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UNIVERSITY OF BOLTON

INSTITUTE OF MANAGEMENT

MSc ACCOUNTANCY & FINANCIAL MANAGEMENT

SEMESTER 1 2018/19

ADVANCED TAXATION

MODULE NO: ACC7506

Date: Thursday 17 January 2019 **Time: 2.00 – 5.00**

INSTRUCTIONS TO CANDIDATES:

There are FOUR questions on this paper.

Answer ALL questions in SECTION A

Answer ONLY 2 questions in SECTION B

Please refer to tax tables for rates & allowances

This is a closed book exam

You must hand in the exam paper with your answer booklet

Section A

QUESTION 1

I attach a schedule received this morning from Bob Smith, the managing director of Global plc, a UK resident trading company.

He has requested a meeting next week to discuss the tax implications of various transactions planned or undertaken by the company during the year ended 31 October 2018.

This email will make more sense when you have read Bob's schedule, so I suggest you read that first.

I would like you to prepare briefing notes for me to take to my meeting with Bob. Your notes should cover the following:

– Advice for Global plc on the corporation tax implications of transactions (1) to (5). I need you to support this with calculations where possible.

– Could you also set out some explanations of how Global plc will be affected by the requirement to make quarterly instalment payments in respect of its corporation tax liability for the year ended 31 October 2018? Bob is not sure how this system works, and wants to know when the company will have to pay its tax, as they have never had to pay by instalments in the past. You don't need to calculate the corporation tax liability here.

– Advice on the conditions that must be met for Global plc to register with Star Ltd as a group for VAT purposes, together with an explanation of the consequences of being group VAT registered. Could you also set out some thoughts as to whether or not you think this would be beneficial for Global plc?

– An explanation of the VAT implications if Global plc imports goods from overseas, either from a VAT registered company within the European Union or from Narnia. Note that from our tax files you will see that:

– In all cases, the overseas forecast profits are the same for accounting and taxation purposes.

– The double taxation treaties between the UK, Rightland and Leftland provide that overseas taxes are relieved as a tax credit against UK corporation tax.

Question 1 continued over the page

Question 1 continued

– Global plc has not made the election to exempt profits of an overseas permanent establishment.

– Global plc is a large company for the purposes of research and development and transfer pricing legislation.

The schedule from Bob Smith is set out below:

Global plc – year ended 31 October 2018

Global plc has forecast trading profits for the year ended 31 October 2018 of £3,000,000.

The following transactions have taken/will take place during the year to 31 October 2018:

(1) On 1 January 2018 Global plc purchased an 80% shareholding in Octopus Inc, a manufacturing company resident in and controlled from the country of Rightland. At the same time it lent the company £6,000,000 at 6% interest, which is an appropriate market rate. Octopus Inc has forecast profits for the year ended 31 October 2018 of £950,000, and these will be subject to corporation tax at the rate of 21% in Rightland.

On 15 May 2018, Octopus Inc is planning to pay a dividend of £400,000, and this will be subject to withholding tax at a rate of 7%.

During the year ended 31 October 2018, the interest payable by Octopus Inc is £300,000, and this will be subject to withholding tax at a rate of 5%.

(2) During June 2018, Global plc is planning to sell 15,000 units of a product to Octopus Inc at a price of £17 per unit. This is 20% less than the trade selling price given to other customers.

(3) On 1 December 2017, Global plc set up a branch in the country of Leftland. The branch is controlled from Leftland, and its forecast profits for the period to 31 October 2018 are £240,000. These are subject to tax at a rate of 35% in Leftland. Half of the profits after tax will be remitted to the UK.

(4) On 30 April 2018, Global plc is planning to sell its 75% shareholding in Excess Ltd, an investment company resident in the UK, for £2,350,000. The disposal, if chargeable, will result in a gain (after indexation allowance) of £1,120,000.

Question 1 continued over the page

Question 1 continued

Global plc transferred an office block to Excess Ltd on 20 July 2013, when the office block was valued at £840,000. The office block originally cost Global plc £350,000 on 17 June 2007. It is still owned by Excess Ltd, and is currently valued at £960,000. The indexation allowance from June 2007 to July 2013 is £63,700, and from June 2007 to April 2018 it is £119,700. Excess Ltd prepares its accounts to 31 October.

(5) On 1 March 2018, Global plc purchased a 90% shareholding in Star Ltd, a UK resident company. The company is forecast to make a trading loss of £320,000 for the year ended 31 October 2018. On 20 January 2017, Star Ltd sold investments for £570,000, resulting in a capital loss of £230,000.

VAT issues

Global plc and Star Ltd are not currently registered as a group for VAT purposes, but are considering the possibility of registering as a VAT group.

Global plc's sales are all standard rated, whilst Star Ltd's are zero rated. The purchases for both companies are standard rated.

In addition, Global plc expects to incur standard rated overhead expenditure of £300,000 in the year ended 31 October 2018 that cannot be directly attributed to either of the companies' sales.

