

Examiner's report

P6 Advanced Taxation (UK)
September 2016



ACCA

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 sufficiently well to achieve a pass in this exam were weak in the following areas:

- They did not appear to spend sufficient time carefully reading the question and thinking before they started writing. This meant that they failed to address the question from the required angle, produced an unstructured answer which tended to lead to unnecessary repetition, or omitted part of the requirements.
- They did not attempt every part of four questions.
- They did not have sufficient, precise knowledge of the tax rules within the syllabus, particularly some of the more fundamental rules contained in the F6 syllabus.

However, it was also noted that a considerable number of candidates wasted time providing information that had not been asked for. In particular, providing detailed general explanations where none were required, or (to a lesser degree), providing calculations when explanations were 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, which remains very important and is clearly a 'weak link' for a number of candidates.
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
 - 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 pay particular attention to the command words (calculate, explain etc), any matters which are not to be covered, or facts to be assumed and the precise issues you have been asked to address.**
 - 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.
 - 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/provide calculations, without any mention in the requirement of supporting explanations, inclusion of such explanations will not gain marks, but will probably waste time – 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. Remember that at P6 you will be asked to apply your knowledge, rather than just reproduce information you have learned.
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, or providing lengthy, repetitive explanations.
- Make sure that you earn the professional skills marks and that you are prepared to address the ethical issues that may be examined.

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 demonstrate a professionally acceptable style and presentation, provide calculations and explanations that were clear and logical and demonstrate effective communication and problem-solving skills. On the whole, the performance of candidates in this area was reasonably good with the majority of candidates producing a document in a style that was easy to follow and appropriately written, but, in many cases, failed to demonstrate problem-solving skills. The main problem in this question was the relief of a trading loss within a group of companies. A significant number of candidates went ahead with this without setting out a strategy for taking relief at the outset and so were unable to provide a structured solution which addressed the particular criteria stipulated in the requirement.

Specific Comments

Question 1

Question 1 concerned the amount of investment needed for a company to obtain full rollover relief, relief for a trading loss within a group, consideration of the appropriateness of a single group VAT registration, and an ethical issue relating to an unexpected VAT refund.

Part (a), which was in two parts, related to a group of UK resident companies. The first of these parts required candidates to calculate the amount to be reinvested in qualifying assets in order to leave no gain on the disposal of a building chargeable to corporation tax. Most candidates made a reasonable attempt at this, but a very significant proportion also included detailed explanations to accompany their calculations, despite these clearly not being required. The fact that this question part was worth only three marks should have led candidates to realise that a lengthy discussion was not required. Accordingly, these candidates wasted time, which could have beneficially been spent elsewhere. Candidates would be advised to double check what is required by each question before making a start. The main technical error was a failure to realise that the total investment needed must equal the sale proceeds of the building, not the chargeable gain.

The second part of part (a) required candidates to relieve a trading loss within a group so as to minimise the amount of corporation tax payable by the group companies in instalments. Clearly, the majority of candidates were not aware of how this could be achieved, and therefore did not state a strategy for relieving the loss. The loss was therefore relieved in a somewhat random manner within the group. With the introduction of a unified rate of corporation tax, cashflow issues such as this are going to be more important for groups of companies and are therefore likely to appear in future questions. It was, however, pleasing to see that almost all candidates were aware that all the companies would pay tax at the same rate, so they didn't try to relieve the loss so as to save the maximum amount of tax, which has, in previous years, been a major planning point.

There were a good number of easy marks in this part for calculating the amount of corporation tax payable by each company, which most candidates achieved, but a few didn't appear to have read this part of the requirements and so failed to produce the necessary schedule. The answers to the requirement to state the due dates for payment of the instalments, where necessary, elicited a significant number of incorrect answers in relation to the starting date as many candidates thought that this was after the end of the accounting period, rather than within it. Practical issues such as due dates for payment of tax by both companies and individuals are essential knowledge within many tax planning scenarios at P6.

