

# Tolley<sup>®</sup> Exam Training

## **CTA ADVANCED TECHNICAL PAPER**

## **TAXATION OF LARGER COMPANIES AND GROUPS**

## **PRE REVISION QUESTION BANK**

### **FA 2025**

May and November 2026 Sittings

PQ123

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise without the prior written permission of the publisher.

This material contains general information only. Whilst every care has been taken to ensure the accuracy of the contents of this work, no responsibility for loss occasioned to any person acting or refraining from action as a result of any statement in it can be accepted by the author or the publishers.

Unless otherwise agreed to by LN in writing, use of the Online Services is permitted only via individual users engaged in an active user session and may not be collected via automated or robotic methods.

Regardless of the data delivery method, content may not be used in conjunction with a generative AI solution.

## INTRODUCTION

This Advanced Technical Pre Revision Question Bank contains 15 exam standard questions all with answers updated to Finance Act 2025. This question bank forms an important part of your preparation for the examination - question practice is the key to passing exams.

As you answer the questions you may refer to either a hard copy or on-screen version of the **CTA Tax Tables 2026** and your own personalised version of the approved online legislation.

### Using this question bank

All the CTA Advanced Technical exams are **3.5 hours** in length.

We suggest you **allocate 2 minutes per mark** which allows for 10 minutes initial reading time.

10 mark question = 20 minutes

15 mark question = 30 minutes

20 mark question = 40 minutes

You should attempt each question as if you were in the real exam. Try to **avoid just reading the answers** to questions - it is all too easy to nod as you read the answer saying “yes I know that point, yes I understand that advice given” - the test is would you have actually put those points in your answer? You won't find this out unless you **type up the answers and we recommend you do this using the on-screen version of this QB**. Ensuring you type up “proper” answers also gives you a good idea of how long an exam standard answer will take you to produce.

### Preparing your answers

Questions set on the Advanced Technical papers **do not require a specific format** of answer - all questions will require a direct answer (rather than a letter to a client or an email to the tax partner). Requirements will start with words like “Explain”, “Discuss”, “Compare” and “Calculate”.

There may be scenarios where there is no single correct answer or where the answer is not definitive. You will be expected to **make recommendations** as to actions which should be taken by the subject of the question.

You are expected to produce **full and reasoned answers** sufficient to demonstrate your knowledge and application in order to gain the available marks. **Brief bullet points are unlikely to be sufficient.**

Key **presentation considerations** include spacing your answer out, cross referencing your workings and using subheadings and short paragraphs.

The CIOT do not award “presentation and higher skills” (PHS) marks on individual questions nor will they form part of the 100 marks available on a paper. Instead, when they carry out their normal review of a script that is just below a pass, **up to two bonus PHS marks per paper** can be awarded which could therefore boost a candidate from a fail to a pass.

When awarding these bonus marks, the CIOT have stated they will consider:

- The accuracy of spelling and grammar.
- Whether full sentences have been used where appropriate (in some cases appropriately detailed lists may be appropriate, for example setting out the conditions for a relief to apply).
- Whether answers flow well and are presented in a logical order.
- Whether conclusions have been reached where it is appropriate to expect a conclusion.

**Reviewing your answers**

It is essential to read through your answer when you have finished typing it (within the time allocated for that question). We thought it might be useful at this stage to pass on some tips about how to review your answers effectively – **before** you look at the model answer.

Remember the first thing the marker will do is read your answer through as a whole – what overall impression are you giving of your ability? A good question to ask yourself is would the reader pay money for your advice? Have you put the marker in a good mood as soon as they see your script or are they going to be dreading marking what you have handed in?

You may be able to make some small corrections at this review stage – you may find you have missed out a vital word such as “not” or you may at this stage think of another point or two to add while reading through your answer. This approach could increase your marks much more effectively than carrying on with the point you were making before you stopped to do this final review.

**Reviewing the model answer**

In the advanced technical papers, it is quite likely that there is no single right answer. The model answer is only one possible solution. You may well have included valid points which are not included in the model answer. Review critically both your answer and the model answer. Are there points in the model answer which you could have included in your answer to get extra marks? Are there points you have included which, with the benefit of hindsight, you should have left out?

## CONTENTS

## QUESTIONS

NO	NAME	TOPIC	MARKS
1	Polish Home Ltd	Capital allowances	15
2	Underground group	Degrouping, successions, SSE	20
3	Lentil plc	Outward investment PE or subsidiary	20
4	Midnight plc	TP and PEs	15
5	Swift Group	CTSA errors and penalties	20
6	Challenger plc	Sale of shares and property transactiions	20
7	The Barley Group	Reorganisations	20
8	Theta plc Group	CFCs, Hybrids and anti-avoidance	20
9	UniComms Group	Residency/PE/Royalties per treaty	20
10	Tripletree Group	CFCs	20
11	Luczo Ltd	CT comp long POA	20
12	Circle Ltd	Adjustment of profits comp & group relief comp	20
13	Charlese plc	Capital allowances	20
14	Trouble plc	LRs dividends, CFCs WHT	15
15	Blue Buildings Ltd	Group capital gains/share sale for earn-out	20



## INCOME TAX - RATES AND THRESHOLDS

	2025/26	2024/25
<b>Rates</b>	%	%
Starting rate for savings income only	0	0
Basic rate for non-savings and savings income only	20	20
Higher rate for non-savings and savings income only	40	40
Additional and trust rate for non-savings and savings income	45	45
Dividend ordinary rate	8.75	8.75
Dividend upper rate	33.75	33.75
Dividend additional rate and trust rate for dividends	39.35	39.35
<b>Thresholds</b>	£	£
Savings income starting rate band	1 – 5,000	1 – 5,000
Basic rate band	1 – 37,700	1 – 37,700
Higher rate band	37,701 – 125,140	37,701 – 125,140
Dividend allowance	500	500
Savings allowance		
– Taxpayer with basic rate income	1,000	1,000
– Taxpayer with higher rate income	500	500
– Taxpayer with additional rate income	Nil	Nil
<b>Scottish Tax Rates<sup>(1)</sup></b>	%	%
Starter rate	19	19
Scottish basic rate	20	20
Intermediate rate	21	21
Higher rate	42	42
Advanced rate	45	45
Top rate	48	48
<b>Scottish Tax Thresholds<sup>(1)</sup></b>	£	£
Starter rate	1 – 2,827	1 – 2,306
Scottish basic rate	2,828 – 14,921	2,307 – 13,991
Intermediate rate	14,922 – 31,092	13,992 – 31,092
Higher rate	31,093 – 62,430	31,093 – 62,430
Advanced rate	62,431 – 125,140	62,431 – 125,140
Top rate	125,140+	125,140+

## INCOME TAX - RELIEFS

	2025/26	2024/25
	£	£
Personal allowance <sup>(2)</sup>	12,570	12,570
Married couple's allowance <sup>(3)</sup>	11,270	11,080
– Maximum income before abatement of relief - £1 for £2	37,700	37,000
– Minimum allowance	4,360	4,280
Transferable Tax allowance for married couples and civil partners <sup>(4)</sup>	1,260	1,260
Blind person's allowance	3,130	3,070
Enterprise investment scheme relief limit <sup>(5)</sup>	1,000,000	1,000,000
Venture capital trust relief limit	200,000	200,000
Seed enterprise investment scheme relief limit	200,000	200,000
De minimis trusts amount	500	500

- Notes:** (1) Scottish taxpayers pay Scottish income tax on non-savings income.  
(2) The personal allowance of any individual with adjusted net income above £100,000 is reduced by £1 for every £2 of adjusted net income above the £100,000 limit.  
(3) Only available where at least one partner was born before 6 April 1935. Relief restricted to 10%.  
(4) The recipient must not be liable to tax above the basic rate. The recipient is eligible for a tax reduction of 20% of the transferred amount.  
(5) The limit is £2 million, where over £1 million is invested in knowledge intensive companies.

# CTA EXAMINATIONS

2026

## TAX TABLES



ISA limits	2025/26	2024/25
Maximum subscription:	£	£
'Adult' ISAs	20,000	20,000
Junior ISAs	9,000	9,000

### Pension contributions

	Annual allowance <sup>(1)</sup>	Minimum pension age
2025/26 and 2024/25	£60,000	55
Basic amount qualifying for tax relief	£3,600	
Lump sum allowance	£268,275	

**Note:** (1) Tapered by £1 for every £2 of adjusted income above £260,000 for individuals with threshold income above £200,000. It cannot be reduced below £10,000.

### ITEPA mileage rates

Car or van <sup>(2)</sup>	First 10,000 business miles	45p
	Additional business miles	25p
Motorcycles		24p
Bicycles		20p
Passenger payments		5p

**Note:** (2) For NIC purposes, a rate of 45p applies irrespective of mileage.

### INCOME TAX - BENEFITS

#### Car benefits – 2025/26

Emissions	Electric range (miles)	Car benefit %	
0g/km	N/A	3%	
1-50g/km	≥130	3%	
1-50g/km	70-129	6%	
1-50g/km	40-69	9%	
1-50g/km	30-39	13%	
1-50g/km	<30	15%	
51-54g/km		16%	
55-59g/km		17%	
60-64g/km		18%	
65-69g/km		19%	
70-74g/km		20%	
75g/km or more		21%	+ 1% for every additional whole 5g/km ab 75g/km
155g/km or more		37%	

	2025/26	2024/25
<b>Fuel benefit base figure</b>	£ 28,200	£ 27,800
<b>Van benefits</b>		
No CO <sub>2</sub> emissions	Nil	Nil
CO <sub>2</sub> emissions > 0g/km	4,020	3,960
Fuel benefit for vans	769	757

<b>Official rate of interest (assumed)</b>	<b>from 6 April 2025</b> 3.75%	<b>from 6 April 2024</b> 2.25%
--	-----------------------------------	-----------------------------------

# CTA EXAMINATIONS

2026

## TAX TABLES



### CAPITAL ALLOWANCES

Annual investment allowance for plant and machinery (AIA) <sup>(1)</sup>	100%
WDA on plant and machinery in main pool <sup>(2)</sup>	18%
WDA on plant and machinery in special rate pool <sup>(3)</sup>	6%
WDA on patent rights and know-how	25%
WDA on structures and buildings (SBA) <sup>(4)</sup>	3%

- Notes:** (1) On first £1,000,000 of investment in plant & machinery (not cars).  
 (2) The main pool rate applies to cars with CO<sub>2</sub> emissions of not more than 50g/km (prior to April 2021 not more than 110g/km).  
 (3) The special pool rate applies to cars with CO<sub>2</sub> emissions greater than 50g/km (prior to April 2021 greater than 110g/km).  
 (4) A 10% rate applies in respect of special tax site expenditure.

### 100% First year allowances (FYA) available to all businesses

Capital expenditure incurred on research and development.  
 New zero-emission goods vehicles (until 31 March/5 April 2025).  
 New cars that either emit 0g/km of CO<sub>2</sub> (50g/km prior to April 2021) or are electric (until 31 March/ 5 April 2026).  
 Electric vehicle charging points (until 31 March/5 April 2026).

### First year allowances (FYA) available to companies only

	Main pool assets	Special rate pool assets
Expenditure on new plant and machinery (other than cars) from 1 April 2023 onwards <sup>(5)</sup>	100%	50%
Expenditure on new plant and machinery (other than cars) in a special tax site	100%	100%

- Notes:** (5) 130% for main pool expenditure and 50% for special rate pool expenditure between 1 April 2021 and 31 March 2023.

### INCOME TAX - SIMPLIFICATION MEASURES

	2025/26	2024/25
	£	£
<b>'Rent-a-room' limit</b>	7,500	7,500
<b>Property allowance/Trading allowance</b>	1,000	1,000

### Flat Rate Expenses for Unincorporated Businesses

Motoring expenses		
Cars or vans	First 10,000 business miles	45p per mile
	Additional business miles	25p per mile
Motorcycles		24p per mile
Business use of home	25 – 50 hours use	£10 per month
	51 – 100 hours use	£18 per month
	101+ hours use	£26 per month
Private use of business premises	No of persons living there:	
	1	£350 per month
	2	£500 per month
	3+	£650 per month

# CTA EXAMINATIONS

2026

## TAX TABLES



### NATIONAL INSURANCE CONTRIBUTIONS

Class 1 limits	2025/26			2024/25		
	Annual	Monthly	Weekly	Annual	Monthly	Weekly
Lower earnings limit (LEL)	£6,500	£542	£125	£6,396	£533	£123
Primary threshold (PT)	£12,570	£1,048	£242	£12,570	£1,048	£242
Secondary threshold (ST)	£5,000	£417	£96	£9,100	£758	£175
Upper earnings limit (UEL)	£50,270	£4,189	£967	£50,270	£4,189	£967
Upper secondary threshold for under 21 (UST)	£50,270	£4,189	£967	£50,270	£4,189	£967
Apprentice upper secondary threshold for under 25 (AUST)	£50,270	£4,189	£967	£50,270	£4,189	£967
Special tax sites upper secondary threshold	£25,000	£2,083	£481	£25,000	£2,083	£481

#### Class 1 primary contribution rates

Earnings between PT and UEL	8%	8%
Earnings above UEL	2%	2%

#### Class 1 secondary contribution rates

Earnings above ST <sup>(1)</sup>	15%	13.8%
----------------------------------	-----	-------

**Note:** (1) Rate of secondary NICs between the ST and the UST, AUST & special tax sites upper secondary threshold is 0%.

	2025/26	2024/25
<b>Employment allowance</b>		
Per year, per employer	£10,500	£5,000
<b>Class 1A contributions</b>	15%	13.8%
<b>Class 1B contributions</b>	15%	13.8%
<b>Class 2 contributions</b>		
Rate	£3.50 pw	£3.45 pw
Small profits threshold (SPL) <sup>(2)</sup>	£6,845	£6,725
Lower profits limit (LPL)	N/A	N/A

**Note:** (2) From 2024/25, self-employed individuals with profits below the small profits threshold can pay Class 2 NICs voluntarily to get access to contributory benefits including the State Pension.

<b>Class 3 contributions</b>	£17.75 pw	£17.45 pw
<b>Class 4 contributions</b>		
Annual lower profits limit (LPL)	£12,570	£12,570
Annual upper profits limit (UPL)	£50,270	£50,270
Percentage rate between LPL and UPL	6%	6%
Percentage rate above UPL	2%	2%

### OTHER PAYROLL INFORMATION

<b>Statutory maternity/adoption pay</b>	First 6 weeks @ 90% of AWE Next 33 weeks @ the lower of £187.18 and 90% of AWE
<b>Statutory shared parental pay /paternity pay/parental bereavement pay/neonatal pay</b>	For each qualifying week, the lower of 90% of AWE and £187.18
<b>Statutory sick pay</b>	£118.75 per week

# CTA EXAMINATIONS

2026

## TAX TABLES



<b>Student Loan</b>	Plan 1:	9% of earnings exceeding £26,065 per year (£2,172.08 per month/ £501.25 per week)
	Plan 2:	9% of earnings exceeding £28,470 per year (£2,372.50 per month /£547.50 per week)
	Plan 4:	9% of earnings exceeding £32,745 per year (£2,728.75 per month /£629.71 per week)
<b>Postgraduate Loan</b>		6% of earnings exceeding £21,000 per year (£1,750 per month/£403.84 per week)

### National living/minimum wage (April 2025 onwards)

Category of Worker	Rate per hour £	Category of Worker	Rate per hour £
Workers aged 21 and over	12.21	16–17 year olds	7.55
18–20 year olds	10	Apprentices	7.55

**Accommodation Offset** £10.66 per day

### CHILD BENEFIT

Year to 5 April 2026	Weekly rate £
First child	26.05
Each subsequent child	17.25

Child benefit charge	Withdrawal rate
Adjusted net income >£60,000	1% of benefit per £200 of income between £60,000 and £80,000
Adjusted net income >£80,000	Full child benefit amount assessable in that tax year

### HMRC INTEREST RATES (assumed)

Late payment interest	7%
Interest on underpaid corporation tax instalments	5.50%
Repayment interest	3.50%
Interest on overpaid corporation tax instalments	4.25%

### CAPITAL GAINS TAX

	2025/26	2024/25
Annual exempt amount for individuals	£3,000	£3,000

#### CGT rates for individuals, trusts and estates

Gains qualifying for business asset disposal <sup>(1)</sup> /investors' relief <sup>(1)</sup>	14%	10%
Gains for individuals falling within remaining basic rate band <sup>(2)</sup>	18%	18%
Gains for individuals exceeding basic rate band and gains for trusts and estates <sup>(3)</sup>	24%	24%

- Notes:** (1) From 6 April 2026 the rate will be 18%  
 (2) For disposals prior to 30 October 2024, the rate was 10% for assets other than residential property  
 (3) For disposals prior to 30 October 2024, the rate was 20% for assets other than residential property

Business Asset Disposal relief	2025/26	2024/25
Relevant gains (lifetime maximum) <sup>(4)</sup>	£1 million	£1 million

Investors' relief	2025/26	2024/25
Relevant gains (lifetime maximum) <sup>(5)</sup>	£1 million	£1 million

- Note:** (4) For qualifying disposals made before 11 March 2020 the lifetime limit was £10 million.  
 (5) For qualifying disposals made before 30 October 2024 the lifetime limit was £10 million.

# CTA EXAMINATIONS

2026

## TAX TABLES



### Lease percentage table

Years	Percentage	Years	Percentage	Years	Percentage	Years	Percentage
50+	100.000	37	93.497	24	79.622	11	50.038
49	99.657	36	92.761	23	78.055	10	46.695
48	99.289	35	91.981	22	76.399	9	43.154
47	98.902	34	91.156	21	74.635	8	39.399
46	98.490	33	90.280	20	72.770	7	35.414
45	98.059	32	89.354	19	70.791	6	31.195
44	97.595	31	88.371	18	68.697	5	26.722
43	97.107	30	87.330	17	66.470	4	21.983
42	96.593	29	86.226	16	64.116	3	16.959
41	96.041	28	85.053	15	61.617	2	11.629
40	95.457	27	83.816	14	58.971	1	5.983
39	94.842	26	82.496	13	56.167	0	0.000
38	94.189	25	81.100	12	53.191		

### Retail Prices Index

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
<b>1982</b>	—	—	79.44	81.04	81.62	81.85	81.88	81.90	81.85	82.26	82.66	82.51
<b>1983</b>	82.61	82.97	83.12	84.28	84.64	84.84	85.30	85.68	86.06	86.36	86.67	86.89
<b>1984</b>	86.84	87.20	87.48	88.64	88.97	89.20	89.10	89.94	90.11	90.67	90.95	90.87
<b>1985</b>	91.20	91.94	92.80	94.78	95.21	95.41	95.23	95.49	95.44	95.59	95.92	96.05
<b>1986</b>	96.25	96.60	96.73	97.67	97.85	97.79	97.52	97.82	98.30	98.45	99.29	99.62
<b>1987</b>	100.0	100.4	100.6	101.8	101.9	101.9	101.8	102.1	102.4	102.9	103.4	103.3
<b>1988</b>	103.3	103.7	104.1	105.8	106.2	106.6	106.7	107.9	108.4	109.5	110.0	110.3
<b>1989</b>	111.0	111.8	112.3	114.3	115.0	115.4	115.5	115.8	116.6	117.5	118.5	118.8
<b>1990</b>	119.5	120.2	121.4	125.1	126.2	126.7	126.8	128.1	129.3	130.3	130.0	129.9
<b>1991</b>	130.2	130.9	131.4	133.1	133.5	134.1	133.8	134.1	134.6	135.1	135.6	135.7
<b>1992</b>	135.6	136.3	136.7	138.8	139.3	139.3	138.8	138.9	139.4	139.9	139.7	139.2
<b>1993</b>	137.9	138.8	139.3	140.6	141.1	141.0	140.7	141.3	141.9	141.8	141.6	141.9
<b>1994</b>	141.3	142.1	142.5	144.2	144.7	144.7	144.0	144.7	145.0	145.2	145.3	146.0
<b>1995</b>	146.0	146.9	147.5	149.0	149.6	149.8	149.1	149.9	150.6	149.8	149.8	150.7
<b>1996</b>	150.2	150.9	151.5	152.6	152.9	153.0	152.4	153.1	153.8	153.8	153.9	154.4
<b>1997</b>	154.4	155.0	155.4	156.3	156.9	157.5	157.5	158.5	159.3	159.5	159.6	160.0
<b>1998</b>	159.5	160.3	160.8	162.6	163.5	163.4	163.0	163.7	164.4	164.5	164.4	164.4
<b>1999</b>	163.4	163.7	164.1	165.2	165.6	165.6	165.1	165.5	166.2	166.5	166.7	167.3
<b>2000</b>	166.6	167.5	168.4	170.1	170.7	171.1	170.5	170.5	171.7	171.6	172.1	172.2
<b>2001</b>	171.1	172.0	172.2	173.1	174.2	174.4	173.3	174.0	174.6	174.3	173.6	173.4
<b>2002</b>	173.3	173.8	174.5	175.7	176.2	176.2	175.9	176.4	177.6	177.9	178.2	178.5
<b>2003</b>	178.4	179.3	179.9	181.2	181.5	181.3	181.3	181.6	182.5	182.6	182.7	183.5
<b>2004</b>	183.1	183.8	184.6	185.7	186.5	186.8	186.8	187.4	188.1	188.6	189.0	189.9
<b>2005</b>	188.9	189.6	190.5	191.6	192.0	192.2	192.2	192.6	193.1	193.3	193.6	194.1
<b>2006</b>	193.4	194.2	195.0	196.5	197.7	198.5	198.5	199.2	200.1	200.4	201.1	202.7
<b>2007</b>	201.6	203.1	204.4	205.4	206.2	207.3	206.1	207.3	208.0	208.9	209.7	210.9
<b>2008</b>	209.8	211.4	212.1	214.0	215.1	216.8	216.5	217.2	218.4	217.7	216.0	212.9
<b>2009</b>	210.1	211.4	211.3	211.5	212.8	213.4	213.4	214.4	215.3	216.0	216.6	218.0
<b>2010</b>	217.9	219.2	220.7	222.8	223.6	224.1	223.6	224.5	225.3	225.8	226.8	228.4
<b>2011</b>	229.0	231.3	232.5	234.4	235.2	235.2	234.7	236.1	237.9	238.0	238.5	239.4
<b>2012</b>	238.0	239.9	240.8	242.5	242.4	241.8	242.1	243.0	244.2	245.6	245.6	246.8
<b>2013</b>	245.8	247.6	248.7	249.5	250.0	249.7	249.7	251.0	251.9	251.9	252.1	253.4
<b>2014</b>	252.6	254.2	254.8	255.7	255.9	256.3	256.0	257.0	257.6	257.7	257.1	257.5
<b>2015</b>	255.4	256.7	257.1	258.0	258.5	258.9	258.6	259.8	259.6	259.5	259.8	260.6
<b>2016</b>	258.8	260.0	261.1	261.4	262.1	263.1	263.4	264.4	264.9	264.8	265.5	267.1
<b>2017</b>	265.5	268.4	269.3	270.6	271.7	272.3	272.9	274.7	275.1	275.3	275.8	278.1

# CTA EXAMINATIONS

2026

## TAX TABLES



### CORPORATION TAX

Financial year	2025	2024
Main rate	25%	25%
Standard small profits rate	19%	19%
Augmented profit limit for standard small profits rate	£50,000	£50,000
Augmented profit limit for marginal relief	£250,000	£250,000
Standard marginal relief fraction	3/200	3/200
Marginal rate	26.5%	26.5%
Patent rate	10%	10%

### EU definition of small and medium sized enterprises

	Small <sup>(2)</sup>	Medium <sup>(2)</sup>	Extended definition for R&D expenditure
Employees <sup>(1)</sup>	< 50	< 250	<500
Turnover <sup>(1)</sup>	≤ €10m	≤ €50m	≤ €100m
Balance sheet assets <sup>(1)</sup>	≤ €10m	≤ €43m	≤ €86m

- Notes:** (1) Must meet employees criteria and either turnover or balance sheet assets criteria.  
(2) Thresholds apply for transfer pricing and distributions received by small companies.

