

Examiner's report

P6 Advanced Taxation (UK)

June 2013



General Comments

The overall standard in the June 2013 exam was higher than that in June and December 2012. Most of the scripts were concise and included attempts at virtually all of the parts of four questions.

The exam was divided into section A and section B and was in its new 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 section B, question 4 was the most popular question and question 5 was the least popular.

In general terms, those candidates who did not perform as well as they could were unsatisfactory in the following three areas.

- They did not have sufficient, precise knowledge of the rules in relation to the purchase by a company of its own shares, groups of companies, the remittance basis and losses in relation to the unincorporated trader.
- They did not take sufficient time to identify all of the points that needed to be made before they started writing.
- They did not take sufficient care when preparing calculations, such that marks that could have been won were lost.

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 material
 - Successful candidates are able to demonstrate sufficient, precise knowledge of the UK tax system.
 - This knowledge must be up to date. Candidates must familiarise themselves with the changes introduced by the recent Finance Acts as summarised in the Finance Act articles published in Student Accountant magazine and on the website.
2. Practise questions from past exams with the aim of adopting the style of the model answers.
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 solve the problem set.



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.
- 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 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 use the information provided in the question correctly and then provide clear calculations that were easy to understand together with appropriate relevant explanations in an appropriately formatted memorandum. On the whole, the performance of candidates in this area was satisfactory with the majority of candidates producing a memorandum in a style that was easy to follow.

Specific Comments

Question One

Question 1 concerned a group of companies and one of its shareholders. It was in four parts.

Part (a) required candidates to prepare corporation tax computations for a group of companies in each of two situations. In the first situation an existing dormant company was to purchase a new business and commence trading. In the second situation the business would be purchased by an existing trading company.

Candidates needed to realise that where the business is purchased by the existing dormant company there would be an increase in the number of associates. This is because a dormant company is not an associate for the purposes of determining the rate of corporation tax. There were also brought forward trading losses, current year trading losses and chargeable gains and capital losses in different companies that had to be matched in the most tax efficient manner. The other issue here was that candidates needed to prepare two sets of computations and recognise that they were not the same. This meant that candidates had to be confident of their knowledge and to look for the rationale behind the question. From a commercial point of view, candidates had to recognise that the proposed transaction involved a company buying a business and not a company buying a company.

This part of the question was done well by the majority of candidates. Most candidates were comfortable with the group relief and the matching of the capital losses with the chargeable gains. In addition, it was particularly pleasing that the majority of candidates provided an appropriate level of relevant narrative rather than writing about all aspects of groups and corporation tax. Having said that, some candidates need to take care that they do not take their knowledge for granted. The question required explanations of the use of the losses, such that notes setting out the reason for the manner in which the losses were to be relieved needed to be provided in addition to the calculations; some candidates who clearly knew what they were doing failed to do this.

Common mistakes by some candidates included offsetting the brought forward trading losses against the profits of a different trade or group relieving them and, somewhat surprisingly, offsetting capital losses against trading profits.

Part (b) was for two marks and concerned the VAT implications of importing goods from a country that is not a member of the European Union. This was simply something candidates either knew or didn't know: fortunately, most did.

Part (c) related to the purchase by a company of its own shares and was in two parts.

The first part required candidates to review each of the conditions for capital gains tax treatment of the transaction. This was done well by a majority of candidates. Those who did not do as well as they perhaps could have done wrote too much about each condition rather than ensuring that they addressed as many of the conditions as possible. It would perhaps have helped if they had made a brief note of all of the conditions and then wrote briefly about each of them. In addition, a minority of candidates listed the conditions but did not earn all of the available marks as they failed to relate the conditions to the specific facts of the question.

Some candidates missed the point of the question, and addressed capital gains tax and entrepreneurs' relief generally, or did not have sufficient knowledge of the conditions.

The second part required calculations of the increase in the shareholder's tax cost of the transaction being subject to income tax as opposed to capital gains tax. As always, when it comes to calculations, great care is necessary if marks are to be maximised. Accordingly, although this part was done well by many candidates, the following mistakes were common:

- Treating the amount received as the distribution rather than the excess of this amount over the amount originally subscribed.
- Failing to gross up the distribution.
- Failing to consider the effect of the distribution on the level of taxable income and hence on the personal allowance.
- Omitting the tax credit in respect of the distribution.

The final part of the question concerned the acceptability or otherwise of being appointed tax advisers to both the companies and their directors. Candidates were expected to identify the potential problems associated with such an appointment together with appropriate safeguards. This was done well by the majority of candidates. However, as always, a minority of candidates wrote at length about one or two matters rather than thinking about all of the possible issues and writing briefly about each of them.

Question Two

Question 2 concerned an individual, Brad, and was in two parts. Part (a) related to capital gains tax and part (b) to inheritance tax. This question was done well by many candidates.

