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RELEVANT TO ACCA QUALIFICATION PAPER P6 (UK)

Exam technique and fundamental technical issues for Paper P6 (UK)

This is the Finance Act 2011 version of this article. It is relevant for candidates sitting the Paper P6 (UK) exam in December 2012. Candidates sitting Paper P6 (UK) in 2013 should refer to the Finance Act 2012 version of this article which will be published on the ACCA website in 2013.

This article emphasises the importance of two exam techniques and outlines 12 fundamental technical issues. The exam techniques will help you to use your time in the exam more efficiently and to maximise the marks obtained. The technical issues are important in that they are part of the foundation on which answers can be constructed, such that they cover as many of the relevant issues as possible.

This article makes no attempt to be comprehensive; there are other important exam techniques and, of course, a vast number of technical rules that may be examined. Instead, the techniques and issues highlighted here are particularly significant in that they will help you to maximise your marks in the exam.

There is more guidance on exam technique and technical issues in the examiner's report published after each exam. The following articles are also available on the ACCA website: 'Approach to P6 (UK)', 'From Paper F6 to Paper P6' and 'Guidance on approach to questions in Section A of Paper P6 (UK)'.

This article is relevant to students who are beginning their studies for Paper P6 (UK) as it provides guidance on the approach they need to take in the exam and, therefore, the approach they should be taking while studying. It is also relevant in the period immediately prior to the exam as it emphasises fundamental issues to consider when answering exam questions.

EXAM TECHNIQUE

1 Answer the question

Marks are available in the exam for answering the question. They are not given for other parts of an answer, regardless of how well they are written or how technically correct they are. Consequently, it is necessary to determine *precisely* what you have been asked to do and then to make every attempt to do it without doing anything else. There will be sufficient time in the exam provided you do not allow yourself to be sidetracked.

Think about the best way of satisfying the requirements and relate your approach to the time available (by reference to the number of marks). Work your way through the tasks in an organised and consistent manner.

Pay attention to the verb used in the requirement. 'Explain' requires you to give reasons for your statements whereas 'state' does not. 'Calculate' does not require explanations, although explanations may be requested in respect of certain aspects of the calculations.

Explaining tax implications is not easy and needs to be practised. Practising will improve your ability to make a point in a clear and precise manner. It is likely that there will only be one mark for each particular point that you make – so you must think first in order to make the point in one or two sentences.

You should not think of a question as being about a particular technical area. If you do there is the possibility that you will answer the question in too narrow a manner. For example, where a question includes a group of companies, one of which has made a loss, it is not helpful to think of the question as being a 'group relief' question. This is because there may be marks available for many other technical areas – for example, single company loss relief, inter group transfer of assets, transfer pricing, VAT and so on.

Also, if a question is thought of as relating to a technical area, there can be a temptation to write about that area in great detail when such detail is not part of the requirement. Your answer should focus on the specific issues and facts of the question and you should avoid generalising.

Accordingly, rather than thinking of a question as being about a technical area you should see it as being about a set of circumstances and a series of requirements that relate to those circumstances. You should take the time necessary to understand the circumstances and to determine how best to satisfy the requirements.

2 Stop… and think

Imagine a client coming into your office and setting out a relatively involved scenario for you with facts and figures. You would not read the paperwork and then immediately explain the tax implications. Instead, having read the paperwork, you would think about it before explaining some of the implications. Then perhaps you would think some more before explaining one aspect in more detail and so on. You should behave the same way in the exam.

The thinking gives you time to be clear as to the facts of the question and what you have been asked to do. It then gives you the chance to identify as many of the relevant implications as possible and the various aspects of each of the implications, such that you maximise the marks scored. By thinking before you write, you should also avoid covering irrelevant matters that will not score marks.

TECHNICAL ISSUES

1 Income tax – the structure of the computation

A preparation of a comprehensive income tax computation with many different sources of income, tax rates and credits is an unlikely task in a Paper P6 (UK) exam. However, the structure of the income tax computation is of fundamental importance. By 'structure' I mean the way the income tax computation works; the calculation of taxable income, the availability of the personal allowance, the operation of the tax rates, tax reducers and the availability of tax credits. It is only by having a good understanding of this structure that you will be able to think your way through the computation and identify an efficient way of answering a question (for example, working at the margin). This knowledge will also ensure that you consider all the relevant points (for example, the personal allowance) while avoiding the preparation of full tax computations.

