



# Examiner's report

## P6 Advanced Taxation (UK)

### June 2017

#### General Comments

The exam was in its standard format; section A consisting of the compulsory questions 1 and 2, worth 35 marks and 25 marks respectively, and section B where candidates were required to answer two out of the three questions worth 20 marks each.

In general terms, those candidates who did not perform well did not spend sufficient time carefully reading the question and thinking before they started writing. This meant that they did not include sufficient relevant points and/or they wasted time providing information that had not been asked for.

Candidates should pay particular attention to the following in order to maximise their chances of success in the exam in the future.

1. Know your stuff
  - Successful candidates are able to demonstrate sufficient, precise knowledge of the UK tax system.
  - This includes knowledge brought forward from the F6 syllabus.
2. Practise questions from past exams with the aim of adopting the style of the model answers. In particular, candidates should practise the often more intellectually demanding Section A style questions.
3. Address the requirement
  - Read the requirement carefully – in the Section A questions the detailed tasks that you are to perform will be set out in one of the documents. It may be helpful to tick off the tasks as you address them. Marks are awarded for satisfying the requirements and not for other information even if it is technically correct.
  - The requirements of each question are carefully worded in order to provide you with guidance as regards the style and content of your answers. You should note the command words (calculate, explain etc), any matters which are not to be covered, and the precise issues you have been asked to address.
  - You should also note any guidance given in the question or in any notes following the requirement regarding the approach you should take when answering the question.
  - Pay attention to the number of marks available – this provides you with a clear indication of the amount of time you should spend on each question part.
4. Don't provide general explanations or long introductions.
  - If you are asked to calculate, there is no need to explain what you are going to do before you do it; just get on with it – only provide explanations when you are asked to.
  - Think before you write. Then write whatever is necessary to satisfy the requirement.
  - Apply your knowledge to the facts by reference to the requirement.
5. Think before you start and manage your time
  - Ensure that you allow the correct amount of time for each question.
  - Before you start writing, think about the issues and identify all of the points you intend to address and/or any strategy you intend to adopt to satisfy the requirement.

If you are preparing to resit the exam, think about the number of additional marks you need and identify a strategy to earn them. For example:

- Identify those areas of the syllabus where you are weakest and work to improve your knowledge in those areas. This should include any technical areas brought forward from F6 where necessary.
- Practise past exam questions in order to familiarise yourself with the style of questions that you will have to deal with.

- Ask yourself whether you could improve the way you manage your time in the exam and whether you address all of the parts of all four questions or whether you waste time addressing issues which have not been asked for.
- Make sure that you earn the professional skills marks and that you are prepared to address the ethical issues which may be examined.

Finally, you should read the various non-technical articles aimed at improving performance in the P6 (UK) exam, which are on the website.

### **Marks available in respect of professional skills**

Marks were available for professional skills in question 1. In order to earn these marks candidates had to take a sensible approach to solving the problem set in relation to the alternative business structures, provide explanations and calculations that were clear and logical, keep their answer specific rather than general, and adopt a professionally acceptable style. On the whole, the performance of candidates in this area was reasonably good.

### **Specific Comments**

#### **Question 1**

This question concerned an individual and was in three parts.

The first part concerned a plan to start a new unincorporated business. Candidates were asked to prepare a table of figures in order to determine the individual's cash position for two alternative business strategies after two years of trading. One of the strategies required the individual to take on two employees.

The technical content of this part of the question was reasonably straightforward and required candidates to:

- recognise the availability of the annual investment allowance
- determine the relief available in respect of a trading loss in the first tax year of trading
- deal with the tax implications for the employer of paying a mileage allowance to the employees
- calculate the employer's class 1 contributions in respect of the employees
- calculate the income tax, class 4 and class 2 liabilities of the individual

Accordingly, in order to do well, candidates needed to concentrate on the detail, be brisk in their approach and avoid any unnecessary narrative. Many candidates were able to do this and there were some very high quality answers to this part of the question.

Weaker candidates were less willing to commit themselves to the numbers and instead wrote about the tax implications in more general terms. Some candidates also let themselves down by failing to consider the individual's national insurance contributions position, such that they did not attempt quite a few of the marks on offer.

There were few technical problems with this part of the question. The one common error was the implications of the mileage allowance, with most candidates knowing there was a rule regarding the excess over 45p per mile but many thinking it related to the tax deductibility of the payments made as opposed to the class 1 contributions due.

