ADIT

Chartered Institute of Taxation
Excellence in Taxation

# THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2019

# MODULE 2.09 – UNITED KINGDOM OPTION

## ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

TIME ALLOWED – 3¼ HOURS

This exam paper has **three** parts: **Part A**, **Part B** and **Part C**.

You need to answer **five** questions in total. You will **not** receive marks for any additional answers.

You must answer:

- **Both** questions in **Part A** (25 marks each)
- **One** question only from **Part B** (20 marks)
- **Two** questions only from **Part C** (15 marks each)

**Further instructions**

- All workings should be made to the nearest month and in Pound Sterling, unless otherwise stated.
- Start each answer on a new page and clearly indicate which question you are answering. If you are using the on-screen method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately half of your time answering Part A, and the other half answering questions in Parts B and C.
- The first 15 minutes of the exam is reading time. You will be allowed to annotate the question paper during this time; however, you will **not** be permitted to start writing or typing your answer, or use a calculator. The Presiding Officer will inform you when you can start answering the questions.

For your information this paper is accompanied by:

**ADIT Examinations 2019 Tax Tables**

## PART A

**You are required to answer BOTH questions from this Part.**

1. Maude plc is the United Kingdom-incorporated and resident head of a small group of manufacturing companies, all of which have a 31 March year end.

Following an economic downturn, some companies within the group have significant carried forward Corporation Tax losses. However, other companies in the group have now recovered and are starting to generate profits.

You have been provided with the following summary of the profit and loss position of the UK resident group companies:

- Matilda Ltd has substantial carried forward trading losses and non-trading loan relationship deficits for both the years ended 31 March 2017 and 31 March 2018.

- Richard Ltd made trading profits in both the years ended 31 March 2017 and 2018.

- Eleanor Ltd had a substantial carried forward trading loss in the year ended 31 March 2017, but made a small trading profit in the year ended 31 March 2018 and is expected to be profit making going forwards.

In addition to these UK-resident companies, the group also has two non-UK trading companies that are loss making, one of which is incorporated and tax resident in France and the other in India.

Maude plc also has a permanent establishment in Italy which has incurred significant losses.

**You are required to:**

1) **Provide a brief outline of the changes to the rules on utilisation of carried forward Corporation Tax losses for periods before and after 1 April 2017 (as introduced by Finance (No.2) Act 2017).** (7)

2) **Explain the options available to utilise the carried forward losses in Matilda Ltd and Eleanor Ltd at 31 March 2017 and 31 March 2018, including any impact of the Finance (No.2) Act 2017 changes. For these purposes you should ignore any time limits which may prevent a loss relief claim from being made.** (10)

3) **Consider whether there is any possibility for the losses of the French and Indian subsidiaries and Italian permanent establishment of Maude plc to be utilised against profits of the UK-resident companies in the group. Consider how any current or future election under s.18A CTA 2009 could affect the utilisation of the Italian permanent establishment losses.** (8)

Total (25)

2. You have recently received an email from Fiona, an existing client who is a United Kingdom-resident taxpayer. Fiona has read your firm's circular on rebasing for certain deemed domiciled taxpayers and is keen to benefit from this opportunity. Fiona is also a United States citizen and is up-to-date with her US tax filings.

Fiona is domiciled in the US and moved to the UK in January 1995, acquiring an apartment in London in July 2007. Fiona is an artist and, while she carries on a small trade, her living expenses are mainly funded by a large inheritance she received in 2012, comprising a valuable share portfolio which she holds directly and upon which she received comprehensive taxation advice at the time of acquisition. Fiona has not applied for a UK passport, preferring to travel under her US passport.

In her email to you, Fiona mentions that in 2015/16 she received a second inheritance, comprising an investment portfolio valued at US$10 million, upon the death in 2015 of her aunt, a US citizen. You subsequently learned from further correspondence that Fiona's late aunt had been life tenant of a very old US trust, and that the $10 million had been distributed to Fiona on the winding up of that trust upon her aunt's death. You understand the trust assets consisted of a valuable foreign portfolio of shares and non-reporting funds. Fiona has also advised that, prior to her aunt's death, all trust income had always been distributed to her aunt and that all US taxes had been paid, including US capital gains tax on trust assets disposed of. Fiona has confirmed that the entire distribution has been retained offshore. Your firm was unaware of the trust distribution received by Fiona after her aunt's death, and no reporting has been made in respect of this on Fiona's 2015/16 tax return. An expert colleague has reviewed the trust deed and advised you that the trust will be treated as an offshore trust for UK tax purposes.

