. (6 marks)

(20 marks)

4 Your client, Jessica, has requested advice in relation to the tax liability arising on a redundancy payment, the options available to relieve her share of a partnership trading loss, and the maximum contribution she can make to a personal pension scheme.

Jessica:
– Is resident and domiciled in the UK.
– Was employed by Berens Ltd up to 31 March 2018, when she was made redundant.
– Will become a partner in the Langley Partnership on 1 July 2018.
– Has never made any disposals for capital gains tax (CGT) purposes.

Jessica – income from Berens Ltd:
– Jessica received an annual salary from Berens Ltd of £145,000 each year from the tax year 2015/16.
– From 6 April 2017, Jessica was provided with a new company laptop computer, which cost Berens Ltd £850. Jessica had significant private use of this laptop computer.

Jessica – other income:
– Prior to the tax year 2017/18 Jessica had no other source of income.
– Starting from the tax year 2017/18, Jessica receives rental income of £6,000 each tax year.

Jessica – redundancy package from Berens Ltd:
– The package, received on 31 March 2018, included a statutory redundancy payment of £18,000 and an *ex-gratia* payment of £32,000.
– As part of the package, Berens Ltd also allowed Jessica to keep the laptop computer, which had a market value of £540 on 31 March 2018.

The Langley Partnership:
– Prior to 1 July 2018, there were two partners in the partnership – Issa and Finn.
– From 1 July 2018, the profit sharing ratio will be: Issa 20%, Finn 40%, and Jessica 40%.
– The budgeted tax-adjusted trading (loss)/profit of the partnership is:
  – Year ending 31 March 2019 – (£160,000)
  – Year ending 31 March 2020 – £205,000.

Jessica – personal pension plan contributions:
– Jessica joined a registered personal pension scheme on 1 May 2018.
– She has not previously been in any pension scheme.
– She wishes to make the maximum possible contributions which will qualify for tax relief in each of the tax years 2018/19 and 2019/20.

Required:

(a) Explain, with supporting calculations, the taxable amount of the redundancy package received from Berens Ltd on 31 March 2018, and calculate the income tax payable on it by Jessica. (5 marks)

(b) (i) Advise Jessica of the options available to her to relieve her share of the Langley Partnership loss for the year ending 31 March 2019, on the assumption that she does not wish to carry any of her share of the loss forward. (3 marks)

(ii) Determine, by reference to the amount of income tax saved in each case, which of the available loss relief options (as identified in (i) above) will result in the highest overall income tax saving for Jessica. (7 marks)

(c) Explain, with supporting calculations, the maximum amount of the contributions Jessica can pay into her pension scheme in each of the tax years 2018/19 and 2019/20 without incurring an annual allowance charge. (5 marks)

(20 marks)

End of Question Paper