The second part of the question concerned inheritance tax and was done reasonably well. Candidates were very comfortable with the basic mechanics of the tax including death within seven years of a potentially exempt transfer (PET), the nil rate band and the availability of taper relief. Weaker candidates did not always relate the

facts of the question to the requirement, such that they ignored the chargeable lifetime transfer which was made prior to, but in the same tax year as, the PET. This meant that they wrote in general terms about the availability of the annual exemption and the nil rate band rather than applying the rules to the specific facts of the question.

The final part of the question required candidates to explain the tax liabilities on the sale of shares in respect of which income tax relief under the enterprise investment scheme and EIS deferral relief had been claimed.

As is so often the case, in order to score well, candidates needed to stop and think. In particular, they needed to identify the three separate implications of the sale of the shares. It was important to do this first because candidates then knew how much needed to be explained in the relatively short amount of time available.

The three implications which needed to be explained were:

- the gain which was deferred when the shares would become chargeable
- an element of the income tax relief obtained when the shares were acquired would be withdrawn
- there would be a chargeable gain on the sale of the shares themselves

Weaker candidates identified one of these points and wrote about it at length rather than identifying all of the points which needed to be made.

## Question 2

This question concerned the rules in relation to corporation tax and groups of companies and was in four parts.

The first part required candidates to prepare guidance for a tax assistant on how to minimise the corporation tax payable in instalments by the group companies by transferring chargeable gains and capital losses between them.

This was a slightly unusual requirement. It was vital that candidates spent some time thinking about how **they** would carry out the assistant's task before they started trying to explain to the assistant how to do it.

Candidates needed to think in terms of what needed to be done (objectives), and how it was to be achieved (strategies). The objectives were

- where possible, to reduce the taxable total profits (TTP) of each company below the limit of £1,500,000 (divided by the 18 companies in the group)
- to reduce the TTP of any company required to pay tax in instalments.

These objectives can be achieved by:

- matching gains and losses in a particular company
- transferring gains from a company with TTP above the threshold to one with TTP below the threshold

As expected, candidates found this task difficult and there was a tendency to fall back on describing the rules in general terms as opposed to trying to address the specific requirement.

The second part of the question concerned the proposal to transfer the trades and assets of five of the group companies to another of the group companies and was also challenging. The challenge here was to address all of the issues set out in the manager's email in the time available. Only four points needed to be made but there was only one mark for each point.

Having said that this was a challenging question, many candidates made a good job of it. In particular, they kept their answers brief and tried to address all of the issues raised. Weaker candidates focussed on only one or two of the manager's issues which restricted the number of marks which could be obtained.

The one common technical error concerned the capital allowances treatment. The point here is that the assets would be automatically transferred at tax written down value because the companies are all under 75% common control both before and after the transfer of the trades.

The third part of the question concerned a whether a company making zero rated supplies was required to register for VAT and the benefits of registering. This part was not done particularly well. This was partly due to candidates writing standard answers to the whether or not to register question without focussing on the fact that the company was making zero rated supplies. This meant that the following two points were often missed:

- the company could apply to be exempt from registration even if its supplies exceeded the registration limit
- if the company were to register, there would be no effect on its customers, even though they are members of the public.

The final part of the question concerned the disclosure of information to HM Revenue and Customs and was done well by the vast majority of candidates.

### Question 3

This question concerned inheritance tax on an estate which included overseas assets, the determination of UK residence status and the disposal of a US residential property by a non-UK resident individual. It was in two main parts.

The first part concerned inheritance tax on assets situated overseas. Candidates performed quite well and displayed a strong knowledge of the rules. However, a minority did not score as many marks as they could have done because they did not follow the instructions in the question sufficiently carefully. In particular, they failed to finish off their answers by calculating the value of the inheritance after deduction of all taxes and liabilities

The second part of the question required an explanation of an individual's resident status and a calculation of a chargeable gain on the sale of a property including the relief available in respect of a principal private residence.

The majority of candidates had a sound knowledge of the rules in connection with the determination of UK residence. There were just two minor problems; some candidates failed to note that there were only five marks available and simply wrote too much, whilst others did not do enough to apply the rules to the facts of the question.

The calculation of the chargeable gain was not done particularly well. The requirement stated that the gain needed to be calculated 'under the residential property rules applicable to non-UK residents'. This required a computation based on the market value of the property as at 5 April 2015 and then a further computation where the gain based on the original cost of the property had to be time apportioned pre and post that date. Unfortunately, many candidates simply calculated a gain in the normal manner.