### Research and development expenditure

Financial year	2025 and 2024
RDEC	20%
Enhanced R&D Intensive Support (ERIS) - total relief for loss making R&D intensive SMEs	186%
R&D tax credit for R&D intensive SME losses	14.5%

### VALUE ADDED TAX

	Standard rate	VAT fraction
Rate	20%	1/6
<b>Limits</b>	<b>2025/26</b>	<b>2024/25</b>
	£	£
Annual registration limit	90,000	90,000
De-registration limit	88,000	88,000
<b>Thresholds</b>	<b>Cash accounting</b>	<b>Annual accounting</b>
	£	£
Turnover threshold to join scheme	1,350,000	1,350,000
Turnover threshold to leave scheme	1,600,000	1,600,000

### ADVISORY FUEL RATES (from 1 March 2025)

Engine size	Petrol	LPG	Engine size	Diesel
1400cc or less	12p	11p	1600cc or less	12p
1401cc to 2000cc	15p	13p	1601cc to 2000cc	13p
Over 2000cc	23p	21p	Over 2000cc	17p
<b>Electricity rate</b>	7p			

# CTA EXAMINATIONS

2026

## TAX TABLES



### OTHER INDIRECT TAXES

	2025/26	2024/25
<b>Insurance premium tax<sup>(1)</sup></b>		
Standard rate	12%	12%
Higher rate	20%	20%

**Notes:** (1) Premium is tax inclusive ( $\frac{3}{28}$  for 12% rate and  $\frac{1}{6}$  for 20% rate).

### Landfill Tax (pro rated for part tonnes)

Standard rate	£126.15 per tonne	£103.70 per tonne
Lower rate	£4.05 per tonne	£3.30 per tonne

<b>Landfill Communities Fund (LCF)<sup>(2)</sup></b>	5.3% x landfill tax liability	5.3% x landfill tax liability
--	-------------------------------	-------------------------------

**Notes:** (2) Relief for 90% of qualifying contributions

<b>Aggregates Levy</b> (pro rated for part tonnes)	£2.08 per tonne	£2.03 per tonne
--	-----------------	-----------------

<b>Plastic Packaging Tax (PPT)</b> (pro rated for part tonnes)	£223.69 per tonne	£217.85 per tonne
--	-------------------	-------------------

### Climate Change Levy (CCL)<sup>(3)</sup>

	2025/26	2024/25
Electricity	0.775p per kwh	0.775p per kwh
Natural gas	0.775p per kwh	0.775p per kwh
Liquified petroleum gas (LPG)	2.175p per kg	2.175p per kg
Any other taxable commodity	6.064p per kg	6.064p per kg

### Carbon Price Support (CPS) rates

Natural gas	0.331 per kwh	0.331 per kwh
LPG	5.28p per kg	5.28p per kg
Coal & other taxable solid fossil fuels	£1.5479 per GJ on GCV	£1.5479 per GJ on GCV

### Tobacco products duty

	From 6pm 30.10.2024	Before 6pm 30.10.2024
Cigarettes	16.5% x retail price + £334.58 per thousand cigarettes (or £446.67 per thousand cigarettes <sup>(4)</sup> )	16.5% x retail price + £316.70 per thousand cigarettes (or £422.80 per thousand cigarettes <sup>(4)</sup> )
Cigars	£417.33 per kg	£395.03 per kg
Hand-rolling tobacco	£476.83 per kg	£412.32 per kg
Other smoking/chewing tobacco	£183.49 per kg	£173.68 per kg
Tobacco for heating	£343.91 per kg	£325.53 per kg

**Notes:** (3) For holders of a Climate Change agreement (CCA), the rate charged is a percentage of the main rate given in the table. For 2025/26 (2024/25 in brackets) for electricity the rate is 8% (8%), for gas it is 11% (11%), for LPG it is 23% (23%) and 11% (11%) for any other taxable commodity

(4) The £446.67/£422.80 per thousand cigarettes is a minimum excise duty (if higher than the first calculation)

# CTA EXAMINATIONS

2026

## TAX TABLES



### Alcohol Duty<sup>(1)</sup>

From 1 February 2025

	Duty in £ for each litre of pure alcohol in the product		Duty in £ for each litre of pure alcohol in the product
<b>Beer (ABV)</b>		<b>Spirits/Spirit based products (ABV)</b>	
0 to 1.2%	0.00	0 to 1.2%	0.00
1.3% to 3.4%	9.61	1.3% to 3.4%	9.61
3.5% to 8.4%	21.78	3.5% to 8.4%	25.67
8.5% to 22%	29.54	8.5% to 22%	29.54
Stronger than 22%	32.79	Stronger than 22%	32.79
<b>Cider (not sparkling) (ABV)</b>		<b>Wine/sparkling wine (ABV)</b>	
0 to 1.2%	0.00	0 to 1.2%	0.00
1.3% to 3.4%	9.61	1.3% to 3.4%	9.61
3.5% to 8.4%	10.02	3.5% to 8.4%	25.67
8.5% to 22%	29.54	8.5% to 22%	29.54
Stronger than 22%	32.79	Stronger than 22%	32.79
<b>Sparkling cider (ABV)</b>		<b>Other fermented products like fruit ciders (ABV)</b>	
0 to 1.2%	0.00	0 to 1.2%	0.00
1.3% to 3.4%	9.61	1.3% to 3.4%	9.61
3.5% to 5.5%	10.02	3.5% to 8.4%	25.67
5.6% to 8.4%	25.67	8.5% to 22%	29.54
8.5% to 22%	29.54	Stronger than 22%	32.79
Stronger than 22%	32.79		

**Notes:** (1) There are reduced rates for qualifying draught products

### ANNUAL TAX ON ENVELOPED DWELLINGS (ATED)

Residential property value	From 1.4.25	From 1.4.24
>£0.5m - ≤ 1m	£4,450	£4,400
> £1m - ≤ 2m	£9,150	£9,000
> £2m – ≤ 5m	£31,050	£30,550
> £5m – ≤ 10m	£72,700	£71,500
> £10m – ≤ 20m	£145,950	£143,550
> £20m	£292,350	£287,500

**CTA EXAMINATIONS**  
**2026**  
**TAX TABLES**



**INHERITANCE TAX**

Death rate	40% <sup>(1)</sup>	Lifetime rate	20%
------------	--------------------	---------------	-----

**Note:** (1) 36% rate if 10% or more of the deceased person's net chargeable estate is left to charity.

**Nil rate bands**

6 April 1996 – 5 April 1997	£200,000	6 April 2003 – 5 April 2004	£255,000
6 April 1997 – 5 April 1998	£215,000	6 April 2004 – 5 April 2005	£263,000
6 April 1998 – 5 April 1999	£223,000	6 April 2005 – 5 April 2006	£275,000
6 April 1999 – 5 April 2000	£231,000	6 April 2006 – 5 April 2007	£285,000
6 April 2000 – 5 April 2001	£234,000	6 April 2007 – 5 April 2008	£300,000
6 April 2001 – 5 April 2002	£242,000	6 April 2008 – 5 April 2009	£312,000
6 April 2002 – 5 April 2003	£250,000	6 April 2009 – 5 April 2030	£325,000

**Residence nil rate bands<sup>(2)</sup>**

6 April 2017 – 5 April 2018	£100,000	6 April 2019 – 5 April 2020	£150,000
6 April 2018 – 5 April 2019	£125,000	6 April 2020 – 5 April 2030	£175,000

**Note:** (2) An additional nil rate band is available where a main residence is passed on death to a direct descendant. Tapered withdrawal for estates > £2million.

**Taper relief**

Death within 3 years of gift	Nil%
Between 3 and 4 years	20%
Between 4 and 5 years	40%
Between 5 and 6 years	60%
Between 6 and 7 years	80%

**Quick Succession relief**

Period between transfers less than one year	100%
Between 1 and 2 years	80%
Between 2 and 3 years	60%
Between 3 and 4 years	40%
Between 4 and 5 years	20%

**Lifetime exemptions**

Annual exemption	£3,000
Small gifts	£250
Wedding gifts	
Child	£5,000
Grandchild or remoter issue or other party to marriage	£2,500
Other	£1,000

**STAMP DUTY/SDRT**

<b>Stamp duty<sup>(3)</sup></b>	- On shares transferred by physical stock transfer form	0.5%
<b>Stamp duty reserve tax (SDRT)<sup>(4)</sup></b>	- On agreements to transfer shares <sup>(2)</sup>	0.5%
	- On shares transferred to depositary receipt schemes	1.5%

**Notes:** (3) Does not apply to UK securities traded on a recognised growth market (eg AIM).

(4) Does not apply to units in UK unit trust schemes or shares in UK OEICS bought from fund managers.

**STAMP DUTY LAND TAX (SDLT)**

Qualifying purchases in a Freeport receive full SDLT relief

# CTA EXAMINATIONS

2026

## TAX TABLES



### Stamp Duty Land Tax on purchase price / lease premium / transfer value – England & NI

From 1 April 2025

Basic Rate % <sup>(1)(2)(3)(4)</sup>	Residential <sup>(1)(2)(3)(4)</sup>	Rate %	Non-Residential
0	£0 - £125,000	0	£0 - £150,000
2	£125,001-£250,000	2	£150,001 - £250,000
5	£250,001 - £925,000	5	£250,001 +
10	£925,001 - £1,500,000		
12	£1,500,001+		

- Notes:** (1) The basic rates are increased by 5% (the 'higher rates') where the purchase is of an additional residential property for individuals. Companies and trusts pay the additional 5% on all purchases of residential properties, subject to Note 2 below.
- (2) Companies (and certain other entities) pay 17% on purchases of residential property valued > £500,000 (subject to exceptions).
- (3) First-time buyers purchasing a single dwelling as their only/main residence may benefit from a reduced rate. (This includes qualifying shared ownership properties.) SDLT will be 0% on the first £300,000, for a property bought for a maximum £500,000 (5% on the excess up to £500,000). No relief is available for a property over £500,000.
- (4) Non-resident individuals and companies will pay an additional 2% surcharge for purchases of residential property. This is in addition to the basic rate, the higher rate (where applicable, in Note 1), and the 17% rate (where applicable, in Note 2).

### New leases – Stamp Duty Land Tax on lease rentals – England & NI

Rate (%)	Net present value of rent	
	Residential	Non-residential
0	Up to £125,000	Up to £150,000
1	Excess over £125,000	£150,001-£5m
2	N/A	Over £5m

### Land and Buildings Transaction Tax (LBTT) on purchase price – Scotland

2025/26

Basic Rate % <sup>(5)(6)(7)</sup>	Residential	Rate % <sup>(5)</sup>	Non-Residential
0	up to £145,000	0	£0 - £150,000
2	£145,001 - £250,000	1	£150,001 - £250,000
5	£250,001 - £325,000	5	£250,001 +
10	£325,001 - £750,000		
12	£750,001 +		

- Notes:** (5) Rates are charged on the portion of consideration that falls in each band. The same tax is payable for a premium granted for a land transaction, except for residential leases which are generally exempt. Special rules apply to a premium for non-residential property where the rent exceeds £1,000 a year.
- (6) The 'Additional Dwelling Supplement' (ADS) of 8% of the relevant consideration applies broadly to purchases of an additional dwelling by individuals & trusts (over which the beneficiary has substantial rights) & to purchases of a dwelling by certain businesses, companies & other trusts.
- (7) There is a relief for first-time buyers where a 0% rate is applied to the first £175,000 of the purchase consideration.

### New leases – Land and Buildings Transaction Tax (LBTT) on lease rentals - Scotland

Rate (%)	Net present value of rent <sup>(8)</sup>	
	Non-residential	
Zero	Up to £150,000	
1%	£150,001 to £2,000,000	
2%	£2,000,001+	

- Note:** (8) Residential leases are generally exempt

QUESTIONS

- Polish Home Ltd operates a chain of restaurants in North London. The company has estimated taxable profits of £700,000 before capital allowance claims for the year to 31 March 2026.

During the year Polish Home Ltd acquired a dilapidated shop, completely gutted and refurbished it before opening it as a new restaurant. The company's surveyor has prepared a summary of costs as follows:

<u>Works</u>	£
Removal of old wooden floor, installation of new floor and fixed plasterboard walls	20,000
Toilet stalls and washbasins	4,000
Mains electrical systems	15,000
Hot and cold water systems	10,000
Fixed ceiling and wall lighting	4,500
Built-in air conditioning system	5,000
Fixed seating	4,000
Loose rugs	2,000
Kitchen equipment	5,500
Tables and chairs	3,500
Cash tills and computer hardware	2,000
Preliminaries	<u>5,000</u>
Total	<u>80,500</u>

The surveyor estimates that the works have an expected life of ten years except for the tables, chairs, cash tills and computer hardware, all of which have a five-year life.

The tables and chairs were assorted items bought second-hand to add to the ambience of the restaurant.

The company has already spent sufficient on plant and machinery at its other restaurants to use its Annual Investment Allowance.

**Requirement:**

**Draft appropriate notes to explain the plant and machinery allowances available for the above expenditure. A summary of the basic principles may be included but cover only what is relevant. Calculations are NOT required.** (15)

2. The Underground group of companies consists of a non-trading holding company, Circle Ltd, and the following wholly owned subsidiaries: District Ltd, Jubilee Ltd, Northern Ltd, Victoria Ltd, Central Ltd, Metropolitan Ltd and WCL Ltd. All of the subsidiaries have been trading for many years except WCL Ltd which is dormant and Metropolitan Ltd (which is a company with investment business and which does not carry on any trade). All companies make up their accounts to 31 December each year.

On 1 November 2022, Jubilee Ltd sold a freehold property for £55,000 to District Ltd. The market value of the property at the time of sale was £150,000 and its base cost was £80,000.

On 1 November 2022, Jubilee Ltd purchased a registered trademark for £50,000 from an unconnected third party. The cost of the trademark is being amortised on a straight line basis over 20 years. The amortisation is calculated on a monthly basis from the date of purchase. On 1 November 2023, Jubilee Ltd sold the trademark to Metropolitan Ltd for £55,000. The estimated market value of the trademark at the time of sale was £60,000. Jubilee Ltd is considering purchasing further trademarks in the future.

On 1 November 2026, Circle Ltd sold its entire interests in District Ltd and Metropolitan Ltd to an unconnected third party for £500,000. The base cost of the shares in District Ltd was £10,000.

Circle Ltd purchased WCL Ltd in January 2013. At the time the company was trading and had realised capital losses brought forward of £100,000. The company's trade was completely transferred to Northern Ltd in June 2013 and WCL Ltd then became dormant. After this time Northern Ltd has operated this trade and no other. In October 2013, Northern Ltd acquired a building for use in its trade for £80,000 from an unconnected third party. The building was sold for £240,000 in July 2026.

In June 2026, Victoria Ltd, which has been operating its trade since 2001, transferred the entire trade plus all of its equipment to Central Ltd for a consideration of £30,000. In addition, Central Ltd has agreed to pay £5,000 to Victoria Ltd's creditors for unpaid utility bills. No other assets or liabilities were transferred. After the transfer, Victoria Ltd plans to commence a new, unrelated trade. Trading losses brought forward at the time of transfer were £75,000, all incurred before 1 April 2017, and the balance on the capital allowance general pool was £15,000.

Victoria Ltd's balance sheet at the date of transfer is summarised as follows:

	£
Freehold property	70,000
Equipment	10,000
Trade debtors	<u>45,000</u>
	125,000
Trade creditors	(115,000)
Bank overdraft	<u>(65,000)</u>
	<u>(55,000)</u>
Share capital	60,000
Deficit on reserves	<u>(115,000)</u>
	<u>(55,000)</u>

**Requirement:**

**Explain the Corporation Tax treatment of the above transactions and provide supporting calculations where appropriate. You are NOT required to refer to indexation in your answers.** (20)

3. Lentil plc is a fast-growing manufacturer of speciality bakery products, which is rapidly expanding overseas. The company has decided to start a new operation in Thousisland, to commence in late 2026.

There will be significant start-up costs in Thousisland, including advertising and marketing costs, and the company expects to make losses in the first two years. However, the forecasts show a break-even position for year three and then profits for year four and onwards.

It is likely that Lentil plc will continue manufacturing the products in the UK in the first two to three years before setting up a new manufacturing plant in Thousisland, to be owned by the Thousisland entity. The manufacturing plant in Thousisland would only supply the Thousisland market. In addition, Lentil plc will provide head office services to the Thousisland entity on an on-going basis.

The corporate tax rate in Thousisland is marginally lower than the main rate in the UK and Thousisland is not regarded as a tax haven.

Lentil plc is a large company for UK Corporation Tax purposes.

Assume that the main rate of Corporation Tax applies to all UK taxable profits.

**Requirement:**

**Explain the advantages and disadvantages of setting up the new operation as a permanent establishment versus a subsidiary and recommend the preferred structure from a UK tax perspective. You are not required to consider the tax implications of financing the overseas operations.** (20)

4. Midnight plc is a UK headquartered manufacturing group. The Midnight group has a December year end, operates throughout Europe and employs over 250 people. Twilight Ltd is a wholly owned UK subsidiary of Midnight plc.

Twilight Ltd manufactures electrical components from raw materials bought from third parties. The components are used to create finished products, which are then sold to third parties.

On 1 January 2024, the Belgian branch of Twilight Ltd was incorporated into Dusk BVBA, a wholly owned subsidiary. Dusk BVBA is tax resident in Belgium and carries on the same trade as Twilight Ltd. All of Dusk BVBA's sales are to third parties in Belgium.

From 1 January 2024, Twilight Ltd began selling some of its manufactured electrical components to Dusk BVBA for Dusk BVBA to use in its own manufacturing processes.

On 1 March 2026, HMRC opened an enquiry into Twilight Ltd's Company Tax return for the year ended 31 December 2024 and have asked to see the intercompany sales agreement between Twilight Ltd and Dusk BVBA. The agreement reveals that Twilight Ltd has been selling electrical components to Dusk BVBA without any mark-up on cost.

HMRC have also asserted that Twilight Ltd is habitually acting on behalf of Dusk BVBA. Twilight Ltd has signed some contracts on Dusk BVBA's behalf in January 2024 before Dusk BVBA had set up its own authorisations.

**Requirement:**

**Assuming it is April 2026, explain the Corporation Tax implications of the matters raised by HMRC and the steps the group should take to address the issues.**

**You should assume that the double tax treaty between the UK and Belgium is identical to the OECD Model Treaty and that the tax rates and rules applying in FY 2025 also applied in previous years.**

(15)

5. The Swift group has 10 UK tax resident, wholly owned subsidiaries and consolidated group turnover of £100 million per annum. The UK corporation tax compliance has been neglected. The group's UK tax affairs need to be brought up to date as quickly as possible.

In relation to the UK companies:

- 1) Corporation Tax computations and returns for the year ended 31 December 2022 were submitted on time. However, the return for one of the UK trading companies, Wren Ltd, erroneously showed its trading income to be £60,000 instead of £600,000.
- 2) Corporation Tax computations and returns for the year ended 31 December 2023 have not yet been submitted. The UK group was in an overall loss making position and so no Corporation Tax payments have been made.
- 3) Corporation Tax computations and returns for the years ended 31 December 2024 and 31 December 2025 have not yet been submitted. Timely Corporation Tax payments based upon the tax audit provision calculation for the purpose of preparing the group's financial accounts were made under Corporation Tax Self-Assessment for both years. Recently prepared draft Corporation Tax computations show that some of the individual UK companies have underpaid Corporation Tax for the year ended 31 December 2024 but the group is still in an overpayment position overall.
- 4) On 1 January 2025, one of the UK companies, Bluebird Ltd, entered into a royalty agreement to pay for the use of certain patent rights held by Robin B.V., an associated company resident in The Netherlands. There is no documentation that explains how the price was determined nor any evidence that withholding tax has been applied on any payments made.
- 5) Following a group reorganisation in August 2025, the Finance Director thinks that one of the UK companies may fall within the charge to the diverted profits tax.

**Requirement:**

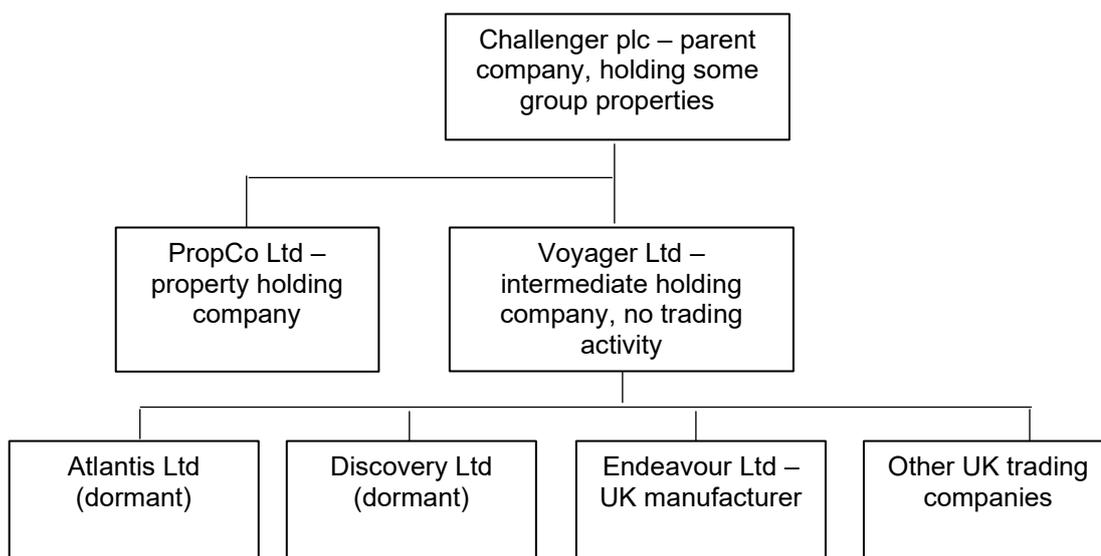
**Prepare notes to explain the tax and penalty implications of the above information.**

(20)

**Assume that you are writing in July 2026.**

6. The Challenger group operates solely in the UK and is primarily a manufacturing group, which has grown significantly over the last ten years, mainly as a result of corporate acquisitions. However, the group has now decided to focus on certain core activities and a programme of divestment is planned to occur during the year. The first proposed divestment is of the trading activities carried on by Endeavour Ltd.

The group structure is set out below, including the activities of each subsidiary. All subsidiaries are wholly owned.



Atlantis Ltd was acquired in 2016 and Discovery Ltd was acquired in 2020. Each company continued to trade until the 31 December following acquisition. The property of each company used for trade purposes was then transferred at net book value to PropCo Ltd, while the trade and remaining assets were transferred to Endeavour Ltd, again at net book value.

Since any purchaser of Endeavour Ltd would want to acquire the properties with the trades, it is proposed that the shares of PropCo Ltd, as well as the shares of Endeavour Ltd, will be sold. Details of the original acquisitions of these companies and the anticipated sale proceeds are set out below.

	<u>Acquisition date</u>	<u>Note</u>	<u>Acquisition cost</u> £million	<u>Anticipated sale proceeds</u> £million
Endeavour Ltd	1 January 2001	Acquired from a third party	20	60
PropCo Ltd	1 January 2010	Acquired from a third party. Propco Ltd's only asset at that time was a property the group wished to purchase.	15	30

As well as operating in the three premises held by PropCo Ltd (the one held on acquisition plus the two transferred by Atlantis Ltd and Discovery Ltd), Endeavour Ltd also operates from properties in Manchester and York. Challenger plc holds leases on these properties, which will be made available by Challenger plc to a new purchaser to enable the business to continue in its current form in the immediate future. Details of these properties are set out below.

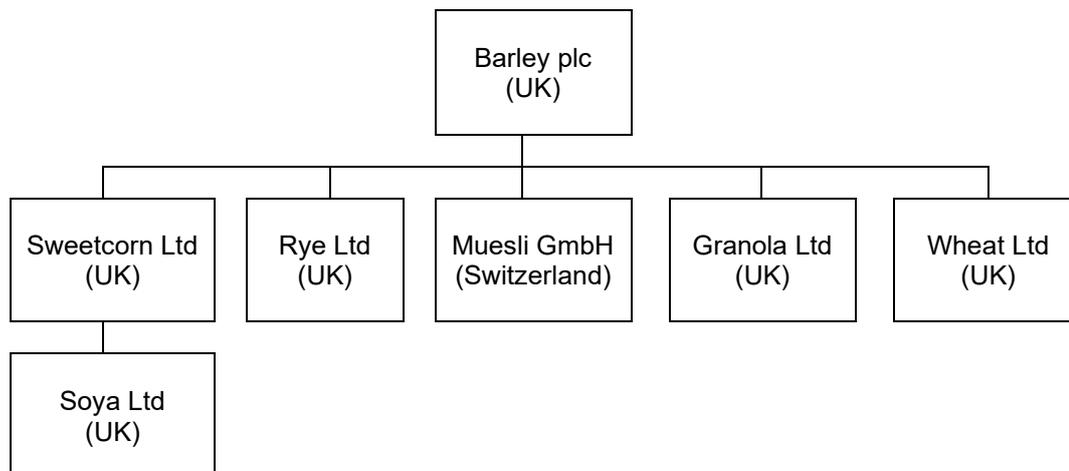
	<u>Interest held by Challenger plc</u>	<u>Lease period if applicable</u>	<u>Lease premium paid by Challenger plc</u>	<u>Proposal</u>
Manchester property	Leasehold	70 years from 1 March 2016	£1 million	10 year sub-lease to be granted by Challenger plc for £250,000
York property	Leasehold	15 years from 1 January 2022	£500,000	To be assigned by Challenger plc for £300,000

All transactions will occur on 1 June 2026.

