**BPT – ACA Simplified additional notes**

**Ch.1. – Corporation Tax aspects**

Exempt Dividends

* Receipt of exempt dividends -> if received from a >50% owned company, not taxable and not part of FII so no tax impact at all; if received from a <50% owned company, not taxable but part of FII. Gross up by 100/90 and add to total taxable profits to find the augmented profits. So exempt dividends received from non-associates is not taxable in itself buy may increase the tax rate applied to the company’s overall profit
* Dividends received by a small company may be exempt on three grounds: 1) received from UK company or a company resident in a country with which UK has a double tax treaty; 2) dividend not paid as part of a scheme with the purpose of gaining a UK tax advantage; 3) paid out of chargeable profits no subject to CFC rules
* Dividends received by a large company may be exempt on five grounds: 1) received from a company controlled by the recipient; 2) relate to non-redeemable ordinary shares; 3) received from a <10% holding; 4) relate to a transaction not concerned with reducing UK tax; 5) relate to shares accounted for as liabilities

Associated Companies

* Associated company -> one company is under the control of the other or both are under the common control of a third party, where under control means >50% of the issued share capital. Overseas companies are still associates, but neither dormant companies nor passive holding companies are (passive = non-trading, no assets other than shares in its subs, no income or gains other than dividends which it has distributed to shareholders)
* Classification as a passive holding company could be a tax benefit as these companies are not counted as an associate therefore the main rate upper limit will be divided by fewer associates so could lead to a lower tax rate being payable

Research and Development Deductions

* SME companies for R&D -> <500 employees and turnover of <100mn euros or annual balance sheet of <86mn euros
* R&D tax credit surrenderable loss -> lower of: trading loss after s37 CY relief regardless of whether an actual claim is made or 225% of the qualifying R&D expenditure. The tax credit is given at 14.5%. Claiming the R and D tax credit reduces trading losses c/f by the amount of the loss surrendered to obtain the tax credit
* Example of the above rule: trading loss = 500k, capital gain = 30k, R&D spend = 100k. Surrenderable loss for tax credit would be the lower of: 225% of £100k = £225k or the ‘adjusted trading loss’ on which a possible s37 claim could be made = (500k – 30k) = £470k, so a maximum claim of £225k, as the tax credit is an incentive so HMRC will offer as little as possible to be used as part of the tax credit. Tax credit itself will be 14.5% x 225k = £32,625

Large Companies above the line tax credit

* Above the line tax credits for large companies -> these are the new rules where the credit is recorded in arriving at pre-tax profits, election for this rule applies from 01/04/13. Election will no longer be required from 01/04/16
* Large company R&D calculation: amount of relief is 10% of the qualifying R&D expenditure, this is used first against the CY CT liability and then determine if any surplus remains after CY relief.
* For amounts within the capped amount, this is treated as paying the CT liabilities of other period, with any remaining balance used to offset any other amounts due to HMRC. Any remaining balance is paid by HMRC to the company, unless the company is not a GC or has outstanding PAYE or NIC liabilities

Intangible IFAs and Rollover Relief

* Intangible fixed assets -> on disposal, if normal accounting treatment is followed then there is no special tax approach and accounting profit or loss is used; if 4% straight line amortisation has been followed, find the difference between the proceeds and the TWDV of the IFA
* Rollover relief for IFAs -> similar to normal rollover relief. Deduct relief amount from the gain, rollover into the base cost of the acquired asset by reducing the base cost of the new asset by the total relief claimed; -1/+3 years reinvestment period, if proceeds not fully reinvested restrict rollover relief to amount reinvested. The difference from normal RoR is that the relief can be rolled over into purchase of shares in a company where the value reflects the IFAs held by that company or a sub. The deemed expenditure on IFAs where rollover relief is claimed on share purchases is lower of: cost of acquiring shares in the company or the TWDV of the IFAs the company holds

Patent Box

* Patent box rules -> qualifying developments include both the patent itself or of products incorporating the patent. Group patent box rules: claimant company must be the company that carries on the active management of the patents
* Rules list -> apply from 01/04/13, election can be made to put profits related to patents into the patent box and effectively suffer CT at a lower rate. Company then determines its patent profits and can then deduct a notional 10% of the costs allocated to the patent business excluding interest and R&D, notional marketing royalty can also be deducted
* Patent box formula: between 60% to 100% depending on what year we’re in from 2013 to 2017 so for FY2014 it’s a 70% constant: Profits in the patent box\*70%\*((21-10)/21)

NTLR deficit relief

* CY NTLR deficit relief -> offset wholly or partly against CY profits – note that this partial offset is unusual for losses but allowed for NTLR – AFTER b/f trading loss but before CY or carry back claim for trading losses and CY property loss offset

MCINOCOT and shell companies

* MCINOCOT cases -> either a major change in the nature of conduct of trade within 3 years before or 3 years after a change in ownership, or trading activities which were small/negligible increase considerably after the change in ownership. MCINOCOT can include: services/facilities provided, nature of customers of the trade, nature of assets traded, location of business premises, suppliers, management or staff changes, manufacturing methods and pricing/purchasing policy. MCINOCOT losses do not apply to capital losses, but other rules may apply to capital losses on change in ownership
* A major change in ownership occurs where > half the ordinary share capital is acquired by a single person or >1 person where each person holds at least 5%
* Shell company rules -> apply to changes in ownership post 20/03/13. NTLR debits and deficits and non-trade debits and losses on IFAs cannot be carried backwards or forwards through the date of the change in ownership. Shell companies have no trade, no investment business and no UK property business

SSE

* SSE: capital gains become exempt from CT and capital losses are not allowable. To qualify for SSE a 10% holding of ordinary shares is required and must be beneficially entitle to at least 10% of distributable profits and assets on winding up and these conditions must be satisfied for a continuous period of 12 months out of the last 24 months pre-disposal. From a group perspective, if company A holds 5% in company X and company B holds 7% in company X and then form a 51% group then the 12% total holding in X counts for the period A and B have had their individual holdings so clock does not reset at the point of the group being formed
* New SSE rules, important when considering corporate restructuring, e.g. a share sales versus a trade and assets sale -> from 01/04/11, by early commencement election or otherwise from 19/07/11, when a new company is incorporated and receives trade and assets of another group company, the new company will be treated as though held for 12 months and having traded for 12 months

REITs

* REITs -> qualifying property income and gains are CT exempt, non-qualifying income and gains are taxable at the main rate. Distributions from tax exempt income or gains are taxed as though they were property income and distributions from taxable income/gains are taxed as a UK dividend

**Ch.2 – Raising Finance**

NTLR Deficits

* Relieving an NTLR deficit -> can be done in three ways: 1) in whole or in part against current period total profits (partial offset being unusual for losses); 2) surrender in whole or part as group relief; 3) offset in full against NTLR profits of the previous 12 months, after prior period deductions for losses
* Relief for NTLR deficits is different from other reliefs, as the current period relief is not an all or nothing claim, a partial claim is possible. Therefore planning strategies can be used to preserve the use of double tax relief credits or other CT reliefs
* Priority of using the various possible current period losses: 1) NTLR deficits 2) property losses 3) trading losses
* Profit/loss on disposal of a loan, along with interest costs and fees in relation to the loan, are all treated as NTLR

Tax advantage of paying interest over dividends

* Advantages to a company of paying investors interest rather than dividends -> interest is tax deductible so cost to company is only 79% the interest amount, whereas dividends are not tax deductible so the cost = the interest amount
* Tax advantages of debentures over dividends -> debenture issue costs and interest costs are tax deductible, dividend equivalents are not as share issues are capital in nature and dividends are distributions

Foreign Exchange

* Foreign exchange gains/losses on trading transactions (buying and selling goods) -> treat as trading profits/expenses
* Foreign exchange gains/losses on monetary items (receivables and cash) -> treat as NTLR
* Foreign exchange gains/losses on capital monetary items (e.g. long term loans) -> these are only taxed when they hit the P and L
* Foreign exchange gains/losses on non-monetary capital assets -> treat these as part of the capital gain/loss comp once the profit/loss on disposal has hit the P and L
* For disposals post 01/09/13 involving gains on ships, aircrafts and SHARES, calc should be based on company’s tax currency and converted into sterling at the spot rate on the date of the transaction. In cases other than this, transactions should convert both the original cost and proceeds at spot rates

Connected party loans

* Connected party loans -> where there is a loan between two companies when one controls the other. Tax relief for the payment of interest is delayed until the actual payment if paid > 12 months after the relevant accounting period, there is no relief for bad debts

Hedging Transactions

* Tax treatment of hedging transactions -> key point is to treat them based on commercial substance rather than on their Financial Instruments treatment per IAS39. If the transaction hedged is a trading transaction then the forex amount will generally be taxed in the same period as the transaction it is designed to hedge hits the P and L. If SSE applies, the ForEx gains and losses on the hedge are also exempt

Long-funding leases

* Long funding leases -> a lease of more than 5 years. A lease may still be short if it is a finance lease of 5-7 years, value is < 5% of initial market value and rentals do not vary by > 10%. To be a funding lease at least of one of: 1) finance lease per UK GAAP/IFRS 2) PV of MLP at least 80% FV and 3) term is > 65% remaining UEL, must be fulfilled. So this relates to two separate tests, the ‘long’ test and the ‘funding’ test

**Ch.3 – Group relief and Consortium relief**

Group relief background and tax planning

* Group relief is a current period relief only, brought forward losses and losses carried back cannot be group relieved
* The loss making company may surrender its current period losses as group relief prior to using them against its own profits – no rules forcing them to use the losses in a particular way
* Group relief may be a partial claim so from a tax planning perspective, need to make sure that not too much group relief is claimed to waste QCDs; excess QCDs may also be surrendered as group relief

Overseas PE

* Losses of an overseas PE -> these can be group relieved back to the UK provided the losses are not relievable overseas, no election was made to exempt profits/losses of the PE and the trade does not amount to a separate trade carried out wholly overseas

Group Relief of UK PEs

* What about a UK PE of a non-resident company? -> if the UK PE is within the charge to corporation tax, it is treated as just another element of the group and group relief can be claimed and surrendered to and from the UK PE. A loss arising in a UK PE of a non-UK resident company can only be surrendered to other companies in the UK group if those losses are not relievable in the overseas country. As of 01/04/13, this rule will only refer to losses actually relieved overseas, i.e. if it is possible to claim relief but none is actually claimed then it will be possible to claim in the UK

Non-resident subsidiaries rules

* Loss relief in relation to overseas losses of a non-resident sub -> if a 75% sub and current and future loss relief options have been exhausted overseas, the loss can be relieved to other companies in the UK group, recomputed using UK tax principles. The sub must be either EEA resident or must be carrying on a trade in the EEA through a PE. Loss relief is denied where the main purpose of the arrangement is to obtain UK relief

Group Relief and MCINOCOT

* Occasions where group relief can be broken, where group transformations occur -> MCINOCOT within +3/-3 years of the change in ownership, revival of trade following change in ownership, where arrangements for a company to leave a group are in place, where a liquidator has been appointed for a holding company

Group/Consortium Companies

* Group/consortium companies -> this refers to a consortium company which also has its own group underneath it. When a company like this makes a loss, need to make a calculation to determine the amount available to consortium members. It is assumed that the group/consortium company first deals with the group and then the balance available is then surrendered upwards to the consortium members. So, order of loss relief: 1) assume loss is set against the G/C company’s other profits in the year 2) assume max. group relief surrenders to group are made 3) surrender consortium members’ share upwards. Stages 2 and 3 require tax planning, as choices will be made over group relief surrenders within the group

Link Company

* Link company -> a member of the consortium and also of the group. Different from a group/consortium company which is a company owned by a consortium with its own group. It must be either UK related or EEA established if accounting period begins after 12/07/2010 or if EEA established before this date must be part of a group with the claimant or surrenderer without involving a company not established in the EEA. There is no priority between group relief and consortium relief

Marginal Rates vs. FY 2013 and FY 2014 comparison

* Using group relief in consideration of both FY 2013 and FY2014 -> key normally is to target profits in the marginal rate as this will be the top rate for each respective FY. However tax rates have been falling over time, so marginal rate for FY 2014 is 21.25 vs main rate of 23% in FY2013. Therefore if we have a main rate company in FY13 in the scenario should ignore this normal logic of targeting the marginal rate and instead target the main rate payer in FY13. Also if there is any DTR involved, make sure sufficient tax is left in charge to make best use of the DTR available. This would be another occasion where it may be wisest to leave a higher amount of tax in charge to make full use and therefore to not target the marginal profits in full

Disclaiming Capital Allowances

* Disclaiming capital allowances -> where a company already makes a loss and capital allowances are claimed, the loss will then increase and be carried forward as a trading loss which may only be used against future trading profits. If capital allowances are disclaimed, a larger amount can be claimed in a future year against total profits which will allow greater flexibility

Group Payment arrangements

* Group payment arrangements -> at least ONE member of the group must pay by instalments. Parent companies, their 51% subs and their 51% subs are eligible, and it is possible to have several GPAs within one overall group

**Ch. 4 – Chargeable Gains Groups**

Intro to Group Transfers

* Group must be of 75% subs but the principle company must have an indirect holding of at least 50% e.g. 80% holding 80% holding is fine but if the second 80% holds a 75% this can’t be in the CG group as the effective holding is only 48% for the parent company at this point
* Intra group transfers for CG purposes are generally made NGNL. On sale the cost is the original acquisition cost to the group (not to the selling company) plus the indexation allowance up to the date of transfer
* NGNL transfers -> may occur between a UK tax resident company to another UK tax resident company, from a UK branch of a non-UK tax resident to a UK tax resident company or from a UK tax resident to the UK branch of a non-UK tax resident company. Where a UK branch is involved in the transfer the assets must remain chargeable to UK corporation tax after the transfer in order for NGNL to apply

De-grouping Charges

* DGC occurs if a company ceases to be a part of the gains group < 6 years after an NGNL transfer
* Impact of the new FA 2011 rules on de-grouping charges -> apply from 19/07/11 or 01/04/11 by early commencement election. Under the new rules it is no longer the liability of the departing company if it leaves the group due to a qualifying share disposal, i.e. by means of an issue of shares to anything other than an unconnected company
* Under the new rules the de-grouping gain is added to proceeds received on disposal to increase the gain. A de-grouping loss is added to the allowable cost on disposal to reduce the gain
* Base cost of asset carried forward by the departing company under both old and new rules is MV at the date of the original NGNL transfer. The departing company gets indexation allowance from that date onwards when they subsequently sell
* ‘just and reasonable claim’ -> this is in relation to giving an exemption to a de-grouping charge. If the consideration paid is roughly equal to base cost to the group, the departing company has the ‘correct’ base cost carried forward so will have to pay the correct, higher CGT when the asset is sold so no de-grouping charge will apply in cases like this

SSE and hive downs

* SSE and hive downs -> where the hive down strategy is applied and the new company is incorporated, receives the trade and assets of another company before being sold on, this would not normally qualify for SSE as the new company has not been held for 12 months. However, shares in the new company are treated as having been held for 12 months and it will be treated as having traded for 12 months so SSE applies and therefore this is a normal qualifying share disposal which will prevent any de-grouping charges applying to a hive down. For the exam it might still be worth calculating what the de-grouping charge arising would be, even though it is will not actually be applied where SSE is going to be given

Transfer capital asset into trading stock

* Transfer of capital asset into trading stock of another company in the same gains group -> acquiring company can treat the resulting gain/loss as a trading gain/loss rather than a capital gain/loss. Capital gain would be the default position and under this method the transfer is at NGNL but then deemed disposal is at MV leading to a capital gain and the asset becomes trading stock in the acquiring company. By election, both the increases from NGNL to MV at transfer and later increase between transfer value and sales proceeds can be treated as trading profit. HMRC may also attack an election to go the other way and convert a capital loss into a trading loss if the transaction is not deemed to be genuine

Transfer trading stock into capital asset

* When a transfer occurs the other way and a trading asset is transferred into the capital assets of a company in the same gains group, this is treated as trading profit/loss by the transferring company
* For questions like this need to consider the nature of the trades of the two companies involved in the transfer to determine the nature of the asset; generally if the question mentions the trade of the companies for a reason so look out for this