You have discussed Fiona's case with a partner in your firm, who has emphasised that, while Fiona is non-domiciled, she has hitherto always filed on an-arising basis.

You may accept that Fiona is non-domiciled, and that significant historical trust gains were realised and retained in her aunt's US trust. You do not need to consider any Worldwide Disclosure Facility (WDF) or non-compliance issues, as these will be addressed by your tax investigations partner.

**You have been asked to provide Fiona with detailed advice on the following questions:**

1) **How would the 2015/16 distribution be subject to UK tax:**

   a) **on the assumption that the distribution was remitted to the UK in 2015/16; and** (7)

   b) **on the alternative assumption that Fiona wishes to make a remittance basis election? Your advice should include a description of the procedure for claiming the remittance basis.** (5)

2) **What are the necessary conditions for Fiona to qualify for rebasing of foreign assets introduced in the Finance (No. 2) Act 2017, in relation to her 2012 inheritance?** (6)

3) **What are the tax consequences for Fiona of the disposal of:**

   a) **shares in an Italian investment company; and**

   b) **an Italian office building?**

   **Fiona seeks to learn which country will be awarded taxing rights over the disposals under the UK-Italy tax treaty, and whether relief will be available for any Italian tax deducted, under either the treaty or UK domestic rules. You should assume that the UK-Italy tax treaty follows the OECD model.** (7)

Total (25)

## PART B

**You are required to answer ONE question from this Part.**

3. Your client, the Octagon Group, comprises a number of companies incorporated and tax resident in the United Kingdom, which produce state-of-the-art laboratory equipment.

The activities of the Octagon Group to date have been focused solely on the UK; however, an opportunity has recently arisen for the group to acquire a competitor which owns a number of overseas subsidiaries.

You have received the following email from the Finance Director at the Octagon Group:

> Hi,
>
> Further to our meeting, we have more details about the proposed acquisition.
>
> We are looking to acquire the entire share capital of Nonagon, which is the Spanish tax resident holding company of a small group with operations around the world. We are currently undertaking due diligence to get a full picture of what each company in the group does, but we do know the following:
>
> - The main manufacturing company produces high specification products at a manufacturing facility in Germany which employs several hundred individuals.
> - Most of the group's intellectual property is held by a Cayman Islands company (IP Holdco). Other group companies (none of which are UK-based) pay royalties to IP Holdco. IP Holdco has access to a couple of desks in a commercial office, where its only staff (an administrator and a part time IP lawyer) carry out their duties.
> - There is a finance company based in Ireland which makes loan to other group companies to finance their activities.
>
> I will share more information with you as I receive it, but for the time being it would be good to know if we should be worried about the Controlled Foreign Company (CFC) rules applying to any of these three companies, and if so, what would be the consequences?
>
> In addition to the Nonagon acquisition, we are also looking to invest in a Singapore LLP to work on a joint venture in Asia-Pac. I'm not sure how this investment would be taxed from a UK perspective, so if you could advise me on the possibilities and what to look out for that would also be helpful.
>
> Kind regards
> Derek
> Finance Director – Octagon Group

**You are required to draft a reply to Derek, including:**

**1)** **A high level analysis of whether the UK Controlled Foreign Company (CFC) rules could apply to the German, Cayman Islands and Irish companies if the acquisition of Nonagon goes ahead. You are not required to carry out a detailed analysis, but should look at the potential application of the rules and identify areas which may require more detailed consideration.** (15)

**2)** **A brief outline of whether the Singapore LLP would be viewed as opaque or transparent by the Octagon Group for UK tax purposes, and the factors that will need to be considered to reach a final conclusion.** (5)

Total (20)

4. Your client Robert, a recently retired entrepreneur, is a United Kingdom-resident, non-domiciled taxpayer who first settled in the UK in 1995. Prior to 6 April 2017 Robert had always elected for the remittance basis of taxation.

In 2012 Robert created an excluded property trust (the RK Trust); the trust contains various foreign assets including a valuable share portfolio which generates very significant foreign investment income and foreign chargeable gains. In addition, Robert continues to directly hold 10% of the ordinary shares in a foreign incorporated company, EPA (Bahamas) Ltd, that pays large dividends. In previous years Robert has used these dividends to meet his foreign living expenditure and to add to his art collection, which is housed abroad.