**Requirement:**

- 1) **Explain the proposed disposals of the shares in Endeavour Ltd and PropCo Ltd.** (12)
  - 2) **Explain the tax treatment of the Manchester and York property transactions to be carried out by Challenger plc including calculations.** (8)
- Total (20)

7. Barley plc is the holding company of a large multinational group and is listed on the London Stock Exchange. A relevant extract from the group structure, together with the country of incorporation and tax residency for each company, is as follows:



Barley plc holds a 5% shareholding in Wheat Ltd. All other companies in the group are wholly owned subsidiaries. All companies are trading, except for Muesli GmbH and Barley plc; the non-trading activities of these companies do not constitute a substantial amount of non-trading activity for the group as a whole.

Barley plc is in the process of undergoing a reorganisation for genuine commercial reasons, with the following transactions planned for November 2026:

- 1) Barley plc intends to accept an offer from a third party to purchase the shares in Sweetcorn Ltd for £35 million, having acquired the shares for £15 million in June 2005. However, the purchase price is dependent on the following transactions being completed before the sale takes place:
  - a) Firstly, Sweetcorn Ltd does not own any property; it leases its business premises from Granola Ltd. The business premises will therefore be transferred to Sweetcorn Ltd at their market value of £11 million. The base cost of the business premises in Granola Ltd is £7.5 million. There will be no joint election under s.198 CAA 2001 in respect of fixtures.
  - b) Secondly, as the purchaser does not wish to acquire Soya Ltd, the shares in Soya Ltd will be transferred to Barley plc at their market value of £13 million. Sweetcorn Ltd acquired the shares for £8 million in December 2017.
- 2) Barley plc has accepted an offer from Clementine Ltd, a third party, to acquire 40% of the shareholding in Rye Ltd. As consideration, Barley plc will receive shares in Clementine Ltd worth £7 million. Barley plc paid £8 million for the entire shareholding of Rye Ltd in December 2025.
- 3) Barley plc has accepted an offer from a third party resident in Switzerland to acquire its shareholding in Muesli GmbH. Muesli GmbH was incorporated by Barley plc in May 2024 with share capital of £500,000, and has been carrying out very technologically advanced research and development with the eventual aim of developing a marketable product. It has not yet commenced trading activities. The agreed purchase price is £6 million payable upfront, plus a further £2 million if Muesli GmbH completes development of a marketable product and commences trading within five years of the sale.

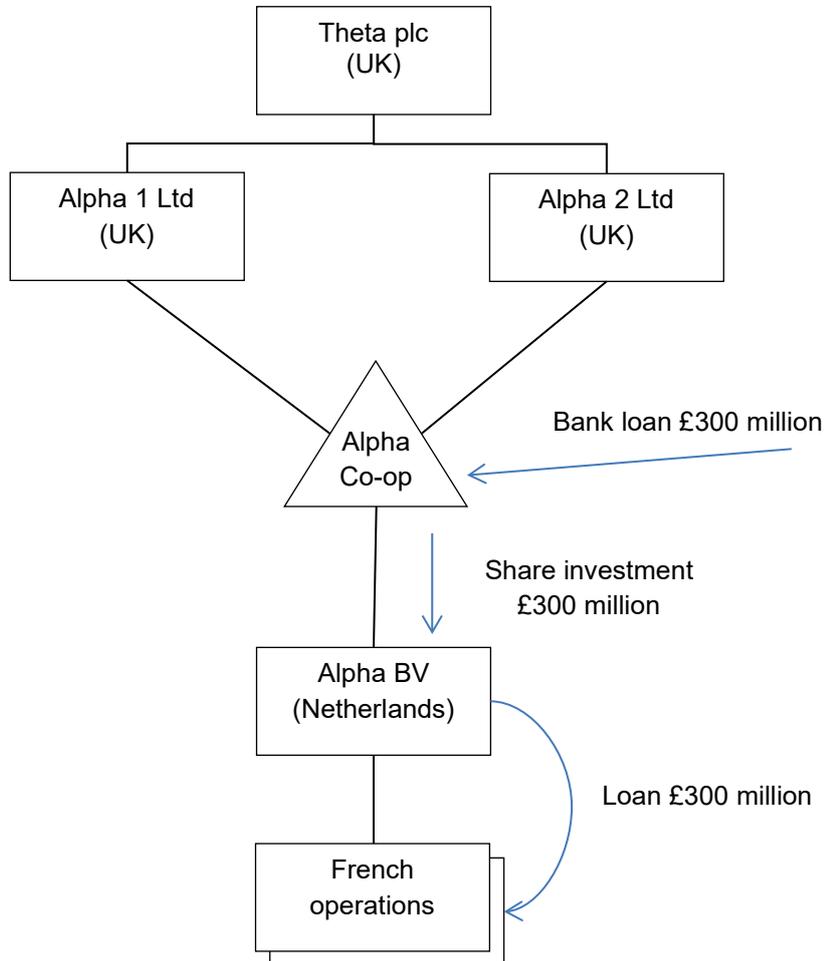
- 4) Barley plc has also accepted an offer from a third party to acquire its 5% shareholding in Wheat Ltd, which it acquired for £6 million in October 2017. The purchase price is £9 million payable upfront, and Barley plc will be entitled to a further payout on a future flotation of Wheat Ltd, the payout being determined by the share price on flotation.

**Requirement:**

**Explain the tax implications of the proposed transactions on the Barley group. You do NOT need to consider indexation, VAT or payment dates.** (20)

8. Theta plc are looking to resolve numerous issues with HMRC. One particular issue is the group's 'Dutch Co-op' financing structure. This was a tax planning arrangement implemented by the group.

The abbreviated structure of the Theta plc group, together with the country of incorporation and tax residence of each company, is as follows:



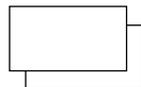
Key:



A partnership for UK tax purposes



A company for UK tax purposes



Multiple companies for UK tax purposes

The following information has been provided:

- 1) Alpha Co-op is a Dutch Cooperative. The group has obtained clearance from HMRC that it should be regarded as a partnership for UK tax purposes. The group has also obtained a ruling from the Dutch tax authorities that it should be regarded as a company for Dutch tax purposes.
- 2) Alpha 1 Ltd and Alpha 2 Ltd are investment companies. Their only activity is being members of Alpha Co-op. Each member is entitled to half of the profits of Alpha Co-op.
- 3) On 1 April 2025, Alpha Co-op borrowed £300 million from a third-party bank at an interest rate of 8%. It invested the funds in Alpha BV in exchange for the issue of ordinary shares. The bank loan is guaranteed by Theta plc.
- 4) Alpha BV is the holding company for the group's French operations. It used the £300 million share investment from Alpha Co-op to lend £300 million to its French subsidiaries. The terms of the loan mirror those of the Alpha Co-op bank loan.
- 5) Each year Alpha BV voluntarily pays dividends on the ordinary shares sufficient to fund the interest payments on the Alpha Co-op bank loan.
- 6) Alpha BV pays minimal corporate tax in the Netherlands on the interest income from the £300 million loan. This is because it can obtain tax relief for the interest paid by Alpha Co-op under the Dutch 'fiscal unity' rules.

**Requirement:**

- 1) **Explain the UK Corporation Tax treatment of Alpha 1 Ltd and Alpha 2 Ltd (ignoring the potential application of any anti-avoidance rules and the corporate interest restriction regime).** (6)
  - 2) **Explain the UK Controlled Foreign Companies rules in respect of Alpha Co-op and Alpha BV.** (8)
  - 3) **Set out potential challenges that HMRC may raise in respect of the structure and potential defences against the challenges.** (6)
- Total (20)

9. The UniComms group is a global telecommunications group specialising in the creation of low-cost cellular networks in emerging markets.

UniComms plc, the UK incorporated and tax resident parent company of the group, is listed on the FTSE 250 index. UniComms plc incorporated a wholly owned UK subsidiary, UZamm Ltd. UZamm Ltd registered a branch in Zamunda on 30 November 2024 which commenced trading on 1 January 2025. Its activities are limited to the construction and operation of a cellular network in Zamunda.

UZamm Ltd needs to properly manage exposures arising from an ongoing tax audit in Zamunda. The Zamunda Revenue Authority have raised the following queries:

- 1) Please explain why UZamm Ltd is not tax resident in Zamunda.
- 2) We note that a number of employees of UniComms plc were frequently in Zamunda during the period 1 January 2025 to 31 December 2025. During this period, UniComms plc negotiated a contract with the Government of Zamunda to design and distribute low cost smart phones. Please explain why UniComms plc does not have a permanent establishment in Zamunda.
- 3) In accordance with the Zamundan Income Tax Act 2013, withholding tax should have been applied at a rate of 20% on £50 million of royalties and management and consultancy fees paid to UniComms plc in the period 1 January 2025 to 31 December 2025. Please remit £10 million of withholding tax immediately.

The following additional information is available:

- 1) UZamm Ltd has both a UK resident director and a Zamundan resident director. All Board meetings to date have been convened and attended in person by both directors in the UK.
- 2) The Zamundan Income Tax Act 2013 states that a foreign incorporated company is tax resident in Zamunda where it undertakes the majority of its trading operations in the country.
- 3) The employees of UniComms plc physically present in Zamunda during the period 1 January 2025 to 31 December 2025 were engineers responsible for designing telephone masts for UZamm Ltd in its network. UniComms plc charged UZamm Ltd a £30 million fee for this service under the Intra-Group Services Agreement. The fee was calculated on an arm's length basis in accordance with the group's transfer pricing policy.
- 4) The Executive Sales Director of UniComms plc negotiated the contract for the design and distribution of smart phones in the UK and Zamunda. The contract was executed in the UK.
- 5) UZamm Ltd paid £20 million to UniComms plc in order to utilise patented technology relating to design of the telephone masts.

**Requirement:**

**Explain how the provisions of the UK / Zamunda Double Tax Treaty could have an impact on the response to the queries received from the Zamunda Revenue Authority.** (20)

Relevant extracts from the UK-Zamunda Double Tax Treaty, which is based upon the OECD Model Treaty, are provided on the next page.

Extracts from UK-Zamunda Double Tax TreatyArticle 4 (Residence)

- 3) Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, the competent authorities of the Contracting States shall endeavour to determine by mutual agreement the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention.

Article 5 (Permanent Establishment)

- 1) For the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the business of an enterprise is wholly or partly carried on.
- 2) The term 'permanent establishment' includes especially:
  - a) a place of management;
  - b) a branch;
  - c) an office;
  - d) a factory;
  - e) a workshop; and
  - f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.
- 5) Notwithstanding the provisions of paragraphs 1 and 2, where a person is acting in a Contracting State on behalf of an enterprise and in so doing habitually concludes contracts or habitually plays the principal role in leading to the conclusion of contracts [in the name of the enterprise without material modification by the enterprise], the enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise...

Article 7 (Business Profits)

- 1) Profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits that are attributable to the permanent establishment in accordance with the provisions of paragraph two may be taxed in that other State.

Article 12 (Royalties)

- 1) Royalties arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.
- 2) However, such royalties may also be taxed in the Contracting State in which they arise, and according to the laws of that State, but if the beneficial owner of the royalties is a resident of the other Contracting State, the tax so charged shall not exceed 5% of the gross amount of the royalties.
- 3) The term 'royalties' as used in this Article means payments of any kind received as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trade mark, design or model, plan, secret formula or process, or for information (know-how) concerning industrial, commercial or scientific experience.

10. The Tripletree group is a multi-national enterprise headed by Tripletree plc which is resident in the UK. The group operates in the telecommunications industry with Tripletree plc's wholly owned UK resident subsidiary, Tripletree (UK) Ltd, as the main trading company.

Tripletree (UK) Ltd has four wholly owned overseas subsidiaries. In addition, it has a 25% shareholding in Tripletree (Deo) Ltd, with the other shares held by individuals, none of whom are resident in the UK. All companies have been operating or trading for at least five years.

<u>Company</u>	<u>Resident jurisdiction and local corporate tax rate</u>	<u>Activity</u>	<u>Additional information</u> (Where profit amounts are stated, they refer to the year ended 31 December 2025.)
Tripletree (Ena) Ltd	Enamark, 12%	Distributor to third parties.	Trading profits of £80,000 and interest income of £10,000.
Tripletree (Deo) Ltd	Deoland, 10%	Distributor to third parties.	Trading profits of £100,000.
Tripletree (Tria) Ltd	Trialand, 22%	Distributor to third parties.	Trading profits of £600,000.
Tripletree (Tesera) Ltd	Teseraland, 20%	Provides routine support services to other group companies.	The company charges cost plus a mark-up of 7% for its routine support services.
Tripletree (Pende) Ltd	Pendeland  The normal corporate tax rate is 15% but Tripletree (Pende) Ltd was established five years ago and under an 'incentive to invest' scheme, the company is exempt from the corporate tax for the first 10 years.	Provides management and high value technology services to other group companies. All staff and management are resident in Pendeland and there are only occasional visits from senior UK management to the company's offices.	Trading profits are £2 million (and this is the only source of profit).  The company charges cost plus a mark-up of between 12% and 20% (which is an arm's length rate) for its services.

None of the jurisdictions mentioned in the table above are on the list of excluded territories for Controlled Foreign Companies purposes.

**Requirement:**

**Explain how the UK's Controlled Foreign Companies legislation applies to the Tripletree group.** (20)

11. Luczo Ltd is a UK incorporated trading company with no associated companies. It manufactures playground equipment and has 450 employees.

The following profit and loss account has been prepared for the 15-month period ended 30 June 2025:

<u>Profit and Loss Account</u>	£
Turnover	87,896,152
Cost of sales	<u>(59,235,128)</u>
Gross profit	28,661,024
Administrative expenses	(17,796,568)
Interest received	1,986,125
Interest paid	(2,359,789)
UK dividend received	42,000
Other income	<u>5,600,323</u>
Profit before tax	<u>16,133,115</u>

An extract from the company's balance sheet for the period shows the following:

<u>Tangible Fixed Assets</u>	Plant and machinery
<u>Cost</u>	£
At 1 April 2024	28,254,444
Additions	435,000
Disposals	<u>0</u>
At 30 June 2025	<u>28,689,444</u>
 <u>Depreciation</u>	
At 1 April 2024	6,567,222
Charge for the year	<u>871,347</u>
At 30 June 2025	<u>7,438,569</u>
 <u>Net book value</u>	
At 1 April 2024	<u>21,687,222</u>
At 30 June 2025	<u>21,250,875</u>

The following further information is available in respect of the above:

- The company's plant and machinery pool had a tax written down value brought forward at 1 April 2024 of £18,258,190. On 2 January 2025, the company purchased second-hand plastic moulds costing £400,000. Luczo Ltd had an unconditional obligation to pay for the plastic moulds on delivery. These were delivered on 15 January 2025, when the company paid £100,000. The remaining consideration of £300,000 was due and paid on 1 June 2025.

In addition, on 30 June 2025, the company acquired new production machinery costing £35,000.

- Luczo Ltd has a 2% shareholding in another UK company, Stanmarky Building Ltd, which is held as an investment. The company took out a loan in 2023 to acquire the shares. The interest payable by Luczo Ltd during the period ended 30 June 2025 was £1,357,888. The remainder of interest payable by the company during the period related to the company's overdraft, which is used for working capital. On 28 April 2025, Luczo Ltd received a dividend from Stanmarky Building Ltd of £42,000.
- At 1 April 2024, Luczo Ltd has non-trade loan relationship deficits of £1,590,076 brought forward from the previous year. The company has made a claim for deductions allowance.

- 4) Luczo Ltd has a large pension deficit, so has made a contribution of £912,500 in the period. Normally the company pays £100,000 annually into the scheme.
- 5) In November 2024, a director of Luczo Ltd who is also a minor shareholder was dismissed for having created fraudulent invoices from a fictitious company amounting to £50,000. This amount is included in administrative expenses.
- 6) The company gifted crystal vases bearing Luczo Ltd's name to its 100 best customers. The cost was £70 per item.
- 7) The managing director authorised an amount of £5,500 to be spent on a party at a local dinner venue to thank 100 staff for their hard work and also awarded bonuses of £500 to each of these staff members, which were accrued in the accounts in the period ended 30 June 2025. The bonuses were paid on 30 April 2026 (all staff members remained employed by the company at this date).
- 8) The company made a bad debt provision of £1,100,567 in the period. £700,567 related to a debt owed by a company that had gone into liquidation. For the first time the company felt it appropriate to carry a general provision, which comprised the balance of the expense.
- 9) In April 2025, the company let out a small part of its factory to an unconnected third party for six months to raise some minor additional funds. Rental income of £60,000 was received. The company normally uses the area to store finished goods and began re-using the area in Autumn 2025 following receipt of a large order from a new customer.
- 10) As a result of the large order from a new customer, the company may build an extension to the factory and spent £5,000 on planning permission fees on 17 May 2025.
- 11) Luczo Ltd sold shares in Jessie plc on 19 November 2024 that had been acquired on 1 November 2024, making a profit of £4,512,347, which has been included within other income. The company did not hold any other shares in Jessie plc.

**Requirement:**

- 1) **Prepare a computation of the Corporation Tax payable by Luczo Ltd for the 15-month period ended 30 June 2025, with supporting explanations as appropriate.** (18)
  - 2) **Calculate the deferred tax balance sheet provision at 30 June 2025.** (2)
- Total (20)

**You may assume that the interest capacity of the company is sufficiently large so that none of its tax-interest expense is disallowed under the CIR regime.**

12. Circle Ltd is a UK tax resident pipe manufacturer. It has no associated companies.

The draft profit and loss account and fixed asset note are as follows:

Circle Ltd  
Year ended 30 September 2026  
Draft profit and loss account

<u>Circle Ltd</u>	£
Turnover	21,432,574
Cost of sales	<u>(14,863,663)</u>
Gross profit	6,568,911
Administrative expenses	<u>(6,952,084)</u>
Bank interest receivable (gross)	27,218
Interest payable	<u>(98,247)</u>
Loss on disposal (land)	<u>(17,000)</u>
Loss on disposal (plant)	<u>(40,000)</u>
Net loss	<u>(511,202)</u>

<u>Tangible fixed assets</u>	<u>Freehold land</u>	<u>Factory buildings</u>	<u>Plant and equipment</u>	<u>Motor vehicles</u>	<u>Total</u>
	£		£	£	£
At 1 October 2025	270,000	150,000	552,078	55,000	1,027,078
Additions	0	0	250,000	43,000	293,000
Disposals	<u>(17,000)</u>	<u>0</u>	<u>(223,000)</u>	<u>0</u>	<u>(240,000)</u>
At 30 September 2026	<u>253,000</u>	<u>150,000</u>	<u>579,078</u>	<u>98,000</u>	<u>1,080,078</u>

<u>Depreciation</u>					
At 1 October 2025	0	30,000	278,000	22,000	330,000
Charge for the year	0	19,000	178,000	14,000	211,000
Eliminated on disposal	<u>0</u>	<u>0</u>	<u>(78,000)</u>	<u>0</u>	<u>(78,000)</u>
At 30 September 2026	<u>0</u>	<u>49,000</u>	<u>378,000</u>	<u>36,000</u>	<u>463,000</u>

<u>Net book value</u>					
At 1 October 2025	<u>270,000</u>	<u>120,000</u>	<u>274,078</u>	<u>33,000</u>	<u>697,078</u>
At 30 September 2026	<u>253,000</u>	<u>101,000</u>	<u>201,078</u>	<u>62,000</u>	<u>617,078</u>

All income and expenses are included within the profit and loss account unless otherwise stated. The depreciation charge is included within administrative expenses.

The following information is available:

- Circle Ltd took out a loan in 2024 to purchase a 4% shareholding of WCL Ltd, a UK tax resident company. The interest payable by Circle Ltd on this loan during the year ended 30 September 2026 was £30,000. The remainder of the interest payable related to another loan used to fund working capital for the trade. On 1 April 2026 Circle Ltd received a dividend of £45,000 from WCL Ltd (included in turnover).
- Circle Ltd made a contribution of £800,000 to a registered pension scheme set up for its employees. The purpose of the contribution was to clear a funding deficit. Circle Ltd makes a regular annual contribution of £250,000. The contribution for the year to 30 September 2026 was fully paid to the pension scheme during that year.
- In November 2025, Circle Ltd gifted a piece of freehold land to the recently disabled widow of a former employee so she could build a house on it adapted to her needs. The employee died two years ago. The land was purchased for £17,000 in December 2009 and valued at £38,000 at the time of the gift.

- 4) Legal fees of £73,000 were spent on an abortive application for planning permission relating to the extension of a factory building owned by Circle Ltd. A further £20,000 of legal fees were incurred in defending title to three acres of land adjacent to the factory building following a dispute over ownership with a neighbour.
- 5) Entertaining costs incurred were £15,000 for the accounting period. £600 of this expense related to pens which were gifts for clients, had the company's name on them and cost £60 each. £2,000 of the entertaining costs was incurred on the annual staff party.
- 6) Compensation of £50,000 was paid to another neighbour when a tree on the factory site fell on the neighbour's house and badly damaged it.
- 7) On 1 October 2025, the tax written down value of the general pool was £275,000 and the special rate pool was £196,000.
- 8) Fixed asset additions during the year were as follows:

Plant and equipment

- a) New pipe cutting equipment, £50,000, purchased on 1 November 2025.
- b) New electrical and hot water systems, £162,500, purchased on 1 January 2026.
- c) New IT equipment, £25,000, purchased on 8 January 2026.

The IT equipment has an expected useful life of five years. The other plant and equipment has an expected useful life of 15 years.

<u>Motor vehicles</u>	£
New lorry	15,000
New Audi car	25,000 (CO <sub>2</sub> emissions 150g/km)
Second hand Nissan car	3,000 (CO <sub>2</sub> emissions 48g/km)

The lorry was purchased in November 2025 and the cars were purchased in March 2026.

- 9) The equipment disposed of was packing equipment purchased new in May 2021 on which maximum capital allowances had been claimed.
- 10) In the year to 30 September 2025, Circle Ltd had taxable profits of £120,000 and paid £28,050 in Corporation Tax. The company did not receive any dividends in that year.

**Requirement:**

**Prepare a Corporation Tax computation for Circle Ltd for the year ended 30 September 2026 with supporting explanations as appropriate and showing clearly the use of any losses.** (20)

13. Charlese plc is a large animal food manufacturer. Its only subsidiary, Francis Ltd, which is wholly owned, transferred its trade and assets to Charlese plc on 1 July 2025. Both companies make up their accounts each year to 31 December.

The following information relates to Charlese plc for the year ended 31 December 2025:

- 1) At 1 January 2025, the main capital allowances pool tax written down value brought forward was £1,070,000.
- 2) The depreciation charge for the year was £4 million.
- 3) The company's depreciation policy is as follows:

Land		No depreciation
Buildings		2% straight line on buildings
All other assets	20% straight line with a full year's charge in the year of acquisition	

- 4) Extract from the tangible fixed assets note from the accounts:

	<u>Land and buildings</u> <u>Note 1</u> £	<u>Fixtures, fittings and equipment</u> <u>Note 2</u> £	<u>Motor vehicles</u> <u>Note 3</u> £	<u>Plant and machinery</u> <u>Note 4</u> £	<u>Total</u> £
Cost – additions	2,233,333	800,000	3,100,000	6,250,000	12,383,333
Cost – disposals	–	–	–	250,000	250,000
Depreciation – disposals	–	–	–	150,000	150,000

Note 1

New warehouse:	£
Building	1,333,333
Land	500,000
Electrical and water system	250,000
Air conditioning system	100,000
Lift	50,000
<b>Total</b>	<u>2,233,333</u>

Charlese plc entered into a contract with a third party to build the new warehouse on 1 January 2025. The payment was made on 25 March 2025 and the building was brought into use on 1 April 2025.