2 Income tax – individuals who are non-UK resident

Individuals who are non-UK resident are not subject to income tax on their non-UK source income. Accordingly, once non-UK residency has been determined, all that should then be said is that the individual's overseas income will not be subject to income tax.

There is no need to consider the remittance basis as it is not relevant to non-UK residents. The remittance basis concerns the manner in which income is taxed – that is to say, whether it is taxed on the arising basis or on the remittance basis. But for a non-UK resident overseas income is simply not taxable and that is the end of the matter.

When thinking about the remittance basis you should think of it applying to UK residents who are not ordinarily resident in the UK and/or not domiciled in the UK – but they must be resident.

There is more detail on this in my article 'International travellers' at www.accaglobal.com/content/dam/acca/global/PDF-students/2012s/sa_mar12_p6_travellers.pdf.

3 Income tax – the unincorporated trader

The tax position of the unincorporated trader in relation to both profits and losses is examined regularly. In order to perform well in respect of these questions, you must know the opening and closing year rules and the rules relating to loss relief. There are two articles on this area available on the website.

4 Capital gains tax – temporary non-residents

The temporary non-resident rules need to be considered when an individual becomes non-resident and non-ordinarily resident for a period of less than five tax years. Under the rules, and depending on the circumstances, such an individual may find that he continues to be liable to capital gains tax in respect of disposals while absent from the UK.

The temporary non-resident rules do not have any effect on the individual's residence status. This makes sense because it is the fact that the individual is non-resident that has brought about the consideration of the temporary non-resident rules. It would be horribly circular if those rules then affected the individual's residence status.

There is more detail on this in my article 'International travellers' at www.accaglobal.com/content/dam/acca/global/PDF-students/2012s/sa_mar12_p6_travellers.pdf.

5 Capital gains tax – reliefs

Capital gains tax reliefs should be considered whenever there is a capital gains tax disposal. You should have a mental checklist that enables you to think about the availability of all of the possible reliefs (entrepreneurs' relief, rollover relief, gift relief, EIS deferral relief, incorporation relief and principal private residence relief), such that you can then address those that are relevant to the question. Rollover relief is the only one of the reliefs that is available to companies.

There are conditions, particularly in relation to the property disposed of and time periods, that need to be satisfied in order for each particular relief to be available. You must learn the conditions.

6 Inheritance tax – the structure of the tax

Inheritance tax consists of an underlying structure or framework with lots of detailed rules. The key to a strong performance is to be absolutely sure of the underlying structure and to know as many of the detailed rules as possible. A weak knowledge of the underlying structure is likely to be fairly costly, whereas forgetting one of the detailed rules is unlikely to matter as much.

The underlying structure can be thought of as being in two parts: lifetime transfers and the tax due on death.

Lifetime transfers

When dealing with a lifetime transfer it is necessary to:

1. value the transfer (taking into account the valuation rules, fall in value and related property).
2. deduct exemptions
3. deduct reliefs (see below).

If the transfer is a chargeable lifetime transfer (ie not a potentially exempt transfer) inheritance tax will be charged on the amount of the transfer that exceeds the nil band **at the time of the gift**. The nil band at the time of the transfer will be reduced by **chargeable lifetime transfers** (ie ignore any potentially exempt transfers at this point) in the seven years prior to the transfer. The rate of tax will be either 25% (if the donor is paying) or 20% (if the donee is paying). Where the donor is paying the tax, the gross gift is the gift (the amount after step 3 above) plus the tax.

Tax due on death
Where the taxpayer has died, the transfers in the seven years prior to death and the death estate itself must be dealt with. The three steps set out above must be carried out for each transfer in chronological order. Inheritance tax will be charged at 40% on the amount of the transfer that exceeds the nil band **at the date of death**. The nil band at the date of death will be reduced by **chargeable transfers** (ie all transfers, potentially exempt and chargeable lifetime) in the seven years prior to death. Finally, deduct taper relief and any lifetime tax paid before moving on to the next gift.

The death estate should be treated as a final gift in accordance with the previous paragraph. The point to watch for here is that the annual exemption is not available in respect of the death estate.