Global plc charges Star Ltd a management charge of £10,000 per quarter in respect of the services of its accountancy department.

It is likely that Global plc will start importing goods in the near future; either from VAT registered companies within the European Union, or from Narnia, a country outside of the European Union.

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Required:

Prepare the briefing notes requested by your manager.

You should assume today's date is 15 April 2018.

You should assume that the rates and allowances of the Financial Year 2017 will continue to apply for the foreseeable future. The marks are allocated as follows:

(a) Corporation tax implications of transactions (1) to (5) with supporting calculations. (18 marks)

(b) The effect of making quarterly instalment payments. (5 marks)

(c) Group VAT registration issues. (8 marks)

(d) VAT implications of importing goods. (4 marks)

Professional marks will be awarded for the appropriateness of the format, the clarity of explanations and calculations, the effectiveness with which the information is communicated, and the overall presentation. (5 marks)

(Total: 40 marks)

END OF QUESTION 1

END OF SECTION A

PLEASE TURN THE PAGE

SECTION B

Answer ONLY 2 questions out of 3 questions

QUESTION 2

Javed Khan is a partner in the firm for which you work. He has sent you the following memo by email:

I have received an email from Dania Mahmood and I have forwarded the relevant parts to you.

Dania is an existing client of the firm who is considering setting up her own business. She has a number of queries about this and I would like you to prepare notes for a meeting that I will be having with Dania next week.

Specifically I would like you to prepare notes that cover the differences between trading as a sole trader and as a company covering the following issues:

– rates of tax paid on profits

– liability to national insurance

– payment dates of tax

– withdrawal of profits

– relief for trading losses

At the end of the notes I would like you to give a recommendation as to whether Dania should start trading as a sole trader or through a company.

Question 2 continued over the page

Question 2 continued

I would also like you to prepare computations comparing the total tax and national insurance payable on the estimated figures for the year end 31 March 2020 assuming Dania trades as a sole trader or through a company.

For the purposes of the calculations assume that if Dania trades through a company, she will withdraw a gross salary of £14,460 and will receive cash dividends of £5,000.

You can ignore the loss in the year ended 31 March 2019 for these calculations and you can assume that the rates and allowances for the tax year 2017/18 and the Financial Year 2017 apply.

Lastly, Dania mentioned to me in passing that she had recently received a refund of income tax from HM Revenue and Customs (HMRC), but she has been unable to identify a reason for a refund to be made. I plan to discuss this with her next week. Please could you prepare a summary of the actions which we should take as Dania's tax advisers, and any other matters of which Dania should be aware in respect of the refund.

The extracts from Dania's email are set out below.

Extract 1

As you know I have had enough of city life and have just resigned from my lucrative directorship of ABC plc. The £200,000 salary and perks I have had for the last ten years may sound attractive but I now want to work less and get my work-life balance back in order.

So, on 1 April 2018, I plan to set up my own business which I will operate from the top floor of my house. With the initial set up costs and marketing I need to do, I think that in my first year to 31 March 2019 I will make a small loss of about £4,000.

However, in the year ended 31 March 2020 I estimate that I should have gross income of £60,000 and the following expenses:

Question 2 continued over the page

Question 2 continued

Car running expenses (including petrol) of £3,200. The car will cost £15,500, has CO2 emissions of 133g/km and a manufacturer's list price of £16,750.

I estimate that I will use the car approximately 25% for private purposes and I will fund all of my petrol costs from the business.

I then anticipate steadily increasing income and profits thereafter.

Extract 2

I am unsure as to whether I should initially set up the business as a sole trader or through a company. Either way I will not involve anyone else in the business at this stage. I would be grateful if you could advise me as to the differences in tax treatment of each trading vehicle.

For example, I have been told that there are significant advantages in operating as a company rather than a sole trader, but not necessarily when you are making losses. I am not sure why though.

In either case, I will need to withdraw income net of income tax and national insurance to live on and I think that I need net income of around £18,000 per annum. If the business is run as a company I could have some of it paid as a dividend at the end of the year, say £5,000.

Question 2 continued over the page

Question 2 continued

Required:

Prepare the briefing notes requested by Javed Khan.

The marks are allocated as follows:

(a) Notes contrasting the tax treatment of trading as a sole trader and as a company covering the five issues mentioned in Javed Khan' email and giving a recommendation as to how the business should be set up. (12 marks)

(b) Computations comparing the total tax and national insurance payable on the estimated figures for the year ending 31 March 2020 assuming Dania trades as a sole trader or through a company. (13 marks)

(c) Refund of income tax. (5 marks)

Assume that the tax rates and allowances for the tax year 2017/18 and Financial Year 2017 apply throughout the question. Ignore VAT.

(Total: 30 marks)

Question 3

Martin Smith is the sole shareholder and sole director of Diamond Ltd a UK resident company that provides internet services.

The projected taxable profits of the company in the 12 month accounting period to 31 March 2018 are £135,000 after charging director's remuneration of £22,125 (from which PAYE of £2,125 will have been deducted) and contributions to an occupational pension scheme in respect of Martin of £6,000. A maximum funding check on the occupational pension reveals that there is ample scope for making further contributions without infringing HMRC maximum tax relief limits.