Overall, group aspects of corporation tax remain a key topic at P6 and candidates should endeavour to practise a wide range of questions on these to ensure that they are confident in dealing with different aspects of this area.

Part (b) of this question related to the consideration of specific matters relating to the group of companies when deciding which companies should be included in a group registration for value added tax (VAT) purposes. Despite the requirement stating that candidates were to refer only to the specific matters within the memorandum provided, a significant number wrote in detail about the general advantages and disadvantages of registering as a group, which was not relevant, and so wasted time. However, many candidates did identify the specific issues – one of the companies being partially exempt, and another using the annual accounting scheme and the cash accounting scheme - but then discussed what this meant for the relevant companies themselves, rather than the implications of including that company within a group registration. Unfortunately though, having identified the issues, they didn't go on to score as many marks as they could have done by answering the precise requirement.

Part (c) of this question concerned an unexpected refund of tax from HM Revenue and Customs (HMRC), and the actions to be undertaken by the firm in respect of this. This is a frequently tested area of ethics, and on the whole, candidates' performance was good, with clear explanations of the advice to be given to the client, and the consequences of the client not following this advice. Candidates generally appeared to have practised this type of question, and a good number scored full marks.

Question 2

Question 2 involved incorporation of a UK resident and domiciled individual's sole trader business, discussion of his residence status, and the consequences of the disposal of an investment property in the UK for capital gains tax and inheritance tax following the individual becoming resident overseas.

Part (a) of this question required candidates to deal with various aspects of incorporating a business, including the income tax implications of the cessation of trade for the sole trader, and the capital gains tax implications of a disposal of shares in the new company, on the assumption that incorporation relief was taken, or, alternatively, disclaimed.

An ability to identify the basis periods for taxation of a business in its opening and closing years, is a fundamental skill which candidates are expected to apply at P6. Relatively few candidates were able to do this correctly in the case of the final tax year for this business. This is regarded as essential brought forward knowledge, and is tested on a regular basis.

The assets of the business were transferred to the company on incorporation in return for consideration comprising wholly of shares, such that the total gains on the chargeable assets were eligible for incorporation relief. Alternatively, if incorporation relief was disclaimed, the chargeable gains would be taxable.

The two most common errors in this part of the question were:

- (i) Failure to recognise that goodwill transferred to a company which is a close company and in which the transferor is a participator, will not qualify for entrepreneurs' relief. This is a recent legislative change in FAs 2015.
- (ii) Failure to realise that the nominal value of the shares issued as consideration does not necessarily equal the market value of the shares. The nominal value of the shares issued is irrelevant; their market value must equal the total market value of the assets transferred where they represent the total consideration. This is a commonly tested examination point in this area, but was only picked up by a few candidates.

A logical approach was required for the final aspect of this part of the question, to calculate the capital gains tax liability arising on the subsequent disposal of shares, both with and without disclaiming incorporation relief, and on the alternative assumptions that the taxpayer was UK resident or overseas resident. Candidates needed to take a step back and ensure that they understood the full picture, before embarking on the calculations. This advice is also applicable more generally to Section A questions, where candidates need to stop and think about the scenario as a whole before starting to undertake the detailed work required.

Part (b) required candidates to identify the relevant 'ties' to determine the residence status, which applied to the taxpayer who has left the UK. The question clearly stated that the automatic tests for determining both UK and overseas residence were not satisfied, but a minority of candidates still discussed these rules, gaining no marks, and wasting time. However, overall this part of the question was done well, with candidates being aware of the relevant ties, and applying them to the taxpayer's situation.

Part (c) concerned the capital gains tax implications, both in the UK and overseas, of an overseas resident taxpayer disposing of a UK investment property acquired when previously resident in the UK. Most candidates realised that this was chargeable overseas, but very few appeared to be aware of recent legislation (FAs2015), which now includes disposals of UK residential property by a non-resident individual as being within the scope of UK capital gains tax.