Part (a) required candidates to explain Brad's UK capital gains tax liability and the reasons for him being only temporarily non-UK resident and to state the payment date for the tax due. The majority of candidates had some knowledge of the temporary non-UK resident rules and quite a reasonable knowledge of capital gains tax generally, such that they scored reasonably well. Most candidates knew the five-year rule although a much smaller number stated the four years out of seven rule.

A minority of candidates stated a rule correctly in general terms but failed to apply it to the facts of the question. For example, some candidates stated that assets bought and sold during the period of absence were not subject to UK capital gains tax but then went on to calculate a gain in respect of the antique bed.

Other candidates failed to apply the basics. For example, a minority of candidates omitted the annual exempt amount whilst others either provided an incorrect payment date or failed to provide one at all.

When providing a payment date it is important to make it clear which tax year is being addressed. There were three possible relevant tax years in this question so stating a date without a year could not score unless the candidate explained in general terms how the date is determined, ie 31 January after the end of the tax year.



Part (b) related to inheritance tax and was in two parts. The first part was an invitation to candidates to be general rather than specific as it required an explanation of the advantages of lifetime giving. Many candidates did very well but the performance of the majority was unsatisfactory.

The advantages of lifetime giving are scattered throughout the inheritance tax system with certain exemptions only being available in respect of lifetime gifts, potentially exempt transfers being exempt once the donor has lived for seven years, taper relief once the donor has lived for at least three years, and the value of a gift being frozen at the time of the gift together with the availability of relief for any fall in value of the assets gifted.

Most candidates would have known all of these rules but many did not include them all in their answers. Instead they wrote at length about some of them whilst omitting others. In particular, many candidates did not address the exemptions available in respect of lifetime giving. This is likely to be because candidates simply started writing and kept writing until they felt they had written enough. These candidates would have benefited from thinking their way through the inheritance tax system and noting each of the advantages of lifetime giving before they started writing.

The second part of part (b) concerned a particular gift of shares and required knowledge of the valuation rules and business property relief.

The valuation, which involved fall in value together with related property, was done well with many candidates scoring full marks. A minority of candidates were not aware that it is only the spouse's property that is related whilst others failed to appreciate that it is only the donor's property that is valued (the related property is only relevant when determining the valuation).

The business property relief was done well with the majority of candidates identifying the two year rule and the relevance of the investments. Fewer candidates stated the need for the donee to continue owning the shares until the death of the donor.

Candidates did not do so well when it came to identifying other tax issues. Most candidates simply repeated the basics of the inheritance tax rules in relation to potentially exempt transfers when what was required here was consideration of capital gains tax and stamp duty.

Question Three

This question was in two main parts: part (a) concerned income tax and pension contributions and part (b) concerned the remittance basis.

Part (a) was in two closely related parts. It required candidates to calculate the benefit in respect of accommodation provided by an employer and to appreciate the effect on an individual's income tax liability of making pension contributions in excess of the annual allowance, where contributions of less than the annual allowance had been made in earlier years. Candidates also had to recognise that the pension contributions would affect the personal allowance available and the tax bands.

This was a tricky question to get absolutely correct, and very few candidates did so, but there were plenty of marks available to candidates who knew how to put an income tax computation together and were aware of the rules relating to the determination of the annual allowance for a particular year. On the whole candidates scored reasonably well.

In particular, most candidates handled the accommodation benefit well and knew that the tax bands needed to be extended. Many candidates were also aware that there was a three-year rule in respect of the annual allowance, although many were not absolutely clear as to how the rule worked. Many candidates missed the fact



that the personal allowance would be available in full possibly because they did not pause and think at that stage of the calculation. Tax calculations should be done as a series of small steps with thought at each step in order to ensure that important matters are not missed.

The second part of the question concerned the remittance basis and was not done particularly well. The problem here was that candidates did not have a clear set of rules. Instead, they had an awareness of a series of technical terms and time periods that were all confused. This made it very difficult to score well.

The first thing candidates had to do was to explain whether or not the remittance basis was available to each of three individuals. This required a statement of the availability of the remittance basis together with a reason. For those who did not know the rules there was a 50:50 chance as regards the availability of the remittance basis. However, the reason for its availability or non-availability caused a lot more problems.

Candidates must learn the rules and be able to apply them and state them clearly. In addition, the marks available for giving a reason are only awarded where the whole of the reason given is correct. For example, the remittance basis was available to Lin because he was UK resident but not UK domiciled. Candidates who stated this together with various time periods of residency could not score the mark for the reason as it was not clear from their answer whether it was his residence and domicile status that was relevant or the time periods.

The second thing candidates had to do was to state, with reasons, the remittance basis charge applicable to each of the individuals on the assumption that the remittance basis was available to all of them. Again, this was not done particularly well due to many candidates having a very confused knowledge of the rules. One particular area of confusion related to the automatic applicability of the remittance basis where **unremitted** income and gains are less than £2,000; many candidates thought the rule related to the level of **remitted** income and gains.

Question Four

This question concerned various aspects of corporation tax, VAT and groups and was in three main parts.