Diamond Ltd also paid Martin dividends of £8,000 in the accounting period.

The company is projected to have cash balances at 31 March 2018 of £31,000.

Apart from bank interest of £1,250 Martin has no other income than that referred to above. Assume that it is now February 2018.

Question 3 continued over the page

Question 3 continued

Required:

Using the tax year 2017/18 and FY2017 rates calculate the additional tax and national insurance cost/saving of each of the following options:

(a) paying a bonus to Martin of £27,000 (12 marks)

(b) paying a dividend to Martin of £27,000 (2 marks)

(c) Diamond Ltd making an employer contribution for Martin to the occupational pension scheme of £27,000 (2 marks)

(d) retaining the £27,000 profits in the company. (2 marks)

(e) He would also like advice on the meaning of Principal Private Residence as he is thinking of selling his main home. (6 marks)

(f) He is also considering renting a room out in his main home and would like some advice on the meaning of Rent-a- Room relief. (6 marks)

(Total: 30 marks)

Question 4

Maria Ahmad is resident in the UK, but is not domiciled in the UK. Following her marriage to a UK citizen, Maria is planning to become UK domiciled, and wants to know how this will affect the potential inheritance tax liability on her death.

She would also like you to calculate her income tax for the tax year 2017/18.

The following information has been obtained from a recent meeting

with Maria. **Maria Ahmad – background**

- Born in the country of Iqrastan.
- Lived in the UK since 6 April 2002.
- Employed by the Iqrastanian National Bank in London.

Question 4 continued over the page

Question 4 continued

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Assets owned at 5 April 2018

– Main residence valued at £263,500. This is situated in the UK and has an outstanding endowment mortgage of £80,000.

– A house in Iqrastan worth £60,000.

– 40,000 shares in Swan plc, a company quoted on the UK Stock Exchange at 308p – 316p.

– Antiques worth £35,000. These were bought in Iqrastan but are now situated in Maria's UK residence.

– Bank deposits of £65,000 with the Iqrastanian National Bank, of which £45,000 is held at the London branch and £20,000 at the main branch in Iqrastan.

– An interest-free loan of £15,000 made to Maria's brother who is resident in Iqrastan. The loan was used to purchase property situated in the UK.

Income – tax year 2017/18

– Salary from Iqrastanian National Bank in London £39,030, from which £5,606 income tax was deducted under PAYE.

– Interest from Iqrastanian National Bank of £2,100 credited to the bank account in London.

– Interest from Iqrastanian National Bank of £750 (net of 15% foreign tax) credited to the account in Iqrastan. None of this interest was remitted to the UK.

– Dividends from Swan plc of 15p per share.

Maria's will

– Under the terms of her will, Maria has left all of her assets to her three children.

– If she were to die, Iqrastanian death duty of £21,000 would be payable irrespective of her domicile.

Question 4 continued over the page

Question 4 continued

Notes

- There is no double taxation agreement between the UK and Iqrastan.
- All of the above figures are in pounds sterling.

Required:

(a) Advise Maria of:
- **when she will be treated as domiciled in the UK for the purposes of IHT. (4 marks)**
- **how she could acquire domicile in the UK under general law. (3 marks)**

(b) Advise Maria as to the potential increase in her liability to UK IHT if she were to become domiciled in the UK.

Your answer should include an explanation of why Maria's assets are or are not subject to UK IHT. (14 marks)

(c) Calculate the UK income tax payable by Maria for the tax year 2017/18.

Your answer should include an explanation of why Maria's overseas income is or is not subject to UK income tax. (9 marks)

(Total: 30 marks)

END OF SECTION B

END OF QUESTIONS

TAX RATES AND ALLOWANCES

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 to be made to the nearest £.**
3. **All apportionments should be made to the nearest month.**
4. **All workings should be shown.**

INCOME TAX

		Normal rates	Dividend rates
Basic rate	£1 – £33,500	20%	7.5%
Higher rate	£33,501 – £150,000	40%	32.5%
Additional rate	£150,001 and above	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:	Charge
7 out of the last 9 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

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%
	– Financial year 2016	20%
	– Financial year 2015	20%
Profit threshold		£1,500,000

Patent box – deduction from net patent profit

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

VALUE ADDED TAX

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	
6 April 2017 to 5 April 2018	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**
Over 3 but less than 4 years	20%
Over 4 but less than 5 years	40%
Over 5 but less than 6 years	60%
Over 6 but less than 7 years	80%

CAPITAL GAINS TAX

		Normal rates	**Residential property**
Rates of tax	– 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	2.50%
Rate of interest on underpaid tax	2.75%
Rate of interest on overpaid tax	0.50%

STAMP DUTY LAND TAX

Non-residential properties

£150,000 or less	0%
£150,001 – £250,000	2%
£250,001 and above	5%

Residential properties

£125,000 or less	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%