Robert is concerned that the deemed domicile provisions introduced in the Finance (No. 2) Act 2017 will mean that his offshore income and gains will be taxed on an arising basis. He has also become frustrated at the constant changes to, and growing complexity of, the rules applicable to non-domiciled taxpayers. For these reasons Robert is considering leaving the UK, together with his wife Isabella, to live in what he perceives as a more favourable tax jurisdiction such as Switzerland or Monaco. Robert has reminded you that, while he currently spends about 190 nights in the UK each tax year, he also spends some time each year in his Swiss, French and Italian homes and believes that while he wishes to retain a home in the UK, he may be able to limit his time in the UK to no more than 60 nights per a tax year.

**Robert has asked you to prepare a memorandum explaining:**

1) **How income and gains arising in the RK Trust, Robert's directly held foreign income and his foreign chargeable gains, will each be taxed as a deemed domiciled taxpayer.** (7)

2) **How Inheritance Tax will apply both to assets in the RK Trust and to directly held assets.** (3)

3) **How he may qualify to be treated as non-resident under the statutory residence test.** (10)

Total (20)

## PART C

**You are required to answer TWO questions from this Part.**

5. The Partner to whom you report is attending a meeting with a prospective new client, Trapezium Ltd, and has asked you to produce some briefing notes to help her prepare.

Trapezium Ltd is incorporated and tax resident in the United Kingdom, and a member of a multinational group headquartered in the United States.

Trapezium Ltd's activities to date have been funded by equity from its US parent. However the group is seeking to expand Trapezium Ltd's operations, and to fund this expansion will take out a loan from a group treasury company (Finco) held directly by the group's US parent. Finco is treated as transparent for tax purposes in the country in which it is based, but under US tax law it is treated as a separate taxable entity.

Trapezium Ltd's management team is keen to discuss what the tax consequences may be if they are to take out a loan from Finco, and whether there are any issues they need to be aware of.

**You are required to prepare notes for the partner, addressing the following topics:**

1) **How, and why, may Trapezium Ltd be required to withhold tax on any interest payable to Finco, and what possibilities are there to reduce this liability?** (4)

2) **Are the UK anti-hybrid rules, Diverted Profits Tax and unallowable purpose anti-avoidance provisions likely to apply to the loan, and on what grounds? Can you identify (without detailed analysis) any other relevant provisions which may limit the ability of Trapezium Ltd to deduct the interest payable to Finco?** (11)

Total (15)

6. A client is considering buying a number of properties in the United Kingdom, and would like to set up a company outside the UK to acquire and hold these properties.

The properties being considered are:

- A house worth £750,000, which will be let to an unrelated tenant for a market rent.
- An office block worth £5 million.
- A house worth £2 million, which will be let to a director of the company in exchange for a nominal rent.
- A house worth £150,000, which will be let to the director's son for nominal rent.
- A purpose built halls of residence worth £3 million, containing 100 bedrooms for university students.

**You are required to:**

1) **Comment on how the Annual Tax on Enveloped Dwellings (ATED) rules would apply to each property if acquired by the overseas company. You should assume the company will not be tax resident in the UK. You are not required to calculate the amount of any ATED charge which may arise.** (10)

2) **Provide a general overview of the potential UK tax consequences if the properties were to be disposed of by the company in the future.** (5)

Total (15)

7. Jason is a United Kingdom-resident, non-domiciled client who is a remittance basis user. He has recently explained that he intends to remit funds to the UK, to fund the deposit for a London property which he wishes to acquire.

You have reviewed Jason's offshore bank accounts and note that for several years, non-taxed foreign income and gains have been paid into his offshore savings account held in Guernsey. However, in 2016/17 he transferred into the Guernsey account the disposal proceeds of shares which he had acquired several years previously as a gift from his aunt. You have determined that no taxable gain or loss arose on that disposal.

Prior to the sales proceeds received in June 2016, the balance in the account was £500,000 and entirely comprised income and gains earned prior to 5 April 2016. Following the deposit of the proceeds of £500,000, the mixed fund comprised £500,000 in capital, £400,000 in untaxed foreign income and £100,000 in foreign capital gain.