The taxpayer's domicile, rather than residence status was relevant to the second part of this requirement, which related to the gift of the proceeds from the sale of the investment property. This was not particularly well done, with many candidates not recognising the relevance of the concept of 'deemed domicile, and of the location of the asset being gifted. The definition and relevance of an individual's residence and domicile for the purposes of both capital taxes is a frequently tested area at P6, and candidates should ensure that they are confident with applying these in context.

Question 3

This question concerned a calculation of the inheritance tax saving obtained as a result of a lifetime gift of shares, and the choice of date for cessation of an unincorporated business.

Part (a) examined two key principles in valuing unquoted shares which are gifted in lifetime, namely related property and diminution in value (comparing the value of the shareholding before and after the gift). Both of these were relevant in respect of the gift in this case, and it was pleasing to see that a significant number of candidates identified these, but unfortunately in many cases were not then able to apply them correctly to the figures given. An earlier lifetime gift was included, so that candidates had to recognise that there would be no annual exemption to bring forward, and no nil rate band available. This is a common examination technique which candidates should be familiar with if they have practised similar past examination questions. However, a common issue here was for candidates to provide a full calculation of the inheritance tax payable in respect of this earlier gift, despite this being totally irrelevant in order to address the requirement, which was to focus on the tax payable only in respect of the shares. In some cases, this wasted a considerable amount of time for no marks. This highlights the need to read the wording of the requirement very carefully to ensure that the right approach is taken and time is not wasted on unnecessary calculations.

Follow through marks were given in respect of the valuation of the shares where they were included, alternatively, in the deceased's estate on death, but a surprising number of candidates tried to apply the diminution in value principle again, with 'before' and 'after' figures, when, of course, on death, the whole of a person's holding must be transferred.

Part (b) required advice on which of two proposed dates for ceasing to trade would be beneficial for the taxpayer. The focus of the decision was the additional income after tax and national insurance contributions in each case. The requirement was deliberately worded, instructing candidates to do this by reference to the **increase** in net trading income, to encourage them to adopt a marginal approach to the question, considering only the **additional** income, tax, and national insurance contributions in each case, but the majority of candidates ignored this, and produced full computations, resulting in unnecessary and repetitive computations, including figures which were common to both scenarios. It was still possible to score full marks on this basis, but would have been much more time-consuming, and care had to be taken to ensure that comparable calculations were prepared in each case in order to come to a meaningful conclusion.

In P6 questions involving opening or closing years for an unincorporated business, it is extremely important always to identify the relevant tax years for which the assessments are being calculated. This is something which several candidates omitted to do, and as a consequence missed the significance of the fact that the second proposed cessation date fell into a later tax year such that a new personal allowance, and Class 4 national insurance contributions threshold would be available.

The majority of candidates did not address the final part of the requirements relating to an explanation of the capital allowances available. There were two aspects to this; the first is the need to calculate a balancing adjustment in the final period, and explain why, in this case it is a balancing charge. The second relates to the 'beneficial election' which was referred to in this context in the requirements. This concerns the succession election to transfer assets at written down value when the business is transferred to her daughter. This is an important election, and one which P6 candidates should always consider when a business is being transferred to a connected person.

Question 4

This question was concerned with the tax implications of the provision of shares to one employee, and of a company motor car or a loan to another. A third employee, who is resident but not domiciled in the UK, required advice relating to claiming the remittance basis in respect of her overseas income.

Part (a) of this question required candidates to compare and contrast the tax implications of an employee acquiring and disposing of shares in their company if these are acquired either through an approved company share option scheme (CSOP), or alternatively as employee shareholder shares.

Most candidates demonstrated good knowledge of the tax implications of acquiring the shares through a CSOP, which has been tested many times before, but were much less familiar with the implications of acquiring employee shareholder shares, which is a newer scheme. Some candidates omitted to answer this part of the requirement; a significant number of those who did confused the scheme with a Share Incentive Plan (SIP), whose rules are totally different. Share incentive schemes are tested on a regular basis at P6, so candidates should be confident with the tax implications of each, and ensure that they don't confuse the implications of the different schemes.