Succession of Trade

* Succession of trade -> PPE transferred at TWDV. This arises where trade is transferred between companies in the same ownership. The accounting period ends at the date of transfer, predecessor claims capital allowances as normal, the successor can take on trading losses and use them vs the future profits of the trade in which these losses were incurred
* The trading losses taken forward by the successor are subject to restrictions -> restricted by excess of relevant liabilities over relevant assets which are assets not transferred plus consideration for the transfer of trade and where relevant liabilities are liabilities not transferred excluding shares, reserves and loan stock. Loan stock does however reduce the value of a relevant asset – 5% loan stock of £20k secured over an asset worth £500k would reduce the relevant asset value to £480k but the £20k itself is not treated as a relevant liability
* Where there is no succession to trade, trading losses are lost and cannot be claimed by any transferee company and balancing adjustments arise on assets qualifying for capital allowances, though no WDAs may be claimed in this final period
* Exam points to make in a succession to trade question -> always look to question the nature of the trade of the successor company and whether or not it is closely related to the trade of the predecessor company; if not connected closely enough then the losses will just be lost
* Even if the losses are eligible to be brought forward into the new company, this will only be against the trade of the successor company, not any second trade that this company may carry on
* Should also consider, where the receiver of the old trade carried on a trade of its own prior to acquiring the new trade, whether the two trades have been merged into a new business in which case losses and TWDV cannot be carried forward. Alternatively where there is an old trade and a new trade, it may be deemed that the two trades are being carried on in tandem in which case losses can be brought forward but must only be offset against future profits from the ‘correct’ trade and must be streamed to ensure they are only offset against that trade

Anti-Avoidance

* Anti-avoidance measures for ‘capital loss buying’ -> a company may look to change ownership in order to use the capital losses of either the target company or the acquiring group. HMRC have therefore ruled that no losses can be offset against pre-entry gains and pre-entry losses are not allowable losses within the new group

Tax Planning of Transfer of Trade

* Where it looks as though trading losses brought forward may be restricted by relevant liabilities exceeding relevant assets, tax planning can be used in relation to the consideration paid for the transfer of trade. By increasing the consideration paid, relevant assets will be boosted and so can be lifted just enough to prevent any restriction occurring
* Reallocation of chargeable gains/losses within a group must be made by joint election and must occur within 2 years of the end of the accounting period in which the disposal was made which allows more tax planning to occur – can review gains and losses after the end of CAP to determine the best strategy

**Ch.5 – International Expansion**

UK Residency Status

* Where a company is not UK incorporated, UK tax residency still applies where central management and control resides in the UK, generally determined by where the board of directors sits
* If a company is UK tax resident, it is taxed on worldwide profits, subject to DTR. Remittance of these profits as dividends is irrelevant

Election to Exempt Overseas PEs from UK CT

* As of 2011 an irrevocable election can be made for all foreign PEs to be exempt from UK CT on profits but this also prevents losses from being claimed. This applies from the start of the CAP after the one in which the election is made
* Payments subject to deduction of income tax e.g. yearly interest and royalties are excluded from the election to exempt, as are PEs of small companies (<50 employees, <10mn euro turnover and balance sheet
* profits of a PE where election has been made are not exempt if they are ‘diverted profits’ which would not pass through the CFC gateway (see later notes); if the PE’s local territory tax is not at least 75% of UK tax equivalent, if accounting profits are more than 10% of the operating expenses, if the PE’s taxable profits are >50k in a 12 month period AND the local territory is not listed in HMRC regulations listing of high tax jurisdictions then the profits will not be exempt – i.e. provided one of these criteria is met the profits will be exempted
* So in summary, election should be beneficial where: 1) UK company has low taxed PEs not subject to anti diversion rules; 2) UK company has high taxed PEs and UK tax losses allowing the losses to be preserved for a future offset; 3) there will be administrative savings by making the election, as identifying PE profits to be removed from the UK CT computation are costly to perform due to their complexity
* Changes in PE profit exclusion election -> has become more generous in relation to gains since 01/01/13 with gains on assets used solely for the purpose of that company’s trade in the foreign territory is exempted. Less generous in relation to investment businesses as profits and losses no longer fall under election rules, unless relating to assets effectively connected with the PE through which the trade is carried on

Overseas Subsidiary vs Overseas PE

* Matrix of when it’s better to set up an overseas sub or a branch: where rates of tax are lower overseas than in UK and future profits are forecast a sub will be better, where future losses are forecast a branch; where tax is lower in the UK than overseas and profits are forecast a branch will be best, where losses are forecast either a sub or potentially no difference
* Benefits of using a PE over a subsidiary -> if losses are expected in a host country outside the EEA then a PE will be beneficial as overseas losses of a 75% sub can only be surrendered to the parent if that sub is resident in the EEA but this restriction does not apply to a PE, provided the losses do not relate to trade carried on wholly overseas; once it becomes profitable, a PE is no longer tax-efficient. At this points its profits will be added to the UK parent’s tax comp and taxed at UK rate but if it is incorporated into a sub at this point, profits will be taxed at the host country’s rate which will be beneficial provided this rate is lower than the UK tax rate

UK Parent use of PE losses

* UK parent use of PE losses assuming no exemption has been claimed -> should be relieved against profits in the host country, next they should be relieved against profits of the UK parent provided the losses relate to a trade not carried on wholly overseas. If trade is wholly overseas, losses can only be offset against future profits of that PE trade as they cannot be used against UK profits

UK Resident company ceases to be resident (Migration)

* Migration -> an overseas incorporated company but with UK tax resident status due to its central management location, relocates control outside the UK and so ceases to be resident. At this point the company is deemed to have sold and reacquired all its assets at MV, giving rise to an ‘exit charge’ of the difference between original cost plus IA and the MV at migration. So will need to use the inflation indexes and the index at sale – index at acquisition/index at acquisition formula to get the indexed cost like for a normal gain for a company
* EEA exit charge deferral -> apply to migrations from UK to another EU member state from 01/12/12. Introduced because it was found to be against company’s right to freedom of establishment to collect the exit charge at the time of migration because if the company didn’t migrate, it would not have to pay tax until the underlying assets were sold. Chargeable gains exit charges, profits on disposal of trading stock on cessation of trade and exit charges under IFA and loan relationship provisions can all be deferred.
* The claim to defer the charge must be made within 9 months of migrating. The maximum amount that can be deferred is the amount by which the CT for the period ending with the migration is greater than would have been the case without the exit charges
* There are three deferral options -> 1) standard instalment method of 6 equal annual instalments, the first due 9months and a day after the end of the accounting period of the migration; 2) realisation method – the tax is due on the earlier of asset disposal in the future and the tenth anniversary of the end of the accounting period of the migration. The first instalment is also due 9 months 1 day after the end of the accounting period of migration. For IFAs and loan relationship exit charges, charge is spread over 10 annual instalments; 3) a mixture of numbers 1 and 2. Investments always suffer the exit charge immediately, this deferral only applies to trading assets
* Deferred gain becomes chargeable if: 1) non-UK sub disposes of any relevant assets within 6 years of migration; 2) parent disposes of the shares so the sub is no longer a 75% sub; 3) parent company ceases to be UK resident. Total net gain is apportioned so that only share of gains relating to the relevant assets is charged
* Exit change and gain deferral rules apply to intangible assets created post 01/04/02

Relief on incorporation of an overseas sub

* Potential relief on the chargeable gains on incorporation of an overseas subsidiary -> in order for this to be claimed, all trade and assets except cash must be transferred, at least part of the consideration must be in shares (i.e. not all cash as this would mean that the tax bill could be footed with the cash inflow; where the consideration is part cash part securities, the cash proportion is immediately chargeable to capital gains tax), a claim has to be made as it is not an automatic relief and the transferring company must hold at least 25% of the ordinary share capital of the new sub
* Crystallisation of a gain deferred by incorporation relief -> either when UK parent disposes of the securities or when the new sub disposes of any of the assets on which the gain arose within 6 years. Where the securities are disposed of, gain previously deferred becomes chargeable plus any gain on the securities themselves so effectively there are two gains to now consider. For the disposal of an asset within 6 years, remaining balance of net gain deferred multiplied by the proportion of the gross gain on incorporation attributable to the asset disposed of

Double Tax Relief

* Unilateral relief -> DTR is given as a credit against UK CT on the foreign income
* Expense relief -> overseas tax paid is treated as an expense so this expense is deducted from overseas income in the tax comp. Expenses method prevents unrelieved foreign tax occurring. If the company is already loss-making, there is nothing to credit the DTR against; it is better to include the foreign income net of tax suffered so the smallest possible amount of the losses are required to soak up a smaller overseas profit
* Maximise DTR strategy -> offset losses against foreign income with the LOWEST marginal rate. This is because income from the country with the higher marginal rate will probably only get DTR at UK rate in most cases and this UK tax needs to be kept as high as possible as this is the highest amount of relief which can be claimed against the higher foreign tax

Receipts of Foreign Dividends

* Foreign dividends received key points -> always gross up by 100/90 for FII purposes; completely ignore any foreign tax suffered on the dividend – the question usually states this but it is a red herring when looking at dividends

Withholding Tax

* Withholding tax -> if mentioned in the question, ignore it if it relates to a dividend and always gross up by 100/90 instead; use it if it relates to foreign income relieved, e.g. on foreign profits earned. Add the withholding tax on as the profits earned/income etc needs to go into the tax computation gross. Different from DTR, withholding tax is the amount withheld on sources of overseas income
* Unrelieved foreign tax occurs where the overseas rate of tax is higher than the UK rate -> DTR will be given on the lower of UK and overseas tax so where overseas rate is higher the unrelieved amount is usually just lost. The exception is when it relates to an overseas PE without a separate trade carried on wholly overseas. If this is the case it can be carried forward for use against future tax liability of that PE or carried back 3 years on a LIFO basis against the UK tax liabilities of that PE

Differing definitions of what constitutes a PE

* Definition of a PE -> a little subjective but generally either a fixed place of business through which the business is run or a company-appointed agent has authority to, and regularly does, carry out business on their behalf in the territory
* Under UK rules, a server cannot constitute a PE; under the OECD rules it can do, if the owned/leased server is used for anything more than ‘auxiliary or preparatory’ activities
* Places not constituting a PE -> storage , display or delivery facilities, stock and WIP facilities, purchasing facilities

Anti-Discrimination Provisions

* Non-discrimination provision -> foreign nationals taxable in another country will not be charged any more tax than a native on similar income
* Mutual agreement procedures -> UK nationals taxable in another contracting state may apply to HMRC if they feel they are not being taxed in accordance with the treaty. HMRC will then make a mutual agreement with the other Contracting state to resolve the situation. The case must be notified to HMRC within 3 years of the action being taken

**Ch.6 – Corporate Anti-avoidance**

Close Companies

* Close companies -> controlled by 5 or fewer participators or unrestricted participators who are also directors. ‘Directors’ here includes de facto directors, shadow directors or managers able to control 20% or more of the company’s share capital. Not close if listed with at least 35% voting power in public hands or controlled by other companies which are not close
* Participators may be individuals but can also include trustees of a settlement where either trustee or beneficiary is a participator or an associate of one. Can also include an LLP or partnership in which a participator or associate is partner

Participator Loans

* S455 charge -> 25% charge on a loan made to a participator. Repaid when the loan is repaid or written off. Due at the same time as normal tax under self-assessment = 9 months 1 day after CAP
* No deduction against CT is allowed when a loan to a participator is written off
* From the participator’s perspective, the write off is treated as a dividend. Gross up and give a 10% tax credit so that a BRB payer pays no tax, an HRTP at 25% and an ARTP at 30.56% net tax
* Close company loans and anti-avoidance -> repayments are only counted as such when they exceed the amount of a new loan. New loans are deemed created where either a repayment of at least £5k and a new loan of at least £5k occur in the same 30 day period, or the loan balance was at least £15k and at time of repayment it was intended that a new loan would be made. In the latter case the repayment is treated as a repayment of the new loan. So the new rules are there to prevent repayment of a loan to avoid an s455 charge followed by the creation of a new loan to replace the original
* Where a participator is an employee and a loan is written off they are liable to class 1 NICS
* Loans of < £15k, loans to a full-time close company employee, and loans to borrowers with a <5% stake in the company are not liable to the s455 charge

Benefits Provided to non-employees

* Benefits provided to participators who are not employees of the close company should be treated like dividends, so grossed up by 100/90, no class 1A due from the employer and non-deductible cost for the employer

Qualifying interests

* Qualifying interests -> qualifying interest rules apply from 2014/15 on any purchase of shares in a close company by a 5% plus participator or an employee. IT relief is available on any interest paid, provided the shares have not already been given EIS relief

Close Investment Holding Companies

* Close investment holding companies -> close company which does not trade commercially, let land or hold shares. Close companies become CIHCs on ceasing to trade. These are always taxed at the main rate regardless of level of profits with no tax relief for participators under qualifying interest rules
* Appointment of a liquidator -> if a liquidator is appointed the close company does not become a CIHC for the first accounting period after the appointment. So to prevent taxation at the main rate, the liquidator should be appointed before the cessation of trade

Controlled Foreign Companies

* Controlled foreign companies -> non-UK resident, under UK control (50%+) or at least 40% UK controlled and no more than 55% but at least 40% foreign company controlled, tax charged is <75% of what would be due if UK resident
* CFC profits are apportioned between shareholders and taxed at main rate, applicable to all UK companies owning at least 25%, even though the 40%/55% holding defines CFCs as in the bullet point above
* CFC tax paid abroad -> UK tax payable is reduced by apportioned amount of tax paid. DTR applies and net impact is to bring the tax to the main UK rate on the relevant apportioned amount

Transfer Pricing Rules

* Transfer pricing rules -> applicable to large companies or companies within a large group: at least 250 employees, or revenue of at least 50mn euros and total assets of at least 43mn euros. Profits should be calculated as though the transaction took place at market price, strictly only the company gaining a tax advantage makes an adjustment but usually UK companies make equal and opposite adjustments
* Manipulation of intra-group pricing -> For business reasons they may occur to boost profits where performance bonuses are based on profit or to simplify intra-group costing procedures. For tax reasons manipulations may occur to move profits to low tax jurisdictions or to utilise b/f losses which would otherwise stay in the loss-making company
* Where a tax advantage occurs in this respect, income, expenditure, profits and losses of the advantaged company must be adjusted to ensure arm’s length pricing is applied
* ‘thin capitalisation’ -> where a loan is obtained from a connected company on better than market terms. HMRC applies the rules of debt:equity ratio exceeding 1:1 and interest cover < 3 times. Need to consider whether a market actor would lend to the company, considering just the company on its own and ignoring guarantees another member of the group could make

Worldwide Debt Cap

* Worldwide debt cap -> applies to companies where any member of the group is large and the company is UK resident or trading in the UK and the parent of the worldwide group or a 75% sub of the ultimate parent
* Part 1 of debt cap – gateway test-> average UK net debt 75% or more of average worldwide debt? If not then ignore Part 2 -> the debt cap restriction, disallowance of the ‘tested expense amount’ less the ‘available amount’. As a rule, UK headquartered groups with UK subs will tend to have a lot of UK debt and so are likely to fail the gateway debt and therefore a debt cap restriction is likely to apply. In calculating the net UK debt, dormant companies, companies with net assets and companies with net debt < £3mn are excluded
* Worldwide gross debt includes all companies and is the average of relevant group liabilities at the start and end of the period, per the worldwide group’s accounts
* Tested expense amount (TEA) -> sum of net financing deductions (finance expense less finance income) of each relevant UK group company. If there is net finance income, enter a zero, if less than £500k, also enter as a zero
* Available amount (AA) -> the world-wide group’s gross consolidated finance expenses, both UK and non-UK. AA is the amount which is allowed, any excess over this within the TEA is disallowed
* Excess of the TEA over the AA is disallowed and can be allocated as the group wishes, although any individual company can only have disallowance up to its net finance expense. Financing income up to the lower of the disallowance and the TEA is exempted and the exemption can also be allocated as the group wishes
* Transfer pricing rules are applied first before debt cap rules
* New rules re: de minimis limit within the worldwide debt cap -> the £500k de minimis limit can now be disapplied; this would be beneficial where total income which would be ignored as a result of this limit is more than the deductions which are ignored. The new election to disapply the limits must be made within 12 months of the end of the period of account to which it is first intended to apply

CFC Gateway Profits

* The CFC charge gateway -> CFC profits pass through the charge gateway unless at least one of the following 4 conditions apply: 1) CFC has no assets or risks deriving from tax planning schemes; 2) none of the CFC’s assets or risks are managed from the UK; 3) CFC could manage its own business if UK management were to stop; 4) CFC profit consists solely of non-trading finance profits and/or property business profits
* Under CFC rules, non-trading finance profits are not taxable when they are no more than 5% of total income, income is profits from investment of funds held where none of the profits of the trade have themselves passed through the CFC gateway or if income is profits from the investment of funds held by the CFC for purpose of its UK or overseas property business
* After carrying out the gateway tests, any business profits artificially routed through an overseas entity despite being attributable to the UK company are chargeable. In considering this, we should keep in mind whether a third party would have entered into such arrangements. Certain finance profits would also be chargeable after carrying out the gateway tests
* Indicators for exam questions on profits passing through the gateway -> need to use the question to decide whether the entry conditions will be passed or failed. Remember at all time as well that the company do not want any profits to pass through the gateway. Consider: how does the UK get involved in the management of the CFC? Does it negotiate contracts on their behalf and is whatever role the UK does unlikely to be possible without UK involvement. Does the UK support the CFC financially? Are guarantees given by the UK – i.e. could the CFC carry on without the UK?