Note 2: All expenditure incurred in the three months starting 1 September 2025.

	£
Computer equipment	500,000
Qualifying land remediation expenditure	50,000
Decorating offices	100,000
Moveable partition walls in office*	50,000
Erecting new walls in office	50,000
Painting of new walls in office	10,000
Fire alarm system in office	20,000
New fire doors in office	10,000
Portable air conditioning units	10,000
<b>Total</b>	<u>800,000</u>

\*There are no plans to move the partition walls in the foreseeable future.

Note 3

	£
Commercial vehicles under hire purchase agreements	1,000,000
Commercial vehicles under finance leases	2,000,000
Cars with emissions 115g/km	<u>100,000</u>
Total	<u>3,100,000</u>

This is the first year that Charlese plc has acquired assets under finance lease or hire purchase, and the contracts were entered into on 1 January 2025 when the assets were also brought into use. The commercial vehicles were second-hand when purchased; the cars were new. The company prepares accounts in accordance with FRS 102.

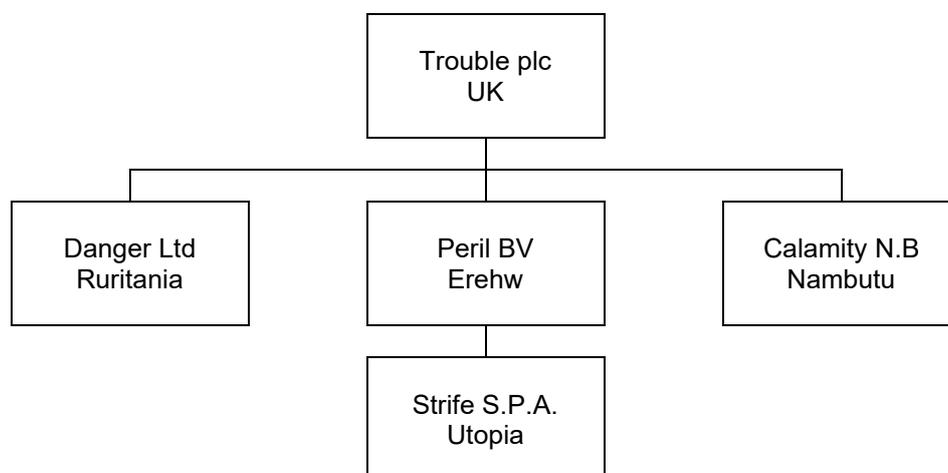
Note 4

	£
Manufacturing equipment – 1 March 2025	5,000,000
Plant transferred from Francis Ltd – 1 July 2025	1,000,000
Qualifying research & development expenditure on second-hand plant – 1 February 2025	<u>250,000</u>
Total	<u>6,250,000</u>
The plant transferred from Francis Ltd had a tax written down value of £1.5 million on 1 January 2025.	
Proceeds from the disposal of an item of machinery purchased in 2018	275,000

**Requirement:**

**Calculate, with explanations, the capital allowances that may be claimed and the other adjustments that are required to arrive at taxable profits in the Corporation Tax computation for the year ended 31 December 2025 for Charlese plc. (20)**

14. Trouble plc is the parent company of an international group specialising in the design and sale of luxury cars. The structure of the group is set out below with companies incorporated and tax resident in the jurisdictions stated. All subsidiaries are wholly owned.



The following information is available in respect of the year ending 31 December 2026:

- 1) Trouble plc sells cars in the UK market. It plans to issue an interest-bearing corporate bond to secure funding from a wide range of investors. It will use the proceeds raised to subscribe for additional ordinary shares in Danger Ltd, currently a dormant company. The directors of Danger Ltd and its registered office are provided by a trust company based in Ruritania. Danger Ltd will use the funds to issue a loan to Calamity N.B. with a market rate of interest, to enable Calamity N.B. to fund ongoing business activities.
- 2) Calamity N.B. sells cars in Nambutu and is due to pay a gross dividend of £10 million in 2026 to Trouble plc in respect of profits realised during the year ended 31 December 2025. The dividend will be paid net of a 10% withholding tax. Calamity N.B. paid corporate tax of £5 million in respect of the profits. A corporate tax deduction will be available for the company in respect of the distribution in Nambutu.
- 3) Peril BV is a holding company and its only source of income is a £22.8 million annual patent royalty from Strife S.P.A. for the use of patents, received net of a 24% Utopian withholding tax. The royalty income is taxed at a rate of 5% in Erehw. The patents have never been held in the UK. On 1 March 2026, Peril BV disposed of an investment property in Erehw for £50 million having purchased the property for £20 million on 15 April 2007.
- 4) Strife S.P.A. is a manufacturing company with all its income derived from its trade. The company is subject to corporate tax at a rate of 23% and is expected to realise accounting profits of £400,000.

**Requirement:**

**Explain the UK Corporation Tax implications of the above. Do NOT discuss the corporate interest restriction regime. Assume that Erehw is an excluded territory but that Nambutu and Utopia are not.**

(15)

15. Blue Buildings Ltd, a holding company of a UK based property investment group has two wholly owned subsidiaries, Pink Properties Ltd and Purple Properties Ltd. Blue Buildings Ltd and its subsidiaries all have 31 December year-ends.

Blue Buildings Ltd subscribed £100 million for 100% of the share capital of Pink Properties Ltd on its incorporation on 30 June 2016. This cash was utilised to build residential investment properties and a supermarket building. Construction finished on 30 June 2018 and since this date, the residential properties have been let to individuals and the supermarket building has been let to a large supermarket chain.

On 31 March 2026, Blue Buildings Ltd sold the entire share capital of Pink Properties Ltd to a rival company, Boutique Buildings plc. The conditions of sale were as follows:

- 1) Boutique Buildings plc did not require the supermarket building. Therefore, the supermarket building was transferred to Purple Properties Ltd for its net book value of £5 million prior to the sale of Pink Properties Ltd. The market value of the supermarket building was £15 million at the time of the transfer.
- 2) Consideration payable at completion comprised £150 million in cash plus £390 million in shares of Boutique Buildings plc.
- 3) Further consideration of 25% of the profit before tax of Pink Properties Ltd for the year to 31 December 2027 will be payable in cash on 31 December 2029. The market value of the right to receive this consideration was estimated to be £60 million on 31 March 2026.

**Requirement:**

**Explain the Corporation Tax consequences of the transfer of the supermarket and the sale of Pink Properties Ltd.** (20)

**You are NOT required to discuss Structures and Buildings capital allowances.**

## ANSWERS

### 1. POLISH HOME LTD

#### Plant and machinery allowances available

Plant and machinery allowances primarily take the form of an annual writing down allowance (WDA) on qualifying expenditure. There are two different rates which are relevant here:

- 1) A rate of 6% per annum (the special rate) is applied to certain specified integral fixtures such as heating and hot water systems, and electrical systems ('special rate items').
- 2) A rate of 18% per annum (the main rate) is applied to other plant and machinery ('main pool items').

Expenditure is generally pooled. Expenditure qualifying for the 6% rate is allocated to the special rate pool. Expenditure qualifying for the 18% rate is allocated to the main pool. The rates are then applied to the total balance in the pool, including any unrelieved balance brought forward from the previous year.

However, there are two other types of allowance which need to be considered before these WDAs are applied. First, first-year allowances (FYAs) are available where plant and machinery (excluding cars) is purchased new and unused. This means that expenditure on main pool items qualifies for a 100% FYA and expenditure on special pool items qualifies for a 50% FYA (with the remaining balance transferred to the special rate pool for relief by way of WDA in subsequent periods).

Secondly, there is an annual investment allowance (AIA) of £1,000,000 for the year ended 31 March 2026. Expenditure may not qualify for both FYAs and AIAs and so it is up to the company to claim whichever allowance is best in its circumstances. So in respect of expenditure that would otherwise qualify for a WDA at 6%, it is usually better to utilise the AIA before the 50% FYA is considered, as this effectively gives relief at a rate of 100%. However, the company has already used this on plant and machinery expenditure at its other restaurants, the AIA will not be available in respect of the expenditure being spent on the current refurbishment.

Purchases of used/second-hand plant do not qualify for the FYAs. Unlike the AIA, there is no annual limit on expenditure qualifying for FYAs.

#### Entitlement to plant and machinery allowances

To qualify for capital allowances the company needs to incur 'qualifying expenditure'. Qualifying expenditure is capital expenditure incurred on the provision for the purposes of a qualifying activity of plant or machinery which it then owns. The company has a trade of operating restaurants and this would be regarded as a qualifying activity.

Each item of expenditure needs to be considered to see whether it qualifies for plant and machinery allowances and if so what type of allowance applies.

#### Fixed wooden floor and fixed partitions

Expenditure on the provision of a 'building' will not qualify for plant and machinery allowances. A building is defined so as to include its walls, floors and ceilings. The installation of the floors and walls will therefore not qualify for plant and machinery allowances. However, as the expenditure is incurred on the renovation of a commercial building, it may qualify for structures and buildings allowances at a flat rate of 3% of the expenditure over a period of 33<sup>1</sup>/<sub>3</sub> years.

### Toilet stalls and washbasins

It is stated in s.23 CAA 2001 that the provision of certain assets is not excluded from qualifying for plant and machinery allowances by virtue of being incorporated in a building. The list of items includes sanitary ware such as toilets and basins.

We must then consider whether what is being provided is plant and machinery. The key test is whether an item of apparatus is used in the trade otherwise than as premises or part of the premises in which the trade is carried on. If an item has such a use then capital allowances may be claimed.

Apparatus which becomes part of the premises instead of merely embellishing them cannot be plant. Apparatus so becomes part of the premises if it loses its identity so as to become part of the premises.

Apparatus which does not become part of the premises (even though it may be attached to the premises) may be plant if it performs a function within the taxpayer's business. So if an item has a functional use in the carrying on of the taxpayer's trade then capital allowances may be claimed.

In this case it seems reasonable to argue, and it is generally accepted by HMRC, that the sanitary ware is not part of the building (it retains a separate identity) but is part of the apparatus of the trade and that plant and machinery allowances may be claimed.

These items do not appear on the list of integral features included in the capital allowances legislation and so are main pool items and qualify for plant and machinery allowances, in this case the 100% FYA.

### Electrical installation, hot and cold-water systems, fixed lighting and air conditioning

These items are all included in the definition of integral features and expenditure on them qualifies for WDA at 6%.

It may be possible to argue that the light fittings installed in the eating area are not an integral feature. Instead they are decorative assets and have as their purpose the creation of an atmosphere or ambience within the restaurant. As such expenditure on them qualifies for WDAs at the 18% rate. This argument would be unlikely to be effective for those light fittings which are located outside of the eating area, such as in the kitchen or washrooms. However, given these are new items, a 50% FYA is given in the year of purchase.

### Fixed seating, loose rugs and kitchen equipment

These items have a use in the trade and as such should qualify for the 100% FYA, being new purchases.

### Tables and chairs, cash tills and computer hardware

These items are moveable items which have a use in the trade and will qualify for plant and machinery allowances as main pool items. The cash tills and computer hardware are new items and so qualify for FYAs at 100%, but the tables and chairs (being second-hand) qualify for WDAs at 18%.

However, given that the tables and chairs items have an expected useful life of less than eight years it may be worthwhile making a short-life asset election for them. The effect of this election is that expenditure on the items is not included in the main pool. Instead each item qualifies for WDAs individually.

If any of the assets are disposed of within eight years after 31 March 2026, a balancing allowance may be triggered, thus accelerating the available capital allowances.

If the asset is not disposed of within this period, the remaining tax written down value is transferred to the main pool. The election must be made within two years of the accounting period in which the expenditure is incurred, so before 31 March 2028.

### Preliminaries

Following the *J D Wetherspoon* case, for capital allowance purposes the cost of preliminaries can be apportioned between the expenditure that qualifies for capital allowances (as special rate or main pool items) and that which does not.

<u>Summary table</u>	<u>CAs available</u>
Removal of old wooden floor and installation of new one and install fixed plasterboard walls	3% (SBA)
Toilet stalls and washbasins	100%
Mains electrical systems	50%
Fixed ceiling and wall lighting	50%
Built-in air conditioning system	50%
Fixed seating	100%
Loose rugs	100%
Kitchen equipment	100%
Tables and chairs (second-hand)	18% (SLA)
Cash tills and computer hardware	100%
Preliminaries	Apportion

### Key:

SBA = structures and buildings allowance

SLA = short life asset

## CIOT MARKING GUIDE

TOPIC	MARKS
Explain WDA rates of P&M allowances	1
Explain requirement to pool most types of qualifying expenditure	1
FYAs	1½
AiAs	1½
Requirement for qualifying activity and qualifying expenditure	1
Fixed wooden floors and walls do not qualify for P&M allowances but may for SBA.	
Explain why	1
Toilet fittings do qualify. Explain why and explain the functional use v setting test	2
Hot and cold water systems, lighting, electrical systems and air conditioning systems qualify as special rate pool items for 50% FYA. Explain why	1½
Light fittings in eating area may qualify as main pool items. Explain why	1
Seating, rugs, tables and chairs and kitchen equipment qualify for P&M allowances. Explain why and the rate.	1½
Availability of short life asset elections on tables and chairs. Outline tax implications	2
Discuss capital allowance treatment of preliminaries	1
<b>TOTAL (MAX)</b>	<b>15</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

Most candidates showed good knowledge of the subject and good exam technique. They tackled the question systematically, beginning with an outline description of capital allowances and then applying it to the scenario. They typically considered each item on the list of works in the question, identified whether or not it qualified for capital allowances and if so what kind. Most candidates also showed good technical knowledge of short life assets.

Some candidates presented the answer in a tabular form and added notes on specific items. This was a time efficient approach, which earned full credit for relevant information.

Some candidates took the opportunity to write down all that they know about capital allowances and waffled somewhat as a result. The key to obtaining a high mark was to only write down the information relevant to answering the question and the scenario.

## 2. UNDERGROUND GROUP

### Sale of District Ltd and Metropolitan Ltd

Ordinarily the sale of a company triggers a chargeable gain equal to the proceeds of the sale less the base cost of the shares. Where the Substantial Shareholding Exemption (SSE) is available, however, any gain arising is exempt from Corporation Tax.

The conditions for obtaining the SSE are as follows:

Circle Ltd must have owned a 'substantial shareholding' – defined as at least 10% of the ordinary share capital of District Ltd and Metropolitan Ltd – for a continuous period of at least twelve months within the six years prior to the sale. This condition appears to be met in relation to both companies.

The company being sold must be a trading company throughout the period beginning with the start of the latest 12-month period required for the substantial shareholding condition and ending with the date of disposal. The condition appears to be met in respect of District Ltd (a trading company) but not Metropolitan Ltd (which does not carry on any trade).

Assuming both conditions are met in relation to District Ltd, the disposal of its shares should qualify for SSE and any gain made by Circle Ltd should be exempt from Corporation Tax.

### Transfer of freehold property to District Ltd

When Jubilee Ltd transferred the freehold property to District Ltd the transaction would have been at no gain/no loss, since both companies were members of a group for the purposes of chargeable gains. A de-grouping charge is triggered because District Ltd is leaving the group within six years of the transfer of the property, still holding the transferred property. The de-grouping charge is calculated on the difference between the market value of the asset at the time of transfer and its base cost. So the potential chargeable gain is £70,000 (£150,000 minus £80,000).

This de-grouping charge is taken into account in the calculation of the gain or loss on the disposal of the shares by the vendor of the company, ie Circle Ltd. However, since the sale of the shares appears to benefit from the SSE, the de-grouping charge would be likewise exempt.

### Transfer of trademark to Metropolitan Ltd

When the trademark (an intangible fixed asset) was transferred to Metropolitan Ltd the transaction would have been 'tax neutral' since both companies were members of a group for the purposes of the intangible assets legislation and so no Corporation Tax would have arisen at the time of the transfer.

As the disposal of the shares in Metropolitan Ltd does not qualify for SSE, a de-grouping charge arises now that Metropolitan Ltd has left the group within six years of the intra-group transfer still owning the asset.

It is calculated as the market value of the trademark at the time of transfer less the tax written down value of the trademark at the time of transfer based on the figure in the accounts.

However, Metropolitan Ltd is entitled to an additional deduction for the amortisation of the trademark for the period between the intra-group transfer and the sale of its shares to reflect the fact that the acquisition cost of the asset is deemed to have been £60,000 since the time of intra-group transfer.

See Appendix 1 for the calculation. The net charge is £10,526.

The de-grouping charge remains a liability of Metropolitan Ltd. However, it may be reallocated to another Underground group company by means of a joint election. As Jubilee Ltd plans to purchase further trademarks it may be possible to defer payment of the tax due by claiming rollover relief in respect of the reallocated charge.

#### WCL Ltd: Pre-entry losses

The £100,000 capital loss in WCL Ltd is a restricted pre-entry loss since it was realised before WCL Ltd joined the Underground group. The loss may however be offset against the gain made by Northern Ltd on the disposal of the building if all of the following conditions are met:

- 1) The gain arises on the disposal of an asset which was acquired after WCL Ltd joined the Underground group. This condition appears to be met.
- 2) The asset was acquired either by WCL Ltd or a company in the same group as WCL Ltd at the time the asset was acquired. Northern Ltd was in the same group as WCL Ltd at the time Northern Ltd bought the building so this condition appears to be met.
- 3) The building was acquired from a person who is not in the same group as WCL Ltd. This condition appears to be met.
- 4) The building has not been used since its acquisition for any purpose other than the trade or business of WCL Ltd. The trade must have been carried on by WCL Ltd immediately before entering the group and carried on by WCL Ltd or another company in the group thereafter. This condition appears to be met.

Accordingly, the pre-entry loss may be offset against the gain arising in Northern Ltd, to produce a chargeable gain of £60,000 (£240,000 proceeds less £80,000 cost, less £100,000 loss offset). A brought forward capital loss is subject to potential restrictions but in this case the deductions allowance of £5,000,000 is available. WCL Ltd must, however, specifically claim a deductions allowance (of £100,000) to utilise the carried-forward loss in full against the gain arising on the disposal of the building.

#### Transfer of Victoria Ltd trade to Central Ltd

Ordinarily the sale of a trade which started before April 2002 to a connected company would trigger a chargeable gain based on the market value of the goodwill transferred less the base cost, if any. However, in this case Victoria Ltd and Central Ltd are wholly owned subsidiaries of Circle Ltd. Accordingly a group exists for Capital Gains purposes and the transfer will take place at no gain/no loss. Being an acquisition of goodwill from a fellow group company, the asset remains within the chargeable gains regime.

Ordinarily the transfer of the trade would trigger the cessation of the trade in Victoria Ltd. Brought forward trading losses would not be carried forward and would be lost, and a balancing allowance or charge might be triggered in relation to the capital allowance main pool.

However, a different treatment applies when the following conditions are met:

- 1) A company ceases to carry on a trade and another company begins to carry it on, AND
- 2) At any time within two years after the cessation, the trade is owned as to at least 75% by the same persons as owned a like interest at any time within a year before the cessation, AND

- 3) Throughout the periods referred to, the trade is carried on by a company which is within the charge to Corporation Tax in respect of it.

Victoria Ltd is ceasing its trade and Central Ltd will start to carry it on. As both companies are wholly owned by Circle Ltd both immediately before and immediately after cessation, Circle Ltd is treated as owning the trade at some time in the requisite qualifying period. Also during that period the two companies that actually carry on the trade are within the charge to Corporation Tax. Accordingly all three conditions appear to be met.

It follows that Central Ltd may succeed to the brought forward trading losses and the balance on the capital allowance main pool of Victoria Ltd.

The trading losses that may be succeeded to are, however, restricted to the extent that Victoria Ltd (the predecessor company) retains more 'relevant liabilities' than 'relevant assets'. The relevant liabilities are broadly liabilities of Victoria Ltd, excluding share capital, which are not transferred to Central Ltd. The 'relevant assets' are broadly assets which are not transferred to Central Ltd plus any consideration received.

In this case the losses that may be transferred are £45,000. See Appendix 2 for workings.

The balance on the capital allowance main pool inherited by Central Ltd (ie £15,000) is not restricted by the non-transfer of assets or liabilities.

The inherited trading losses (having been incurred before 1 April 2017) may only be offset against trading profits of the same trade so in this case the one transferred from Victoria Ltd. Central Ltd must therefore identify for each year the profits (if any) that this trade has made and offset the brought forward trading losses against them only.

APPENDIX 1Calculation of degrouping charge on intellectual property (trademark)

	£
Market value of the trademark at the time of transfer	60,000
Less: Tax written down value of trademark at the time of transfer 50,000 – (50,000/20 years × 1 year)	<u>(47,500)</u>
De-grouping Charge	12,500
Less: extra amortisation deductions	
To 31 December 2023	2,500 – (2,500 × 60,000/47,500) (658)
To 31 December 2024	2,500 – (2,500 × 60,000/47,500) (658)
To 31 December 2025	2,500 – (2,500 × 60,000/47,500) <u>(658)</u>
Net charge	10,526

Note: Alternative calculation of additional amortisation charge:

Revised amortisation = £60,000 / 19 years = £3,158

Amortisation charged in accounts = £50,000 / 20 years = £2,500

Additional amortisation = £3,158 – £2,500 = £658 pa

APPENDIX 2Calculation of transferable losses

	£	£
Relevant liabilities retained		
Trade creditors less creditors transferred (£115,000 – £5,000)	110,000	
Bank overdraft	<u>65,000</u>	
		(175,000)
Relevant assets retained		
Freehold property	70,000	
Trade debtors	45,000	
Consideration received	<u>30,000</u>	
		<u>145,000</u>
Net liabilities		(30,000)
Trade losses at the date of transfer		<u>75,000</u>
Trade losses transferred to Central Ltd		<u>45,000</u>

## CIOT MARKING GUIDE

TOPIC	MARKS
<u>Disposal of District Ltd</u> Explain availability of Substantial Shareholdings Exemption (SSE) on disposal and explain conditions for obtaining exemption and indicate that they will likely be met	2
<u>Transfer of freehold property to District Ltd</u> Explain that de-grouping charge arises on the disposal of District Ltd, explain why and calculate the charge.	1
Explain that Circle is subject to Corporation Tax on the de-grouping charge and that Circle Ltd is likely to be exempt from tax on the charge on the grounds that SSE will apply to the charge.	1
<u>Transfer of trademark to Metropolitan Ltd</u> Explain that a de-grouping charge arises on the disposal of Metropolitan, explain why and explain how the charge is calculated	1
Calculate the de-grouping charge	1
Explain who is liable to pay the charge; explain that the charge may be transferred by joint election to other group companies, that reinvestment relief may be available to defer the tax on the charge. Explain what further information is needed	2
<u>Pre-entry losses</u> Explain that the £100,000 capital loss in WCL Ltd is a pre entry loss and explain why	1
Explain each condition that needs to be met for the pre entry loss to be offset against the chargeable gain in Northern Ltd	2
Calculate the chargeable gain arising in Northern Ltd	1
<u>Transfer of trade to Central Ltd</u> Explain that transfer of trade does not trigger a capital gain and explain why and explain the ordinary treatment of a cessation of trade	1
Explain conditions to be met for a succession to the trade to take place under s.940A et seq CTA 2010	1
Explain that conditions are met and why	1
Explain the beneficial tax consequences of a succession to trade under s.940A et seq CTA 2010	1
Explain restriction of transfer of trading losses where relevant liabilities exceed relevant assets	1
Calculate trading losses that may be transferred and explain that transfer of unused capital allowances is not restricted	2
Explain how trading losses transferred may be offset against future trading profits	1
<b>TOTAL</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question was time pressured but generally well answered. Most candidates identified the degrouping charges that would arise on both the freehold property and trademark when District Ltd left the Circle Ltd group of companies.

Candidates generally showed a good understanding of the Substantial Shareholdings Exemption and noted that if available it would apply to the degrouping charge relating to the transfer of the freehold property.

Few candidates explored how the degrouping charge on the intangibles could be mitigated through the use of rollover relief into a new purchase of trademarks.

Candidates showed a good understanding of the trade succession rules when one trade is transferred to another company under common ownership. Many, however, struggled to calculate the restriction on the trade losses which could be transferred to Central Ltd.

### 3. LENTIL PLC

#### Trading as a permanent establishment

The general position is that UK companies are taxable on their worldwide profits. If the Thousisland operation is set up as a permanent establishment of Lentil plc, the profits/losses of the permanent establishment will be included in Lentil plc's profits, and subject to UK Corporation Tax.

