

Suggested solution

Section A

Question 1

Memorandum for client file

For: Client file

Client: Bridie and Adam

Subject: Personal and unincorporated business taxes

Prepared by: Tax senior

Date: 1 August 2026

These notes are to be used in preparation for a meeting with Bridie and Adam, respectively.

(a) (i) Bridie's personal tax affairs: tax residence and chargeable gains

Tax residence

In the tax year 2026/27 Bridie will not satisfy the 183-day automatic UK tax residence test. However, she will be automatically UK tax resident for this tax year because she will be working full time in the UK for a period of at least 365 days, some of which are in the tax year 2026/27.

The split year basis will apply because Bridie was not UK tax resident in the tax year 2025/26; she became tax resident in 2026/27; and she did not have sufficient UK ties to be UK resident prior to her return to the UK.

Consequently, Bridie will be treated as UK tax resident from 1 November 2026, which is the day she begins full-time employment in the UK as well as the date she acquires a home in the UK.

Chargeable gains

Gains subject to UK capital gains tax (CGT)

Generally, gains are subject to UK CGT where an individual is either tax resident in the UK or only temporarily non-UK tax resident. In the tax year 2026/27 Bridie was temporarily non-UK tax resident prior to being treated as UK tax resident from 1 November 2026. This is because she was UK tax resident for at least four of the seven tax years prior to the tax year of her departure from the UK; and she was non-UK tax resident for less than five years.

Portrait painting

Despite Bridie being temporarily non-UK tax resident, her gain on the sale of the painting will NOT be subject to UK CGT. This is because she both purchased and sold it while she was non-UK tax resident.

Vintage car

Cars are exempt assets for the purposes of UK CGT. Accordingly, the profit on the sale of Bridie's vintage car will not be subject to UK CGT regardless of Bridie's residence status.

Landscape painting – timing of sale

The gain on the sale of the landscape painting will NOT be subject to UK CGT if it is sold before Bridie returns to the UK. This is because Bridie will have both purchased and sold the painting while she was overseas. Accordingly, in these circumstances, Bridie's post-tax sales proceeds would be £39,000.

If the painting is sold after Bridie has returned to the UK, the gain would be subject to UK CGT at 24% (as Bridie will be a higher rate taxpayer in the tax year 2027/28). The post-tax proceeds would be:

	£	£
Proceeds		51,000
Chargeable gain (£51,000 - £24,000)	27,000	
Less: annual exempt amount	(3,000)	
Taxable gain	24,000	
CGT at 24%		(5,760)
Post-tax proceeds		45,240

In view of the above, Bridie should sell the landscape painting after she has returned to the UK.

(ii) Bridie's personal tax affairs: employment contract

Net financial benefit/cost of the alternative benefits for a complete tax year

Bridie should choose the cars because this results in a lower total cost to her. This is demonstrated in the following summary table and supporting workings:

	Cars	House
	£	£
Income tax in respect of benefit (W1)	7,280	13,998
Rent payable to employer	-	2,400
Annual cost of leasing the cars privately	-	9,500
Annual cost of renting the house privately	14,000	-
Total cost to Bridie	21,280	25,898

Workings:**1. Income tax in respect of the benefits**

	Cars	House
	£	£
Salary	78,000	78,000
Employment benefit:		
Cars (£10,400 + £7,800)	18,200	
House (W2)		30,663
	96,200	108,663
PA	(12,570)	
Restricted PA: (£12,570 - £4,332 ((£108,663 - £100,000) x 50%))		(8,238)
	83,630	100,425
Income tax		
£37,700 x 20%	7,540	7,540
£45,930 (£83,630 - £37,700) x 40%	18,372	
£62,725 (£100,425 - £37,700) x 40%		25,090
	25,912	32,630
Less: tax on salary	(18,632)	(18,632)
Income tax in respect of benefit	7,280	13,998

2. Employment benefit in respect of accommodation

	£
Annual value	10,000
Additional charge (£690,000 - £75,000) x 3.75%	23,063
	33,063
Less: rent payable by Bridie (£200 x 12)	(2,400)
Benefit	30,663

Company Share Option Plan

Bridie has asked us to confirm that after the exercise of her option on 1 June 2030, a sale of the shares on the same day will NOT give rise to a chargeable gain. This is incorrect.