NTLR Profits Gateway for CFCs

* Non-trading finance profits can also pass through the gateway -> for this to happen they have to be more than ‘incidental’. The profits are incidental where CFC has an active trade or property business or CFC is a holding company for 51% subs who trade themselves and the non-trading finance profits are no more than 5% of its ‘good’ profits
* Where the non-trading profits are assets/risks where significant people in the UK are involved, or they relate to capital investment from the UK or they relate to UK finance leases, these are not incidental and the profits pass through the gateway
* Qualifying Loan Relationship -> for the purposes of a finance company exemption, a loan is a QLR where the CFC is the creditor, the loan is not specifically excluded by legislation and the ultimate debtor is connected and controlled by the same UK companies which control the CFC. Since 05/12/13 there is a new rule to prevent UK companies effectively exporting a loan receivable to a non-UK company to benefit from the CFC rules. For example, a UK parent company makes a loan to an overseas sub with interest due to the UK company but then the parent sets up a new CFC and transfers the loan to the CFC in exchange for shares in the CFC. This is designed solely to achieve a reduced tax bill through use of a CFC so it is disallowed and the parent company gets no benefit from its attempt to avoid UK tax

Guaranteed Loans

* Guaranteed loans -> these can be beneficial to UK companies. They are loans where another group company provides a guarantee to a bank. These are normally treated in the same way as any other loan and may result in a disallowance under thin capitalisation rules but in some cases may be possible for the guarantor to claim a corresponding adjustment to profits, provided the guarantor would have been able to borrow the amount. Where the guarantor is a subsidiary of the borrower this benefit is not permitted

Value Shifting and Depreciatory Transactions

* Value shifting rules -> aim to ensure that transfers of value such as payment of an inflated dividend before selling a company are not used to convert chargeable gains into exempt income
* Value shifting rules can restrict a loss or create/augment a gain and this is achieved by increasing the consideration received by a just and reasonable amount
* An adjustment will be required under value shifting rules if: 1) arrangements have been made to materially reduce the value of the securities or asset disposed of AND 2) main purpose is to obtain a tax advantage AND 3) arrangements do not consist solely of making an exempt distribution
* Specifically stated occasions per the study manual where value shifting rules do not apply -> 1) a normal pre-sale transaction provided the consideration is a true measure of the value of the disposal; 2) where SSE exempts the share disposal so that reducing the share value will give no tax advantage
* Depreciatory transactions -> apply to companies in gains groups; they reduce allowable loss on disposal to the true commercial loss where shares’ value has been materially reduced. Depreciatory transaction example: moving assets around a group at < MV, cancelling a loan or debt, payments to fellow group members for services or products at < MV, excessive group relief payments. For the rules to apply, time between reduction in value of the asset and crystallisation of the loss must occur within 6 years

**Ch. 7 – Companies: Special Situations**

Company share buy-back

* Sale back to company of shares -> where a company holds the shares, this is treated as a chargeable gain or loss and SSE may apply; where an individual holds the shares it will be treated as either an income distribution or a capital distribution
* For a capital distribution, simply treat as a normal CGT calc. in relation to the entire disposal
* Income route -> this has two elements; the income elements and the capital loss. Income element = (proceeds-subscription price) x 100/90. Capital element = (purchase price – subscription price) x number of shares. This second capital element will not apply if the purchase was originally at par, element one, the income element, will always apply. A deemed tax credit of 10% is given on the income element, as normal with a dividend
* If a BRTP, there will be no tax to pay at all with the income route as the dividend tax credit soaks up the tax on dividends
* Capital route will make the annual exempt amount available and entrepreneur’s relief may also be available

Capital route conditions

* Capital route = mandatory when: purchase is for trading benefit or proceeds settle an IHT liability
* Conditions the purchaser must fulfil for the capital route to apply -> 1) must not be listed 2) shares must be purchased for the benefit of trade 3) purchase must not be to avoid tax
* Conditions the seller must fulfil for the capital route to apply -> 1) UK resident 2) shares owned for 5 years, 3 if inherited 3) may not hold more than a 30% share in the purchaser or in any company in the group above the sale 4) shareholding must be substantially reduced by holding 75% of the pre-sale holding – this 75% rule is a strange one, best thing here is to refer to the TYU example in the Kaplan workbook

Consequences of Liquidation

* Liquidation tax consequences -> liquidator is responsible for paying CT tax post winding-up, CT continues to be charged on any profits arising during winding-up, accounting periods end on anniversary of the winding-up commencement, liquidator becomes beneficial owner of company assets and this is not a chargeable disposal
* Winding-up/liquidation will mean that only losses accrued up to the date of commencement of the liquidation process can be group relieved and group relief could only be claimed up until the date of commencement so the winding-up effectively becomes a wall through which losses cannot be passes, a little like MCINOCOT rules

Capital Gains and Liquidation

* Tax planning for capital gains re: cessation of trade -> it is sensible to try to realise capital gains before the company ceases to trade as once the trade ceases, trading losses cannot be carried forward against gains. If gains are realised whilst current year trading losses are being made, these can be offset against the gains to be more tax efficient
* Distributions before winding-up begins are treated as income, after winding-up begins = capital. A company shareholder may prefer this if SSE applies and ER may be available to an individual. Treated as a disposal of shares even if paid cash from accumulated net profit. Individuals will be taxed on CG as a max of 28% post potential reliefs, companies at marginal rate if SSE does not apply
* Cases where distribution of funds pre –liquidator appointment can be treated as a capital distribution -> company intends to collect debts and pay off creditors or has already done so AND total distribution is no more than £25k – consider stating if beneficial to the shareholder. This can be withdrawn if debts not collected/creditors not paid off two years after the distribution

Winding Up Strategies

* Potential winding-up strategy -> could possibly pay out a large dividend (an income distribution) so that later CG is reduced which may benefit individual shareholders but need to assess on the info given. A dividend artificially creating a capital loss would be a depreciatory transaction and so would not be allowed
* Share premium and share capital may not be distributed as part of a winding-up unless a formal liquidation is in place

Striking Off

* Striking off -> application cannot be made until 3 months after cessation of trade; potential advantage of the striking off is that the cost of appointing a liquidator can be avoided, meaning assets can be distributed before applying to be struck off, saving the shareholders the liquidation costs

Disincorporation Relief

* Disincorporation relief -> applies to disposals between 01/04/13 to 31/03/18. The business must be transferred to individuals holding shares for at least 12 months prior to the transfer date and business must be transferred as a GC, all assets excluding cash must be transferred and the total MV of goodwill and interests in land transferred must not exceed £100k
* Liquidation/strike off is not required for disincorporation relief to apply but ultimately this does often happen. Relief must be claimed within 2 years of the date of transfer and must be claimed jointly by company and shareholders to whom the transfer is made
* Interests in land are transferred at the lower of chargeable gains base cost and MV under disincorporation relief rules. ‘Old’ GW (pre-1/4/02) is also transferred at lower of base cost and MV, ‘new’ GW (post-1/4/02) at the lower of TWDV and MV
* These conditions can create disadvantages to applying disincorporation relief. E.g. if a gain is realised on land purchased in the 1970s and DR is claimed to defer this -> the base cost for later disposals will be much lower creating a larger gain, benefit on the indexation allowance would be permanently lost, in this case 30+ years from 1982
* Matters to consider when a sole trader disposes of a business on which DR was claimed within 12 months of the disincorporation -> first see what reliefs are available, AEA, BRB or losses. If not then may be better not to claim the relief and leave the gain to be taxed in the company at the CT rate rather than leaving as an individual gain to be taxed at 28%. If AEA, BRB and losses are available, then disincorporation relief may make more sense so this shows that the assessment needs to be made on a case-by-case basis

**Ch.8 – VAT and Stamp Duty**

VAT Group choices

* Company making only zero-rated supplies -> usually left out of a VAT group as these companies are usually due a VAT repayment every month
* Company making only exempt supplies -> these companies would make the whole group partially exempt, thereby restricting recoverability of VAT and therefore they are also usually left out of the VAT group
* Key advantages of VAT group registration -> no VAT charged on intra-group supply, only one VAT return so saves on admin costs, if a relatively small wholly exempt company is included in the group it may be possible to recover input tax under de minimis partial exemption rules for the group overall
* Key disadvantages of VAT group registration -> all companies in group are jointly and severally liable for group VAT so one failure makes all companies liable, centralised return may lead to difficulties in collection and collation, bringing in exempt or partially exempt companies may lead to input tax being restricted

Option To Tax

* Commercial buildings -> construction of commercial buildings, sale of new commercial buildings and work on existing commercial buildings are standard rated supplies. Sale of old commercial buildings and leases on commercial buildings, regardless of age are both exempt and subject to OTT
* OTT impact on output and input VAT -> standard rate VAT is charged on the sale or lease and if the purchaser/tenant is not VAT registered or is partially exempt they will not be able to recover all the VAT. VAT on inputs like heating, cleaning and repairs can be recovered. OTT cannot be exercised over only a partial building
* OTT does not transfer to the new owner on a standard sale but on a sale to another group company, transfers within the VAT group are disregarded so there is no ‘sale’ made in legal form to extinguish the OTT
* OTT can be revoked within a 6 month cooling off period, provided not already put into practical effect, it is automatically revoked once a person who made the OTT has not held an interest for 6 years, or after 20 years with HMRC consent

TOGC Conditions

* Conditions for a VAT transfer of a going concern -> transferee must be VAT registered either before or immediately after the transfer, whole business or a part capable of separate operation must be transferred, assets transferred are to be used in the same sort of business, if land/buildings subject to OTT are transferred, transferee must also use the OTT, if a new commercial building is transferred, transfer must exercise an OTT
* If, within a TOGC, the purchaser of a new commercial building or building with an OTT decides not to apply the OTT, then the purchaser can recover the VAT if he uses the building in his taxable business

Capital Goods Scheme

* CGS adjustments on sale -> make the usual adjustment first as the ‘adjustment in use’ in the period of sale, depending on whether the taxable proportion of the building/aircraft/software etc. has changed in the part of the year prior to the sale. Then an adjustment on sale needs to be made, with the taxable percentage on sale being either 100% if a taxable sale or 0% if an exempt sale, for example of an old commercial building, remembering to multiply the result by the number of intervals remaining in the capital goods period (10 years for a building, 5 for anything else in the scheme). Look out for buildings that were new initially but have been held in the scheme for long enough to now make them old (i.e. in use for over 3 years and so now exempt supplies on sale)
* Transferring a CGS asset within a TOGC -> VAT is disregarded so it is neither a taxable nor an exempt sale and so the adjustment on sale is not required. The new owner instead takes on the remaining CGS intervals and adjustments in use, with the benefit/disadvantage of this dependent on the new owner’s taxable usage percentage versus the original percentage
* If a purchase is made by an exempt trader in a TOGC and a building is < 10 years old, the CGS will still be in place and the exempt trader takes on the remaining adjustment intervals with a taxable use of 0% and will therefore have to make payments to HMRC for reduction in taxable use compared to the initial percentage. However this may still be better than no TOGC occurring because the TOGC will have saved them VAT on the purchase of the assets and SDLT would also have been based on the higher VAT inclusive price. If not bought under a TOGC, the CGS would also reset to 10 periods, rather than carrying on from the original

VAT and the EU

* VAT on exports to the EU and outside the EU is zero-rated
* A VAT-registered trader purchasing from the EU must ‘self-charge’ himself and then reclaim this as input tax, which may be subject to partial exemption
* Rule of thumb for location regarding supply of services -> if the customer is a business, VAT registered or otherwise, the supply occurs where the customer is located; if the customer is not a business, the location is where the supplier is located
* New import and export rules from 01/04/12 -> Low Value Consignment Relief on small value items below £15 imported to the UK from outside the EU exempts them from VAT. As of 01/04/12 this specifically does not apply to imports from Jersey and Guernsey, to prevent online suppliers of cheap goods like DVDs and CDs from setting up Channel Island subs to import the goods into the UK without paying VAT

E-Commerce rules

* E-commerce rules -> no special rules for goods, rules ensure that tax arises in the country where the goods are delivered to; for services, there are special rules. The place where the service is ‘used and enjoyed’ is treated as the place of supply
* Non-EU suppliers to private individuals in the EU must register and account for VAT in the EU; EU businesses do not need to charge VAT on supplies used and enjoyed outside the EU; UK-registered customers using electronically supplied services must account for VAT under the reverse charge procedure described above
* Changes to VAT treatment of e-services from 01/01/15 -> e-services supplied from anywhere in the world to non-business customers anywhere in the EU will be deemed to be supplied where the customer belongs. UK consumers of e-services will pay UK VAT no matter where the supplier of the service is located. These changes potentially mean that UK companies may have to register in all EU countries to which it makes e-supplies. This is where the Mini One Stop Shop (MOSS) comes in to allow the UK businesses to register for VAT and make payments and returns with less administration than would otherwise be the case. Registration can be made with one EU member state and all returns and payments made to that state, at which point the receiving state sends details and payments to other relevant member states

Stamp Duty Exemptions

* Stamp Duty exemptions other than in relation to purchasing own shares -> gifts, divorce arrangements, variation of wills, as of 28/04/14 securities traded on growth markets (e.g. AIM) but not listed on the market
* Stamp Duty exemptions in relation to purchase of own shares -> redeeming shares in accordance with terms of issue; cancelling shares on reduction of capital or court scheme arrangement; purchased shares are immediately cancelled

SD and Liquidation

* Transfers of assets in relation to a liquidation are exempted from SD payable when the shareholder does not take over any of the liabilities of the liquidating company

Stamp Duty on Shares

* Stamp Duty reserve tax -> charged at 0.5% and not rounded. Payable on the 7th day of the month following the month the agreement was made or agreement became unconditional; if by CREST then should be paid 14 days after the trade date
* Stamp duty on share warrants -> three times rate on shares so payable at 1.5% percent of the consideration. Normally paid at the time of the issue of the warrant and paid by the shareholder to whom the warrant is initially issued

SDLT Group Relief

* SDLT relief -> can be reclaimed in a group if there is a group relief group AND a 75% right to profits and right to 75% of assets on winding up; relief may be denied if transfer arrangements exist for the 2 companies to cease to be members of the group and if the arrangement is made for tax avoidance reasons/not for bona fide commercial reasons
* Retrospective charge for SDLT applies if the transferee leaves the group within 3 years whilst sill owning the land transferred -> note 3 year rule not 6 years as with de-grouping charges for capital gains

Stamp Duty and Incorporation

* On incorporation, if separate properties are acquired, the SDLT is applied to the aggregate total so if 5 properties are acquired for £200k then SDLT is paid on the total £1mn and so SDLT is due at 4%. If the trader retains ownership on incorporation, incorporation relief cannot apply but Gift Relief could be claimed instead. No SD is payable on any new shares issued on incorporation since SD is only payable on existing shares

SDLT on Residential Property

* FA 2012 key changes in relation to residential property and SDLT -> 7% rate is now applied to property purchases for >£2mn, top rate had previously been 5% applicable to properties >£1mn. The new rate above £2mn climbs to 15% if the purchaser is a company, corporate partnership or investment scheme other than a property developer. From 20/03/14 threshold for the 15% rate has now been reduced to £500k