If the permanent establishment makes losses in the first two years, the loss arising in each year will reduce Lentil plc's taxable profits for those two years accordingly.

Once the permanent establishment becomes profitable, Lentil plc's taxable profits will include the profits of the permanent establishment.

Double tax relief should be available for Thousisland tax payable on those profits and additional Corporation Tax will be due to the extent that the Thousisland tax paid is less than the Corporation Tax rate multiplied by the permanent establishment's profits (as calculated under UK tax principles) would have been.

As the tax rate in Thousisland is lower than in the UK, it is anticipated that additional Corporation Tax will be payable. The total tax payable (Thousisland and UK) will be 25% of the permanent establishment's profits.

However, the UK has an exemption regime for foreign permanent establishments. In order to take advantage of the exemption, Lentil plc will need to elect for the permanent establishment to be treated as exempt from Corporation Tax. This election can be made at any time and will be effective from the start of the next accounting period.

If, however, the Thousisland permanent establishment has been continuously loss making then future profits will not be treated as exempt until the losses in the previous six years have been matched with the profits arising in subsequent periods (in effect the losses are streamed and until they have been matched in full, the permanent establishment's profits will continue to be subject to Corporation Tax).

Once an election is made it is irrevocable and would apply to any other foreign permanent establishments of Lentil plc too.

The permanent establishment exemption is subject to the anti-diversion rule, which is intended to prevent a company from artificially diverting profits out of the UK and into an exempt foreign permanent establishment. This is unlikely to apply here given that Lentil plc is intending to expand and trade in Thousisland.

If the business of the Thousisland permanent establishment is subsequently sold by Lentil plc then Corporation Tax will be due on any chargeable gain arising. For this reason, it may be beneficial to incorporate the branch once profit making if the Substantial Shareholding Exemption might apply (see below).

#### Trading as a company

If a separate Thousisland company is incorporated, the profits arising in the Thousisland subsidiary will not be subject to UK Corporation Tax, but no relief will be obtained for any of the anticipated losses arising in the first two years.

The subsidiary should not be caught by the UK's Controlled Foreign Companies regime, as it will be carrying on a trade in Thousisland and the tax rate in Thousisland is only marginally lower than in the UK.

Profits can be repatriated to Lentil plc by way of dividend and no Corporation Tax should be payable by Lentil plc, as it is likely the dividends would be exempt from Corporation Tax, the Thousisland company being controlled by Lentil plc.

If the Thousisland subsidiary is subsequently sold then the Substantial Shareholding Exemption may be available as it is a trading company, if other qualifying conditions are met.

#### Transfer pricing

If the Thousisland business operates through an overseas permanent establishment of Lentil plc then it will be important to consider the appropriate allocation of profits between the UK headquarters and the Thousisland permanent establishment.

The allocation of profit will need to be at arm's length, focusing on the activities and functions of the permanent establishment undertaken in Thousisland versus the activities and functions undertaken in the UK.

Transfer pricing documentation will be required to support the allocation of profit from a Thousisland tax perspective and, if a permanent establishment exemption election is made, it will also be important from a UK tax perspective.

If the Thousisland business operates as a separate legal entity then it will be important to identify and determine the arm's length price for any transactions between Lentil plc and its Thousisland subsidiary.

Transactions between the two companies are likely to include the sale of any stock from Lentil plc to the Thousisland company and management fees for any head-office services provided from the UK. Again the transactions will need to take place at arm's length and documentation will be required in support. This could be based on third party unrelated comparables or, if none are available, a benchmarking study may be required.

If further certainty is required in relation to the pricing of the transactions between Lentil plc and the Thousisland subsidiary, then it should be possible to approach HMRC to negotiate and agree an Advance Pricing Agreement.

#### Recommendation

Given the new operation is expected to be loss making in the first two years, it would be beneficial to start trading in Thousisland through a permanent establishment as the losses can be offset against Lentil plc's other profits. Profits arising in later years, however, would be taxable in the UK. Once profitable, a decision will need to be taken as to whether to make a permanent establishment exemption election or to incorporate the permanent establishment. This also ensures that flexibility is retained over the structure.

## CIOT MARKING GUIDE

TOPIC	MARKS
<u>Permanent establishment vs subsidiary – pros/cons</u>	
PE	
– Taxed on worldwide profits	½
– Relief for losses in early years	1
– Double tax relief	1
– PE exemption for profits in later years	1
– Reference to election	1
– Need to utilise losses before able to elect for PE exemption	1
– Able to incorporate PE at later date	½
– Anti-diversion rule	1
– Gain on sale	½
Subsidiary	
– No Corporation Tax payable	1
– No relief for losses	1
– Dividend exemption	1
– SSE	1
– CFC	1
<u>Transfer Pricing</u>	
PE	
– Allocation of profit between HQ and PE	1
– Arm's length	1
– Documentation	½
Subsidiary	
– Arm's length	1
– Transactions, eg sale of stock, management fees	1
– Documentation	½
– APA	1
Recommendation	
– Set up as PE to use losses in early years. Flexibility to elect for PE exemption at later date or incorporate.	1½
<b>TOTAL</b>	<b>20</b>

#### 4. MIDNIGHT PLC

##### Intercompany sales agreement between Twilight Ltd and Dusk BVBA

Under UK tax legislation, transactions between Twilight Ltd and its associated companies must be at arm's length (ie pricing is set at the price which two independent parties might be expected to agree on).

Twilight Ltd has been selling parts to Dusk BVBA at cost, which is unlikely to equate to market value. This has potentially resulted in lower profits in Twilight Ltd. Where a UK company has realised a UK tax advantage as a result of a transaction that was not at arm's length, HMRC may make an adjustment to increase that company's taxable profits. Any adjustment is purely for tax purposes and does not impact the company's statutory accounts or the actual price payable.

Such an adjustment would lead to tax inefficiency on the assumption that a lower amount is being deducted in Dusk BVBA than is being taxed in Twilight Ltd. It should, however, be possible for Dusk BVBA to claim a compensating adjustment if a Mutual Agreement Procedure (MAP) is initiated under the double tax treaty and agreement is reached with the relevant competent authorities in both jurisdictions.

The appropriate price for this transaction should be determined by reference to the OECD Transfer Pricing guidelines. These guidelines state that the company should use the 'most appropriate' method for its circumstances. Twilight Ltd is selling components to Dusk BVBA that it would otherwise be using in its own manufacturing processes. No components are sold to third parties and so Twilight Ltd has no comparable uncontrolled price (CUP) to base the transfer price on.

In such a situation, the most appropriate transfer pricing method may instead be the cost plus method, whereby Twilight Ltd applies an appropriate mark-up to the costs that it has incurred manufacturing the components. A benchmarking study should be undertaken to calculate an appropriate mark-up.

Twilight Ltd may be able to apply to enter into a bilateral advance pricing agreement (APA) with the two competent authorities, potentially alongside the MAP process. This would allow Twilight Ltd and Dusk BVBA to have certainty over the pricing of the transaction.

By filing an incorrect return, Twilight Ltd could be at risk of a penalty of up to 30% of the tax advantage. Also, if the transaction is found to have insufficient economic substance and result in an effective tax mismatch, Twilight Ltd may be charged to Diverted Profits Tax at 31% of the diverted profits less the UK tax already paid on those profits. This is for HMRC to determine.

##### Twilight Ltd as a dependent agent of Dusk BVBA

A dependent agent is a person, other than an independent agent, who acts on behalf of a company and has, and habitually exercises, in a contracting state, the authority to conclude contracts in the name of that company.

If Twilight Ltd has been habitually acting on behalf of Dusk BVBA (other than as an independent agent), the Corporation Tax implications are that Dusk BVBA will be deemed to have a permanent establishment (PE) in the UK. Dusk BVBA would need to file UK Company Tax returns, attributing a proportion of income and costs to the PE and paying UK Corporation Tax on its profits. The double tax treaty should ensure that double taxation on the PE's profits is eliminated by making an appropriate adjustment to the amount of Belgian tax charged on the profits attributable to the PE.

It should be determined exactly which of Dusk BVBA's contracts have been concluded by Twilight Ltd. If it is indeed the case that this only took place in January 2024, it should be possible to argue that Twilight Ltd has not been 'habitually' exercising an authority to conclude contracts on behalf of Dusk BVBA and so does not create a PE of Dusk BVBA in the UK. There are various ways to minimise the risk of a similar situation occurring in the future; for example, ensuring any Twilight Ltd employees involved do not have authorisation to conclude contracts.

## CIOT MARKING GUIDE

TOPIC	MARKS
<u>Trading agreement between Twilight Ltd and Dusk BVBA</u>	
– All transactions between Twilight Ltd and associated companies must be at arm's length	½
– Twilight Ltd received tax advantage as sold components at cost instead of market value	1
– HMRC can make adjustment to Twilight Ltd's taxable profits	1
– Adjustment would lead to double taxation / tax inefficiency	1
– Double taxation / tax inefficiency can be eliminated through MAP to allow compensating adjustment in Dusk BVBA	1
– Must apply OECD guidelines and apply 'most appropriate' method when determining transfer price	1
– No comparable uncontrolled price as components not sold to third parties	½
– Cost plus method likely to be most appropriate in circumstances	1
– Undertake benchmarking study to determine appropriate mark-up	½
– Ability of Twilight Ltd to enter into bilateral APA	1
– Twilight Ltd may be subject to penalty for incorrect filing of return	½
– Potential applicability of DPT	1
<u>Twilight Ltd habitually acting on behalf of Dusk BVBA</u>	
– Definition of habitually acting on behalf of	1
– Would create UK PE of Dusk BVBA, plus consequences of this	1½
– Double tax treaty should eliminate double taxation through tax credit	1
– Determine which contracts concluded by Twilight Ltd	½
– May be able to argue not 'habitual' and so not a PE	½
– Advice on how to minimise future risk	½
<b>TOTAL</b>	<b>15</b>

## 5. SWIFT GROUP

If a taxpayer has taken 'reasonable care' in completing a return and has taken reasonable steps to disclose any errors, no penalty will apply. 'Reasonable care' varies according to the circumstances and abilities of the taxpayer. If taxpayers do not promptly tell HMRC when they discover an error, this will be a careless inaccuracy even when the taxpayer took reasonable care.

### Company Tax Returns 2022

The potential penalty for submitting an inaccurate return is a percentage of the potential lost revenue ('PLR') as a result of the inaccuracy and the percentage depends on the behaviour of the taxpayer. If the behaviour here was carelessness, the penalty is 30% x PLR.

In this case the PLR is likely to be £600,000 - £60,000 = £540,000 x 19% = £102,600 so that the penalty is £102,600 x 30% = £30,780.

This penalty may be reduced to nil provided the company makes an unprompted disclosure and corrects the error.

### Company Tax Returns 2023

The filing due date for Company Tax returns is 12 months after the end of the accounting period so the returns should have been submitted by 31 December 2024. There is an immediate £100 penalty per return, regardless of whether the tax payable has been paid. This increases to £200 if the return is more than three months late. The total fixed penalty for all 10 companies is £2,000.

Where returns are submitted more than 18 months after the end of the accounting period (ie more than 6 months after the normal filing date for a 12 month period) there will be a tax-gearred penalty of 10%. The penalty doubles to 20% where the return is not filed within two years of the end of the accounting period. As the companies are loss making this should not be an issue.

### Company Tax Returns 2024

Since these returns were due to be filed by 31 December 2025, they are over six months late. Fixed penalties will apply as per the 2023 company tax returns.

In addition the 10% tax geared penalties mentioned above could also apply as the returns will not be filed within 18 months of the end of the respective accounting periods. Having said that, due to the group being in an overpayment position overall, the penalties should not be chargeable as there will be no outstanding tax to pay. HMRC may issue the penalties but they should be appealed and the returns filed at the same time.

### Company Tax Returns 2025

These returns are due to be filed by 31 December 2026 and as such no late filing penalties have yet been incurred.

### Royalty payments made to Robin B.V.

#### Withholding Tax

Royalties paid for the use of a patent are subject to the withholding tax provisions as the payment is of an income rather than a capital nature. 20% withholding tax should be deducted from the royalty payment and accounted for to HMRC on a quarterly basis.

However, Bluebird Ltd may choose to make the royalty payment at the reduced treaty rate of deduction (if applicable) if it reasonably believes that the Dutch entity is entitled to the benefit of the treaty.

#### Corporation Tax

Patent royalties are dealt with under the rules for intangible fixed assets and are taxed on an accruals basis. The royalty payment should be deducted from Bluebird Ltd's trading profits.

#### Transfer Pricing

If Robin B.V. and Bluebird Ltd are under the same participation (ie if Swift plc controls both Robin B.V. and Bluebird Ltd), the transfer pricing provisions may apply if there is a UK tax advantage – for instance, if Bluebird Ltd's trading profits are reduced as a result of an over-priced royalty payment or losses are increased as a result of the royalty payment.

The price of the royalty payment should adhere to the arm's length provision, determined by OECD guidelines. So the price should be based on the terms and conditions that independent parties would adopt. If not comparable, then transfer pricing rules will apply and the taxable profits of Bluebird Ltd must be restated using an arm's length price for the royalty payment.

A transfer pricing adjustment to the profits of Bluebird Ltd could lead to double taxation (if the same profit is taxed in the UK and in the Netherlands) if it is not matched by an adjustment to the profits of Robin B.V. It may be possible to achieve mutual agreement between the two countries' authorities to avoid such double taxation arising.

Under Corporation Tax Self-Assessment a company is required to self-assess its liability under the transfer pricing rules, supported by documentation. Companies must keep all records used in making and delivering a correct tax return until the latest of:

- Six years from the end of the accounting period;
- The date after which enquiries may not be commenced; and
- The date any enquiries are completed.

Failure to keep records could result in a maximum penalty of £3,000.

#### Diverted Profits Tax ("DPT") notification

If a company is potentially within the charge to DPT, it must notify HMRC in writing accordingly within three months of the end of the accounting period. As the accounting period ended on 31 December 2025, the notification was due by 31 March 2026. As the company has failed to notify HMRC within the relevant time frame, a tax-gearred penalty may be issued.

## MARKING GUIDE

TOPIC	MARKS
Wren Ltd 2022	
Reasonable excuse discussion	1
Calculation of penalty for inaccurate return due to carelessness	1
Mitigation	½
Due filing date for returns	1
Tax returns 2023	
Rules for fixed penalty rules for filing late	1
Rules for tax based penalty rule for filing late	1
Tax returns 2024	
Amount of fixed penalty for late filing	½
Amount of tax based penalties	½
Tax returns 2025	
No current penalties as not late	½
Royalties	
Explanation of withholding obligations s.903 ITA 2007	1
Reduction in rate of withholding under DTA s.911 ITA 2007	1
Corporation tax treatment of patent royalties	
Royalties paid – accruals basis	1
Deduction from trading income	1
Transfer pricing	
Special relationship so rules potentially apply	1
OECD guidelines arm's length pricing and independent prices explanation	1
What the UK tax advantage is here	1
Consequences – profits taxed on independent prices	½
Double taxation – MAP	1
CTSA - Documentation requirement for TP	1
Keeping records and penalty for failure	1
Diverted Profits Tax	
Duty to notify	1
Time – 3m from AP. Notification not made and so tax geared penalty may apply	1½
<b>TOTAL</b>	<b>20</b>

**6. CHALLENGER PLC**Disposal of shares of Endeavour Ltd and PropCo Ltd

For tax purposes, each disposal will constitute a chargeable disposal. However when disposing of a substantial shareholding, the Substantial Shareholding Exemption (SSE) may apply which exempts gains and means that losses are not allowable.

The SSE has conditions relating to both the shares owned by the investing company and the company being sold.

Shareholding conditions

The investing company must have held a substantial shareholding (in excess of 10%) throughout a 12-month period beginning no more than six years prior to the disposal. In both cases, the investing companies (Challenger plc and Voyager Ltd) have each held a substantial shareholding throughout the 12 months before 1 June 2026.

Investee Company conditions

The company being disposed of must have been a trading company or the holding company of a trading subgroup in the 12 months ending on the date of disposal. A trading company is one carrying on trading activities that do not include non-trading activities to any substantial extent. In applying this test, all facts and circumstances should be taken into account by reference to the company's activities as a whole. As Endeavour Ltd is a trading company it appears that it would meet this test.

PropCo Ltd requires further consideration. The holding of property for the purposes of generating rental income will not of itself qualify as a trading activity. In a group context, intra-group activities are disregarded for the purposes of assessing the trading status of the group. Where a subgroup is being sold, activities between group companies (which are not in the subgroup) and the subgroup are not disregarded. However, PropCo Ltd is neither the holding company of a group nor a subgroup and these provisions do not assist in determining its status. As such, when considering only the disposal of the shares in PropCo Ltd, the trading company condition will not be satisfied and the SSE will not apply.

The gain would be:

<u>PropCo Ltd</u>		£'000
Proceeds		30,000
Cost	1 January 2010	<u>(15,000)</u>
Unindexed gain		15,000
Indexation	(Jan 2010- Dec 2017)	
	$(278.1 - 217.9)/217.9 \times \text{£}15,000,000$	<u>(4,144)</u>
Gain		10,856

De-grouping charges

When a company leaves a chargeable gains group holding chargeable assets transferred to it intra-group within the past six years, the rules on de-grouping charges must also be considered. A de-grouping charge is calculated as though the chargeable asset had been sold and immediately reacquired for its market value at the time of the original transfer. The de-grouping charge is treated as an adjustment to proceeds when calculating the gain or loss on the disposal of the shares in the company being sold. Where a de-grouping charge arises on a share sale, if the sale of the shares qualifies for the SSE, the SSE rules also exempt the de-grouping charge.

Whilst the transfer from Atlantis Ltd took place more than six years before the proposed disposal of the shares, the transfer from Discovery Ltd took place in December 2020 and therefore, a de-grouping charge may arise if there is a share disposal before 31 December 2026.

Provided the sale of the Endeavour Ltd shares does indeed qualify for the SSE, no de-grouping charge would arise on this sale as a result of the transfers in December 2020 of non-property chargeable assets to it.

However, it is likely that a de-grouping charge would arise on the transfer of the property from Discovery Ltd to PropCo Ltd on 31 December 2020. Details of the original cost of the property and the market value at 31 December 2020 will be needed to calculate the potential adjustment to the gain above. Delaying the disposal (currently proposed to be made on 1 June 2026) until six years from the time of the original transfer may be worth considering if the de-grouping charge would be significant.

The tax treatment of the property transactions by Challenger plc associated with the proposed transactions is set out in the Appendix below.

#### Appendix – Tax treatment of property disposals

##### Manchester

This is the grant of a short lease (less than 50 years) from a long lease (as the head lease has between 59 and 60 years left to run).

Part of the premium will be taxed as property income and part as a chargeable gain.

		£
Premium		250,000
Capital element	2% x 250,000 x (10-1)	(45,000)
Income element		205,000

The chargeable gain calculation is treated as a part disposal with the allowable cost calculated as follows:

$$a/(A+B) \times \text{acquisition cost}$$

where a is the part of the premium treated as capital (ie £45,000), A is the total amount of the premium (£250,000) and B is the value of the reversionary interest in the lease. It would therefore be necessary to determine the value of the reversion in order to calculate the gain arising.

##### York

This is the assignment of a short lease (as it has 10 years and 7 months left on its term). As the lease is less than 50 years it is a wasting asset. A chargeable gain is calculated but the company cannot take a deduction for the whole of the acquisition cost.

The deductible base cost is the original acquisition cost multiplied by S/P where S and P are the 'lease depreciation' percentages for the years of the lease remaining at the dates of sale and purchase respectively.

Lease term remaining on purchase – 15 years – lease percentage 61.617

Lease term remaining on sale – ten years seven months – lease percentage  
 $46.695 + 7/12 \times (50.038 - 46.695) = 48.645$

The chargeable gain based on a disposal of 1 June 2026 would be:

	£
Proceeds (1 June 2026)	300,000
Adjusted cost (500,000 × 48.645/61.617)	<u>394,737</u>
Capital loss	<u>(94,737)</u>

### MARKING GUIDE

TOPIC	MARKS
<u>Share disposal:</u>	
Chargeable disposal, SSE possible	1
>10%, 12 months	1
Investee condition, met by Endeavour	1
Propco fails	2
Gain calc	<u>1</u>
Sub-total	6
<u>Degrouping charge:</u>	
Holding assets transferred intra group in last six years	1
Fixed assets and intangibles	1
Relevant to Discovery transfer, not Atlantis	1
Exempted if SSE so Propco transfer only	1
Need gain at 31 December 2020 and add to proceeds	1
Consider delaying	<u>1</u>
Sub-total	6
<u>Leases:</u>	
Manchester short lease so part income, part gain	1
Income £205,000	1
Gain $a/(A+B)$	1
$a=45,000$	1
$A=250,000$	1
$B$ =value of reversionary interest – to be determined	1
York – assignment of short lease, wasting asset	1
Calculation of deductible base cost (principle, use of %, precise answer)	<u>1</u>
Sub-total	8
<b>TOTAL</b>	<b>20</b>

### Examiner's report:

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question [concerned] proposed share disposals as well as two lease transactions.

In general, candidates performed well on this question with most identifying the key points relating to the share disposals, including discussion of the application of the Substantial Shareholdings Exemption and the possibility of degrouping charges. The best candidates considered planning opportunities such as deferring the transaction and discussed these in commercial terms.

The understanding of lease transactions was less consistent with confusion as to when the consideration needed to be split between capital and income. It was particularly disappointing to see many candidates calculating the gain on the Manchester disposal based on the capital element of the proceeds and then deducting the income element again! A number of candidates also confused the part disposal rules and the adjustment of cost on a depreciating asset.

## 7. THE BARLEY GROUP

### Preparation for the disposal of shareholding in Sweetcorn Ltd

The group, excluding Wheat Ltd, forms a chargeable gains group with Barley plc as the principal company.

The effect of there being a chargeable gains group is that both the transfer of business premises from Granola Ltd to Sweetcorn Ltd and the transfer of shares in Soya Ltd from Sweetcorn Ltd to Barley plc will be treated as occurring on a nil gain/nil loss basis for tax purposes. Therefore, no chargeable gains or losses will arise on the transfers.

However, as Sweetcorn Ltd will be sold, and hence leave the capital gains group, within six years of the transfer of business premises, a de-grouping charge will arise and be charged (subject to exemption) on Barley plc. The de-grouping charge will be equal to the chargeable gain that would have arisen on the intergroup transfer, ie £3.5 million (£11 million - £7.5 million).

Stamp duty land tax (SDLT) will be chargeable on the transfer of the building. Group relief is not available because, at the time of the transfer, arrangements are in place to dispose of Sweetcorn Ltd, the recipient of the building. The SDLT payable will be as follows:

	£
£150,000 x 0%	0
(£250,000 - £150,000) x 2%	2,000
(£11,000,000 - £250,000) x 5%	<u>537,500</u>
SDLT payable	<u>539,500</u>

This will be payable by Sweetcorn Ltd.

No stamp duty will be chargeable on the transfer of the shares in Soya Ltd as beneficial ownership is being transferred to an associated company (ie a group company) and at the time of the transfer there are no arrangements for Barley plc to cease to be Soya Ltd's parent company.

### Substantial shareholdings exemption (SSE)

The conditions to be met for SSE to apply to a disposal of shares are as follows:

- a) the investing company must have held at least 10% of the ordinary share capital of the investee company for a continuous period of at least 12 months in the six years preceding the disposal; and
- b) the company invested in must be a trading company or the holding company of a trading group (or sub-group) from the beginning of the latest 12-month period in which the above requirement is met until immediately before the sale.

If the conditions are met, then any chargeable gain is exempt from Corporation Tax and any capital loss is not allowable.

### Disposal of shareholding in Sweetcorn Ltd

This disposal should qualify for SSE, as:

- a) Barley plc has held at least 10% of Sweetcorn Ltd for more than a year before the disposal;
- b) Sweetcorn Ltd is a trading company.

This not only means that no chargeable gain will arise on disposal of the shareholding, but also that the de-grouping charge arising in respect of the transfer of business premises will be exempt from tax.