Bridie's base cost in the shares for the purposes of CGT will be the amount she paid for them (£23,800 (1,400 x £17)) together with any amount chargeable to income tax in respect of the acquisition of the shares (which is £nil).

Accordingly, when the shares are sold, Bridie will realise a chargeable gain equal to the excess of the sales proceeds over £23,800.

This gain, as reduced by any available amount of annual exempt amount, will be subject to CGT at the rate of 24% (this is on the assumption that Bridie continues to be a higher rate taxpayer).

Ethical considerations

The fundamental principles of ethics which are threatened, and potential safeguards that can be put in place, when working for both Bridie and her employer, Pacoe Ltd, are as follows:

Objectivity

ACCA members should advise their clients by reference to what is best for their clients and should not be influenced by, for example, bias or conflicts of interest. Providing advice to Bridie in respect of her employment contract with Pacoe Ltd would give rise to a conflict of interest because Pacoe Ltd is a client of the firm.

A course of action which is most beneficial for Bridie may not be advantageous for Pacoe Ltd. This could threaten our ability to provide either or both of them with objective advice.

Accordingly, as we act for both Bridie and Pacoe Ltd, we should have pointed out the potential conflict to them and obtained their permission.

In addition, we should have considered using separate teams for each of them.

Confidentiality

ACCA members should not disclose client information to third parties without client permission unless legally or professionally required to do so.

It is possible that information we hold in relation to Bridie could be inadvertently revealed to Pacoe Ltd without Bridie's consent, or vice versa.

Again, we should have considered using separate teams for each of them.

(b) Adam's new unincorporated business

Registration for the purposes of value added tax (VAT)

Implications of Adam voluntarily registering for VAT are as follows:

Once he has registered, Adam would be able to recover all of his input tax because all of the supplies of his business will be standard rated.

He would also be able to recover input tax incurred in respect of goods purchased for business purposes in the four years prior to registration provided he still owns the relevant items; and services purchased for business purposes in the six months prior to registration.

Adam would have to charge 20% VAT on all of his sales. Adam's non-business customers and those business customers who are not registered for VAT would NOT be able to recover this VAT. If Adam is unable to pass on to his customers the price increase resulting from the charging of VAT, the profitability of his business is likely to be reduced.

Tax-allowable expenses

Costs paid are allowable for tax purposes where they are incurred wholly and exclusively for the purposes of the trade and are not specifically disallowed.

Costs of sales brochures

The cost of the sales brochures is allowable for tax purposes because they were paid for by Adam within the seven years prior to commencing to trade and would have been an allowable expense if they had been paid after he began trading.

The costs will be treated as having been paid on 1 December 2026, the first day of trading.

Costs of promoting the business

The travel costs will be allowable for tax purposes in accordance with the above principles.

The cost of buying lunch for prospective customers will be classified as entertaining, which is not allowable for tax purposes.

The proposed gifts will carry a conspicuous advert for Adam's business and will not consist of food, drink or tobacco. Accordingly, the cost of the gifts will be allowable for tax purposes as each one costs no more than £50.

Section B

Question 2

(a) Increase in corporation tax liability

Mtucs Ltd's taxable total profits for the year ending 31 March 2026 will be unaffected by the sale of shares in Werj Ltd (W1) and will increase by £78,300 as a result of the sale of the warehouse (W2). An overall increase in Mtucs Ltd's taxable total profits of £78,300 will therefore occur as a result of the two disposals.