Annual Tax on Enveloped Dwelling

* Annual Tax on Enveloped Dwellings -> introduced to stop residential properties from being transferred to companies to avoid SDLT on a later sale. Applicable on properties of > £2mn from 01/04/13. Property value above £2mn gives rise to an annual charge, ranging from £15,400 from £2mn to £5mn and up to a maximum of £143,750 above £20mn. If a disposal occurs partway through the year, charge is pro-rated based on number of days of ownership
* ATED return must normally be returned within 30 days of the beginning of the chargeable year commencing 01/04 – so different to a lot of other returns in that it is made during the year, not after the end of the tax year. If an ATED is acquired partway through the year, return and tax are due 30 days after purchase or 90 days for a newly built dwelling. A return is still required where an ATED property is exempted from the annual charge
* CGT charge on high value properties cannot be avoided by putting the property into a non-UK resident company. This is despite these companies not normally being within the charge to either CGT or CT on chargeable gains
* Allowable cost used in computing the CGT charge on high value properties is normally the MV on 05/04/13. By election, owner may use the original cost but then pro-rate the gain arising for period where ATED rules are applicable
* e.g. if property bought April 1983 and sold April 2016, total gain would be apportioned over 3 years where ATED is applicable as (3/33)\*gain. Gain charged at 28% but NO AEA applies. If the consideration is marginally > £2mn, cap on the gain falling within ATED rules of 5/3 times the amount by which the consideration exceeds £2mn applies
* Losses on ATED properties are NOT very flexible. Can only be used against gains on ATED properties in the same tax year or in future, with no carry backs of ATED losses as would be allowed with other capital losses. This is to punish the holders of these properties for initially trying to get around tax legislation before the changes were made. Capital losses on non-ATED property cannot be offset against gains on ATED properties

**Ch.9 – Chargeable Gains additional aspects**

Dividend Stripping

* Dividend stripping -> this is paying out dividends now to reduce a future capital gain. This dividend must be paid out of distributable reserves; if a corporate vendor receives a pre-sale dividend which is not paid out of normal profits, HMRC could attack the funds as value shifting because the receipt would be tax free and reduces a chargeable gain on which tax would be charged. Only applies to corporate sellers, does not impact on an individual seller
* Dividend stripping saves the purchaser stamp duty at 0.5% on the reduction in the share price
* A dividend strip is not good news for an additional rate individual tax payer as his effective rate payable on dividends is 30.56%, higher than the capital gain top rate of 28%
* Likewise if ER applies to a dividend strip a higher rate tax payer would rather pay 10% on the capital distribution than 25% effective tax on dividends received

Share-for-Share takeover

* On a share-for-share takeover disposal there is no gain and instead the shares received ‘stand in the shoes’ of the old shares, at their cost brought forward. Cost in the share pool does not change but the number of shares may change if it’s not a 1:1 exchange
* There are 3 separate types of paper-for-paper takeover, each with different charges applying: 1) mixture of ordinary and preference shares are received -> apportion original share pool cost b/f into the new share capital on basis of MV of the new shares; 2) mixture of share and cash is received -> cash is chargeable immediately unless it is 5% or < £3k, even if cash is not charged it is still deducted from the base cost carried forward and will eventually therefore be part of a future gain; 3) loan stock is received -> if loan stock is not a QCB, it is treated in the same way as shares. If a QCB then rules are more complex, as shown in below bullet point

Treatment of QCBs

* QCBs -> sterling denominated, non-convertible, a normal commercial loan in interest is not excessive or dependent on business performance
* If a QCB is received as part of a paper-for-paper takeover, first brought forward share pool cost needs to be apportioned between the different elements as based on MV; immediate gain arises on the QCB element, deferred until loan stock is disposed of; when a company makes a disposal, there will be two gains within charge, the deferred element now brought into charge and the gain on disposal of the QCB itself; for an individual, on disposal of the QCB only the deferred element is now chargeable because the QCB disposal itself is an exempt asset for CGT for individuals

Disapplication of Paper for Paper rules

* An individual may dis-apply paper-for-paper rules if the new holding may not qualify for ER but the old one did. The individual may also want to sell his holding in < 12 months and a Pfp takeover would mean he would have to wait another 12 months to sell and would therefore want to dis-apply the PfP rules
* Interaction between SSE and PfP – SSE takes priority and applies if the disposal would have qualified for SSE had it been for a cash consideration; if the companies are part of a gains group, no SSE applies and so PfP rules do now apply

Entrepreneur’s Relief on associated disposal

* An associated disposal for ER qualification -> assets would normally only qualify for ER on ceasing trade but an ‘associated disposal’ will also lead to ER being available. To be an associated disposal: 1) whole or part of individual’s interest in a partnership or shares in a company must be disposed of; 2) disposal is made as part of the individual’s withdrawal from the business; 3) assets must have been used for the purpose of the business for one year prior to disposal/cessation
* Treatment of properties as associated disposals -> rent paid is the key factor to consider. ‘Associated disposals’ rules are designed to give ER on an individual’s assets used in the business on the basis that the individual has allowed the business to use the asset without charge. If the individual received market rent for using the property they have not put the property into the business really and instead have been holding an investment
* If no rent is received then the property has genuinely been put into the company for them to use -> so individuals get full ER if no rent was paid, no ER if market rate rent was charged. There is then a proportionate reduction to ER if a discounted rent was paid (so if market rate was £1,000 but £400 is paid then ER would be restricted to 60% of the full amount)

**Ch.10 – Personal Taxation**

Exempt Income

* Types of exempt income: interest on NSC, ISA income, dividends on shares in a VCT, gambling and premium bonds winnings, housing and child benefit, first £30k of statutory redundancy pay, first £4,250 gross annual rents under rent-a-room scheme, scholarships and interest received from HMRC on overpaid tax

Difference between individual and company CY/PY trading losses

* CY/PY use of individual trading losses differs from the company equivalent in that losses may be carried back straight away for individuals, whereas in companies a carry back can only be made after a current year claim

Different sole trader loss relief claims

* Loss in first 4 years (s72 claim) -> used against individual’s total income in the prior three years, against the EARLIEST year first (FIFO); designed to give a sole trader some relief when loss-making in the early years of their trade
* Some loss reliefs are more flexible than others -> carry forward claims (s83) can only be used against future profits of the same trade; CY and/or PY claims (s64) can be used against total income; loss in first 4 tax years (s72) can be used against total income; Terminal loss relief (s89) can be used against trading profits only

Terminal Loss Relief

* With terminal loss relief, remember to add on any overlap relief from commencement in the last tax year
* If profits are made in the final full year before the period of loss when applying TLR, it is likely that there will be some profits within the final 12 months of trading. This will reduce the loss available for TLR but this loss which is restricted will still be available for use in others claims, e.g. for an s64 claim against non-trading income

Transfer losses on incorporation

* S86 claims -> use unrelieved losses from a sole trader business at incorporation against future income from the company to which the business is transferred, namely salary and dividends. To qualify for this the consideration must be at least 80% shares and these must be held through the tax year in which the loss relief is given

IT relief limits

* Limits on income tax reliefs against total income apply from 2013/14. The limit is the higher of £50k and 25% adjusted total income for the tax year in which the deductions are offset. CY/PY claims and first four year claims are affected by these limits but only relief for trading losses, not overlap profits or profits from the trade generating the losses

Adjusted Income

* Adjusted total income = total income plus SAYE deductions less grossed up pension contributions to personal pension schemes made under relief at source rules
* Adjusted net income (for defining whether or not a person forgoes some/all of their PA) -> income after deducting trading losses, gross Gift Aid donations and cross personal pension payments

Change unrelieved losses into a capital loss

* After a CY and/or PY claim has been made, unrelieved residual loss can be changed into a current year capital loss (s261B extension claim) -> maximum amount eligible for transformation is the lower of unrelieved trading loss or current year gains less b/f losses. This will be a current year claim and cannot be restricted to preserve the annual allowance, unlike a capital loss brought forward

Loss Restrictions

* Loss restrictions for ‘non-active’ traders -> losses claimed against total income are restricted, on the basis that trading losses should not be allowed to be used flexibly if the individual is not really trading; relief is restricted to a maximum of £25k. A non-active trader spends < 10 hours per week on commercial activities of the trade. Restriction does not affect carry forward of losses against profits of the same trade
* Tax avoidance rule introduced from 21/10/09 -> trader may not offset trading losses against total income or gains if the loss is a result wholly or in part of tax avoidance

**Ch.11 – Employee remuneration**

Taxable and Exempt Benefits

* If a company asset is gifted to an employee, the value of the benefit is the cost to the employer
* De minimis limit for an employment loan before it creates a taxable benefit is £10,000 from 06/04/14, up from £5,000 previously
* If accommodation is job-related, it is not a taxable benefit and there is a 10% limit on amount of benefit occurring when amounts such as repairs and heating are paid for by the employer
* Medical insurance is not a taxable benefit for employees when it relates to overseas duties
* Provision of a mobile phone and share options (but not other options) are exempt benefits
* Employers can pay £8k relocation expenses without triggering a taxable benefit

Share Schemes

* ‘tax-advantaged’ and ‘other’ share schemes -> if a tax-advantaged scheme, all the difference between grant price and disposal price will be taxed as a capital gain; in other schemes, IT is charged at exercise (when the employee purchases the options) and a capital gain (less IT paid) on disposal
* SAYE -> portion of net income is invested each month over a 3 or 5 year period; share option may be offered at the outset to enable employees to buy shares at the end of the plan; if option is not used the employees can take out their investment plus interest as a tax free sum
* Share Incentive Plans -> employees can be given shares or acquire them as – 1) free shares 2) partnership shares 3) matching shares and 4) dividend shares. If held for 5 years there will be no IT and no tax charge, holding for 3 years plus reduces tax and NICs down to amount based on lower of MV and grant value, which will likely be the grant value as tends to be at a discount. The SIP offers the best capital gains treatment of all the share schemes as if held for 5 years and still an employee on disposal there is no CGT to pay

Employee Pension Contributions

* For employees maximum pension contribution on which tax relief can be claimed is the higher of total relevant earnings and £3,600. Relevant income = employment income + trading profits + income from qualifying holiday accommodation. There is, however, an overall limit for employer AND employee contributions of £50k per year for 2013/14 falling to £40k in 2014/15
* Excess contribution charge -> into personal pensions beyond the annual limits above. Excess is charged at the individual’s highest marginal rate, if there is unused allowance from the previous 3 years this can be brought forward and used on a FIFO basis
* Pension contributions by an employer are deductible for corporation tax, however HMRC may insist on pension spreading where contributions exceed £500k

Employee Shareholder Schemes

* New rules on employee shareholder schemes apply from 01/09/13; employees must give up certain employment rights such as right to statutory redundancy pay and right to claim for unfair dismissal in order to acquire shares. Minimum value of shares given under this scheme of £2,000 with no upper limit with the first £2000 of shares not charged to income tax or NICs
* There is also a CGT incentive on employee shareholder shares -> first disposal of the shares is exempt from CGT, applying to the first £50k of shares issued to an individual by each employer; this relief takes priority over tax-free disposals between spouses, paper-for-paper takeover rules and share pooling rules.
* This exemption can apply to company purchases of their own shares once the employee leaves the company as no part of the consideration will be treated as a distribution
* If at any time within 12 months of the shares were issued, the individual or a connected person to that individual had a 25% or greater interest in the company, then neither the income tax nor the CGT exemptions will apply to the employee shareholder shares

SSAS and SIPP

* Small self-administered scheme (SSAS) -> designer for owner-managed small companies. It may borrow up to 50% of fund value and lend up to 50% of fund value to its own company; it may invest up to 5% of net pension fund in its own shares but may not invest in residential property unless held in a REIT and cannot invest in tangible moveable property
* Self-invested Personal Pension (SIPP) -> personal plan subject to normal personal pension plan rules, investor has more control over investments, may borrow up to 50% of fund value but may not lend, may purchase shares in any company including companies in which the person investing in the pension also owns shares. Again may not invest in residential property unless held in a REIT not in tangible moveable property (e.g. in fine wines)
* A SSAS or a SIPP may specifically be set up to hold commercial property used in the business of the sponsoring company (the SSAS) or the pension investor (the SIPP) -> this could have a tax advantage as there will be no CGT to pay given that pension funds do not pay CGT. The rent is tax deductible against company tax but will not be taxable when received into the pension fund. The property will also be protected from creditors, therefore several different advantages at different stages of the process to consider

**Ch.12 – Personal Tax – International Aspects**

Overseas Residency Tests

* ‘automatic overseas tests’ -> 1) resident in at least one of last three previous tax years and spends < 16 days in UK in current tax year; 2) non-resident in any of three previous tax years and spends < 46 days in UK in current tax year; 3) full time work overseas test
* Full time work overseas test -> all of the following conditions must be met: work average 35 hours a week overseas, no breaks of > 30 days in overseas work, maximum 30 UK work days, spends < 90 days in UK

UK Residency Tests

* Automatic UK tests -> 1) spend 183 days or more in UK in the tax year; 2) 91 consecutive days of which 30 are in the tax year where the individual has a UK home and no overseas home and present in the UK home on at least 30 days in the tax year; 3) meets full time work test. If one of these tests is satisfied then the individual qualifies as a UK resident
* ‘full time UK work test’ -> all of the following conditions must be met to qualify: 1) a 365 day period, at least part of which falls in the tax year, where the individual works an average of 35 hours per week; 2) no breaks of > 30 days in the 365 day period; 3) works in the UK on at least 75% of his working days; 4) at least one day in tax year where he works > 3 hours in the UK

Determining Residency by Ties

* Sufficient ties test -> three pieces of information are used as inputs in determining whether the individual has sufficient ties to be considered resident: 1) resident for at least one of 3 previous tax years; 2) how many days present in the UK in the relevant tax year; 3) how many ties they have to the UK. The more ties an individual has, the fewer days they need to be in the UK to be resident, if the individual has not been resident in any of the 3 previous tax years the number of ties per days spent in the UK increases before residency occurs
* Family tie -> individual has a spouse or child <18 who is UK resident but the person needs to see the child more > 61 days in the tax year to count
* Accommodation tie -> UK place to live is available continuously for 91 days in the tax year, and the individual spends at least 1 night at the property. If the accommodation belongs to a close relative other than spouse, child or grandchild the tie only counts if the individual spends 16 nights there per year
* Work tie -> works in the UK for at least 3 years on at least 40 days in the tax year
* 90 days tie -> spends > 90 days in the UK in either or both of the 2 tax years immediately before the tax year we are determining
* Country tie -> individual is present at midnight in the UK more commonly than he is in any other country, this one is only a potential tie for individuals not UK resident in any of the previous three tax years
* Table below shows number of ties needing to be satisfied to be considered UK resident, depending on how many days spent in UK and UK residency status in the previous 3 tax years:

|  |  |  |
| --- | --- | --- |
| **Days in UK** | **Number of ties – resident in the previous 3 years** | **Number of ties – not resident in any of previous 3 years** |
| < 16 | Automatic overseas test | Automatic overseas test |
| 16-45 | At least 4 (out of 5 ties) | Automatic overseas test |
| 46-90 | At least 3 | All 4 (out of 4 ties) |
| 91-120 | At least 2 | At least 3 |
| 121-182 | At least 1 | At least 2 |
| 183+ | Automatic UK test | Automatic UK test |

Split Year Treatment

* Split year treatment on individual leaving the UK -> individual needs to have been UK resident in both the current and previous tax year but not UK resident the next year as they satisfy the full time overseas work test As soon as the individual works > 3 hours overseas to the end of the tax year they must not work in the UK for > 3 hours or spend more than the permitted number of days in the UK, pro-rated according to when they go overseas. If these conditions are met, the individual is non-resident from the day they work at least 3 hours overseas, not from the date they leave the UK
* Split year relief can also be claimed when the individual goes abroad with a spouse or partner who has left for full time overseas work or from time in the tax year of departure where an individual no longer has a UK home
* Split year treatment for individuals coming to the UK -> there are four main cases where this could apply, described in the following bullet points

Split Year Scenarios

* Situation 1: arrives to work in UK and does not meet sufficient ties test for the part of the tax year before work starts -> here there is a 365 day period starting the tax year meeting the full time UK work criteria, same criteria as for the automatic UK tests. The individual is UK resident from the date he starts to work in the UK
* Situation 2: individual returns to the UK after working abroad -> must be UK resident in the current tax year and at least part of the following tax years but not UK resident last tax year due to full time overseas work and UK resident in at least one of the four years preceding that. The other requirement is that they have a period of any length in the current year satisfying the full time overseas work criteria. If all these conditions are met the individual is UK resident after the end of the period satisfying the full time work overseas criteria
* Situation 3: individual arrives to live with a partner who has returned from work overseas
* Situation 4: an individual acquires a home partway through the tax year or an individual’s home becomes his only home part way through the tax year