#### Disposal of shareholding in Rye Ltd

This disposal will not qualify for SSE as Barley plc has not held the shares in Rye Ltd for a continuous period of at least 12 months. However, as Barley plc is exchanging shares in Rye Ltd for shares in Clementine Ltd, and Clementine Ltd would be acquiring more than 25% of the ordinary share capital of Rye Ltd, 'share for share' relief is available. Barley plc will be treated as having made neither a disposal nor an acquisition and so no chargeable gain will arise. Instead, for chargeable gains purposes, the new shares (ie the shares in Clementine Ltd) will 'stand in the shoes' of the old shares (ie the shares in Rye Ltd). This means the base cost and date of acquisition of the old shares becomes the base cost and date of acquisition of the new shares.

The transfer of the shares in Rye Ltd will be liable to a Stamp Duty charge of £7 million x 0.5% = £35,000, payable by Clementine Ltd.

#### Disposal of shareholding in Muesli GmbH

This disposal will not qualify for SSE as Muesli GmbH is not a trading company or the holding company of a trading group.

The sales proceeds include an element of contingent but ascertainable consideration. As a result, Barley plc will be taxed upfront by reference to the full £8 million proceeds, resulting in a chargeable gain of £7.5 million (£8 million - £0.5 million).

If Muesli GmbH does not commence trading by the end of the five-year period, Barley plc will be able to make a claim to have the gain recalculated using actual proceeds received of £6 million.

#### Disposal of shareholding in Wheat Ltd

This disposal will not qualify for SSE as Barley plc does not hold at least 10% of the ordinary share capital of Wheat Ltd.

The sales proceeds include an element of contingent and unascertainable consideration. The value of this right to receive future contingent consideration must be estimated and will be added to the £9 million cash proceeds. There will therefore be a chargeable gain equal to £3 million (£9 million - £6 million) plus the value of the right.

The onus will be on Barley plc to provide a valuation of the right. However, the valuation may be agreed with HMRC after the disposal has taken place in order to obtain certainty over the transaction.

When the contingent consideration is received, this is treated as a disposal of the right. There will therefore be a further chargeable gain calculation in the period in which the contingent consideration is received, based on the difference between the original value of the contingent element and the actual amount that is eventually received.

## CIOT MARKING GUIDE

TOPIC	MARKS
<u>Preparation for disposal of Sweetcorn Ltd</u>	
– The group, excluding Wheat Ltd, forms a chargeable gains group.	½
– Transfers of business premises and shares done on nil gain nil loss basis	1
– De-grouping charge arises on business premises as Sweetcorn Ltd leaves group within six years of transfer	1
– Calculation of de-grouping charge	½
– SDLT due on transfer as group relief not available, with explanation	1
– Calculation of SDLT	1
– No Stamp Duty payable on transfer of shares, with explanation	1
<u>Substantial shareholdings exemption</u>	
– Conditions required for SSE to apply	1½
– Effect of SSE if conditions are met	1
<u>Disposal of shareholding in Sweetcorn Ltd</u>	
– Disposal of Sweetcorn Ltd covered by SSE, with explanation	1
– De-grouping charge exempt from tax as SSE applies to the disposal	½
<u>Disposal of shareholding in Rye Ltd</u>	
– Disposal will not qualify for SSE	½
– ‘Share for share’ relief available, with explanation	1
– No chargeable gain and new shares ‘stand in the shoes’ of old shares	1
– Calculation of Stamp Duty charge on transfer of Rye Ltd shares	1
<u>Disposal of shareholding in Muesli GmbH</u>	
– Disposal will not qualify for SSE	½
– Contingent but ascertainable consideration must be included in upfront gain calculation	1
– Calculation of chargeable gain	½
– Future claim available if Muesli GmbH does not commence trading	1
<u>Disposal of shareholding in Wheat Ltd</u>	
– Disposal will not qualify for SSE	½
– Value of right to receive contingent and unascertainable consideration must be estimated and taxed upfront	1
– Valuation may be agreed with HMRC after disposal has taken place	½
– Calculation of chargeable gain	½
– Second chargeable gain calculation will arise in period in which contingent consideration is received	1
<b>TOTAL</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

Almost all candidates showed a good understanding of SSE principles, although many either forgot to apply the SSE conditions to each disposal, or applied them incorrectly to at least one of the disposals. Many correctly identified the contingent consideration although some failed to appreciate the difference in treatment between ascertainable and unascertainable consideration.

It was disappointing that so few mentioned, and even fewer calculated stamp taxes, despite its applicability to the land and building transfer, the transfer of Soya Ltd shares and the acquisition of Clementine Ltd shares.

**8. THETA PLC GROUP**Co-op financing structure1) Alpha 1 Ltd / Alpha 2 Ltd

- These are UK resident companies, subject to Corporation Tax on their worldwide profits.
- For UK tax purposes, Alpha Co-op is treated as a partnership. Where a company is a partner, the partnership profits should be calculated as if the corporate partner had undertaken the activities of the partnership itself. As a result, Alpha 1 Ltd and Alpha 2 Ltd will be taxed on their respective share of the profits of Alpha Co-op.
- The bank loan represents a loan relationship for the corporate partners, as it is a money debt that has arisen from a transaction for the lending of money.
- Each of Alpha 1 Ltd and Alpha 2 Ltd will therefore obtain relief for their respective share of the interest payable and any other losses or expenses in respect of the loan in line with the amounts recognised to the partnership's income statement. These will be non-trading loan relationship debits and can be deducted against any taxable profits arising in the same period, carried back against non-trade loan relationship profits of the previous year, carried forward against future total profits (subject to a restriction on the maximum amount which can be offset over £5m) or surrendered as group relief to other UK group companies.
- Any dividends received by Alpha Co-op (and so Alpha 1 Ltd and Alpha 2 Ltd) from Alpha BV will be exempt income given that they are in respect of ordinary shares.

2) Controlled Foreign Companies (CFC) rulesAlpha Co-op

- For UK tax purposes, Alpha Co-op is not considered to be a company and so it cannot be a CFC.

Alpha BV

- Alpha BV is a foreign company that is controlled by UK persons (Alpha 1 Ltd and Alpha 2 Ltd acting together in partnership) and so it will be considered to be a CFC.
- It is necessary to consider whether Alpha BV is covered by an exemption.
- The Excluded Territories Exemption may apply as The Netherlands is on the list of excluded territories. However, this exemption is not available where the company is involved in an arrangement, the main purpose of which is to obtain a tax advantage. On this basis, it is possible that the exemption would not apply.
- The other exemptions will not be relevant:
  - Exempt period exemption – not relevant as not a newly acquired company.
  - Low profits exemption – not available as profits are more than £50,000.
  - Low profit margin exemption – not available assuming profits are more than 10% of relevant operating expenditure.

- Tax exemption – not available as local tax paid is less than 75% of the corresponding UK tax.
- On the basis that none of the exemptions apply, the gateway tests need to be considered.
- The interest income receivable on the loan will fall under the non-trading financial profits gateway given the funds originated from the UK and were contributed to Alpha BV (the funds originated from Alpha 1 Ltd and Alpha 2 Ltd acting together in partnership).
- Alpha BV may claim the 'Finance Company Partial Exemption' so as to exempt 75% of the profits as they arise from qualifying loan relationships.
- A 'qualifying loan relationship' is a loan relationship (derived from UK capital investments and not generated by UK activities) where the CFC is the creditor and the ultimate debtor is another group company that is not UK resident and which is controlled by the same UK resident persons as control the CFC. As such, the profits on the loan, which ultimately goes to the group's French subsidiaries, should be able to be reduced in this way. In addition, the CFC must have business premises in the territory in which it is resident.
- It can therefore be expected that 25% of the interest on the loan made by Alpha BV may be subject to a CFC apportionment, 12.5% to each of Alpha 1 Ltd and Alpha 2 Ltd.
- The CFC apportionment cannot be offset by the non-trading loan relationship debits arising on the interest payments made by Alpha 1 Ltd and Alpha 2 Ltd. However, relief will be available against the CFC tax for any corporate tax paid by Alpha BV on its interest income.

### 3) Potential challenges

#### Unallowable purpose (s.441 CTA 2009)

- An unallowable purpose in the context of the loan relationship regime is where a loan has no business or other commercial purpose. This includes where one of the main purposes of entering into a loan is tax avoidance. HMRC may argue that one of the main purposes of Alpha 1 Ltd and Alpha 2 Ltd borrowing from the bank through Alpha Co-op is to obtain a UK tax advantage. Any debits attributable to the unallowable purpose would be restricted.
- It would be important to establish the commercial purposes for which the companies borrowed the funds and invested in Alpha BV. The company needs to ask whether the transaction would have been structured in that way but for its ability to claim a tax deduction for its finance expense. Where the tax advantage is mere 'icing on the cake' – an incidental benefit to the commercial purpose – then the rule would not be invoked. We should review the documentation to provide support for the reasons for the structure.

#### Hybrid mismatch rules (Part 6A TIOPA 2010)

- HMRC may argue that the hybrid mismatch rules should apply. These rules, amongst other cases, would restrict deduction in the UK on a financial instrument where relief is also obtained in another jurisdiction.
- These rules apply to counter the effect of a 'double deduction' or a 'deduction/non-inclusion' mismatch. The rules are limited to specific circumstances, but in this case the structure would fall into the hybrid entity category. This is because Alpha

Co-op is treated as a taxable person in The Netherlands and tax-transparent in the UK.

- The hybrid mismatch rules apply regardless of the purpose of the arrangement and therefore it is difficult to see why this would not restrict the whole of the relief claimed in the UK.

#### Residence

- HMRC may look to examine the residence of Alpha BV. For example, if the management of the company is in the UK then it will be subject to UK Corporation Tax on the whole of the interest income. This would be reduced by any double tax relief for tax suffered in The Netherlands, although this is anticipated to be minimal.
- Determining the residence depends on a close examination of the facts. It would be important to show the directors of Alpha BV had control of the company in The Netherlands, and key decisions were not being made in the UK. It would be necessary to consider 'central management and control' for determining UK residence. However, if the company is resident in both the UK and The Netherlands, the tax authorities of both states will have regard, in addition to other criteria, to its 'effective management' in the application of the tie-breaker test to determine the residence of the company.

#### CIOT MARKING GUIDE

TOPIC	MARKS
<u>Alpha 1 Ltd / Alpha 2 Ltd</u>	
– UK companies taxable on their worldwide profits	2
– Each company has a share of the gross debits and credits	1
– Loan relationship definition	1
– Non-trading loan relationship debits	1
– Dividends exempt	1
Sub total	6
<u>CFC</u>	
– CFC Definition	1
– Alpha Co-op not a CFC / Alpha BV is a CFC	1
– No charge if exemption applies	½
– Exemptions	2
– Need to consider if profits fall into one of the gateways	½
– Non-trading financial profits gateway	1
– Finance Company Partial Exemption	1
– Chargeable profits to companies with 25%+ holdings	1
Sub total	8
<u>Potential challenges (*)</u>	
– Unallowable purpose	2
– Anti-hybrid rules	2
– Residency	2
Sub total	6
<b>TOTAL</b>	<b>20</b>

(\*) Credit will be given for other potential challenges that could apply, for example outlining the potential transfer pricing issues with the structure.

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question contained a relatively sophisticated scenario, which candidates may not have come across, but they should have been able to identify the relevant tax technical issues. There was a wide range in the quality of the answers. Those who failed to appreciate that this was essentially a financing arrangement struggled.

It was reassuring that some had a broad understanding that partnerships were treated as transparent but hardly any explained how the taxation of partnerships works. Many went into detail on the rules for investment companies and management expense, without any mention of the loan relationship rules.

On the CFC aspects, most had a reasonable grasp of the rules. However, not everyone identified that the CFC rules only apply to controlled foreign companies. Few showed any knowledge of the full and partial exemptions for qualifying loan relationships under the non-trading financial profits gateway.

Many made valid points around the application of the transfer pricing rules and hybrid mismatch rules. But many incorrectly provided detailed explanation of the diverted profit tax rules and failed to note that they do not apply to profits diverted through holding loan relationships. Hardly any mentioned the possible application of the unallowable purpose rule.

## 9. UNICOMMS GROUP

A number of the provisions in the UK / Zamunda Double Tax Treaty (DTT) are directly relevant to the queries raised by the Zamundan Revenue Authority (ZRA) and should mitigate the potential tax exposures arising from the tax audit.

### Company residence

UZamm Ltd (UZL) is tax resident in the UK by virtue of the fact it was incorporated in the UK. In accordance with the Zamundan Income Tax Act 2013, the company is also likely to be regarded as tax resident in Zamunda as all trading operations are carried out there.

In the absence of a tie breaker test under the DTT, the company would be dual resident. However, Article 4(3) of the DTT addresses the issue where a company is resident in two contracting states under their domestic law.

It states that where a company is a resident of both contracting states, the competent authorities should try to determine in which state it is to be deemed resident by mutual agreement. The commentary to the convention gives details of factors to be considered by the competent authorities in making their decision. These include the usual location of board meetings, where the CEO and other senior management usually carry on their activities, where the company's headquarters are located, which country's laws determine its legal status and where its accounting records are held. This approach differs from the application of the UK concept of central management and control (used to determine whether non-UK incorporated companies are UK resident), which is designated as the place where the Board of Directors meet.

It will be necessary to examine the operating model to determine the likely state in which UZL will be treated as resident; however, it may be the UK if key decisions have been taken there (eg at Board meetings). If the company is Zamundan resident, this would be unlikely to have an immediate impact but may broaden the local tax base in the future as any income or gains realised by UZL from a non-Zamundan source could be subject to tax in Zamunda.

### Permanent establishment

On the basis that UZL is a UK tax resident company, the total taxable profits of the company are taxed in the UK. It would then be sensible to consider making a branch exemption election for UK tax purposes to exempt future income or gains of the branch from UK Corporation Tax.

At present only the activity of the Zamundan branch of UZL is subject to income tax in Zamunda as the branch creates a permanent establishment for UZL in Zamunda.

The ZRA are querying whether the activities of UniComms plc also give rise to a Zamundan permanent establishment. A permanent establishment can be created in a jurisdiction in two ways:

- 1) A fixed place of business – it seems unlikely that UniComms plc has a physical office, branch or place of management in Zamunda (on the basis UZL does) and as such would not have a fixed place of business.
- 2) A dependent agent - The activities of UniComms plc employees and directors in Zamunda could be construed as giving rise to a dependent agent permanent establishment. Article 5(5) of the DTT states that a permanent establishment is created if such individuals habitually conclude contracts in the name of UniComms plc while present in Zamunda.

The engineers are unlikely to meet this test because they did not have the authority to conclude contracts. Their role was to design the telephone masts as part of the services UniComms plc provided to UZL under the Intra-Group Services Agreement.

The activities of the Executive Sales Director should be closely reviewed going forward. As the key contract referenced was executed in the UK and there is nothing to suggest that such contracts are *habitually* negotiated in Zamunda, it is unlikely that a permanent establishment has been established there with regard to prior activities.

#### Management and consultancy fees

The £30 million charge in respect of design work by the engineers employed by UniComms plc has been designated a 'Management and Consultancy Fee'. Such amounts are subject to withholding tax (WHT) under local legislation at a rate of 20%.

Article 7(1) of the DTT is clear that the profits of a Contracting State (in this case the UK) shall be taxable only in that State unless attributable to a permanent establishment in the other Contracting State. On the basis that UniComms plc does not have a Zamundan permanent establishment, the profits should be solely taxed in the UK with no Zamundan WHT applicable.

The local WHT on management and consultancy fees of £6 million should not be payable as it is excluded under the DTT.

#### Royalties

Article 12(3) of the DTT defines 'royalties' as including any consideration paid for the use of a patent. The £20 million payment to UniComms plc for patented technology should therefore meet this definition.

Pursuant to Article 12(2), any tax withheld at source should be limited to 5% where the beneficial owner of the royalties is a resident of the other Contracting State. This condition is satisfied as UniComms plc is the owner of the patent and a UK tax resident company.

The WHT due in respect of the royalty payments should therefore reduce to £1 million (ie 5% of the £20 million gross payments).

#### Conclusion

The provisions of the DTT are relevant to the tax audit as follows:

- 1) UZL is likely to be solely a UK tax resident company although the company's operating model should be reviewed in detail to determine this.
- 2) UniComms plc should not have a Zamundan permanent establishment during the period under audit. Care should be taken in this area going forward.
- 3) The £10 million WHT assessment should be reduced to £1 million.

#### **Tutorial Note:**

The articles of the UK/Zamunda DTT reproduced in this question are based on the 2017 Update to the OECD Model Treaty; the original question quoted from the pre-2017 version of the treaty. The majority of the UK's Double Tax Treaties were negotiated before 2017 and so use the wording from older versions of the Model Treaty, and the UK has not adopted all of the changes to Article 5. You can find a copy of the UK/Germany double tax treaty, which is based on an earlier version of the OECD Model Treaty, at Misc 39 in Part 2 of your Yellow Tax Handbook; but do take care that the wording of Articles 4(3) and 5(5) of the Model Treaty has now altered.

## CIOT MARKING GUIDE

TOPIC	MARKS
<u>Company residence:</u>	
State UZamm Ltd UK tax resident by virtue of incorporation	1
State company also likely tax resident in Zamunda based on the fact all activities conducted there	1
Comment that in the absence of treaty tie breaker test UZamm Ltd would be a dual resident company	1
State residency determined by mutual agreement under Article 4(3) of double tax treaty but looks at a number of factors	2
Explain that central management and control carried out in the UK	1
Draw distinction between central management and multi-factorial approach	1
Note that if UZamm Ltd Zamundan tax resident, may broaden tax base in the future	½
<u>Permanent establishment:</u>	
Recommendation that UZamm Ltd make a branch exemption election	1
State that UniComms plc should not have a fixed place of business	1
Note risk of dependent agent permanent establishment	1
Refer to Article 5(5) and requirement to habitually conclude contracts	1½
Comment why engineers unlikely to be regarded as dependent agents	1
Comment why Executive Sale Director unlikely to be regarded as dependent agent	1
<u>Management and consultancy fees:</u>	
State Article 7(1) should be applicable such that fees only taxable in UK	1
Comment that should result in £6 million reduction in WHT assessable on the basis UniComms plc has no Zamundan permanent establishment	1
Refer to guidance on OECD Model Treaty around non-resident services	1
<u>Royalty:</u>	
State that payment for use of patents should meet the definition of a Royalty under Article 12(3) of the treaty	1
Comment that reduced WHT rate of 5% should be applicable under Article 12(2) of the treaty	1
Calculate reduced WHT assessable applying treaty rate of WHT	1
<b>TOTAL</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

The issues regarding company residence were generally dealt with well by candidates and most correctly identified that UZamm Ltd (UZL) is dual resident company that is likely to be resident in the UK. Most could demonstrate a good understanding of the principles relating to central management and control and place of effective management.

A good number of candidates could identify the risks of Unicomms plc having a permanent establishment in Zamunda. A minority conflated these issues with company residence as opposed to focusing on the activities of UZL.

The withholding tax issues related to payment of the patent royalty were dealt with relatively well. Many candidates identified the applicability of Article 12(3) of the double tax treaty (DTT). Only a small number of candidates were able to determine that no withholding tax should apply to payment of the management and consultancy fees in view of Unicomms plc having the sole right to tax business profits under Article 7(1) of the DTT.

Few candidates pointed out that a branch exemption election could be usefully made by UZL, but most highlighted the potential for double tax relief.

## 10. TRIPLETREE GROUP

### Definition

A controlled foreign company (CFC) is a company which is not resident in the UK and which is controlled by a UK resident person or persons.

Control of a non-UK resident is established if a person has:

- the power to secure that the affairs of the company are conducted in accordance with their wishes, or
- a shareholding of more than 50% in the company.

Control is also established where two persons together control the non-UK resident company and one is UK resident with a shareholding of at least 40% and the other is non-UK resident with a shareholding of not more than 55%.

All the non-resident companies apart from Tripletree (Deo) Ltd are controlled by UK persons as they are 100% owned by Tripletree (UK) Ltd. They are all therefore CFCs apart from Tripletree (Deo) Ltd.

When a company is a CFC, it is possible that the profits it makes will be taxable in UK. If the profits are taxable, they will be taxed at the main UK Corporation Tax rate, but the company should get credit for any foreign tax paid.

The profit of the CFC may be apportioned to the UK company holding the shares based on its percentage interest in the CFC.

However, there are entity-focussed exemptions and other tests commonly known as gateway tests, which may eliminate the CFC charge.

The CFC legislation does not specify an order between the exemptions and the gateways and companies can consider the exclusions in any order.

### Exemptions

- 1) Exempt period. This is a temporary exemption which can apply in the 12-month period when a company first becomes a CFC. As Tripletree (UK) Ltd has owned all the companies for more than five years this does not apply to any of the CFCs.
- 2) Excluded territories. Companies which are resident in certain territories named in Statutory Instrument can be exempt subject to meeting certain criteria. The criteria include that the company must carry on a business in the excluded territory and that the company must be liable to tax in the relevant territory. A list of the excluded territories is available online at gov.uk but none of the countries in the Tripletree plc group are on that list.
- 3) Low profits exemption. This applies if a company's accounting profits, or taxable total profits are less than £50,000. It also applies where accounting profits or total profits are less than £500,000 and not more than £50,000 is non-trading income. This exemption should apply to Tripletree (Ena) Ltd, and no CFC apportionment will be necessary for this company.
- 4) Low profit margin exemption. Where a company's profit margin is less than 10%, this exemption can apply. The operating expenditure brought into account in determining accounting profits for the relevant period is used as the basis for calculating the profit margin for the purposes of this exemption. This exemption should apply to Tripletree (Tesera) Ltd since it charges cost plus 7% for its services.

- 5) Tax exemption. If the tax paid in the territory where the CFC is resident is more than 75% of the UK Corporation Tax that would be paid if the CFC were UK resident, this exemption may apply. As the rate of corporate taxes in Trialand is 22% then this exemption applies to Tripletree (Tria) Ltd.

None of the exemptions apply to Tripletree (Pendeland) Ltd. It is necessary to consider the gateway tests to identify if any of its profits need to be apportioned to Tripletree (UK) Ltd.

#### The five gateway tests

The above exemptions look at a CFC as an entity and therefore if they apply, all the company's profits will be exempt. The gateway tests may apply to some or possibly all of a non-exempt CFC's profits. For profits of a CFC to be apportioned to Tripletree (UK) Ltd, they must pass through at least one of five gateways. However, as Tripletree (Pende) Ltd only had profits from the provision of management and technology services to other group companies, the following four gateways do not apply:

- non-trade finance profits,
- trade finance profits,
- captive Insurance, and
- solo consolidation.

The fifth gateway is 'profits attributable to UK activities'. Profits do not pass through this gateway if any of the following conditions are met:

- 1) The motive test - there are no assets held or risks undertaken with the main purpose of reducing or eliminating UK tax.
- 2) The company has no assets managed from the UK and bears no UK risks.
- 3) The company can operate effectively without any assistance from the UK.
- 4) The company's profits are only from property or from non-trading loan relationships.

#### Significant people functions

Any CFC profits for which the related significant people functions are undertaken outside the UK will not be subject to a CFC charge as they will not pass through this gateway. Significant people functions are the key business and management functions relating to the control of assets and the management of risk. The significant people functions should be considered in the context of the business, and would involve functions that require active decision-making regarding the management of business risks and business asset.

#### Safe harbour conditions

This gateway also does not apply to the company's trading profits if all of the following 'safe harbour' conditions are met.

- 1) Business premises. The company must have a physical presence in the country of residence. This must be where its main activities are carried out and have a degree of permanence (usually more than twelve months).
- 2) The company must derive no more than 20% of its relevant trading income directly or indirectly from the UK.
- 3) The company must not incur costs of management in the UK which exceed 20% of its total costs of management expenses.

- 4) The company must not derive income from intellectual property which was transferred from the UK within the last six years.
- 5) The company must not derive more than 20% of its income from the export of goods from the UK.

Tripletree (Pende) Ltd has offices in Pendeland and most of the other conditions appear to be met, although it is unclear how much of the company's trading income comes from charges to the group's UK companies.

However, all profits of Tripletree (Pende) Ltd are from management services carried out in Pendeland. There does not appear to be any significant people functions carried out in the UK and the company does not manage and control any UK assets or risks.

Therefore, the profits of the company do not pass through any of the gateways and there will be no need to apportion any of those profits to Tripletree (UK) Ltd.