For the accounting period ending 31 March 2026, Werj Ltd is an associated company of Mtucs Ltd, as Mtucs Ltd will have had a shareholding of more than 50% throughout this accounting period. The upper limit for augmented profits for determining the rate of corporation tax payable for the financial year 2025 will therefore be £125,000 (£250,000/2). Mtucs Ltd's taxable total profits prior to making these disposals were forecast to be £130,000, such that it would already be paying corporation tax at the main rate.

Accordingly, as a result of these disposals, there will be an increase in corporation tax of £19,575 (£78,300 x 25%).

(W1) Sale of shares in Werj Ltd

The gain arising on the sale of Mtucs Ltd's 80% shareholding in Werj Ltd on 31 March 2026 will be exempt from corporation tax under the substantial shareholding exemption (SSE). This is because Mtucs Ltd owned at least 10% of the shares in Werj Ltd for a continuous 12-month period during the six years prior to the sale, and Werj Ltd is a trading company.

(W2) Sale of warehouse

	£
Sales proceeds	255,000
Add: Structures and buildings allowance (SBA) claimed (Working)	15,300
	270,300
Less cost (Note 1)	(192,000)
Gain	78,300

Working:

Qualifying cost for SBAs – building only	102,000
SBAs: 1 April 2021 – 31 March 2026 (Note 2) (£102,000 x 3% x 5 years)	15,300

Note 1: Mtucs Ltd and Werj Ltd were in a chargeable gains group on 1 April 2025 as Mtucs Ltd owned at least 75% of the ordinary shares in Werj Ltd. Therefore, for tax purposes, the transfer of the warehouse will have been a no gain no loss transfer such that Mtucs Ltd will be treated as if it had acquired the warehouse on 1 April 2021 for its cost to Werj Ltd of £192,000.

Note 2: There is no balancing adjustment for SBA purposes in respect of a building on which SBAs have been claimed, so Mtucs Ltd will have continued to claim SBAs on the original qualifying cost. However, because Mtucs Ltd received the warehouse in a no gain/no loss transfer from Werj Ltd, the total allowances claimed by both companies will be added to the sale proceeds on this disposal to an unconnected person.

(b) The overseas business is carried on through a permanent establishment (PE)

The profits of the PE in Daylia will be included within Mtucs Ltd's taxable total profits and charged to UK corporation tax on Mtucs Ltd. Double tax relief will be available to compensate for the 22% tax which will be due in Daylia in respect of the £30,000 of PE profits generated. The UK corporation tax due on the £30,000 PE profits will be £7,307 however, the £6,600 of tax paid in Daylia can be offset via double tax relief (DTR) which will result in UK corporation tax due on the PE's profits of £707 (see calculation below). This will be paid in addition to the £6,600 of tax due in Daylia.

Total tax payable

UK corporation tax payable

	£	£
Trading profit:		
UK		145,000
Daylia PE		30,000
Taxable total profits		175,000
Corporation tax at 25%		43,750
Less: ((£250,000 (W) - £175,000) x 3/200 x £175,000)/£175,000		(1,125)
Corporation tax before DTR		42,625
(average rate = 24.357% (£42,625/£175,000 x 100%))		
UK tax on overseas income		
Double tax relief – the lower of:		
Overseas tax on overseas income (£30,000 x 22%)	6,600	(6,600)
UK tax on overseas income (£30,000 x 24.357%)	7,307	
UK corporation tax payable		36,025

(W) Following the sale of the shares in Werj Ltd on 31 March 2026, Mtucs Ltd will have no associated companies in the year ending 31 March 2027 such that the upper limit for augmented profits for determining the rate of corporation tax payable for the year ending 31 March 2027 will be £250,000.

The overseas business is carried on by a subsidiary company

The overseas subsidiary will be a separate legal entity to Mtucs Ltd and will be liable to corporation tax on the £30,000 of profits generated separately based on the subsidiary's tax residence. Mtucs Ltd will therefore not have any UK corporation tax liability in relation to the profits of its overseas subsidiary.