Implications of Overseas earnings

* Non-UK domiciled person resident in the UK has overseas earnings -> if the employer is also non-resident the remittance basis may apply; if employer is UK resident the earnings will be taxed on a receipts basis
* Employers must deduct NICs under PAYE if any employees are in receipt of UK taxable earnings even if the duties are performed wholly outside the UK
* Tax free benefits allowed when an individual is employed abroad -> employer can pay for board and lodging and for the employee to return home any number of times plus up to 2 return visits per spouse and child, if absence to work abroad is > 60 days

Remittance Basis

* Automatic application of the remittance basis -> the individual is not domiciled or not normally resident and has unremitted foreign income and gains of < £2k or no UK income or gains or tax investment of £100 or less. They must not remit any foreign income or gains and must be either under 18 for the whole tax year or UK resident in no more than 6 of the previous 9 tax years. In these automatic cases there is no charge to pay and the personal allowance is maintained
* Others must claim the remittance basis -> charge of £30k each year and no PA available; charge rises to £50k per year if UK resident for 12 of the previous 14 years
* Foreign investment income is taxed as non-savings income where the remittance basis applies, still included at the 100/90 rate

Double Tax Relief on income

* DTR for individuals -> the lower of actual overseas tax and UK tax on overseas income. Find UK tax on the overseas income by computing IT in total including the foreign income then doing the calc. again with foreign income excluded. The difference is the foreign tax. Where there is > 1 stream of foreign income start with the source incurring HIGHEST rate of overseas tax

DTR on Capital Gains

* UK CGT is not applicable to a non-resident individual; if the person is resident but not domiciled CGT may be subject to the remittance basis. If remittance basis is claimed the AEA for CGT is lost
* In order to maximise DTR for CGT, the AEA and 18% rate should be set against UK gains in priority to foreign gains to ensure that UK tax on foreign gains is maximised so DTR will be as high as possible. This will prevent the UK tax on foreign gains being low and so potentially reducing the DTR to an amount lower than the overseas tax

Tax Planning for overseas employees

* Tax planning when employed abroad -> 1) timing – if the individual leaves just before a tax year ends this may enable them to spend a complete tax year outside the UK so qualify as non-resident for the whole period; 2) remittance basis application – in this case should keep funds separate so it is easy to see which monies have been remitted; 3) ISAs – no ISA contributions can be made while non-resident but existing ISAs can be maintained; 4) termination payments – special rules to consider if a significant amount of overseas service

Remittance for Investment Purposes

* Remittances for investment purposes -> new rules apply from 06/04/12 and apply to loans or shares in unquoted trading companies either UK resident or trading in the UK through a UK PE; election to use these rules must be made by the 31/01 following the end of the tax year in which the funds would otherwise be considered remitted and funds brought into the UK must be invested within 45 days to be covered by the rules. Proceeds from sale of an investment in the UK must be sold or reinvested within 45 days
* From 06/04/12/, relating to assets brought into the UK to be sold in the UK, there is no tax charge if the individual receives the entire proceeds of sale within a year of 05/01 following the tax year of the property sale and the proceeds are taken offshore within 45 days of receiving the final amount

Temporary non-residence rules

* Temporary non-residence rules -> aim to prevent tax avoidance by individuals choosing to dispose of assets or receive income where they can control the timing of being non-resident which had previously been exploited to provide tax advantages; the rules apply to: capital gains/losses on acquisitions made while UK resident and sold while non-resident, dividends from close companies where the individual had a 5% interest at some stage in the tax year of departure or the previous 3; income relating to loan write offs from close companies; income remitted but accrued during residence and remitted during the temporary non-residence
* For these temporary rules to apply the individual must cease to be UK resident and have been resident for 4 of the last 7 tax years and not be a UK resident for a period of 5 years or less
* As of the finance act 2014, overseas gains accruing in the overseas portion of a split residency year are not charged to tax, regardless of when they are remitted in the year

**Ch.13 – Choice of Business Structure**

Benefits of Unincorporated Businesses

* Unincorporated business are more flexible in their use of losses than incorporated ones -> losses in the first 4 years can be offset against total income of the previous 3 years, whereas for a company losses are normally against total profits of CY and PY and carried forward against trading profits only
* The unincorporated business also offers a tax cash flow advantage – 2 payments on account are made during the year followed by the balance on the 31/01 after the tax year. A company must operate PAYE monthly in respect of salaries

Methods of profit extraction by a business owner

* There are 4 primary methods of profit extraction for the owner of an owner-managed business -> 1) dividends; 2) remuneration; 3) pension contributions; 4) loans
* Main remuneration option is salary. The benefits of this are that the gross amount is deductible as a trading expense, discriminatory policy can be applied and only paid to certain directors, can be treated as part of employment income for pension purposes. The downsides are that income tax may be payable at a high rate and the employer’s NIC liability is not limited
* Extracting profits through dividends is good in that the effective tax rates with the 10% tax credit factored in are likely to be lower than on employment income for high earners. There are also no employer’s NICs and no NICs payable by the recipient. The downsides are that dividends are not tax deductible for corporation tax, they must be paid to all shareholders, cannot be paid unless there are retained earnings and they are not relevant earnings for pensions purposes
* Pension payments are advantageous in that they are CT tax deductible, you can discriminate between employees, there are no NICs for employer or employee, payments are an exempt benefit for employees and funds in the scheme grow tax free. The downsides are that withdrawals cannot be made for some time and only a max. of 25% can be withdrawn later tax free, with the balance being used to purchase a taxed annuity

Exit routes for shareholders in owner-managed companies

* There are also 4 main exit routes open to shareholders in owner-managed companies -> 1) sell shares to third party; 2) sell shares back to company; 3) liquidate an insolvent company; 4) liquidate a solvent company

IR35 Legislation – anti-avoidance for setting up companies

* IR35 legislation -> this was introduced to stop self-employed people setting up companies to receive fees and so have the option to extract profits through dividends. It is hard to enforce as HMRC has to prove that but for the intermediary company the person would be an employee and this has to be assessed on a contract-by-contract basis for every company. From 06/04/14 arrangements using offshore intermediaries are now also subject to the legislation
* Composite personal service companies -> a company adapted to exploit the fact that IR35 rules do not apply where a substitute is provided, with the effect that groups of freelance consultants join together to form companies where they can substitute workers to circumvent the rules
* Managed service companies -> these are formed at employers’ request to reduce headcount allow previous employees to be treated as self-employed. In exchange the previous employer ensures that all administration of the new company is done for the worker. This is treated specially under IR35 with different tax treatment. If all income is paid out as salary then the company will just be treated like any other
* A personal service company may be set up as the client company avoids paying employer NI since the staff are not employees, the company may also pay a lower wage below the NI lower limit to avoid employer’s NI, remaining profits are paid out of dividends to pay at lower tax rates than equivalent income tax – these are some of the key tax advantages

Deemed Employment Income Computation under IR35

* Deemed employment income computation -> stage 1: find the total income earned from relevant engagements and deduct 5% allowable deduction (relevant engagement = occasions where an individual has provided services to a client via an intermediary company where they would otherwise be treated as an employee); stage 2: deduct salary and employer’s NIC on the salary; stage 3: gross down the balance by 100/113.8 (13.8% NICs) to find deemed employment income net of NICs; stage 4: difference between the gross amount and grossed down amount is the employer’s NIC; stage 5: tax the deemed employment income as normal, with any salary already having reduced the available nil rate band; stage 6: charge NI on the deemed employment income, remembering that salary will already be included in the amount below the upper limit
* Allowable expenses for personal service company -> expenses paid by the intermediary company which would be deductible under employment income rules; capital allowances deductible under employment income rules; employer NICs paid in the year including NICs due on deemed employment income; employer pension contributions; flat 5% deduction
* Deemed employment in the case of a managed personal service company arises on any actual payments made to workers not paid out after deduction of income tax and NICs through PAYE; for a managed personal service company only expenses allowable under normal employment income and employer’s NICs on the deemed employment income is deductible

Potential Drawback of a consortium structure

* Importance of the shareholding/structuring of a consortium -> losses of a consortium company can become trapped and in this sense a JV could be better as losses automatically arise in the investee’s computation as a deduction from their share of any income from the JV

50% vs 75% group comparison

* The key advantage of a >50% group is that a VAT group may be formed, avoiding intra-group VAT. The key advantage of a >75% group is that group loss relief is available, NGNL transfers can occur and capital gains and losses can be transferred

**Ch.14 – Transformation of Owner Managed Businesses**

Implications of Incorporation

* Some implications to consider when a sole trader or partnership incorporates to become a company, listed in the bullets below:

Closing Year Rules

* Closing year rules for the unincorporated business, deduct overlap profits from final tax assessment of the unincorporated business
* Choice of incorporation date could affect the marginal rates of tax

Options for existing losses

* Can carry back losses under TLR, or offset against total income of tax year and/or preceding year – any losses which cannot be used under TLR due to profits in the slice of a year before the final period can be used against total income instead; or can carry losses forward to use against company income

PAYE implications

* Must start using PAYE in salary after incorporation

Close Company Possibility

* The new company commences to trade for CT purposes on incorporation and this new company could be a close company

Balancing Adjustments

* Balancing adjustments on assets may be subject to deemed disposal by the unincorporated business; these adjustments can be avoided by a succession election, transferring the assets at TWDV

Impact on IFAs

* Amortisation on new (post 1/4/02) IFAs will now be allowable as it is a company not a sole trader anymore

Disposals and reliefs on incorporation

* Deemed disposal of stock, consider making elections for increased efficiency, e.g. treating capital as trading stock
* Disposal of assets leads to CGT charge for the individual – however incorporation relief applies automatically against these, but disapplication may be worthwhile in some cases
* Consider the possibility of manipulating the cash consideration paid to leave a gain covered by capital losses or annual exempt amount
* Consider using gift relief if not all assets are transferred
* It may be beneficial not to incorporate appreciating assets (usually property) to prevent a double tax charge in future -> the corporation tax on the gain now and charge to IT when the property is later extracted out of the company

Stamp Duty Implications

* SDLT due on the deemed transfer of land at MV, even if no consideration is paid -> another reason to retain property is therefore to save on SDLT

Possible BPR

* Replacement shares in the company may qualify or BPR at 100%; BPR also of 50% on property used by not owned by the company if the owner has control over the company

TOGC Rules and VAT

* Apply TOGC rules to prevent a supply of goods and therefore move the incorporation outside the scope of VAT; provided at least some goodwill is transferred, then assets can still be retained and the transfer remains a TOGC. Also from a VAT perspective need to consider any CGS assets and charges that may apply to those
* The company might also take over VAT registration of a number of unincorporated businesses but may also want a clean start

Reasons to dis-apply Incorporation Relief

* Reasons to dis-apply IR -> if the individual would have qualified for ER on old holding but does not on the new holding; i.e. if the individual is not an employee of the new company, the new company is a PLC or the individual wants to sell his holding within 12 months of incorporating. An application to dis-apply IR must be made within 34 months of the end of the tax year of incorporation, to give time to decide on the best strategy

Benefits of Gift Relief Over Incorporation Relief

* Advantages of Gift Relief over Incorporation Relief -> it allows the trader to pick and choose which assets will be transferred to the company, since IR requires all assets to be transferred across. GR would therefore allow the avoidance of payment of SDLT on incorporation as land would not be transferred across; GR also avoids the double tax charge on the eventual sale of appreciating assets; GR provides a tax efficient means of extraction in the form of rent – consider however that this may restrict the availability of ER on an associated disposal, restriction being higher the nearer the rent is to market value

Entrepreneur’s Relief on share considerations

* ER requires shares as consideration, the cash element is immediately taxable, an element which can be used to make use of the annual exemption by deliberately paying the exempt amount as cash. GR does not require shares to be included as the consideration. Any consideration received in excess of the original cost of the business restricts the amount of relief available

Treatment of base cost of shares and assets under IR and GR

* Treatment of the base cost of shares under IR and GR -> under IR the base cost of the shares is reduced by the gain deferred, but not under GR. Base Cost under IR is the MV of the shares less gain deferred; base cost under GR is the nominal value of the shares with no deferred gain. Therefore GR gives the lower base cost unless there is a very large deferral of gain under IR
* Treatment of the base cost of assets under IR and GR -> under IR the base cost is MV; under GR base cost is original cost less deferred gain, usually giving a lower base cost than under IR. Therefore GR could raise the potential for a double taxation charge with a higher gain for the company on disposal followed by tax on extracted income – this can be avoided by ensuring that appreciating assets are not transferred, as discussed above
* Gains crystallise under IR when the shares are sold and under GR when the assets are sold
* The main disadvantage of GR is that the base cost of both assets and shares is lower than under IR storing up gains which will potentially be subject to double tax

Disincorporation implications for company and owner

* Key implications of disincorporation for the company -> all assets are transferred to the owner and therefore chargeable gains/losses arise based on MV at disposal -> this is a disposal to a connected person so always treat as MV under connected person rules
* Key implications of disincorporation for the owner -> owner has to sell his shares, leading to potential gains and realising any deferred gains on the shares

Further Disincorporation points to consider

* Some other implications to consider for disincorporation, all listed out in the bullet points below. In general disincorporation can be thought of as the reverse of the effects of incorporation
* Trading ceases, accounting period end. CT is due for that period 9 months and 1 day after the cessation
* The company will most likely become a close investment holding company, paying the main rate of CT unless the cessation occurs in the first accounting period after the liquidator’s appointment – therefore an important tax planning point is to ensure that gains are realised in this first accounting period after cessation to avoid paying CT at the main rate
* Trading losses will be lost but TLR may be used to carry back losses of the final 12 months by up to 3 years against total profit
* Trading losses may not be offset against gains realised after cessation because of the disappearance of the trading losses on cessation, therefore gains should be realised before cessation wherever possible
* Again there will be balancing adjustments for capital allowances but succession election is again possible as it is a transfer to a connected person
* Amortisation of goodwill transferred to owner/shareholder is not allowable for the sole trader, as it was for the company
* Consider the possibility of rolling over some gains into the purchase of goodwill
* Stock – elections may be possible as this is a transfer to a connected person
* Remember to notify HMRC of the disincorporation as soon as possible and the liability to IT and NIC on trading income as a sole trader to avoid a penalty
* Overlap profits should be considered as these may impact on the choice of accounting date for the sole trader
* Any large redundancy payments to the individual are likely to be chargeable to IT and will most likely be taxed as CT on the company
* Net gains may well be very large if GR was used, due to the low base cost on assets and shares
* Conversely if IR was used, the gain will be particularly large on the disposal of shares
* Consider the possibility of SDLT being payable
* Asset transfer may be subject to TOGC rules, leading to no VAT being due – in order for TOGC to apply no goodwill must be left in the company

Sole Trader ceases to trade with no subsequent incorporation

* Implication of a sole trader ceasing to trade with no incorporation off the back of this listed below:
* Closing year rules apply, overlap profits are deducted from the final assessment
* Losses may be carried back versus trading profits of the unincorporated business under TLR or be offset against total income of the tax year of cessation and/or previous year
* Capital allowance assets are treated as having been disposed of at MV at cessation, giving rise to balancing adjustments
* Disposal of stock and assets at MV at cessation lead to capital gains/losses; net gains may be deferred under rollover relief
* TOGC may apply but sales of individual assets would not be part of the TOGC and would be a vatable supply if the trader is VAT registered and it is a taxable supply
* The trader needs to deregister for VAT and may be liable to deregistration VAT on assets/stock on hand on which input VAT was reclaimed, if its value if above £1,000

**Ch.15 – Corporate Reorganisations**

Implications when disposing of a business through a share sale

* for both corporate and individual investors:
* capital gains/losses on shares; capital losses may be used to reduce gains
* a pre-sale dividend strip could be possible to reduce net assets before the disposal
* the gain may be deferred through a share-for-share exchange
* stamp duty is payable buy the purchaser at 0.5%
* the share sale is VAT exempt
* if a corporate investor, SSE may well apply
* group issues may be affected for a corporate investor -> associates, group relief, de-grouping charges, gains group
* the individual investor may be able to use EIS reinvestment relief and/or ER