### MARKING GUIDE

TOPIC	MARKS
Definition of a CFC	1
Meaning of control	1
Identify the CFCs (all but Deo)	1
Apportionment subject to exemption and gateway tests	<u>1</u>
Subtotal	4
Exempt period	$\frac{1}{2}$
Excluded territories	1
Low profits exemption Tripletree (Ena) Ltd	1
Low profits margin exemption Tripletree (Tesera) Ltd	1
Tax exemption (Tesera)	1
No exemptions apply to Pende	<u><math>\frac{1}{2}</math></u>
Subtotal	5
The four gateway tests that do not apply to Pende	<u>2</u>
Subtotal	2
UK activities – four tests	1
The four tests	2
SPF define and explain	1
Safe harbours	1
Business premises	1
Four other safe harbours	<u>2</u>
Subtotal	8
Conclusion	1
<b>TOTAL</b>	<b>20</b>

#### Examiner's report:

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question concerned a UK headed multi-national telecommunication group with interests in a number of non-UK resident companies. Candidates were provided with information about shareholdings, activities, and financial data, and were required to explain how the UK's Controlled Foreign Companies legislation applied to the group.

The question was answered well for the most part. Most candidates correctly identified which of the overseas companies came within the legislation, and where the appropriate exemptions applied. None of the exemptions applied to one of the companies and therefore the profit

gateways needed to be considered. In general, candidates dealt with the exemption rules much better than the gateway rules.

The main area where some candidates lost marks was consideration of what constitutes control for the purposes of this legislation, with candidates confusing the 25% shareholding required to be subject to apportionment, and the control tests.

Many candidates correctly stated that only one of the exemptions needed to apply to a company but having identified one such exemption, then went on to discuss why the other exemptions did not apply, which was not required.

## 11. LUCZO LTD

Corporation Tax Computation

Period ended 30 June 2025

	Notes	£	£	
Profit before tax per financial statements			16,133,115	
Add:				
Depreciation		871,347		[½]
Excess pension contribution	1	387,500		[½]
Fraud by Director	2	50,000		[½]
Gifts	3	7,000		[½]
Employee bonuses (100 x £500)	4	50,000		[½]
General bad debt provision	5	400,000		
Non-trading interest paid	6	1,357,888		[½]
Planning fees	7	<u>5,000</u>		[½]
			3,128,735	
Less:				[½]
Bank interest received		1,986,125		
Dividends received		42,000		
Profit on disposal of shares		4,512,347		[½]
Property income	8	<u>0</u>		[½]
			<u>(6,540,472)</u>	
Adjusted profit for the 15 m/e 30 June 2025 before capital allowance			<u>12,721,378</u>	
	Notes	y/e	3m/e	
		31/3/25	30/6/25	
		£	£	
Adjusted profit (time apportioned)		10,177,102	2,544,276	[½]
Capital allowances	10	<u>(3,386,474)</u>	<u>(960,977)</u>	[½]
Trading profit		6,790,628	1,583,299	
Chargeable gain ( <b>SSE not available</b> )		4,512,347	0	[½]
Non-trade loan relationships	9	<u>502,590</u>	<u>125,647</u>	
Total Profits		11,805,565	1,708,946	
Relief for NTLRD b/f	11	<u>(1,590,076)</u>		[½]
Taxable Total Profits		<u>10,215,489</u>	<u>1,708,946</u>	
Tax at 25%		<u>2,553,872</u>	<u>427,237</u>	[1]

**Tutorial Note:**

This computational question should offer easy marks, but only if you start with the correct approach for a **long period of account**. First **identify the two chargeable accounting periods**. Set up your answer with clearly labelled columns showing the relevant dates. You must then allocate the different income streams and gains to the two periods.

Trading profits are **time apportioned** but make sure you perform the apportionment at the correct stage, that is, **after** making the adjustments to profit, and **before** deducting capital allowances. There are many marks available for the adjustments, most of which rely on knowledge from your earlier studies, and for the two separate capital allowance calculations. The key is taking a moment to get your approach right, before rushing to start the calculations.

By contrast, the **gain is allocated to the period in which it arises** (ie when the disposal takes place, which, in the case of a sale, is the date the contract is made, not completed). If you have laid out your answer correctly, it will be easy to slot this figure into the correct column.

When concentrating on these aspects, it is easy to forget the basics – remember to finish addressing the requirement by calculating the tax itself, at the appropriate rates, for an easy final mark.

Notes

1. The additional pension contributions are **more than 210%** (or 2.1 times) the amount in the previous period. As such there is an excess. The excess is the amount of the contribution in the current period (£912,500) that **exceeds 1.1 times** the contribution in the previous period, adjusted to reflect the longer period ( $£100,000 \times 1.1 \times 15/12 \text{ months} = £137,500$ ). [1]

The excess amount is £775,000 (£912,500 – £137,500). As the amount of the **excess is more than £500,000** the deduction of the excess amount is **spread over two periods**. So it is **£387,500 per period**. The total deduction for the period ended 30 June 2025 will be £525,000 (£137,500 + £387,500). The remaining £387,500 paid will be deducted in the tax computation for the next chargeable period. [1]

**Tutorial Note:**

There are several steps to the spreading provisions, with two relevant percentages. **210%** is used when working out whether contributions must be spread. **110%** is used when calculating the excess amount to spread. The amount of the excess determines the number of periods over which the excess is spread. If the excess is less than £500,000, no spreading is required.

After performing the calculations, make sure you make the correct adjustment. It is the disallowable amount (**the amount spread to future periods**) that **must be added back**.

In this question the calculation is further complicated by the long period of account but remember that follow-through marks should be awarded if you struggle with that aspect.

2. The fraud by the Director is not an allowable deduction as it is **not** a loss **connected with** or arising out of **the trade**. In this instance directors are not treated the same as employees, where the deduction is permitted (see the *ATA Advertising Ltd* case) [½].
3. The expenditure on the gifts was **over £50 per item** per customer. Despite the fact that the vases advertised the company's name, the amount is disallowed [½].
4. The bonuses were **not paid within nine months of the period end** so will be deducted in the period when paid [½]. Staff entertaining is an allowable deduction [½].
5. The provision against the specific debt is allowable, but the general provision of £400,000 (£1,100,567 – £700,567) will be **added back** as it is **unlikely to have been ascertained in accordance with GAAP**. A deduction will be permitted if and when the debt is actually written off. [½]

**Tutorial Note:**

Under both IAS 37 and FRS 102, the rules on recognition of provisions are very strict and do not permit the recognition of general provisions. Thus, if the accounts are compatible with either IAS or UK GAAP, any provision permitted for accounting purposes must also be allowable for tax purposes. Since the question specifically states that there is a general provision in the accounts, the assumption must be either that the accounts are not GAAP compliant (in which case, you would need to disallow the general provision) or that the accounts are GAAP compliant, in which case the 'general' provision must have been measured with sufficient accuracy to permit it to be deducted for tax as well as accounting purposes. As long as you explain your reasoning, therefore, you can choose which assumption to make and thus whether there is a disallowance for the general provision or not.

6. The interest in respect of the company's overdraft used to fund working capital for Luczo Ltd's business is an allowable deduction against trading profits (a trading loan relationship debit). The interest paid in respect of the loan to acquire the shares in Stanmarky Building Ltd is a **non-trading loan relationship debit as the shares are held as an investment**. As the interest capacity of the company is sufficiently large, the full amount of the net interest payable is deductible and none is subject to disallowance under the CIR regime. [½]

**Tutorial Note:**

The **non-trading interest payable is added back** in the adjustment to profit calculation to give trading profits. Remember adjustments are made for the entire 15-month period (before apportionment) so the whole figure is added back.

7. It is assumed that the planning fees have been deducted in the profit and loss account so are **added back as they are capital expenditure**. They will not qualify for structures and buildings capital allowances but will be deductible as enhancement expenditure should the factory be sold. [½]
8. The part of the company's factory which has been rented out is not treated as property income as it is assumed that it is **temporarily surplus** to requirements and the receipts are small. It is assumed that the company is using the factory for its trade [½].

**Tutorial Note:**

Rent receivable from letting a property is usually treated as property income but do not forget this exception, which is not frequently tested.

9. Non-trade loan relationship debits and credits are time apportioned.

	15 months	ye 31/3/25	3m/e 30/6/25	
	£	£	£	
Interest payable	(1,357,888)	(1,086,310)	(271,578)	
Interest receivable	1,986,125	<u>1,588,900</u>	<u>397,225</u>	
		<u>502,590</u>	<u>125,647</u>	[½]

**Tutorial Note:**

When calculating **non-trade loan relationships**, the **interest payable is time apportioned** between the periods provided the loan existed for the whole 15-month period. Otherwise a calculation will have to be performed showing the interest accruing in each accounting period.

## 10. Capital allowances

	AIA/FYA £	General Pool £	Allowances £	
<u>YE 31/3/25</u>				[½]
TWDV b/f @ 1/4/24		18,258,190		
Additions:				
15 Jan 2025 – Plastic moulds	100,000			
AIA	<u>(100,000)</u>		100,000	
WDA@18%		<u>(3,286,474)</u>	<u>3,286,474</u>	
TWDV c/f @ 31/3/25		14,971,716		
Total allowances			<u>3,386,474</u>	
 <u>3me 30/6/25</u>				
Additions:				
1 June 2025 – Plastic moulds	250,000	<u>50,000</u>		
AIA (max 1,000,000 × 3/12)	<u>(250,000)</u>		250,000	[1]
		15,021,716		
WDA @18% × 3/12		<u>(675,977)</u>	675,977	[1]
30 June 2025 – Plant	35,000			
FYA @ 100%	<u>(35,000)</u>		35,000	[½]
TWDV c/f @ 30/6/25		<u>14,345,739</u>		
Total allowances			<u>960,977</u>	

The writing down allowance and annual investment allowance (AIA) are time apportioned in the three-month accounting period. The first-year allowance for the new plant is not time apportioned.

**Tutorial Note:**

When a question involves a **long period of account**, there will be **two separate capital allowance computations**. You will need to consider the effect on your calculations of the **second period being shorter than 12 months**. Here, the AIA and WDA are affected, but the FYA is not.

The expenditure on the plastic moulds has been split between the two periods as the second payment was made **more than four months after the unconditional obligation** to pay for them arose (ie date of delivery on 15 January 2025). The FYA is not available as the assets were not new when purchased, so use of the AIA is prioritised for these assets, with 100% FYA claimed on the new plant. [1]

**Tutorial Note:**

Take care to apply the rules for when expenditure is incurred. The different dates given in the question should have prompted you to consider the **four-month rule** given in CAA 2001, s.5(5).

11. The **non-trading loan relationship deficits** brought forward at 1 April 2024 can be **offset against total profits** in the period ended 31 March 2025. The relief is not automatic, and the company must submit a **claim by 31 March 2027**, stating the amount of the deficit to be offset. Having claimed the deductions allowance the relief available is the lower of the NTLR deficit carried forward of £1,590,076 and £5,000,000 + ½ × (£11,805,565 – £5,000,000) = £8,402,783. [½]

**Tutorial Note:**

Make sure you go back to the question, after performing lots of calculations, and check that you have dealt with all information and amounts. This deficit could easily be forgotten but would give a quick mark if remembered.

Deferred Tax

		£	
Net book value c/f at 30 June 2025		21,250,875	
Main pool c/f at 30 June 2025		<u>(14,345,739)</u>	
		6,905,136	[½]
Bonuses not paid		(50,000)	[½]
Pension payment spread		(387,500)	[½]
General bad debt provision		<u>(400,000)</u>	[½]
		<u>6,067,636</u>	
Deferred tax provision at 30 June 2025	(25%)	<u>1,516,909</u>	[½]

**Tutorial Note:**

The deferred tax provision is the future tax expected due to **timing differences between accounting and tax treatments**. As the **net book value of plant exceeds the remaining tax written down value**, depreciation in future will exceed capital allowances, **increasing the future tax charge**. However, deductions will be available in the following period for the bonuses and the pension payments, which have so far been disallowed. Also, a future release of the general bad debt provision will not be taxed but will increase profits in the accounts. Therefore, **the bonuses, pension spread, and bad debt provision reduce the expected tax charge in future**, that is, they **reduce the deferred tax provision**.

The rate used in the deferred tax calculation should reflect the **corporation tax rate applicable when the timing differences are expected to unwind**. The corporation tax main rate for FY 2025 and FY 2026 is 25%, and so this is the rate used here.

## MARKING GUIDE

TOPIC	MARKS
<u>Tax computation</u>	
– Add back depreciation:	½
– Add back/discussion of bad debt general provision (s.55 CTA 2009)	½
– Staff party not adjusted (s.1299 CTA 2009)	½
– Deduction of capital gain in trading profit calculation and allocation to correct period, including note that SSE not available	1
– Deduction of bank interest receivable and dividends in trading profit calc	½
The following adjustments score ½ for add back or not as appropriate and ½ for supporting explanation:	
– Fraud by the Director (s.54 CTA 2009)	1
– Gifts (s.1300 CTA 2009)	1
– Staff bonus (s.1288 CTA 2009)	1
– Rental of part of the factory (s.44 CTA 2009)	1
– Planning fees (allowance if assumed capitalised or expensed)	1
– Treatment of trading & non-trading interest paid (s.297 CTA 2009)	1
<u>Capital allowance computations</u>	
– Computation separating out the two periods and acquisitions	1
– Apportionment of writing down allowances for short period	1
– Apportionment of AIA for short period	1
– S.5(5) CAA 2001 application on plastic moulds	1
– First year allowance	½
<u>Pension</u>	
– Spreading calculation	1
– Relevant excess contributions	1
– Disallowable amount	½
Apportionment of trading profit and NTLR between accounting periods	1
Calculating tax on taxable total profits	1
Relief for NTLR deficits brought forward (s.463G CTA 2009)	1
	Max 18
<u>Deferred tax</u>	
– ACAs	½
– Bonus	½
– Pension payment	½
– Bad debt general provision (if disallowed above)	½
– Calculation	½
	Max 2
<b>TOTAL</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question was a straightforward computational question covering a long period of account. Most candidates scored well on the computational elements of the question, but struggled with the pension spreading element. Whilst many candidates recognised that there was an excess pension contribution which needed to be spread; only a very small number of candidates were able to work out the excess contribution and calculate the disallowance correctly. The longer accounting period made this more challenging. The fifteen month accounting period also caused many candidates difficulty, whilst most recognised that the capital allowances needed to be split into two periods, many did not apportion the writing down allowances for the second three-month period and gave allowances for the whole period. In addition, many candidates were confused as to which point to apportion trading profits, gains and Non-Trade Loan Relationship Debits and Credits and to which period they should be allocated exclusively or apportioned across the fifteen months. Many candidates also struggled with the Non-Trade Loan Relationship Deficit brought forward and how this could be relieved. Candidates either forgot about this or thought it could only be relieved against the interest received. A significant proportion of candidates attempted the deferred tax part of the question. Most however did not recognise that the pension spreading, staff bonuses not paid within nine months of the period end and bad debt provision formed part of the calculation.

## 12. CIRCLE LTD

Circle LtdTax computation – year ended 30 September 2026

	£	
Trading profit	Nil	
Non-trade loan relationship credit	Nil	
Chargeable gain (Note 1)	16,308	
Less non-trading loan relationship deficit (Note 2)	(2,782)	
Less current year trading loss	<u>(13,526)</u>	
Taxable total profit	<u>Nil</u>	
Tax to pay	<u>Nil</u>	
Taxable profit in previous year (y/e 30 September 2025)	120,000	
Loss carried back	<u>(84,194)</u>	[1]
Taxable profits (revised)	<u>35,806</u>	
Tax at 19%	6,803	[½]
Tax already paid	<u>(28,050)</u>	
Tax to be repaid	<u>(21,247)</u>	[½]

**Tutorial Note:**

Corporation tax for the previous year, the year ended 30 September 2025, was originally paid at 25% less marginal relief. Therefore, the loss carried back saves tax mostly at 26.5% (on £70,000 profits falling between the upper and lower limits), and some tax at 19%. If the company is expected to make sufficient profits in the future, it may be that **carrying the losses forward could save tax at a higher rate** (all at 26.5%). However, the additional tax saving would be small, and this use of the loss **would not be beneficial for cash flow** – a refund now, by carrying the loss back, may well be preferred.

Tax Adjustments

Loss before tax	Note	£	£
			(511,202)
Add:			
Depreciation		211,000	[½]
Excess pension contribution	3	262,500	
Loss on disposal of land	1	17,000	
Legal costs	4	73,000	
Compensation costs	5	50,000	
Entertaining costs	6	13,000	
Interest payable re loan	2	30,000	
Loss on disposal re plant		<u>40,000</u>	[½]
			696,500
Less:			
Dividend receivable	7	45,000	
Capital allowances	8	210,800	
Interest receivable	2	<u>27,218</u>	
			<u>(283,018)</u>
Trading loss			<u>(97,720)</u>

Loss working

	Trading losses £	Non-trade loan relationship deficit £	
Loss arising during the year	97,720	2,782	
Offset against chargeable gain arising in the year	(13,526)	(2,782)	<b>[1]</b>
Carried back against prior year profits	<u>(84,194)</u>		
Carried forward at 1 October 2026	<u>Nil</u>	<u>Nil</u>	

**Tutorial Note:**

Relief is given for the NTLR deficit **before** relief for trading losses in the current period by virtue of s.463D(4) CTA 2009. Although it does not arise in this question, current year relief for losses incurred in a UK property business are relieved after NTLR deficits and before trading losses.

Capital allowance working

Note	AIA £	Main pool £	Special rate pool £	Allowances claimed £	
TWDV at 1 Oct 2025		275,000	196,000		
<u>Additions not qual for AIA:</u>					
New Audi car 8(a)			<u>25,000</u>		
Second hand Nissan car 8(a)		<u>3,000</u>			
<u>Additions qual for AIA:</u>					
Electrical and hot water systems 8(c)	162,500				
Pipe cutting equipment 8(c)	50,000				
IT equipment 8(c)	25,000				
Lorry 8(c)	<u>15,000</u>				
	252,500				
AIA	<u>(252,500)</u>			252,500	<b>[½]</b>
	<u>Nil</u>				
		278,000	221,000		
WDA (18%/6%)		<u>(50,040)</u>	<u>(13,260)</u>	<u>63,300</u>	<b>[½]</b>
TWDV at 30 Sept 2026		<u>227,960</u>	<u>207,740</u>		
CAs claimed				<u>315,800</u>	
Total allowances <b>less balancing charge</b> (note 8(b))					
= £315,800 – £105,000					
= £210,800 <b>[½]</b>					

Notes

- 1) The gift of land will be treated as a disposal of a chargeable asset. Proceeds of sale are deemed to be the market value at time of sale.

	£	
Deemed sale proceeds (= <b>market value</b> of land)	38,000	
Cost of land	(17,000)	
Indexation factor (December 2009 to December 2017) (0.276 x 17,000)	<u>(4,692)</u>	
Chargeable gain on disposal of land	<u>16,308</u>	<b>[1]</b>

Calculation of indexation factor:  $(278.1 - 218.0)/218.0 = 0.276$  (to 3dp).

- 2) Interest payable (£30,000) in the current year relating to the **loan to purchase an interest in WCL Ltd** is a **non-trade loan relationship debit** and will **automatically be offset against the interest receivable** (£27,218) in calculating the **net NTLR credit/deficit** for the year [½]. The NTLR deficit (£2,782) incurred in the year can then be used to **offset against other profits** in the period [½]. This would be **used before the trading loss** [½]. Assuming the rest of the interest relates to a **loan used to obtain working capital** for use in the trade, a **deduction against trading profits** may be claimed for the remaining interest payable [½].
- 3) The additional pension contributions (£550,000) are **more than 210% of the amount in the previous period** (£250,000) [½]. There is, therefore, an 'excess' which is the amount of the contribution in the current period that is **more than 1.1 times the contribution in the previous period** – so £525,000 ((£800,000 – (1.1 × £250,000)) [½]. £525,000 is **greater than £500,000** and therefore the deduction for the £525,000 will need to be **spread over two periods**. This amount is split equally (£525,000/2 = £262,500) over the current chargeable period and the next chargeable period [½]. **£262,500** will therefore be **disallowed** in the year to 30 September 2026 and deducted in the next period [½].

**Tutorial Note:**

The spreading provisions use two relevant percentages. **210%** is used when working out whether contributions must be spread. **110%** is used when calculating the excess amount to be spread. The amount of the excess determines the number of accounting periods over which the excess is spread. **As the excess here is over £500,000, it is spread over two periods.**

Make sure you make the correct adjustment to trading profits. The disallowable **amount to be added back is the amount spread to the later periods.**

- 4) Legal costs
- a) £73,000 relates to **proposed capital expenditure**, being the extension of the factory, and so is **disallowed**. The fact the plans to extend were abortive does not impact on this [1].
- b) £20,000 relates to **defending title to land already owned** by Circle Ltd, which is **used in the trade**. The expenditure is incurred to maintain the existing position **without addition or improvement**, so is **allowable** [1].
- 5) The damage to the house triggered by the collapsing tree is caused by Circle Ltd in its capacity as property owner not as a trader, and so the compensation payment is **not deductible**. It is **not a loss connected with** or arising out of the **trade** [1].
- 6) The **staff party costs** of £2,000 are **deductible** [½]. The pens are **not deductible** since they **cost more than £50 each**. The rest of the entertaining costs are **disallowable** [½].

7) The dividend of £45,000 from WCL Ltd **benefits from the portfolio exemption** within the dividend exemption legislation on the basis that Circle Ltd **owns less than 10%** of the share capital of WCL Ltd [1]. So the dividend is **not taxable**.

8) Capital allowances

a) The Nissan has vehicle emissions of **less than 50g/km** so the cost is allocated to the **main pool** [½]. The Audi's emissions are **higher than 50g/km** and so the cost is allocated to the **special rate pool** [½].

b) The proceeds on disposal are:

Net book value of assets disposed of (plant)	£	
(= 223,000 – 78,000)	145,000	
Loss on disposal (plant)	<u>(40,000)</u>	
Proceeds on disposal	<u>105,000</u>	[1]

A **balancing charge** arises as the **super-deduction would have been claimed** on the equipment purchased new on or after 1 April 2021 and on or before 31 March 2023. The charge is 100% of the disposal value (proceeds) ie the balancing charge is **£105,000** [1].

**Tutorial Note:**

Where items of plant are disposed of, remember to think about **whether the company will have claimed enhanced first year allowances** when the plant was bought, as **this will determine the disposal treatment**. Here the question clearly indicates that the equipment was bought new, within the period between 1 April 2021 and 31 March 2023, and that maximum allowances were claimed, ie the super-deduction was claimed.

Where the super-deduction has been claimed on an asset which is then disposed of, the disposal proceeds are not deducted from the main pool. Instead, for an accounting period of disposal beginning on or after 1 April 2023, **a balancing charge is calculated as 100% of disposal value**.

c) All items of plant are **newly purchased**, and so, except for cars, qualify for enhanced first year allowances [½]. The **electrical and hot water systems** qualify for **50% FYA**, but as the **Annual Investment Allowance (AIA)** is also available giving 100% relief, it is **better to claim AIA** [½]. The **pipe cutting equipment, IT equipment and lorry** qualify for the **100% FYA (full expensing)** or the 100% **AIA** [½]. As there is sufficient AIA available (£1,000,000 limit), it is **better to claim the AIA to avoid the immediate balancing charge** that would arise on a future disposal of plant on which the FYA has been claimed [½].

**Tutorial Note:**

The plant purchases qualify for the enhanced FYAs as they were **purchased new**. However, the AIA is usually the preferred option, if the limit is not exceeded. As the requirement asked for supporting explanations, you should explain this decision.

Although the computers have a useful life of less than eight years, there is **no advantage** to be obtained in making a **short life asset election** as the expenditure on them qualifies for the AIA, and so immediate 100% relief is given.

## CIOT MARKING GUIDE

TOPIC	MARKS
Add back depreciation and loss on disposal	1
Excess pension contribution and explanation	2
Gift of land	1
Legal costs re abortive expenditure	1
Legal costs re defending title to land	1
Compensation payment to neighbour (Strong & Co of Romsey Ltd v Woodifield (1906) 5 TC 215).	1
Entertaining costs	1
Treatment of dividend	1
Plant additions: first year allowances vs Annual Investment Allowance	3
Allocation of motor vehicles	1
Calculate disposal proceeds and balancing charge	2
Compute writing down allowance and capital allowance claim	1
Trading loss	1
Loan relationship debits and credits, priority rules. (S463D CTA 2009)	2
Loss carry back and tax refund.	2
<b>TOTAL (MAX)</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

Overall, the question was very well answered. Candidates showed a good knowledge of how to compute the taxable trading profits of a company and were able to identify the disallowable costs incurred by Circle Ltd.