Part (b) of this question tested the income tax implications of two very commonly provided taxable benefits – a company motor car, and a beneficial loan. This is essentially brought forward knowledge from F6, but there were quite a lot of details to assimilate, and the majority of candidates did not take all of these into account. In order to provide a meaningful comparison of the income tax cost of each benefit, a candidate must ensure that all aspects of each scenario are considered. In particular, the car was to be provided for a three year period, before being transferred to the employee, and the loan was to be made for the same three year period, before being written off. The majority of candidates focused on the annual benefit calculation, but failed to consider that this situation would apply for three years, and then recognise the impact of the transfer/writing off. This is what essentially distinguished this as a P6 question – the ability to ‘see the full picture’ and advise on a holistic basis, taking into account all relevant details within a scenario. Candidates should be prepared for more questions of this style in future exams.

Part (c) dealt with the consequences of a UK resident, but non-domiciled individual claiming the remittance basis of taxation in respect of overseas income. This was clearly a question which candidates were prepared for and most scored well on this question part, recognising the need to compare the individual’s income tax liability for the tax year on both an arising and a remittance basis, to determine which was lower. Almost all identified and dealt correctly with the remittance basis charge, which would be charged for the first time in the current tax year due to the individual’s period of residence in the UK. However, very few actually answered the precise question set, which was to calculate the increase in the taxpayer’s income tax liability in this tax year, compared with previous years, rather than just the difference between the arising and the remittance basis for the current year only. While this didn’t lose the candidate many marks, it does highlight the need to read the question carefully, and ensure that the actual requirement is being addressed, rather than a requirement which the candidate is perhaps more used to seeing.

Question 5

This question was in two discrete parts, dealing with two separate companies. The first part examined the tax consequences of a company being put into liquidation, and the tax implications for its shareholders of the timing of a distribution. The second part related to a lossmaking company which was ceasing to trade, and included a brief explanation of its obligations relating to VAT.

Part (a)(i) required candidates to state the corporation tax implications arising for a company as a result of the appointment of a liquidator. The commencement of winding up/appointment of a liquidator is one of the factors which will bring a company’s accounting period for corporation tax purposes to an end. This was worth only two marks, but most candidates appeared to not be aware of the impact on a company’s accounting periods and so scored zero on this question part.

Part (a)(ii) was a ‘textbook’ question requiring an explanation of the tax implications for both an individual and a corporate shareholder of a distribution being made alternatively before the commencement of liquidation or on completion of the winding up. Answers were very mixed. A good number of candidates realised that the distribution would be taxed as a dividend prior to commencement of liquidation, but as a capital receipt once liquidation had commenced, although a surprising number were not aware of this distinction. For those candidates who realised this, the

majority were able to go on and correctly identify the tax implications for the individual shareholder, but, disappointingly, not for the corporate shareholder. Many candidates referred to the corporate

shareholder paying corporation tax on both of these, thereby failing to recognise that dividends are not taxable on corporate shareholders, and that the substantial shareholding exemption would apply in the case of the capital receipt. These are both fundamental points which candidates at P6 need to be very familiar with, as they can be tested in a variety of different scenarios.

In part (b)(i) candidates were required to show how a company could relieve trading losses incurred in its last few periods of account. This involved consideration of loss relief in an ongoing company, in addition to the availability of terminal loss relief. It is important in any question dealing with relief for losses that a well-considered and chronological approach is taken. Precise explanations of the reliefs are required in these sorts of questions. Well-prepared candidates were able to deal correctly with the earlier losses in accounting periods prior to the final period, and were aware that, on cessation, an extended three year carry back is available, but almost all neglected to correctly calculate the loss which was available for this terminal loss relief. Nevertheless, those who adopted a sensible, logical approach scored well on this question part.

Part (b)(ii) required candidates to explain the VAT implications for the company of ceasing to trade. Many candidates were clearly confident with this situation and scored the full three marks available.