7 Inheritance tax – reliefs
Agricultural property relief and business property relief are important as they do not have an upper limit and they can potentially relieve the whole of a transfer. There are detailed conditions that must be satisfied in order for the reliefs to be available. The conditions relate to the type of property and the period for which it has been owned. You must learn the conditions.

8 Corporation tax – accounting periods
A corporation tax computation is prepared for an accounting period. The length of the accounting period affects the limits when determining the rate of corporation tax. The end of the accounting period affects the date on which corporation tax is payable.

Each time an accounting period ends a corporation tax computation is required and a new accounting period starts. An accounting period also starts when a company comes within the charge to UK corporation tax (for example, by acquiring a source of income) and when a company begins to trade.

The accounting period will end on the earliest of:
- 12 months after it began
- the end of the company's period of account
- the company ceasing to trade
- the company becoming or ceasing to be UK resident
- the company ceasing to be within the charge to UK corporation tax
- the company entering or ceasing to be in administration.

You should note that an accounting period does not come to an end when a company is purchased, even though it may be necessary to time apportion its profits pre and post the date of the change of ownership for the purposes of group relief.

9 Corporation tax – associated companies
The number of companies with which a company is associated is important in determining the rate of corporation tax. It is often a relevant issue in exam questions with marks being available for considering the matter.

Two companies are associated where one controls the other or they are both controlled by the same person(s). A person is an individual or a company, such that where an individual owns more than 50% of two companies those two companies are associated even though they are not members of a group.

When determining the upper and lower limits of a company (for the purposes of computing its corporation tax rate) you must take account of all companies (including non-UK resident companies) with which the company is associated at any time in its accounting period. This means that where a company leaves one group of companies and joins another, it will be associated with companies from both the old and new groups for that particular accounting period.

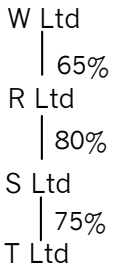
10 Corporation tax – distinguishing a company from its trade/business
A company is a legal entity that is owned by its shareholders and managed by its directors. It will use its resources to trade and/or carry out investment activities. The trade/business carried on by a company is separate from the company.

When a company sells its business (often described as its trade and assets) there may be chargeable gains in the company on each of the assets sold. The sales proceeds will be in the company and rollover relief may be available. It can then acquire a new business or use the proceeds of sale to acquire investments.

When a company (ie the shares in the company) is sold, its shareholders have made a disposal, which may result in a capital gain or loss. The company's activities carry on as normal and a corporation tax computation will be required by reference to its accounting period as set out above.

Before you begin answering a question, make sure you are clear as to the transactions that have taken place, or are to take place in the future, such that you address the appropriate implications.

11 Corporation tax – groups of companies
The definitions of a group for the purposes of group relief and chargeable gains are not the same. The gains group definition tends to be the most problematic as it refers to both 75% and 50%. The direct ownership must be at least 75%. In addition, the principal company (that is the company at the top of the group) must have an effective ownership of more than 50% in each of the companies in the group.



W Ltd owns less than 75% of R Ltd and so the two companies are not in a gains group. R Ltd is the principal company of a gains group consisting of R Ltd, S Ltd and T Ltd. R Ltd owns at least 75% of S Ltd which, in turn, owns at least 75% of T Ltd. R Ltd's interest in T Ltd is 60% (80% x 75%), which is more than 50%.

There are examples of both types of group in my article 'Corporation Tax groups for P6 (UK) – Parts 1 and 2'.

12 Value added tax (VAT) – zero rated and exempt supplies

The terms zero rated and exempt are not interchangeable; the correct terminology must be used in the exam in order to earn marks.

Zero rated supplies are taxable supplies for the purposes of the need to register and partial exemption. However, the rate of tax is 0%. Input tax in respect of inputs relating to zero rated outputs is recoverable. Where the vast majority of the supplies of a business are zero rated the business may request exemption from the requirement to register.

Exempt supplies are not taxable supplies. They are not relevant when considering the need to register and it is not possible to recover input tax in respect of inputs relating to exempt outputs unless the *de minimis* rules are satisfied. A business that makes only exempt supplies is not permitted to register for VAT.

Stop and think in the exam (always a good idea!) – make sure you are using the appropriate term for the circumstances.

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Rory Fish is examiner for Paper P6 (UK)