Part (a) concerned chargeable gains and rollover relief and was in three parts.

Part (i) required a calculation of the chargeable gain on the sale of a building and the correct treatment of the various expenses incurred in acquiring, enhancing and maintaining the property. This was a gentle introduction to the question and was done well.

Part (ii) concerned rollover relief and groups for the purposes of chargeable gains. It was done well by those candidates who knew the rules and who expressed themselves carefully.

This part required candidates to know three things: that rollover relief can be claimed where one company in a gains group sells a qualifying business asset and another company in the group buys one, the definition of a gains group, and the time period in which a replacement asset needs to be purchased in order for rollover relief to be available.

The majority of candidates knew the first and third points although a small minority failed to address the third point despite, probably, knowing the rule. The difficulty came in dealing with the second point and the definition of a gains group where a minority of candidates revealed a level of confusion. This stemmed from a problem in distinguishing the 75% aspect of the rule from the 51% aspect and led to some candidates concluding erroneously that Vault Ltd and Bar Ltd were in a gains group. For there to be a chargeable gains group, the direct holding between each company in the chain must be at least 75%; if it isn't, the two companies cannot be in a group regardless of the level of the indirect holding.



The final part of part (a) concerned the amount that needed to be invested in order for the maximum amount of gain to be rolled over. This was the hardest part of the question and was not done particularly well.

It required candidates to know the basic rule whereby the whole of the relevant proceeds has to be spent on replacement assets in order for the maximum gain to be rolled over, whilst recognising the relevance of the non-business use of both the asset sold and the asset acquired. Almost all candidates knew the basic rule but the majority struggled to apply it in these particular circumstances.

Part (b) concerned the availability of capital allowances in respect of electrical, water and heating systems acquired as part of a building and was done well.

The final part of the question concerned VAT groups. The idea here was to test another aspect of groups in order to ensure that candidates appreciated the difference between a group for the purposes of VAT and one for the purposes of chargeable gains as tested in part (a). Candidates were also required to identify the advantages and disadvantages of registering as a group for the purposes of VAT.

The majority of candidates made a reasonable job of discussing the advantages and disadvantages of registering as a VAT group and made a series of concise points. However, the definition of a group for the purposes of VAT was not handled particularly well. In particular, a sizable minority of candidates thought that the required holding was 75% as opposed to control. In addition, many candidates did not appreciate that control could be exercised by an individual, ie Liza, as well as by a company, such that all of the companies in the question were able to register as a single group.

As always, a minority of candidates wrote in general terms, for example, about partial exemption, rather than addressing the specifics of the question, such that they wasted time.

Question Five

This question concerned various aspects of income tax in relation to the unincorporated trader and the employee and was in two main parts.

Part (a) concerned losses realised on a cessation of trade and was in two parts. Part (i) was short and direct; it was intended to ensure that all candidates attempting this question addressed the two possibilities that needed to be considered when they went on to part (ii) and had to explain the reliefs available in respect of the loss.

In part (i) candidates were required to calculate the trading loss in the year of cessation and the terminal loss of the last 12 months. Very few candidates made a reasonable job of this; the majority of candidates simply did not know the rules. Accordingly, many candidates simply did not appreciate the difference between the loss of the tax year and the terminal loss. Of those candidates who were aware that the terminal loss is calculated in its own particular way, very few knew how to do it. In addition, many candidates deducted the overlap profits from the loss rather than using them to increase the loss.

In part (ii) things did not really improve. Although many candidates were aware that there was the possibility of carrying back a loss on cessation to the three years prior to the loss, there was a general lack of precision as regards the rules and a confused approach to the figures.

When dealing with losses, there are only really two things that need to be known: the years in which the losses can be offset and the type of income or gains that the losses can be offset against. Marks were available in part (ii) for knowing these fundamental rules but they were not awarded as frequently as one might have expected.

The approach of most candidates to part (ii) was not as measured or considered as was necessary. Candidates would have benefited from clearly defining the possibilities in their minds and then writing brief, precise points



that addressed each of the possibilities. Instead, most candidates wrote too much that was confused and often contradictory. In addition, because they did not give themselves sufficient time to consider the possibilities, many candidates did not consider the possibility of relieving the capital gains. Those that did often did so in general terms as opposed to addressing the particular gains in the question.

Part (b) was in two parts and concerned share options and a relocation payment. It was done reasonably well.

Part (i) concerned the tax implications of the grant and exercise of an unapproved option to purchase shares and the eventual sale of the shares. The question made it clear that the option was not part of an approved scheme and it was important that candidates identified this point.

There were many satisfactory answers to this question but also many unsatisfactory ones. The candidates who did well tended to be those who were better organised and were methodical in their approach. In particular, the requirement listed the three matters to address: the grant, exercise and sale of the shares. Some candidates did not address all three of these matters, making it much more difficult to pass this part of the question.

Part (ii) concerned the £8,000 exemption available in respect of relocation costs and was answered well.