Candidates showed a strong knowledge of capital allowances and were able to establish what assets qualified for each allowance. Many candidates ... dealt effectively with [calculating] the disposal proceeds in relation to the packing equipment. [The treatment of the disposal of the equipment has changed since the question was originally set.]

Most candidates were able to distinguish between trading and non-trading interest and were able to identify and compute the loss carry back.

Points of difficulty included the disposal by way of gift, which is a chargeable gain with proceeds deemed to be market value. Some candidates thought that the amount spent on the ownership dispute with the neighbour were capital in nature when in fact they were likely to be deductible from the trading profits.

## 13. CHARLESE PLC

Capital allowances claim:

Detail	Amount	Reference to Notes
	£	
Main pool – WDA	147,600	N1
Main pool – annual investment allowance	1,000,000	N1
R&D allowances at 100%	250,000	N1
Main pool – full expensing (FYA @ 100%)	5,530,000	N1
WDA on assets acquired from Francis Ltd	135,000	N2
Special rate assets – FYA @ 50%	200,000	N3
Special rate assets – WDA	6,000	N4
Structures and Buildings allowance	<u>30,000</u>	N5
Total	<u>7,298,600</u>	

**Tutorial Note:**

There are many items of expenditure in the question that you must use to calculate capital allowances. You may not have set out your answer like this, but you need a methodical approach, working through the information and dealing with each item. Consider whether the expenditure is on **buildings or plant**, the **relevant pool**, **whether FYAs are available and at what rate**, the **best use of the AIA** and the availability of **SBA**s.

In addition to capital allowances, the requirement also asks for '**other adjustments** required to arrive at taxable profits'. Therefore, you also need to consider **revenue deductions**, the treatment of **depreciation** (including that for the special case of **finance leased** assets), the effect of a **profit on disposal** (on trading profit and in terms of the gain arising) and the result of a **land remediation claim**. This answer presents deductions and additions separately. However, credit would be given for alternative presentations provided your answer is clearly labelled so your treatment of each adjustment is clear.

Other deductions from taxable profits:

Detail	Amount	
	£	
<b>Finance lease – depreciation is claimed</b> as the asset is not owned (£2m x 20%)	400,000	[1]
Decorating – this is <b>revenue expenditure – claim for depreciation</b> (£100,000 @ 20%)	20,000	[1]
<b>Land remediation claim at 150%</b> (£50,000 x 150%)	75,000	[1]
Profit on disposal (£275,000 – (£250,000 - £150,000))	<u>175,000</u>	[½]
Total	<u>670,000</u>	

**Tutorial Note:**

Land remediation is a rather obscure point. Land Remediation Relief is a relief from corporation tax only. It provides a deduction of 100%, plus an additional deduction of 50%, for qualifying expenditure incurred by companies in cleaning up land acquired from a third party in a contaminated state. Land Remediation Relief is available for both capital and revenue expenditure.

Additions to taxable profits:

Detail	Amount £	
Depreciation	4,000,000	
Capital gains on machinery sold for in excess of cost (£275,000 - £250,000)	<u>25,000</u>	[½]
Total	<u>4,025,000</u>	

**Tutorial Note:**

Credit is given if the full amount of the decorating expense was deducted in the period. There is also a strong argument for **claiming SBAs** in relation to the expenditure on the **new walls** in the office and the **new office fire doors**. By virtue of CAA 2001, s.270BJ(1) the conversion of part of a building is treated as the construction of that part of the building. Erecting the new walls in the office could be regarded as the **conversion of part of the office**. Similarly, the new fire doors could be regarded as a **renovation of part of a building** and treated in the same way as CAA 2001, s.270BJ(1) applies also to the renovation of part of a building. The examiner has not considered these points in the answer but credit would be given if candidates gave SBAs in relation to this expenditure and explained their reasoning.

<u>Notes</u>	<u>Detail</u>	<u>Amount</u> £	
N1)	Main pool written down value brought forward	1,070,000	[½]
	Additions not qualifying for FYA:		
	Hire purchase ( <b>owned asset so capital allowances</b> are available, but no FYA as second-hand assets)	1,000,000	[1]
	<b>AIA in preference</b> to use in respect of SRP additions	(1,000,000)	[1]
	Proceeds from sale are <b>limited to original cost</b>	<u>(250,000)</u>	[1]
		820,000	
	Capital allowance claim @ <b>18%</b>	(147,600)	[½]
	FYA:		
	R&D plant expenditure 1 February 2025	250,000	
	<b>R&amp;D allowances at 100%</b>	(250,000)	[1]
	New additions:		
	Manufacturing equipment	5,000,000	[½]
	Computer equipment	500,000	[½]
	No claim for moveable partitions as <b>no confirmation intended to be moved</b>	Nil	[1]
	No claim for the new walls as <b>part of building</b> and painting is <b>revenue expense</b>	Nil	[1]
	Fire alarm system is plant	20,000	[½]
	Doors are non-qualifying as <b>part of building</b> irrespective of their use as fire doors	Nil	[1]
	Portable air conditioning units are <b>not part of the structure</b> of the building	<u>10,000</u>	[½]
	Total additions qualifying for <b>100% FYA (full expensing)</b>	<u>5,530,000</u>	
	<b>FYA @ 100%</b>	(5,530,000)	[1]
N2)	£1,500,000 <b>TWDV @ 18%</b> = £270,000 x <b>6/12</b>	(135,000)	[1]
N3)	Qualifying for FYA @ 50%: Electrical & water system (named integral feature)	250,000	

<u>Notes</u>	<u>Detail</u>	<u>Amount</u> £	
	Air conditioning (named integral feature)	100,000	
	Lift (named integral feature)	<u>50,000</u>	
	Total special rate pool FYA additions (FYA claimed rather than AIA, as <b>better use of AIA is in respect of non-FYA qualifying main pool additions</b> ) <b>FYA @ 50%</b>	400,000	<b>[1]</b>
		(200,000)	<b>[1]</b>
N4)	Cars as emissions <b>&gt;50g/km</b> Capital allowance claim <b>@ 6%</b>	100,000 (6,000)	<b>[1/2]</b>
N5)	£1,333,333 <b>building cost only</b> is eligible for structures & buildings allowance as <b>land does not qualify</b> and the other three items qualify for plant and machinery capital allowances and therefore do not qualify for SBAs <b>[1]</b> .	(30,000)	
	SBAs are available from the later of the date that the building was paid for and <b>when brought into use [1/2]</b> , so SBAs are available from 1 April 2025 <b>@ 3% [1/2]</b> ( <b>9/12 × £1,333,333</b> ) <b>[1/2]</b>		

**Tutorial Note:**

The AIA is £1 million for this period and so its use requires some thought. It will generally be used for expenditure which does not qualify for the full expensing FYA. Here, neither the hire purchase additions (as the vehicles are not new) nor the integral features (special rate pool items) qualify for full expensing. However, the **integral features qualify for FYA @ 50%** and so it is **preferable to use the AIA for the hire purchase additions** which would **otherwise only benefit from an 18% allowance** in this period.

The main pool additions purchased new **qualify for 100% FYA** (full expensing).

The new special rate pool additions qualify for **50% FYA**.

## MARKING GUIDE

TOPIC	MARKS
<u>Main pool</u>	
Including WDV of plant brought forward	½
Including £1m hire purchase additions with explanation, no FYA	1
Claiming AIA of £1m against these, and not SRP additions	1
Disposal proceeds from sale and limiting to cost	1
WDA	½
R&D allowances claim	1
Including manufacturing equipment	½
Including computer equipment	½
Not claiming for partitions as no intention to move	1
Not claiming for walls or painting new walls with explanation	1
Claiming for fire alarm system	½
Not claiming for fire doors as still considered part of the building	1
Claiming for A/C units as are portable	½
FYA @ 100%	1
<u>Assets transferred in</u>	1
<u>Special rate assets</u>	
Claiming for cars with explanation	½
Claiming for all integral features	1
Claiming FYA @ 50% on integral features	1
<u>Buildings allowance</u>	
Confirming SBAs only available on building costs	1
Confirming correct date that SBAs are due from	½
Using the rate of 3%	½
Calculating the SBA	½
<u>Adjustments to taxable profits</u>	
Claim for depreciation on finance leases	1
Revenue expenditure claim for depreciation	1
Qualifying land remediation claim	1
Deducting profit on disposal & adding capital gains on proceeds in excess of cost	1
<b>TOTAL (MAX)</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

This was a routine capital allowances, other reliefs, and capital-versus-revenue question. Candidates were provided with facts about a UK manufacturing company's spending programme and asked to describe the available capital allowances and other required computational adjustments.

The question was well answered by the majority of candidates, who generally addressed nearly all the points and mostly gave technically correct answers. Some candidates provided unnecessary explanations of why capital allowances are given, how they are claimed and the different types available. Areas less well answered included the distinction between hire-purchase and finance leases, the scope of Structures & Buildings Allowance and the availability of a revenue deduction for re-decorating. Unfortunately, few candidates dealt with the disposals correctly, failing to limit proceeds to cost, disallowing profits on sale and taxing a capital gain.

**14. TROUBLE PLC**Trouble plc – UK tax consequences of transactionsProposed financing of Calamity N.B.

Interest accruing on the corporate bond ought to be tax deductible for Trouble plc under the loan relationship rules. Dependent on the jurisdiction of residence of the bondholders, **interest payments** by Trouble plc **may be subject to withholding tax** (“WHT”) [½]. It may be possible to **mitigate any WHT** exposure through claiming relief **under double tax treaties** [½].

Danger Ltd is a Controlled Foreign Company (“CFC”) under UK tax legislation. In broad terms, the CFC legislation is designed to prevent profits being diverted offshore to low tax territories from the UK. Profits of the CFC are chargeable to Corporation Tax if they pass through what is termed a “gateway” and the company cannot qualify for an exemption.

**Tutorial Note:**

A **non-UK resident company controlled by UK resident persons** is a CFC (s.371AA TIOPA 2010). When you see such a company in a question, consider whether the profits of the CFC will be apportioned to relevant UK resident companies.

In the case at hand, the income should constitute “**non-trading finance profits**” as the **company does not carry on a trade** and the income can be traced to **capital investment from the UK**. The conditions of the “non-trading finance profits gateway” are therefore met and the **profits pass through the gateway** [½].

**Tutorial Note:**

The rules bringing **profits from investment of UK monetary assets** into the **non-trading finance profits gateway** are given in s.371EC TIOPA 2010.

Danger Ltd should, however, qualify for the “**finance company partial exemption**” (“FCPE”). The FCPE offers partial exemption for non-trading finance profits derived from “qualifying loan relationships”.

The loan should be regarded as a “**qualifying loan relationship**” as:

- 1) Non-trading finance profits are **derived from UK capital investment** and are **not generated by UK activities** [½];
- 2) The **creditor (Danger Ltd) is a CFC connected with the debtor** (Calamity N.B.) and both are **under the control of the same UK resident person** (Trouble plc) [½];
- 3) Calamity N.B. is not resident in the UK and so is **not within the charge to UK tax** in respect of the debt payments it makes [½]; and
- 4) Danger Ltd has **business premises in Jersey** (the trust company offices) [½].

As a consequence, **75% of the interest should be exempt from CFC apportionment** [1]. Further exemption may be available under the “**matched interest**” rules subject to review at year-end [½].

**Tutorial Note:**

The definition of a **qualifying loan relationship** is given in s.371IG TIOPA 2010. The restriction of qualifying loan relationship profits to non-trading finance profits **derived from UK capital investments** (rather than UK activities) is given in s.371IA(4) TIOPA 2010. The **75% exemption** is given in s.371ID TIOPA 2010.

Nambutu may impose WHT on interest payments by Calamity N.B. to Danger Ltd. Any WHT may be credited against any Corporation Tax payable on chargeable profits of Danger Ltd.

Dividend from Calamity N.B.

The **dividend will not be exempt** from Corporation Tax **because a tax deduction is available** for the distribution in **Calamity N.B [1]**. The gross dividend of £10 million is subject to tax.

Trouble plc can claim a **tax credit for the £1 million WHT [½]** together with any “underlying tax” (“ULT”) being foreign tax paid in respect of the profits. The ULT will be £5 million calculated as:

$$\frac{\text{£10 million (gross dividend received)}}{\text{£10 million (profits available for distribution)}} \times \text{£5 million (actual tax paid)} \quad [1]$$

This results in maximum double tax relief (“DTR”) of £6 million; however, this may **only be relieved against the UK tax arising on the same source of income**, ie the dividend. Assuming it is fully taxable, the dividend will be subject to Corporation Tax at a rate of 25% **capping the DTR at £2.5 million [1]**. If a foreign tax credit cannot be claimed, the WHT credit of £1 million may be expensed as a tax deduction [½].

**Tutorial Note:**

The **dividend exemption is denied** due to the **deduction being allowed** in a territory outside the UK (s.931D(c) CTA 2009). However, **double tax relief** is given for WHT and ULT on the dividend under ss.12-14 TIOPA 2010.

The **Tax Exemption may apply** to exempt chargeable profits of Calamity N.B. from CFC apportionment **if the Nambutan corporate tax liability is at least 75% of the corresponding UK tax** that would have been due on the profits [1].

**Tutorial Note:**

The basic rule for the **tax exemption** is given in s.371NB TIOPA 2010.

Income and gains arising in Peril BV

Peril BV is also a CFC. However, the company is resident in Erehw, which is an “**Excluded Territory**”, meaning that if certain conditions are met, the income of Peril BV will be **fully exempt** from CFC apportionment [½]. As **the royalty exceeds £50,000** and **is the only source of income** in the company, this exemption is unlikely to be available due to the fact the income is subject to a reduced rate of tax in Erehw [½].

**Tutorial Note:**

The **income condition** must be met for the excluded territories exemption to apply by virtue of s.371KB TIOPA 2010. The **CFC’s relevant income** must **not exceed the greater of 10% of its accounting profits or £50,000** (s.371KD TIOPA 2010). The relevant income here is the royalty income taxed at the reduced rate which clearly exceeds these limits.

The “**Tax Exemption**” may not apply in relation to Peril BV as **Erehw appears to have a more favourable tax regime** for intellectual property, despite the possible application of the UK patent box [1]. As the **IP has never been held in the UK**, however, the **profits should not pass through the gateway** and as a consequence no CFC apportionment will arise [1].

**Tutorial Note:**

Although none of the exemptions is met, there is no CFC apportionment to the UK resident company Trouble plc because **the profits do not pass through the ‘profits attributable to UK activities’ gateway**. The IP held by the CFC is **not part of an arrangement which has as its main purpose the reduction of UK tax** (as the IP was never held in the UK). In other words, **the motive test** in s.371CA TIOPA 2010 **is not met**.

The **gain arising on sale of the investment property** is **outside the scope of the CFC rules** and will not be apportioned to the UK [1].

**Tutorial Note:**

**Chargeable gains are excluded** from the CFC rules by virtue of s.371SB(3) TIOPA 2010.

Strife S.P.A.

The company should **qualify for the CFC Low Profits Exemption** provided **no more than £50,000 of the profits relate to non-trading income** [1/2]. The Tax Exemption may also apply [1/2].

**Tutorial Note:**

The limits for the **low profits exemption** are given in s.371LB TIOPA 2010.

## MARKING GUIDE

TOPIC	MARKS
<u>Proposed financing of Calamity N.B.:</u>	
Comment on potential WHT on corporate bond	½
Reference to mitigating WHT under double tax treaties	½
Reference to the non-trading finance profits gateway	½
Reference to “qualifying loan relationship” and conditions in s.371IG & s.371IH TIOPA 2010	2
Comment that 75% of income exempt pursuant to s.371ID TIOPA 2010	1
Reference to matched interest exemption in s.371IE TIOPA 2010	½
<u>Income and gains of Peril BV:</u>	
Reference to Excluded territories exemption	1
Reference to Tax Exemption	1
Comment that motive test likely met as pre-gateway carve out	1
Reference to capital gain outside scope of CFC rules	1
<u>Dividend from Calamity NB:</u>	
Comment that dividend not exempt as tax deductible pursuant to s.931D(c) CTA 2009	1
Credit for WHT	½
Calculation of underlying tax	1
Comment of restriction of DTR to tax on dividend	1
Comment that WHT can be expensed	½
Comment that Tax Exemption may apply	1
<u>Profits of Strife SPA:</u>	
Comment that Low Profit Exemption potentially available	1
<b>TOTAL</b>	<b>15</b>

## 15. BLUE BUILDINGS LTD

Transfer of Supermarket Building

Blue Buildings Ltd, Pink Properties Ltd and Purple Properties Ltd form a capital gains group, as Blue Buildings Ltd holds **75%** or more of the share capital of the other entities and appears to have an economic interest of **at least 51%** in each [1].

The transfer of the supermarket building from Pink Properties Ltd to Purple Properties Ltd would therefore have been a **no gain/no loss transfer**. The base cost of the building for Purple Properties Ltd will be **cost plus indexation allowance**. [1]

The transfer of the property could fall within the '**value shifting**' rules. These rules apply to **the sale of shares** in a company by another company where:

- **Arrangements materially reduce the value of shares**; and
- One of the **main purposes** of the arrangement is the **obtaining of a tax advantage** [1].

The **transfer of the supermarket building is at less than market value** and therefore it does reduce the value of Pink Properties Ltd shares [½]. However, the reason for the transfer is not to gain a tax advantage but for **commercial reasons, linked to a proposed sale**. The **value shifting rules are therefore unlikely to apply** [½].

**Tutorial Note:**

There are some easy marks for explaining **the gains group** and the **nil gain nil loss** group transfer.

Harder to spot is the relevance of the **value shifting rules** as given in s.31 TCGA 1992. You should think of these rules when you see a **sale of shares** when **their value has been materially reduced** – here by the transfer of the supermarket building at significantly below market value. In the event, the rules do not apply here as the **main purpose of this arrangement is not to obtain a tax advantage**. If the rules had applied, the gain on the disposal would have to be adjusted by **increasing the consideration by a just and reasonable amount**.

De-grouping charges

De-grouping charges arise where a chargeable asset is transferred between two **companies in a group** under a **no gain/no loss** transfer and the **company receiving the asset later leaves the chargeable gains group**, whilst still **holding the asset, within six years** of the transfer [1]. In this case, the intra-group transfer of the supermarket building at no gain/no loss could create a future de-grouping charge. However, as the **company receiving the asset (ie Purple Properties Ltd) remains in the chargeable gains group** with the principal company, ie Blue Buildings Ltd, a **de-grouping charge does not arise** when Pink Properties Ltd is sold to Boutique Buildings plc [1]. A de-grouping charge could still arise if Purple Properties Ltd left the chargeable gains group within six years and at that time, it still owned the supermarket building.

**Tutorial Note:**

Whenever there is a **group transfer of a chargeable asset** and a **company leaves the group**, you should think about a **de-grouping charge**. However, be careful that you apply the rules to the actual scenario. Here, the company leaving the group is the transferor (vendor), not the transferee (receiving company). The **receiving company does not leave the group** with the asset and so there is no de-grouping charge.

Substantial shareholdings exemption (SSE)

**SSE automatically exempts gains** on the sale of shares subject to certain conditions being met [1]. SSE will not be available as the conditions required for a sale on 31 March 2026 will not be met since **Pink Properties Ltd is not a trading company** [1].

Gain on disposal of Pink Properties Ltd

## Cash

A taxable **chargeable gain** will arise on 31 March 2026 in Blue Buildings Ltd in respect of the **cash consideration** [½]. But as some of the consideration is in shares, a **part-disposal** takes place [½].

## Shares in Boutique Buildings plc

Where **shares are exchanged for other shares**, there may be **no disposal** for capital gains purposes and **no gain** arises [½]. Instead, the **new shares take on the base cost and date of acquisition of the old shares** [½]. As Boutique Buildings plc will **own 25% or more** of Pink Properties Ltd, this treatment applies automatically as long as the exchange is carried out for **bona fide commercial reasons** and does **not form part of a scheme which has tax avoidance as one of the main purposes** [1].

Blue Buildings Ltd can **apply for clearance from HMRC** to obtain certainty that, for tax purposes, the transaction will be treated as being performed **for commercial reasons** [1].

## Cash payable in the future

As it is not possible to calculate now exactly how much Blue Buildings Ltd will receive, the future payment is **deferred unascertainable consideration** [1]. Under the *Marren v Ingles* principle, the **right to receive the future consideration** is treated as a **separate asset: an 'earn-out'** [½]. The **present value of the earn-out is taxed now** and forms the base cost of the earn-out [½]. When the cash is eventually received, the earn-out is treated as having been disposed of. A **gain or loss will arise when the cash is received** if the cash received is greater or smaller than the base cost [1].

If a **loss is made on the disposal of the earn-out**, that loss can be **utilised against any other capital gains** made in the year of disposal of the earn-out or carried forward [½]. It **cannot be carried back** against the disposal of the shares in Pink Properties Ltd [½].

**Tutorial Note:**

The question gives information about three elements to the consideration on the sale of the shares in Pink Properties Ltd, and you must explain the treatment of each. As cash is received, a **gain must be calculated** with the cash included in the proceeds figure.

The shares received are not included as proceeds in the gains calculation as the conditions are met for **share for shares exchanges** under s.135 TCGA 1992. The new shares are then **treated as the same asset as the original shares** under s.127 TCGA 1992 and there is no disposal. However, the **value of the shares** received is still required to determine the allowable cost, using the **part disposal** fraction.

The gains calculation is further complicated by the future cash payment that may be received. When **consideration is deferred**, you should **consider whether it is ascertainable**. Here the amount of the **future consideration is unascertainable** (unknown) and so the rule in *Marren v Ingles* applies. The value of the **right to receive it is valued as a separate asset** and is included as proceeds for the disposal of the shares and in the part disposal fraction.

Calculation of chargeable gain

	£	
Proceeds on disposal (150+60)	210,000,000	[1]
Less: cost		
A/(A+B) x original cost		
(150+60)/(150+60+390) x 100,000,000	<u>(35,000,000)</u>	[1]
Gain on disposal of shares	175,000,000	
Indexation allowance on cost		
June 16 – Dec 17		
(278.1-263.1)/263.1 x 35,000,000	<u>(1,995,439)</u>	[1]
Chargeable gain	<u>173,004,561</u>	

Tax payments

Due to the amount of the chargeable gain, tax payments will be made on a quarterly basis on 14 March 2026, 14 June 2026, 14 September 2026 and 14 December 2026 in respect of the year to 31 December 2026 [1]. Interest will be charged if the quarterly payments are less than the total tax payable for the year. If the sale has not been considered in the tax payments already made an additional payment should be made in December to ensure the tax on the chargeable gain has been paid.

## CIOT MARKING GUIDE

TOPIC	MARKS
Companies in a capital gains group	1
Transfer of supermarket building would be no gain/no loss	1
Rules for a de-grouping charge to arise	1
Recognition that a de-grouping charge does not arise	1
Value shifting rules may apply	1
Discuss conditions for rules to apply	1
Substantial shareholding exemption automatically exempts gain if conditions met	1
Conclude conditions not met	1
Cash element of consideration taxable now	1
Share for share rules mean no disposal	1
Conditions for share for share rules to apply	1
Application for clearance	1
Recognition that there is deferred and unascertainable consideration	1
Explain application of Marren v Ingles rules re PV being taxed now	1
Gain or loss arises in future on receipt of cash	1
Availability of relief for losses if future cash less than market value of earn-out	1
Calculation of proceeds	1
Calculation of base cost	1
Calculation of indexation (not 3.d.p)	1
Tax payment dates	1
<b>TOTAL</b>	<b>20</b>

**Examiner's report:**

[Being reproduced with the permission of The Chartered Institute of Taxation]

This question considered chargeable gains relating to a take-over. The majority of candidates scored well on this question showing an understanding of the Substantial Shareholdings Exemption, the share-for-share rules and in most cases the principles arising from Marren v Ingles.

Very few candidates realised that a discussion on value shifting would be appropriate as well as a discussion on depreciable transactions. A large number of candidates erroneously believed a degrouping charge had arisen; those who did failed to spot that the asset remained in the capital gains group as it was the seller, not the purchaser, who had left the group. Many candidates did not realise that one capital gains part disposal calculation would be performed for the sale of the shares, and instead treated each part of the consideration as a separate disposal. Some candidates failed to note that, due to the level of taxable profits arising purely due to the capital gain, the company would be paying tax in quarterly instalments.