Implications when a company disposes of assets

* capital gains/losses; capital allowance adjustments unless a succession election is made for connected parties. Rollover relief may be available
* if the only trade of the company is being sold, the company ceases to trade, the accounting period ends and trading losses are lost
* SDLT is payable at 4% by the purchasers of land and buildings
* Consider VAT TOGC rules and CGS adjustments
* Extra after tax proceeds of the sale may be distributed via a dividend which is not taxable for a company
* An individual investor may be able to structure a capital or income route
* There is the potential for a double taxation charge

Advantages of a share deal

* Advantages of a share deal for the vendor -> only the gain on the shares is taxed whereas for a sale of assets, a double tax charge will arise – the company pays tax on gains and then income tax when extracted; SSE is possible; an accounting period does not end; there are no balancing adjustments
* Advantages of a share deal for the purchaser -> the losses of the company being purchased may still be available – subject to MCINOCOT rules; stamp duty is payable but only at 0.5%, although this 0.5% is applicable to the whole consideration, compared against 4% on land and buildings only for an assets deal; the process is legally straightforward, with all contracts passing over

Advantages of a trade and assets deal

* Advantages of a trade and assets deal for the vendor -> very few but potential for rollover relief would be one
* Advantages of a trade and assets deal for the purchaser -> MV is likely to be higher than TWDV and goodwill amortisation, as there is no uplift on these if a share deal; tax deductible goodwill may be created; gains can be rolled over into the new assets; base cost of assets is uplifted to MVs; the legal liabilities remain with the vendor; flexibility is there to pick and choose assets and leave liabilities

Disadvantages of a trade and assets deals

* Disadvantages of a trade and assets deal for the vendor -> balancing charges may arise and a further gain may arise when the company is liquidated
* Disadvantages of a trade and assets deal for the purchaser -> losses remain with the vendor so cannot utilise these going forward; SDLT is payable at 4%, but only on land and buildings (so as above compare this against 0.5% on all consideration as with a share deal); irrecoverable VAT may arise; transfer of contracts is more legally complex

Company Repurchase of Shares

* If an individual shareholder wants to exit his shareholding, a company repurchase of those shares may offer more structuring possibilities than a sale of the shares to a third party as these can be manipulated into being income or capital in nature if repurchased by the company, whereas a sale of shares to a third party will always be capital in nature

Group Implications for a corporate sale of shareholding

* associates are counted as associates for the whole accounting period in which the sale takes place
* FII – where a shareholding is retained but is now <50%, dividends received from this holding will still be exempt for taxation purposes but they will count as FII so may increase the tax rate paid on all profits through the augmented profits calc.
* VAT group – the Vat group may end if < 50% holding, at which point HMRC needs to be notified and VAT will become chargeable on intra-group sales now
* group relief – this will end when arrangements for sale are made, so some time apportioning will be needed in the computation
* de-grouping charges are possible although SSE may well apply
* if not a result of a qualifying share disposal, de-grouping charge is taxable on the departing company
* for IFAs, adjustment needs to be made for additional annual amortisation which should have been charged if disposal had not been at NGNL – as the de-grouping would mean that NGNL treatment no longer applies so need to adjust

De-merger relief

* Demerger relief -> distribution exempt and counts as neither income nor FII for the recipient. No de-grouping charge applies to a company leaving a group solely as the result of a demerger; MCINOCOT restrictions will be considered more ‘sympathetically’ as HMRC takes into consideration that part of the purpose of the demerger is to improve management on the trade which usually leads to major changes

Implications of a sale through a share deal

* Implications when a company is sold through a share deal -> pre-entry trading losses may only be used against the same trade of that company, not the whole group as pre-entry capital losses are not surrenderable via group relief
* de-grouping charges, if they apply, will be passed to the vendor if a qualifying share sale, otherwise to the departing company
* assets stay at TWDV value for capital allowance purposes, which is unfavourable if they are appreciating assets

Allocating consideration in trade and assets deal

* Allocations of consideration in trade and assets deal -> HMRC may require a ‘just and reasonable’ apportionment, which means the allocation must be commercially justifiable and professional valuations should be sought
* Vendors will prefer an allocation towards buildings and investments when assets have high base costs and so lower gains, capital losses are available and rollover and other reliefs are available
* Vendors will prefer an allocation towards new IFAs, capital allowance assets, stock and debtors if there are available trading losses, there are no gains on the P and M, stock and debtors being sold, and if capital allowances are to be transferred at TWDV where connected persons are involved and succession election made or if there is a corporate reorganisation without a change in ownership

Trade and Assets sales of unincorporated businesses

* CGT implications -> gain/loss on each separate chargeable asset, consideration includes a future contingent consideration; potentially there will be rollover relief, restricted if not fully reinvested; where the new asset is depreciating, deferred gain is deferred for a maximum of 10 years and therefore allocating gains to non-depreciating assets (e.g. land and buildings) will defer the gain for longer; potential EIS reinvestment relief is cash purchase of new shares is made in a qualifying unquoted trading company for cash; also consider the possibility of entrepreneur’s relief and possible usage of capital losses
* Income tax implications -> cessation of trade rules and relief of overlap profits; balancing adjustments on capital allowances assets; TLR rules apply

Implications of Intra-Group Trade and Assets transfers

* for the selling sub: NGNL transfer; unrelieved capital losses stay with the seller; trading losses less net liabilities transfer to the receiving sub; transfer capital allowances at TWDV
* For the receiving sub: no SDLT unless they leave the group within 3 years; de-grouping charges on NGNL assets apply if sold on within 6 years, arising on this initial receiving company, unless a qualifying share disposal in which case the charge arises on the shareholding company and SSE may apply; receiving company does receive the trading losses but they are ring-fenced for use against profits of the same trade

Hive Downs

* Hive downs -> the transfer of trade and assets of one company into a new company, then followed by the sale of this new company to an unconnected third party
* With a hive down, unlike other trade and assets deals, trading losses transfer with the trade and no capital allowance adjustments are involved; the losses are however ring-fenced for use against profits of the same trade and excess of relevant assets over relevant liabilities needs to be deducted from the total loss transferred
* Rationale for a hive down -> advantages of a share sale in that trading losses are transferred and there are no balancing adjustments, but also avoid the main disadvantages of the share sale as there is no exposure to contingent liabilities; the purchaser gains by getting a ‘clean company’ with no tax or historic problems. Other losses – capital losses, NTLR deficits and IFA losses on non-trading IFAs are not transferred
* We would normally expect to see a de-grouping charge given that the new company is going to leave the group immediately and therefore well within 6 years. However there is a special rule which states that if the trade and assets transferred had been held and used in the disposing company for 12 months pre-transfer, the shares are treated as held for 12 months too and therefore qualify with SSE and so avoid the de-grouping charge
* There will be an SDLT disadvantage with a hive down as the exemption on L and B transferred between companies in the same 75% group are not available as the new company is sold to the third party within 3 years of the transfer

Management Buyouts

* if managers acquired shares at < market value, an assessable benefit arises as employment income equal to difference between MV and price paid; there will be a beneficial loan if shares are partly paid on the outstanding amount; close company stats for the new company

Implications for Company Managers

* Managers -> if EIS income tax relief is not claimed, may be IT relief on the loan taken out to buy shares, provided the company is close when the loan is applied and the manager holds > 5% ordinary shares, or at least some shares and is a full time employee or officer of the company

**Ch. 16 – Ethics**

Resolving Conflict

* In resolving conflict, we need to consider: relevant facts, relevant parties, issues involved, the key fundamental principles involved, established internal procedures and alternative action
* An effective and well-documented and publicised complaints system and an explicitly stated duty to report breaches of ethical requirements are good safeguards to mention to deter unethical behaviour
* Safeguards to list out where this a conflict of interest -> notify the client and all relevant parties; notify the client that the accountant may act for other clients in the same industry; use separate engagement teams; put procedures in place to limit access to information; communicate clear guidelines to the teams on security and confidentiality; use actual and perceived confidentiality agreements; have a regular independent review by someone senior of safeguards in place
* Points to consider in a question on working for a company which is a rival of an existing client -> a potential conflict of interest arises, evaluate the threat to deem if it is significant and if significant then apply safeguards – notify both parties, obtain consent from both to continue to act, all the while ensuring confidentiality is maintained. If the threat cannot be reduced to acceptable levels, do not act for both parties and not accepting the new client may be the best course of action

Disclosure

* A professional accountant may disclose confidential information where law permits it and the client or employer authorises it, where law requires it, or where there is a professional duty or right to disclose and not prohibited by law
* Should also consider re: disclosure: whether any third party interests could be harmed by disclosure; where info to be disclosed is known and substantiated; type of communication expected and to whom it should be addressed; whether information is privileged, perhaps under the Legal Professional Privilege

Disclosure of Tax Avoidance schemes

* Disclosure of tax avoidance schemes legislation -> introduced so that HMRC can detect avoidance schemes quicker, making it easier to police holes in tax law and avoid loss of revenue
* Avoidance ‘hallmarks’ -> 1) the premium fee hallmark – the arrangement requires the taxpayer not to disclose details to other promoters or HMRC; 2) mass-marketed tax products – high net worth individuals use these schemes, also schemes involving leasing of high value plant and machinery; 3) standardised tax products – mass-marketed schemes but do not include regulated pension schemes, EIS etc. Failure to notify HMRC of such schemes can be penalised by £5k and a maximum of £600 penalty per day
* Scheme promoters should normally disclose their scheme within 5 days of that scheme being made available but this is extended to 30 days for overseas schemes and schemes designed in house
* Exemption from being a promoter -> benign test, non-adviser test, ignorance test

The Engagement Letter

* For a taxation engagement letter, need to state whether the accountant will be agent (prepare documentation, client takes responsibility for correctness so low-risk) or principal (accountant advises and indicates likelihood of different outcomes therefore higher risk), the scope of client and accountant responsibilities, contractual relationship and whether there is authority to disclose errors to HMRC
* If authorisation to disclose errors is not included in the engagement letter, when an error arises the accountant should first ask the client to authorise advising HMRC of the error, warn the client of the potential for interest, penalties and criminal prosecution if they do not authorise and finally advise that if consent is not given then the client-accountant relationship will cease. The accountant should keep a written record of all these discussions

Theft and Money Laundering Implications

* If there is a deliberate attempt to benefit from an HMRC error, both the Theft Act and money laundering regulations may be relevant, the latter if a crime has been committed
* Money laundering prevention procedures -> register with supervisory authority; appoint an MLRO and implement internal reporting; train staff regarding money laundering; establish internal procedures to manage risk, deter and prevent perpetration; carry out customer due diligence; verify the identity of and carry out background research into new clients; report suspicions to SOCA using a SAR (suspicious activity report)
* Maximum penalties: tipping off – 5 years; contravention of systems requirements – 2 years; failure to report – 5 years; primary money laundering offences – 14 years. Unlimited fines apply to all 4 offences

PII

* Professional indemnity insurance limits -> if gross fee income is > £600,000, the minimum is £1.5mn; if gross fee income < £600k then 2.5 X the gross fee income with a minimum of £100k

Tax avoidance v Tax evasion

* Tax avoidance -> legal use of tax rules to one’s benefit, with no intention to mislead HMRC
* Tax evasion -> illegal efforts to mislead HMRC by failing to notify them of tax liabilities, understating gains or income or providing deliberately false or incomplete information
* Case law when considering avoidance vs evasion: 1) Furniss v Dawson. In this case a series of steps were made to defer the gain on sale of a company, House of Lords held that the steps to defer the gain were artificial and held that the gain should be taxed on initial transfer; 2) Craven v White. A share for share exchange with uncertainty over the eventual purchaser of the shares, House of Lords held that there was enough commercial uncertainty to warrant the steps as put in place by the taxpayer; 3) Barclays mercantile business finance ltd v mawson. In this case cash moved in a circular fashion involving a capital allowance claim made by Barclays, court held though that the conditions required for the taxpayer to claim capital allowances had been met; 4) HMRC v Tower McCashback LLP. The supreme court held that software acquired in a series of steps had been artificially inflated in value to increase the claim for FYA. These cases are some that should be considered when considering the merits of a tax planning scheme

Client asks you to ‘bend the rules’ considerations

* Points to consider in a question where there is a case of a client asking you to ‘bend the rules’ when preparing a tax return:
* to behave professionally you need to comply with relevant laws
* impress upon the client that returns must be prepared correctly
* you must not become involved in a return deliberately giving false information and must not assist in tax evasion
* if the client insists on submitting a false return, cease to act
* if ceasing to act, notify the client and HMRC but do not tell HMRC the reason on confidentiality grounds
* consider whether this client relationship should be terminated completely as a result
* Always consider whether more information is needed to establish the facts before immediately accusing anyone of serious wrongdoing in ethics questions
* A failure to supply information in relation to a tax issue could also be indicative of unreliability of the accounts as a whole

Dishonest Conduct rules

* New HMRC rules in respect of ‘dishonest conduct’ of tax agents -> HMRC can issue a conduct notice, enabling them to assess the tax agent’s files, fine between £5k to £50k depending on level of disclosure by the tax agent and their level of compliance with any file access notice, publish details of anyone incurring a fine on the HMRC website. If a notice is issued requiring the tax agent to show their working papers in relation to an issue, they commit a criminal offence of concealing, destroying or disposing of a material document if they do not produce the document

Senior Accounting Officer

* Senior Accounting Officer – where revenue of a company exceeds £200mn, the appointed SAO will be required to certify the adequacy of accounting systems for purposes of accurate tax reporting and specify the nature of any inadequacies. The SAO will be liable for a penalty of £5k if he either fails to establish and maintain appropriate tax accounting arrangements or provide a certificate that contains a careless or deliberate inaccuracy

**Ch.17 – Taxation of Trusts**

Exit charge on assets leaving the trust

* Exit charge before the first 10 year charge -> 30%\*lifetime rate (currently 20%)\*n/40, with n being the number of complete quarters that have elapsed since the trust was first set up. For CGT purposes the disposal is deemed to be at MV
* If assets leave the trust within 3 months of the trust being set up then no exit charge as ‘n’ will be 0; if the assets leave the trust within 2 years of the death on which the trust was created there is also no exit charge
* Available NRB is adjusted with respect to the 10 year charge by deducting any transfers of the settler in the 7 years before setting up the trust and deducting the value of any distributions made by the trustees in the previous 10 years

Interest in Possession Trusts

* IIP trusts -> will not be subject to IHT if the individual set himself up as a life tenant, as IIP property is treated as being owned by the beneficiary so there is no transfer of value. Likewise an IIP set up by an individual with his spouse as the beneficiary/life tenant would not be subject to IHT as the spouse exemption would apply so again no transfer of value; if the IIP is set up with anyone other than the individual himself or his spouse then there is a PET, e.g. an IIP set up for a child. Equally if all property passes out of the trust during the lifetime of the life tenant, there is no charge to the individual himself or a spouse but a charge applies where the beneficiary is anyone else
* IIPs set up on death -> spouse exemption could apply if set up for benefit of a spouse, reducing the death estate by the assets transferred to the IIP. Otherwise the assets remain in the death estate and there is no special treatment
* Income from IIPs -> initially it is taxed on the trustees, reported on the self-assessment trust and estate tax return. There is no personal allowance for the trustees. All trust income is taxed at the basic rate applicable to that type of income. Expenses are deducted against the relevant income – e.g. property expenses deducted against property income; when calculating the trustees liabilities, there is no deduction for trust management expenses – however these can be deducted when assessing the trust’s net distributable income, the amount that can actually be paid to the life tenant and which is then taxable on the life tenant so there is some relief for management expenses. This is deducted first against dividend income
* IIP trusts are required to make a fixed income payment to the life tenant each year; recipient is called an ‘annuitant’, the fixed income payment is paid to the annuitant net of a 20% tax credit. Trustees pay the 20% liability to HMRC BEFORE the income reaches the annuitant, trustees can therefore deduct the whole gross annuity payments including the 20% tax from trust income

Discretionary Trusts

* Discretionary trust expenses -> deductible in the trustees’ income tax comp; expenses are grossed up against the related income as all income is grossed up in the computation; the expenses are allocated against dividends first, then savings and finally non-savings so remember this as being backwards to the normal order when doing an income tax calc.
* Basic rate tax applies to the first £1,000 of total taxable income, then the additional rate 45% applies to NSI/SI and 27.5% to dividends representing the additional rate of 37.5% less 10% tax credit. Income used to pay expenses is taxed at the relevant basic rate, i.e. 10% dividends, 20% SI and NSI. The £1,000 basic rate is allocated to non-savings first, then savings and dividend
* Individual receives income from a discretionary trust -> always apply a grossing up fraction of 100/55 regardless of the type of income and regardless of the individual’s tax band; a tax credit of 45% is given to the individual further down the computation, given regardless again of the rate the taxpayer pays at
* Discretionary trust tax pool -> this is the amount used to pay the 45% tax credit given to the individuals on their income; the tax credit that may result in a repayment to the individual is funded by: tax at the basic rate paid by the trust on trust income within the BRB, tax at 45% paid by the trust on remaining trust income, tax funded from the dividend rate at net taxation of 27.5% - if these sources are not sufficient, then the trust has to make up the difference. Where the trust has paid more into the tax pool than is required to cover tax credits, the balance gets carried forward to the next year to cover tax credits in that year