The profits of the overseas subsidiary will only be subject to UK corporation tax if the subsidiary company is tax resident in the UK. The subsidiary company is to be incorporated overseas. Accordingly, it will not be resident in the UK unless it is managed and controlled from the UK. The overseas subsidiary will potentially be liable to corporation tax in Daylia based on the rules applying there.

Any dividends received by Mtucs Ltd from the overseas subsidiary will be exempt income for the purposes of UK corporation tax. The dividends will also not be included in calculating augmented profits for Mtucs Ltd because Mtucs Ltd and the overseas subsidiary will be associated companies.

The subsidiary company would be an associate company of Mtucs Ltd for the purposes of determining the rate of corporation tax payable in the accounting period the subsidiary is created and future accounting periods. As the subsidiary is to be incorporated on 1 April 2026 it would become associated to Mtucs Ltd in the year ended 31 March 2027. As Mtucs Ltd's taxable total profits are forecast to be £145,000 for the year ending 31 March 2027, they will exceed the reduced upper limit for augmented profits of £125,000 ($£250,000/2$) (before considering any dividends received) such that Mtucs Ltd will pay corporation tax at the main rate on its taxable total profits.

Question 3

(a) Income tax saving from transfer of investments

Kyle is a higher rate taxpayer (total annual income £90,000) and Libby is a basic rate taxpayer (total annual income £14,000). In respect of both gifts, the full amount of the income from the transferred gifts would fall into the higher rate band for Kyle and would fall into the basic rate band for Libby.

Gift of the UK investment property

The income tax saved as a result of this gift would be:

	£
Kyle: Tax saved ($£15,000 \times 40\%$)	6,000
Libby: Additional tax payable ($£15,000 \times 20\%$)	(3,000)
Net tax saving	3,000

Gift of shares in Greeb Ltd

	£
Kyle: Tax saved ($£12,000 \times 33.75\%$)	4,050
Libby: Additional tax payable ($(£12,000 - £500) \times 8.75\%$)	(1,006)
Net tax saving	3,044

Kyle has other dividend income which will utilise the dividend nil rate band (DNRB), so this will not be lost. Libby has no other dividend income, so the DNRB will be available to reduce the amount of the dividend which is taxable at 8.75%.

Therefore, gifting the shares in Greeb Ltd will lead to a greater net annual tax saving for the couple of £3,044.

(b) The gift of the shares in Greeb Ltd

Gift holdover relief is available because:

- (1) Greeb Ltd is an unquoted trading company; and
- (2) Libby (the donee) will be UK tax resident at the date of the gift.

Consequences of a gift holdover relief claim for both Kyle and Libby

The gift of the shares will give rise to a chargeable gain for Kyle of £18,000 (£404,000 - £386,000). However, as Greeb Ltd is Kyle's personal company (because he can exercise at least 5% of the voting rights) the gain eligible to be deferred under a gift holdover relief claim will be restricted to the proportion of the gain which relates to the business assets of Greeb Ltd. This is calculated as the value of chargeable business assets divided by the value of total chargeable assets. Accordingly, £16,286 ($£18,000 \times (£3.8m / (£3.8m + £0.4m))$) of the gain will be deferred. The chargeable gain remaining will be £1,714 (£18,000 - £16,286).

The deferred gain of £16,286 will be deducted from the base cost of the shares for Libby. Consequently, when Libby sells these shares on 1 March 2028, the gain realised by her will be effectively increased by the amount of the gift holdover relief.

(c) Circumstances giving rise to maximum inheritance tax (IHT) liability

Availability of business property relief (BPR) in respect of the gift of shares

The gift of the shares will qualify for BPR at the rate of 100% because Greeb Ltd is an unquoted trading company and Kyle will have owned the shares for at least two years prior to the gift. However, the relief will be restricted due to the 'excepted assets' (assets which have not been used for the purposes of its business in the two years prior to the gift and which are not required for business purposes in the future) in the company. The amount of relief available would be £368,089 (£404,000 x (£4.1m/£4.5m)).

