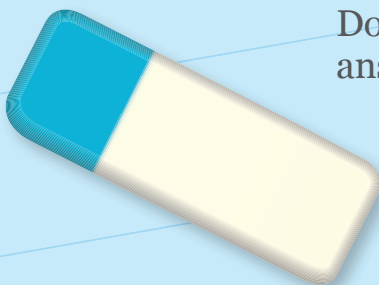




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Explaining technical issues clearly is an essential skill in treasury practice and in your ACT exam. Doug Williamson shows how to structure your answers to pick up easy marks



A common error in preparing for exams is neglecting to practise your explanations. This results in omitting questions, and, sadly, you score no marks for any explanations you don't attempt. Many of those missed marks are easy. Often they are points that candidates know, but don't write down. Writing explanations needs your structured practice. This article provides a reliable three-step structure, a recent example and encouragement to practise it.

An essential practical skill

Explanation, in plain language, is an essential skill to sharpen as part of your treasury training. Technical concepts are difficult for most non-specialists to understand. So every qualified treasury professional needs to master the skill of providing clear explanations about technical issues. For this reason, technical explanations are frequently examined, with significant marks available for your answers.

The April 2013 Corporate Tax exam asked candidates to 'explain' no fewer than eight times in an all-compulsory paper.

Looking more broadly at Corporate Tax papers, there were more marks for narratives than for computations in every sitting from April 2011 to October 2013. Yet, as noted by the examiner, it was on their narratives that many candidates scored relatively poorly.

'Explain' means

- (1) Why?
- (2) How?
- (3) Be specific

Two reminders

"As in previous diets, candidates are reminded that it is important to be able to explain the tax implications of a transaction and not simply to carry out calculations. In addition, a working knowledge of the tax system and its administration is required. Candidates continue to perform less well in parts of the paper focused on these topics."

Examiner, Corporate Tax, April 2013

What is 'explain' asking for?

'Explain' means three things: (1) Say why; (2) Say how; and (3) Be specific.

Some candidates explain technical issues brilliantly and their scripts are a pleasure to mark. Sadly, many candidates don't explain so well. A substantial minority omit explanations entirely, throwing marks away.

Explaining needs understanding

To explain well, we need to understand. This is the reason why 'explain' appears so often in exam questions. It's testing our understanding of important practical issues. Once we understand the reasons for things, they're much easier to explain. Examples include detailed rules in tax, law, accounting and other regulations, and their practical application to commercial situations.

Let's look more closely at a recent question.

Explanation required

Scott Inc is a US-resident company. The directors have calculated a taxable profit of \$17,500,000 for the year ended 31 December 2012. In the previous year, the company had taxable profits of \$14,000,000.

(Part (a) required a calculation of the US corporate income tax on the profit for the year to 31 December 2012. The answer is \$6,100,000.)

(b) Explain and state when the tax for Scott Inc will be payable.

Question 2, Corporate Tax, April 2013

Rules have reasons

All rules are made by people, with a purpose. To remember, explain and apply any rule we need to know:

Comfortable with complexity

“The greatest achievement of AMCT is that it has increased my confidence. I am now comfortable coaching my team through issues and having complex discussions with my clients about their methodology and approach.”

Lucia Hudakova AMCT

- (1) The purpose;
- (2) How the detailed rules aim to achieve the broader purpose; and
- (3) The impact on our company – why the rule is important.

Understanding US tax rules

Let's apply our three-step structure above to the US tax instalment rules.

(1) **Purpose.** The purpose of tax instalments is to collect taxes from larger, richer companies, who can afford to pay within their tax year.

(2) **Detail.** The detailed tax regulations classify companies into (i) the smallest; (ii) the largest; and (iii) all other companies in between. The smallest companies are treated the most favourably (no instalments) and the largest are treated the most harshly (strict instalments). In-between companies get an in-between instalment treatment.

(3) **Impact.** All companies need to know when their tax is payable, and how much they have to pay. Missing tax payments exposes the company to the risk of penalties, interest charges, reputational loss with the tax authorities, more questions to answer, compliance costs and management distraction in responding to further questions.

Now that we know the reasons for the rules, let's see how candidates handled this exam question.

Why? How? Be specific

“Many candidates appreciated that four instalments of US corporate income tax would be required. But few gave an explanation as to why this was the case or of how each instalment was calculated. Instalment dates were often noted as months four, six, nine and 12, without giving the actual dates in Scott Inc's circumstances. Companies are looking for information specific to their own situation, rather than purely theoretical details.”

Examiner, *Corporate Tax*, April 2013

Why candidates didn't explain

With so many marks on offer for explanations, and so many candidates not attempting them, it's useful to identify the possible reasons why they didn't:

(1) Inability or reluctance to provide a response in the exam.

(2) Assuming that the explanations were too easy to have marks allocated.

(3) Assuming that the question 'Explain and state when the tax... will be payable' was a clone of other simpler questions, such as 'State when the tax... will be payable.'

(4) Reading the question too fast.

(5) Not thinking about the significance of the material in advance, making it hard to recall under exam conditions.

Explanations are often easy, once we've noticed that they're needed. Many candidates who missed the marks here would have scored all of them if they had simply invested time in careful reading of the very first word of the question: 'Explain...'

Now, let's recap and expand the rules about tax instalments, having already clarified their important general purpose.

Gruesome details

Who pays instalments? The smallest US companies don't have to pay any tax instalments. The threshold is \$500 tax payable. All other companies must pay instalments. Scott Inc falls into the instalment-paying category.

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When they pay: instalments are paid on the 15th of months four, six, nine and 12 within the company's tax year. So the exact dates depend on the company's year-end date.

How much they pay: the amounts depend on the size of the company. 'Large' companies pay under a strict, simple rule. 'Large' means having taxable profits of more than \$1m, in any one of the preceding three years.

These large companies must pay instalments of 25% of the current year's estimated tax liability. This rule will bite Scott Inc as well.

To summarise, here is a model exam answer, explaining these rules and applying them to our company.

Model answer

(1) Scott Inc's 31 December 2012 tax payable exceeds \$500 – so the tax is payable by instalments.

(2) Instalments are on the 15th of months four, six, nine and 12 within the company's year to 31 December 2012. Namely, 15 April, 15 June, 15 September and 15 December 2012.

(3) Scott Inc is 'large' – having taxable profits greater than \$1m in at least one of the preceding three years. So each instalment will be 25% of the current year's estimated liability

$$= 0.25 \times \$6,100,000$$

$$= \$1,525,000$$

Winning words are worth many marks. Now, practise your three-step structures to make your explanations count.



Doug Williamson FCT is an examiner, tutor and coach who is uniquely qualified to help you pass your ACT exams, having read and carefully marked thousands of students' exam answers