In 2017/18, £200,000 was withdrawn from the account in order to purchase a Spanish property. This payment was made directly to the vendor's Spanish bank account.

Your assistant has prepared a table summarising the transactions in and out of Jason's Guernsey savings account, which opened with a zero balance on 6 April 2013.

| | Capital (£) | Foreign untaxed income (£) | Foreign capital gain (£) | Withdrawal (£) | Balance (£) |
|---|---|---|---|---|---|
| 2013/14 | | 200,000 | | | 200,000 |
| 2014/15 | | 150,000 | | | 350,000 |
| 2015/16 | | 50,000 | 100,000 | | 500,000 |
| 2016/17 | 500,000 | | | | 1,000,000 |
| 2017/18 | | | | (200,000) Spanish property purchase | 800,000 |

On your advice Jason has not made any further payments into this account since 2016/17.

**You are required to:**

**1)** **Advise Jason of the implications for the composition of the mixed fund of the purchase of the Spanish property. In particular, advise Jason of the makeup of capital, foreign untaxed income and foreign capital gain in the mixed fund on 6 April 2018.** (4)

**2)** **Advise Jason of the tax implications of remitting £450,000 to the UK from the mixed fund account on 6 April 2019.** (4)

**3)** **Advise Jason of the cleansing opportunity available to non-domiciled taxpayers in the two years to 5 April 2019.** (7)

Total (15)

8. A large French group of companies is seeking to acquire a number of companies located in the United Kingdom and across Europe. It has established a new UK-incorporated subsidiary (UK Acquisitions Ltd) to purchase the shares of these target companies.

Although UK Acquisitions Ltd will be incorporated in the UK, the majority of its board will consist of French individuals who are also members of the board of the French parent company.

Following the acquisition, the newly acquired companies will pass the profits they generate to UK Acquisitions Ltd by paying dividends. UK Acquisitions Ltd will in turn pass these funds to the French parent company, by way of either dividends or upstream loans.

You should assume that the UK has double taxation agreements with the countries of residence of all of the acquisition targets, following the OECD Model Convention.

The board of the French parent company have asked you for advice on the proposed acquisition.

**You are required to draft a brief report, establishing:**

**1)** **Whether UK Acquisitions Ltd will be UK-resident for Corporation Tax purposes.** (3)

**2)** **Whether UK Acquisitions Ltd will have to pay Stamp Duty in the UK on its purchase of shares in the target companies.** (2)

**3)** **An outline of the UK Corporation Tax treatment of dividends received by UK Acquisitions Ltd, and a general summary of the UK Corporation Tax and withholding tax implications if UK Acquisitions Ltd pays dividends or lends funds to its French parent company.** (10)

**For the purposes of 3) only, you may assume that UK Acquisitions Ltd is UK-resident for Corporation Tax purposes.**

Total (15)

9. Michael is an American entrepreneur, who has recently moved to London. He holds 100% of the share capital of Hopkinton Inc., an international electronics business, headquartered in Boston, Massachusetts, where the company has its main office and the directors reside and regularly meet.

Michael intends to spend 250 days each year in London and the remainder of his time visiting several other countries, including Germany and the United States, mainly on company business. Michael is employed by Hopkinton Inc., with his salary paid into his US bank account. Hopkinton Inc. has no UK offices, although Michael is considering whether a London office should be established.

Hopkinton Inc. is fully subject to US corporate tax and Michael has mentioned that the applicable US tax rates are higher than those applying in the UK.

Michael has explained that the business is currently facing many challenges, including finance, acquisitions and choosing the location of fabrication factories. He has confided that, while the directors work in a collegiate manner and decisions are jointly made, in order to take the business to the next level his ability, as chairman of the board, to be decisive on major issues will be pivotal.

Michael intends to continue to chair board meetings by video conferencing or by other electronic means. If matters are urgent and there is no time to call a formal meeting Michael plans to simply call or text the relevant directors.

In addition, Michael is considering the merits of flying the Boston-based directors into London for twice-yearly meetings.

**You are required to advise Michael on the following matters:**

**1) Michael is aware that the UK operates a management and control test in determining whether non-UK incorporated companies are UK tax resident, and seeks your advice regarding the potential implications of his presence in London to the tax residency status of Hopkinton Inc.** (10)

**2) Michael has asked you to explain how overseas workday relief operates and, in particular, the conditions that must be satisfied to qualify for the relief.** (5)

Total (15)