Candidates who did well in this question:

- applied their knowledge of the detailed rules to the facts of the question
- managed their time carefully
- read the requirements carefully and ensured that they answered the question set

#### Question 4

This question concerned the taxation implications of making an employee redundant, the post-tax proceeds on a sale of shares and the extraction of profits from a company by a director shareholder. It was in three main parts.

The first part concerned the redundancy of an employee. This part of the question consisted of two tasks.

Candidates did not have any particular difficulties with the first task which required them to explain the income tax implications of the redundancy package. Many answers were pleasingly concise and the relevant rules were well known by the majority of candidates.

However, candidates did not fare so well with the second task which required them to calculate the corporation tax deductions in respect of the redundancy package.

The main problem was that many candidates were unable to think in terms of 'allowable cost' as opposed to 'tax'. This led to candidates identifying the employment income benefit as the cost to the company as opposed to the cost of leasing the vehicle.

The second part of the question required candidates to explain the post-tax proceeds on a sale of shares. This is a part of the syllabus which candidates tend to be familiar with, such that most candidates should be able to do well. However, although this part was done very well by some candidates it was done poorly by others.

The problem was that candidates did not spend sufficient time thinking about what was going on in the question. The shareholder was either going to sell the shares to an individual or was going to sell them back to the company. This latter disposal was, of course, a purchase of own shares by the company, but this was missed by many candidates.

Other common errors included; failing to recognise that the sale to the individual would be deemed to take place at market value because the vendor and the purchaser were connected persons and failing to identify the availability of entrepreneurs' relief.

On the plus side, the majority of candidates handled the concept of post-tax proceeds well in that they correctly deducted the tax liability from the proceeds received.

The final part of the question concerned the extraction of profits from a company by a director shareholder. The question required candidates to explain the payments to be made by the **employing company** to HM Revenue and Customs.

Unfortunately, many candidates failed to notice this precise aspect of the requirement, such that they simply focussed on the recipient individual's tax liabilities in respect of the amounts received as opposed to the amounts which would be paid by the company in respect of the payments made. As a result, many candidates did not do as well as they could have in this part.

Candidates who did well in this question:

- had a precise knowledge of the various detailed rules
- read the requirements carefully and ensured that they answered the question set

#### Question 5

This question concerned aspects of corporation tax including intangible fixed assets, an overseas subsidiary and VAT in respect of a commercial building. It was in four main parts.

The first part required an explanation of the corporation tax implications of acquiring goodwill and a patent. The goodwill was a minor point and was handled well by the majority of candidates. The patent, however, was not handled so well. Many candidates treated it as a standard asset as opposed to being part of the intangible assets regime. As a result, the inter-group transfer was treated as a no gain, no loss transfer as opposed to a tax neutral transfer. This, in turn, caused problems when calculating the tax deductions available in the future.

The second part concerned transfer pricing. This part was not done particularly well because many candidates did not identify sufficient mark-scoring points.

It was important to start the explanation at the beginning by identifying why the transfer pricing rules applied. This required a reference to the fact that one of the companies controlled the other and the lack of an arms' length price. Many candidates did not do this but simply took it for granted that the regime applied.

Once the relevance of the rules had been established, candidates should then have explained the effect of the rules by reference to the need to increase the company's taxable profit and the amount of the increase. It was this part which most candidates focussed on.

It was then necessary to consider any other relevant matters including the availability of the exemption where a group is not large and the possibility of obtaining advance approval of the arrangements from HM Revenue and Customs.

The third part concerned the chargeable gains implications of the sale of an item of equipment and of some shares. Candidates needed to concentrate and take care in order to score well.

The equipment was being transferred between two companies in a chargeable gains group. However, the company acquiring the property was not resident in the UK, such that the no gain/no loss treatment would not apply to the transaction. In addition, due to the availability of capital allowances, the loss arising on the disposal would not be available.

When dealing with the sale of the shares, it was important to recognise that the substantial shareholder exemption would not be available because the vendor would not have owned the shares for a 12-month period in the two years prior to the sale.

The final part concerned various aspects of VAT.

The aspects of this part relating to the option to tax a commercial building were generally handled well. However, candidates found the other aspect of this part more difficult.

Candidates were asked to suggest reasons why a company which made taxable supplies did not charge VAT on sales made to an unconnected party. Stronger candidates stopped for a moment to gather their thoughts and then wrote about the registration limit and/or the making of zero rated supplies. Weaker candidates simply wrote about registration in general and often lengthy terms. Candidates need to be in a rhythm throughout the exam of reading, thinking and then writing.