AEA for Trusts

* Annual exempt amount for capital disposals is £5,500 for all trusts other than a bare trust. If an individual sets up several trusts, the £5,500 is split between them to a minimum of £1,100. 28% is charged on all disposals other than those by bare trusts. Bare trusts are treated like individuals so CGT is due at 18% or 28% and the annual exemption is £11k

IHT for Trusts

* Relevant property trusts are subject to IHT when the trust is set up, when property passes to a beneficiary and on each 10th anniversary of the creation of the trust
* Bare trusts -> gifts are always PETs which are treated as gifts to individuals, there is a deemed disposal at MV by the settler when he transfers assets to the trust, GR is available if a qualifying business asset but not otherwise because there is no immediate charge to IHT. For a transfer of assets by bare trustees to a beneficiary there is no IHT or CGT applicable

Interaction between CGT and IHT

* Gifts into relevant property trusts during lifetime of the individual -> a CLT so an immediate charge to IHT; CGT charge on a deemed disposal at MV of the assets with the MV also becoming the base cost for the trustees; CGT only apply if asset is chargeable asset for CGT purposes – for example, cash would not be charged to CGT
* Relief for lifetime gifts into relevant property trusts -> GR may be available as there is an immediate charge to CGT; unusual compared to other examples of GR as it is elected solely by the settlor rather than jointly with the recipient (i.e. the trustees) as with normal GR claims. As with a normal GR claim, though, the base cost of the recipients is still reduced by the GR claim -> i.e. the election does pass the future tax burden onto the trustees even they are not involved in electing to apply it

QIIP Trusts

* CGT issues if a gift is made to a pre-22/03/06 QIIP trust -> deemed disposal at MV for CGT but the transfer is a PET for IHT not a CLT and so there is no immediate charge to IHT; there may only be GR if the asset is a qualifying business asset because the other assets are not subject to an immediate IHT charge
* CGT implications if there is a gift to a QIIP trust set up on death -> no CGT on death, so the trustees take on the assets at MV and get a tax free uplift to MV at the date of death
* Assets leave a QIIP trust during life tenant’s lifetime -> deemed disposal at MV; transfer is usually a PET so no possibility of GR unless a qualifying business asset
* Assets leave a QIIP trust on death -> gains exempt from CGT, the remainderman takes the assets at probate value so gets a tax-free uplift to MV at the date of death; if GR was claimed when the property was transferred to the trust then the lower of actual gain and deferred gain become chargeable unless trust assets are included in the death estate as settled property which will trigger an IHT charge; if the latter scenario is the case, then GR may be claimed

**Ch.18 – Income Tax and NICs**

Minor elements of the computation

* Small point but treat patent royalties received like bank interest -> gross up by 100/80 in an income tax comp
* Deductions made before the personal allowance is deducted -> gifts of assets to charity; qualifying interest payments; losses
* Deductions made after the PA -> MCA, tax already deducted at source, e.g. withheld on bank interest, PAYE deducted from salary by the employer, ‘pension tax’; tax retained on patent royalties paid may potentially need to be added back

Gift Aid Elections

* Gift aid elections -> can elect to carry back the donation to the previous year which may be helpful from a tax point of view if the taxpayer is a BRB payer this year but was a higher/additional rate payer last year and therefore the carry back would give them more tax relief last year than this. The election to apply this option must be made by 31/01 following end of the tax year

EIS

* Subscriptions in EIS shares must be paid fully in cash and must be new fully paid up ordinary shares. The SEIS shares can be issued between 06/04/12 and 06/04/17
* In order to qualify for EIS, company must meet ALL of the following conditions: they must be a qualifying trade and therefore not deal in commodities, property or financial services; they may not control another company other than qualifying 90% subs and must not be controlled by another company; gross asset value must not exceed £15mn before the share issue and £16mn after it; must be < 250 FTEs; they may not have raised > £5mn via EIS and VCT in the last 12 months; must not require the help to stem losses that would otherwise put them out of business

Comparison of EIS and SEIS

|  |  |  |
| --- | --- | --- |
|  | EIS | SEIS |
| Rate of IT relief | 30% | 50% |
| Maximum investment | £1mn | £100,000 |
| Gross assets limit | £15mn | £200,000 |
| Maximum employees | 250 | 25 |
| Maximum funds permitted | £5mn annually | £150,000 total |
| Period for use of funds | 2 years | 3 years |
| Activity required | New qualifying trade or qualifying R and D for 4 months | Use 70% of funds or new qualifying trade for at least 4 months |

EIS Reinvestment Relief

* Individuals must be UK resident to qualify for EIS reinvestment relief, both at the time the gain is realised and when the shares are purchased
* Qualifying time period for realisation of gain and reinvestment for rollover relief is the same as usual for rollover relief -> 12 months before and 36 months after the disposal which led to the gain
* Under EIS reinvestment relief gains are deferred until the EIS shares are disposed of. The maximum relief is the LOWER of the gain and the subscription cost of the new shares. Partial reinvestment relief is possible and from a tax planning perspective should be looking to check whether any annual exemption remains and if so only claim EIS reinvestment relief on the gain - £11k to take the £11k permanently out of tax rather than just deferring

Capital Gains benefits of SEIS

* share disposals are exempt from CGT
* relief can be claimed against a capital gain if the investor also makes a SEIS investment in the same tax year. The relief is given as 50% of the investment so to claim full relief on a capital gain the investor will need to invest double the value of the gain in a SEIS investment – e.g. for a gain of £50k, need to invest £100k in a SEIS. Max reinvestment relief is the lower of the gain and 50% subscription cost of the new SEIS shares up to a maximum of 50% of £100,000 invested

SEIS Conditions

* Owners of 30%+ of shares or voting rights in the SEIS company and current employees of the SEIS company may not invest in the SEIS company
* Criteria to qualify for SEIS: The trade must have been carried out for < 2 years on issuing the shares; gross asset value pre-share issue must be no more than £200,000; must be fewer than 25 employees; the company may not have previously raised funds through either the EIS or VCT schemes; a maximum of £150,000 can previously have been raised in total under SEIS
* SEIS funds must be invested in the new qualifying trade within 3 years
* A company that has already raised funds under SEIS may raise additional funds under EIS or VCT but must spend at least 70% of its SEIS funds first
* None of the available £100k IT relief available to the investing individual can be claimed until the company has invested at least 70% of funds received and IT relief is withdrawn if SEIS shares are disposed of within 3 years. There is no special treatment for dividends received under SEIS

Individual Requirements to qualify for SEIS

* To be a qualifying individual for SEIS -> definition is similar to that for EIS
* the person must not have been connected with the company any time within 2 years of the issues to 3 years after it, so may not, alone or with associates, hold more than 30% of shares or voting rights in the company or be an employee or non-qualifying director (i.e. receives more than just ‘reasonable remuneration’ from the company)
* EIS IT relief could be withdrawn if the individual becomes connected at any point throughout this period
* Investor does NOT need to be UK resident for SEIS and the CGT exemption under SEIS works under the same rules as for EIS
* SEIS capital gains reinvestment relief is, as per IT relief, withdrawn if SEIS shares are sold within 3 years of issue

VCTs

* the individual must subscribe for NEW ordinary shares and the maximum investment on which IT relief may be claimed is £200k. The investor can invest more but the relief is capped at this level. Tax relief is at 30%, but may not create a tax repayment -> i.e. may only reduce the IT liability to nil. VCT relief is applied before EIS relief ad there is a 5 year holding period to ensure that the VCT relief does not come back into charge
* Dividends from the VCT are tax exempt on shares within the £200,000 maximum and this relief is not withdrawn if the shares are disposed of within the 5 year holding period
* Capital losses cannot be claimed on disposal of VCT shares, because gains are exempt, whenever disposed of with a VCT and therefore losses are not allowable. Note the difference here from the EIS where capital losses are always allowable but the gains are only exempt if held for 3 years

National Insurance Contributions (Types)

* Class 1 NICs: payable by employees and employers on the employee’s earnings, collected monthly under PAYE
* Class 1A NICs: payable by employers on most taxable benefits, collected in one amount by 19/07 after tax year or 22/07 if payment made electronically
* Class 1B: payable by employers on grossed up value of earnings under a PAYE settlement, collected in one amount by 19/10 following tax year or 22/10 if paid electronically
* Class 2: payable by self-employed individuals, collected monthly by direct debit or quarterly billing
* Class 4: payable by self-employed individuals, paid through self-assessment

Rates of Payments, thresholds and limits

* Between the earnings threshold and upper limit, employee NICs are paid at 12% and employer NICs at 13.8%; on earnings above the UEL employee contributions fall to 2%, employers continue to pay at 13.8%
* Employers also pay at 13.8% for Class 1B NICs on grossed up value of PAYE settlements; gross up should be at the individual’s marginal rate of tax -> by 100/80 for BRB, by 100/60 for HRB, by 100/55 for ARB
* Small earnings exception limit for Class 2 NICs is £5,885 net accounting profits of the business; this is payable at a flat rate of £2.75 per week
* Class 4 NICs are payable at 9% between lower profits limit of £7,956 and the upper profits limit of £41,865 and then at 2% above the upper limit
* Directors should always be assessed using annual limits, never weekly or monthly limits and for those becoming directors midway through the year, pro-rate for the weeks that they are directors
* Minor point but may be worth a mention -> from 06/04/14 employers may claim employment allowance to reduce secondary contributions payable to HMRC by £2,000 p.a.

ISAs

* conditions up to 30/06/14: maximum subscription is £11,880 each tax year, whole amount may be invested in stocks, shares and insurance products or up to £5,490 may be invested in cash
* conditions from 01/07/14: reformed to create the NISA, maximum subscription of £15k p.a., whole amount can be invested in cash or in stocks, shares and insurance products in any proportion, investor may only have one cash NISA and one stocks and shares NISA each year unless under 18 when you can only have a £15k cash NISA but not a stocks and shares NISA
* All income from ISAs is exempt from IT and all gains are exempt from CGT

**Ch. 19 – Unincorporated Businesses**

Tax planning for individuals

* Difference between CY/PY use of trading losses for individuals versus companies -> for a company a carry back claim may only be made after a current year claim; an individual may carry the loss straight back which could be helpful from a planning perspective

Partnerships

* Partnership v company taxation -> partnerships are not taxable people in itself so partnership itself is not taxed, instead the partners are liable for their share of the partnership’s profits; partnership profits must however be adjusted for non-tax elements like depreciation and capital allowances which is line with how company tax operates
* Changes in the profit sharing ratio midway through the year -> divide the period of account into separate agreements and allocate profits, salaries and interest based on these separate periods
* If a new partner joins an existing partnership -> opening year rules apply to new partner but existing partners should apply current year rules
* Partner leaves an existing partnership -> closing year rules apply to that partner, existing partners continue to apply current year rules

Partnership Loss Relief

* The same loss relief measures are available to partners as to sole traders
* Where a partner joins a partnership, an s72 claim can be made for losses in the first 4 years of membership of the partnership; where a partner leaves a partnership, an s89 closing year relief claim can be made; for continuing partners carry forward (s83) and CY/PY (s64) claims can be made; on the incorporation of a partnership, incorporation relief under s86 is available
* ‘notional profits’ in a partnership -> occurs where the partnership makes a loss but due to the partnership agreement in operation, one of the partners may make a profit – e.g. if one partner receives high income on capital contributions; for tax purposes, that partner is treated as having 0 taxable trading income because the partnership as a whole has not made a taxable profit. The notional profit is reallocated to the remaining partners in proportion to the loss initially allocated to them

**Ch.20 – Capital Gains Tax and Reliefs**

Exempt Disposals

* Disposals not chargeable to CGT -> gifts to charities, disposals on death which are subject to IHT instead, appropriation of an asset to trading stock by election: transfer is treated as NGNL with cost of asset for trading purposes adjusted for gain or loss that would have occurred, changing a potential gain into a potential trading profit
* Quick list of exempt assets to be on the lookout for -> cash, cars, wasting chattels, any other chattel sold for < £6k, gilt-edged securities, qualifying corporate bonds for individuals (these are NTLR for companies), NSCs and Premium bonds, shares investments in an ISA
* Also be on the lookout for allowable costs to deduct from the consideration when calculating the gain -> acquisitions costs, incidental costs e.g. legal fees, surveyor fees, stamp duty; enhancement expenditure

Part Disposals

* Allowable cost on a part disposal -> full original cost X (MV of part disposed of/(MV of part disposed of + MV of part retained)), so we are finding the proportion disposed of based on current market values rather than proportion of land etc. Acquisition costs should also be pro-rated but not disposal costs as these relate entirely to the part disposed of
* Numerical example for base cost -> a husband buys a house for £100k and sells to his wife two years later for £200k when the MV is £250k: £100k is the base cost as this is an NGNL transfer because it’s an inter-spouse transfer so changes after the initial purchase should be ignored. The wife therefore suffers all the tax on any gain and may be subject to Principal Private Residence rules

Tax planning using inter-spouse rules

* Inter-spouse rules can be a useful tax planning tool -> 1) they can make best use of each other’s annual exemptions; 2) they can maximise unrelieved capital losses. There must be a genuine disposal or HMRC may treat the original holder as still holding the asset

Disposals to a connected person

* Disposals to a connected person -> always deemed to be at MV; losses on disposals to each connected person are ring-fenced and can only be offset against gains on disposal to the same connected person
* Order of reliefs to be used when ER applies -> use capital losses and AEA against gains that do not qualify for ER first as these are taxed at 18/28% and ER gains at only 10%

Earn-Outs

* situations where receipt of some of the consideration is dependent on a future event:
* 1) payable by instalments – normal disposal with the total receivable as proceeds; 2) amount to be paid is known – normal disposal using the anticipated total as total proceeds at time of sale and if that future event does not occur go back and amend the calculation; 3) amount to be paid is unknown – ‘chose in action’ rules apply
* Chose in action rules -> this is the right to receive an unknown amount in the future; chose in action is added to proceeds at the time of sale; when proceeds are actually received later, a second computation is done, where the PV of the chose in action is deducted as the cost figure – if a loss arises in the second computation (disposal of chose in action) it may be carried back and offset against the original gain on disposal of the asset

Partial Rollover Relief

* Rollover relief restrictions -> if the asset is not used wholly for business purposes or if proceeds are not fully reinvested with amount not reinvested chargeable immediately and the balancing figure rolled over
* Numerical example for rollover relief -> individual buys plant and machinery for £200,000, sells for £250,000 and reinvests in a business with separately identifiable goodwill valued at £210,000. What RoR is given and what is the base cost of the goodwill going forward? : gain = £50,000, £40,000 has not been reinvested so £40k is chargeable now and £10k is rolled over into base cost of the goodwill, base cost of goodwill is therefore reduced to £200k; rolled over amount is then chargeable when the goodwill is disposed of as there will be an extra £10,000 of gain given that the allowable cost of the goodwill is now £10k lower

Rollover relief for depreciating assets

* RoR for depreciating assets -> for assets with an expected life of 60 years or less, the rolled over gain becomes chargeable on the earliest of: 1) disposal of replacement 2) 10 years after acquisition of replacement 3) replacement asset stops being used in the tread, other than due to the death of the sole trader -> overall this gives a 10 year deferral limit rather than deferring until disposal
* Tax planning example for RoR and a depreciating asset -> a sole trader has deferred the gain into a depreciating asset and has now held it for 8 years since the original gain occurred, how does he stop the gain crystallising in 2 years? : could buy a non-depreciating asset now and transfer the deferred gain into that asset where it will be deducted from the base cost but will not be subject to any time limits now – will only become chargeable on disposal of the non-depreciating asset; this is acceptable any time provided the non-depreciating asset is bought before the gain has crystallised