However, it is also necessary that Libby owns the shares at the date of Kyle's death or, if not, that she has reinvested the proceeds in qualifying replacement business property within three years of the date of sale. As Libby will sell the shares on 1 March 2028, further information will therefore be required as to whether or not a qualifying replacement asset is acquired before 1 March 2031.

Maximum potential liability to IHT

The maximum liability will arise if Kyle dies:

- After 1 March 2028, as BPR will no longer be available if Libby does not acquire a replacement asset, as stated above;
- Prior to 1 July 2030 as he has made one prior gift on 1 July 2023, which will use part of his nil rate band if he dies prior to this date;
- Before 6 April 2029 (three years after the date of the gift on 6 April 2026) as taper relief will be available after this date.

Annual exemptions are available for the tax years 2026/27 and 2025/26, such that the gross chargeable value of the gift will be £398,000 (£404,000 - £3,000 - £3,000).

The maximum potential IHT liability is therefore £72,400 (£398,000 - (£325,000 - £108,000) x 40%) and will arise if Kyle dies between 1 March 2028 and 6 April 2029.

Mark scheme

Question 1

(a)

(i) Tax residency

UK resident 2

Split year basis 3

Chargeable gains

Temporary non-resident 3

Portrait and car 2

Landscape painting 5

Maximum 12 marks

(ii) Employment contract and ethics

Employment benefits

Car calculations 3

Accommodation calculations 5

Recommendation 1

CSOP 3

Ethics

Objectivity 3

Confidentiality 2

Maximum 16 marks

(b)

VAT

Input 3

Output 4

Tax allowable expenses

General rule 1

Cost of sales brochures 2

Promotion costs 3

Maximum 12 marks**Professional skills marks:****Communication**

General report format and structure (use of headings, sub-headings and an introduction)

Style, language and clarity (tone of report response, presentation of calculations, appropriate use of the tools, easy to follow and substantive amount of content)

Analysis and Evaluation

Clear and logical approach taken to the discussion and recommendations of the employment benefit options

Answer clearly analyses both voluntary VAT registration and tax allowable costs for the unincorporated business

Commercial Acumen

Recommendation on the tax implications of capital disposals are appropriate and are valid commercial points

Scepticism

Assessment of Bridie's assumptions re the tax implications of the CSOP shares, and the ethical factors (conflict of interest) in acting for both Bridie and Pacoe Ltd, are challenged

Maximum 10 marks**Total 50 marks**

Question 2**(a)**

Calculation of gain on warehouse	3
Explanatory notes re warehouse	3
Sale of shares in Werj Ltd	2
Additional CT payable	3

Maximum 9 marks**(b)**

Overseas permanent establishment	7
Overseas subsidiary	6

Maximum 11 marks**Professional skills marks:****Analysis and Evaluation**

Clear, logical and systematic approach to calculations which support discussions to draw meaningful conclusions on the tax impact of the disposals.

Commercial Acumen

Application of the two alternative overseas structures are suitably linked to Mtucs Ltd's business.

Maximum 5 marks**Total 25 marks**

Question 3**(a)**

Net saving on rental income	1
Net saving on dividend income	2
Explanations	2
Conclusion	1

Maximum 5 marks**(b)**

Why gift relief is available	1
Consequences for Kyle	3
Consequences for Libby	2

Maximum 6 marks**(c)**

Eligibility of shares	3
Libby's ownership	2
Maximum IHT liability	6

Maximum 9 marks**Professional skills marks:****Analysis and Evaluation**

Clear and logical approach taken to the calculation of the tax savings of each gift.

Comprehensive evaluation of the impact of the claim for both Kyle and Libby.

Commercial Acumen

Advice on inheritance tax for Kyle is focused and raises valid commercial issues.

Maximum 5 marks**Total 25 marks**