Interaction between the different gains reliefs

* RoR can be claimed on assets used in trade of a ‘personal trading company’, as per GR purposes. ER also applies to these companies. So if disposing of personal trading company, the merits of each relief should be considered (this is any company where the individual has 5% of voting rights)
* Stress the order in which the 6 possible capital gains reliefs should be taken in: 1) RoR 2) IR 3) GR 4) SEIS reinvestment relief 5) EIS deferral relief 6) entrepreneur’s relief

Entrepreneur’s Relief

* Assets where ER is applicable: 1) all or part of a sole trader business or partnership share; 2) assets of sole trader business or partnership post-cessation where assets are disposed of within 3 years of the cessation; 3) shares/securities in individual’s ‘personal trading company’; 4) assets owned by individual but used in his personal trading company
* Where ER is applicable but the taxpayer has other gains, any losses and the AEA should be used against the other gains first so that as much of the entrepreneurs gain as possible will remain to benefit from the lower rate of CGT at 10%
* ER may be restricted if there are substantial non-trading activities although this seems to be open to interpretation and ‘some’ non-trading activities does not automatically equal a restriction
* Numerical example for tax treatment of ER and interaction with other tax -> individual has taxable income of £30,000, has a qualifying ER disposal of £1mn and chargeable gain of £10k which does not qualify. Which takes precedent in using up his BRB? -> gain qualifying for ER uses up the remainder of the BRB as these gains are treated as the ‘first slice’ of gains meaning that unfortunately in this case the £10,000 will be taxed at the higher rate of 28%
* ER must be claimed within 12 months from the 31/01 following tax year in which the qualifying disposal is made
* Time periods applicable to ER -> property must be owned for a year pre-disposal; for sale of assets after cessation qualifying period is the year up to cessation and assets must be disposed of within 3 years of the cessation; for EMI shares, one year period runs from the date of the OPTION being granted, not the date the shares are acquired

Gift Relief and Entrepreneur’s Relief

* Interaction between gift relief and entrepreneur’s relief -> gift relief should be claimed first. If amount remaining after GR is < £11k (AEA), do not claim ER because there is no point – it will just use some of £10mn lifetime allowance for ER and would cost 10% tax when it could just be tax free under the AEA. Gift Relief must always be claimed in full, nothing stops the donor charging £11,000 for the gift, leaving that amount covered by the AEA of the recipient if there are no other gains. GR only defers the gain so it is worth stripping out this £11k and keeping it out of tax completely at this opportunity, to be done at the time of the gift

Associated Disposals

* Associated disposals -> case where an individual personally owns an assets used in the company. ER may be claimed if disposal of the share/partnership share is a full disposal as part of the withdrawal from the business, for example a property owned by the individual and used by the company for its business for at least 12 months. If the property is let at market rate there is no ER as the individual has effectively ‘given’ the business nothing. If the property is let rent free full ER is given. If the property is let at reduced rate, there is partial ER given and partial ER may also be given if only part of a building was used for business purposes, e.g. one floor of an office

Gift Relief

* Qualifying business assets for GR -> assets used in a personal company or unquoted shares/securities in ANY trading company or quoted shares/securities in the donor’s personal company. Gift relief DOES NOT apply to company recipients
* For GR to take effect a joint agreement must be signed by donor and donee as GR works by deferring the gain incurred by the donor into the base cost of the asset received by the done therefore the done will be liable to higher tax in future
* Numerical example showing deferral of the gain under GR -> an individual gives a factory to his son when he takes over the business. The factory cost £100k and has MV of £150,000. What base cost does the son assume? : gain = 150 – 100= £50k; the father receives GR on this amount and the gain is deferred onto the son, base cost of acquisition by the son is £100k, the original cost of the factory to the father. When the son then disposes of the factory he will be liable to CGT on proceeds above £100k

Restrictions to Gift Relief

* GR may be restricted by there being non-business assets in the business, applicable where gifted asset is shares in a company which has been the donor’s personal company in the previous 12 months; may also be a restriction if the transfer is not a pure gift. A good indicator of the first restriction which will have to be telegraphed in the exam is that the examiner will have to give a list of assets used in the business (factory, P and M, stock etc) and this should act as a reminder that the gift relief is to be restricted provided that the gifted asset is shares in a personal company
* Equation used to restrict GR on shares if there are non-business assets in use by the company -> amount qualifying for GR is (chargeable business assets/chargeable assets)
* GR is also restricted when there is a monetary consideration -> gain is calculated as MV less original cost (i.e. ignoring the consideration); difference between the consideration and original cost is immediately chargeable and therefore not given GR and the balancing figure is the GR. This can be advantageous as if the item is sold for cost plus £11k there will be an £11k gain which is fully covered by the AE and therefore taken permanently out of tax
* Numerical example of these restrictions in action -> a sole trader uses a factory which he bought for £100k and he sells to his son for £120k when the MV is £150k. Show the gain and GR: gain = £150MV - £100k cost = £50k, the proceeds deemed to be MV as he has sold to a connected person in his son; gain immediately chargeable = consideration – cost = £20k not eligible for GR; GR is the balancing figure = £50k - £20k = £30k. The base cost for the son is therefore £150k - £30k = £120k and this will always be equal to the consideration. The gain of £20k is not completely covered by the AE of £11k. From a tax planning perspective the factory should have been sold for cost plus £11k = £111,000 and then the gain would be covered in full and taken permanently out of tax

**Ch.21 – Inheritance Tax**

Exempt and non-chargeable transfers

* List of transfers which are not subject to IHT, other than exempt ones -> commercial transactions resulting in a loss; transfers made for the maintenance of the transferor’s family; transfers constituting allowable expenditure for IT and CT, e.g. employer’s payments into a pension fund

Some TC IHT Points to remember

* If gifts are made which are bigger than the small gifts allowance of £250 then there is no pro-rating so the whole amount will be subject to IHT
* Use of the ‘normal expenditure out of income exception’ rule to make payments without incurring an IHT liability -> the transfer must be made as part of normal expenditure out of income of the transferor, leave the individual with sufficient income to maintain standard of living and be part of a regular pattern of giving
* Remember that where an exam question does not say who pays the tax we should assume the donor is paying, not the trustees -> so tax should be at 25% not 20% and this amount needs to be added to the value of the chargeable transfer to get the gross transfer value carried forward which will then be used in calculating extra tax due at death

Quick Succession Relief

* QSR formula: tax paid on first transfer X (net transfer/gross transfer) X relevant percentage, where the percentage depends on when the second death occurs within 0-5 years of the first; unlike BPR the property does not have to be in the second individual’s death estate to still get the QSR
* Numerical example of QSR: wife dies in August 2007 and has a chargeable estate of £350k where the NRB was £300k; she passed the whole estate to her son at death. The son dies in February 2010. Find the QSR available on the son’s estate. 1) find tax paid on the first death: = (350,000 – 300,000) X 40% = £20,000. 2) net transfer = total estate – IHT paid = £330,000 and the gross transfer = full £350,000. 3) more than two years have passed between the deaths but < 3 so 60% QSR is available. QSR = £20,000 X (330/350) X 60% = £11,314

Transfer of Unused NRB

* From a tax planning perspective when looking to give unused NRB to the other spouse on the death of the first spouse, it is better to transfer the estate to the surviving spouse death and then hand down to family members on the second death as transferring to surviving children straight away will waste the extra NRB. So if the spouses both die in the period since the NRB went up to £325k, transferring the estate to a surviving husband will pass all £325k to the husband and therefore he gets an NRB on death of £650k to deduct from his death estate when he passes it on to surviving children. One extra point to perhaps make from a tax planning point of view is that generally the NRB has been rising so there is a chance of this ending up as being even more than £650k as it is 100% of the NRB as at the date of the second death so say NRB had risen to £350k by the time the husband died then he would be able to deduct £700k from his death estate

Business Property Relief

* BPR rules -> relates to **R**elevant business property transferred, **O**wnership period of transferor is required. Any **S**ale contract in place denies the relief and **E**xcepted assets reduce the amount of relief -> so using the letters in bold the acronym ROSE can be used to remember BPR rules
* 100% BPR availability -> unincorporated business but not an asset used in that business; shares in an unquoted company (including shares quoted on AIM); furnished holiday accommodation but with the caveat that there must be substantial involvement of the owner or agent in the letting; partnership shares
* 50% BPR availability -> a controlling shareholding in a listed company; land, buildings or P and M owned by the transferor and used by a partnership or company in which the transferor was a controlling party or a partner
* In general assets must have been owned throughout the 2 years prior to the transfer to qualify for BPR

BPR Special Rules

* Special rules in relation to BPR ownership -> ownership period is satisfied if: 1) property transferred is replaced by other business property which between them were owned for at least 2 years within the 5 years prior to transfer; 2) property is passed on death from spouse, ownership period of the deceased spouse is counted towards the normal ownership period; 3) if there are successive transfers of the same property, one on death and the first transfer qualified for relief, then the ownership period is also satisfied
* Contract for sale and BPR -> BPR does not normally apply if there is a contract for sale; however it can still apply even if a contract for sale is in place where: 1) sale is of an unincorporated business wholly or mainly in consideration for shares/securities of the company; 2) sale is of shares or securities in a company for reconstruction or amalgamation purposes

BPR Excepted Assets

* Excepted assets for BPR -> assets neither used wholly/mainly for business purposes throughout the 2 years pre-transfer nor required at the time of the transfer for future use by the business; common examples of this would be: large cash balances, land or shares held as investments
* Formula involving excepted assets -> value of interest in the company X (net assets less excepted assets)/net assets X BPR%. Net assets must be used as the basis, often in the exam you will be given net CURRENT assets and then need to deduct any non-current liabilities before plugging into the equation
* Numerical example using this formula -> a shareholder gives his holding is his unquoted company to his daughter when the shares are worth £100k. The company has assets worth £3mn, non-current liabilities of £2mn and current liabilities of £500k. The £3mn includes a factory costing £50k, not used in the trade for 5 months. Show the BPR which can be claimed and the consequent transfer in value. 1) find net assets first: = total assets – all liabilities so £3mn - £2mn - £0.5mn = £0.5mn. 2) The surplus factory is an excepted asset of £50k so net assets less excepted assets = £450k; 3) now apply the formula above. 100% BPR is available as the company is unquoted; effective BPR depends on ratio of net assets less excepted assets to net assets – higher excepted assets gives a lower BPR - £100,000 share value X (0.45/0.5) X 100% BPR = £90,000; 4) the transfer of value can now be worked out as the share value less the BPR = £100k - £90k = £10,000 -> this example could be a case where we could make an argument that the factory should not be an excepted asset as we could suggest that the factory will be required in the future despite not being in use now; could be something to add for an extra half etc.

Agricultural Property Relief

* APR is also usually disallowed where there is a contract for sale in place, an exception being where the sale is partially or wholly in exchange for shares/securities of a company of which the transferor will have control
* APR is usually given at 100%; 50% applies where a property let out on a lease entered into pre-01/09/1995 and which has > 12 months to run
* Agricultural value only is used for APR; market value should be used for the overall value of the gift. E.g. the deceased owns farmland with an agricultural value of £1mn but redevelopment value of £3mn. £1mn is used as the agricultural value but the gift is worth £3mn - £1mn APR = £2mn total gift value
* Standard ownership periods for APR -> 1) 2 years if owned and occupied by the transferor throughout the period for agricultural purposes; 2) 7 years if owned by the transferor and occupied by him or someone else for agricultural purposes throughout the period

Considering BPR and APR on lifetime gifts

* key issue to consider is whether the person who received the property still owns it or uses it for the same purpose. If not then the BPR/APR may need to be withdrawn and may also need to consider whether there has been reinvestment into replacement property. If withdrawn, the APR is withdrawn in full for the death tax. When assessing how much NRB remains, the gross transfer of value figure is not adjusted so no allowance is made for the withdrawal of the APR

Gift with reservation of benefit

* occurs where a donor gives away property but continues to benefit from the property as though still owned. The rules are in place to stop donors giving away property in legal terms to avoid IHT and instead they are treated as though the property has not really been given away
* Examples of a GWRB -> residence transferred but continue to live there while not paying full market rent; transfer of artwork but retaining it without paying full consideration; transfer of shares whilst still benefitting from the income derived; transfer of property into a trust where the donor is a beneficiary
* GWRB will be subject to potential IHT charges if retained until death -> 2 calculations need to be performed. 1) normal treatment, assuming there is no GWRB, deducting the GWRB value from the death estate 2) GWRB treatment, ignore the lifetime transfer and just treat the transfer as part of the death estate, giving a higher IHT liability if an appreciating asset. Find the higher IHT bill out of the two calculations and apply that treatment
* GWRB gives rise to a potential double tax charge to IHT -> on original transfer and then on either death or a second PET, when the GWR is released. In practice though, as above, HMRC only charge one of the events to IHT, whichever results in the greater charge to tax
* GWRB rules do not apply where donor stays in the property rent free for very short periods (2 weeks where the recipient is not present and a month where they are), where unforeseen changes occur e.g. having to care for an elderly relative in the property

Variations in a will

* Reasons for a variation in a will -> parent receives an inheritance from their parents and IHT is paid; when they pass that inheritance on to their own children IHT will be due again, therefore the parents in the scenario may want to pass the inheritance straight to their children (deceased’s grandchildren) so that there is no IHT due when the parents in the middle of the chain die. Variation may be made within 2 years of death, must be made by the beneficiary and must be in writing and state that the variation is to have effect for IHT purposes
* Variation can also be a tax planning strategy relevant to capital gains tax – the same conditions above apply again and the intermediate parent in the chain will not be regarded as making a capital gains disposal in passing the property directly to their children. Only advisable where the gain would not already covered by the annual exemption
* Numerical example for variations -> son receives shares from his mother as part of his inheritance when she dies. Probate value is £50k. He has not made any other capital disposals during the year, share value has now risen to £55k. The son is considering a variation to the will for IHT and/or CGT purposes. He is paid a salary of £22k: IHT variation seems sensible as an IHT charge is avoided if he dies before his children which is very likely. CGT charge would only be £5k (55 – 50) and this is covered by annual exemption so no CGT variation should be made; children receive the shares at MV later so only pay CGT themselves if the value rises further. If the variation were to be made for CGT, the children take the shares at the probate value of £50k so become liable for any increase from that value (already £5k)

Administration of IHT

* Delivering the IHT account -> for a CLT must be delivered within 12 months after end of month gift was made (transferor responsible); for a PET 12 months after end of month of death (transferee responsible); for the death estate the later of 12 months after end of month of death or 3 months after becoming personal representatives (personal representatives responsible)
* Late submissions of < 6 months are penalised by £100, between 6-12 months by £200 and > 12 months late of £3,000; failure to notify of a variation of will is penalised by £100 if < 12 months late and £3,000 if > 12 months late
* Personal representatives usually deliver the account well within the 12 months after the end of the month of death; this is because assets are released at this point and assets passed on and can be enjoyed therefore giving the incentive to speed up the grant of probate
* Payment deadlines for IHT -> 1) CLT lifetime tax: later of 6 months after end of month of CLT and 30 April in tax year following CLT tax year; 2) CLT death tax: 6 months after the end of the month in which death occurred; 3) PET: 6 months after end of month of death; 4) death estate: at the same time the IHT account is delivered
* IHT payments can be made in instalments -> 1) lifetime IHT on a CLT where the recipient pays; 2) additional IHT due on death on a CLT where the recipient still owns the property when the donor death; 3) additional IHT due on death on a PET with same conditions as no. 2; 4) IHT on the death estate

Special Gift Relief relating to IHT

* Death is not a disposal for CGT purposes so there is not normally a double CGT/IHT charge. This can happen though if an individual gives shares to a trust and CGT and IHT arise on the CLT -> donor in this case can claim special GR. CGT computed as normal but then deferred against base cost of the shares for the recipient, deferring the gain until recipient trust disposes of the shares so passes on the CGT liability to that trust. Shares qualifying for BPR are not eligible for this as there is no immediate charge to IHT
* Further numerical example for special GR -> individual acquires jewellery for £1mn but gifts it to a discretionary trust when MV = £15mn. What relief is available on the gain of £14mn: immediate charge to IHT so special GR can be claimed, reducing the chargeable gain to nil. Base cost for the trust will be the original cost = £1mn (£15mn value - £14mn gain)

IHT and Domicile Status

* if an individual is domiciled for IHT in the UK, he is liable to IHT on worldwide assets, so if he owns shares in a German company these will be liable at death; if not domiciled for IHT purposes in the UK then not liable to UK IHT on the shares though may be liable in his country of domicile. IHT domicile is different to income tax domicile