

THE CHARTERED INSTITUTE OF TAXATION

ADVANCED TECHNICAL

Human Capital Taxes

November 2020

TIME ALLOWED
3 HOURS 30 MINUTES

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- Scots Law candidates may provide answers referring to Land and Buildings Transaction Tax rather than Stamp Duty Land Tax.
- Unless otherwise indicated by the provision of additional information, you may assume that 2019/20 legislation (including rates and allowances) continues to apply for 2020/21 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

1. You are a tax manager in a firm of Chartered Tax Advisers. You have received a telephone call from Martina Cowley, the Procurement Officer of a client, Overbridge Local Authority. After a number of complaints, Overbridge Local Authority have run a series of internal workshops for their housing department on customer care. They ran one workshop per month from April 2019 to March 2020.

The Local Authority's policy is to only engage temporary or specialist workers via agencies. As a result, the individuals who undertook the training were provided to Overbridge Local Authority by Coach.com Ltd, a UK based agency that provides temporary trainers.

In relation to the agreement with the agency:

- 1) Fixed fees were payable by Overbridge Local Authority of £2,500 plus VAT per session per trainer to Coach.com Ltd. For each session, two specified trainers were provided.
- 2) Coach.com Ltd must fulfil all tax obligations arising from the contracts, including any PAYE withholding obligations.

In relation to the training:

- 1) The trainers used the Local Authority's materials and equipment.
- 2) The workshop content was determined in conjunction with Overbridge Local Authority.
- 3) The workshops were held on Overbridge Local Authority's premises, to Overbridge Local Authority's timetable.
- 4) The sessions were supervised by the course coordinator from Overbridge Local Authority's education department. This ensured the sessions covered the agreed content.
- 5) Each trainer had to deliver the work personally and could not provide a substitute or stand in for their designated workshop.

The following UK based trainers were used:

- 1) Sanjit Khula who is the sole director and shareholder of S Khula Training Ltd.
- 2) June and Oscar Cox who are spouses and operate as partners in their own partnership; Customers First LLP.
- 3) Michelle Dennis, who operates as a sole trader.

None of the above trainers are connected to Coach.com Ltd or Overbridge Local Authority.

You have established that the agency paid the trainers £1,800 per day, plus VAT where relevant, and the trainers were paid on the last working day of the month in which the services were provided.

Martina has concerns that the tax treatment of the payments to the trainers may not have been correct. She needs to understand what the Authority's obligations were and any risk arising on them.

Requirement:

Draft an email to Martina Cowley advising on the Income Tax and National Insurance obligations arising as a result of the arrangements. (15)

2. Toriq Inc is a multinational car manufacturer which is headquartered in the US. It sells its vehicles via independent dealer franchises (one franchise per country). Toriq Inc plans to implement a global incentive scheme for sales personnel of the independent dealer franchises. The awards will be based on the quarterly sales schedules for each employee, which will be provided to Toriq Inc by the franchises. The scheme will commence on 1 January 2021.

Quarterly Awards

A quarterly award will be made to the top 50 employees in each country in April, July, October and January based on sales for the preceding calendar quarter. Franchise employees will choose an item from a catalogue. The cost to Toriq Inc of each item is £1,000.

Annual Awards

Each year the top 20 employees, from each country will be invited by Toriq Inc to an annual weekend event held in late February, to celebrate their success and to learn about any new car developments for the coming year. This event will be either at a Caribbean beach resort or a European ski resort, alternating each year. The total costs per attendee will be £5,000.

At the event, the top 10 employees from each country will receive a cash bonus of £10,000.

The UK franchise is operated by Best Motors World Ltd, a UK resident company with 1,000 sales personnel.

Requirement:

Explain, with appropriate calculations, the UK Income Tax and National Insurance implications of the proposed scheme for Toriq Inc and Best Motors World Ltd.

(15)

3. You are the employment tax specialist in a firm of Chartered Tax Advisers. Your client is Saku Group UK Ltd, the UK subsidiary of a Japanese group. You have received the following email from Kerry Taylor, the HR manager.

To: Janette Voss
From: Kerry Taylor
Date: 29 October 2020
Subject: Riku Tanaka's UK Payroll

Hi Janette

I hope you are well. I wanted to check something with you regarding Riku Tanaka, who is our new Head of Sales and who has two employment contracts. Riku has confirmed he is domiciled in Japan, but he is UK tax resident as he has been living here for about five years.

His first employment contract is for 40% of his time and is with our Japanese parent company under which he is VP of Sales. I believe he is paid around £80,000 plus bonuses, which is taxed in Japan and not included on the UK payroll. This role has included work on the launch of their new machinery in the UK. Part of this has been to tell us about the new machines in our management meetings in the UK.

His second contract is for 60% of his time and is with the UK company as Head of Sales. He's responsible for everything to do with the sale and supply of UK machine parts globally and after service to UK customers. We pay him £150,000 plus bonuses, which goes through our UK payroll with PAYE and employer's and employee's National Insurance accounted for. Apparently, Japan has accepted that he is not resident there and accordingly he is not taxed there on the income from his UK contract.

I just wonder if we are doing the correct thing in relation to his Japanese earnings?

Thanks and kind regards.

Kerry

Requirement:

Write an email to Kerry advising on the UK tax implications of Riku's employment.
(20)

Continued

3. Continuation

Extract from the UK-Japan Reciprocal Agreement 2000

Article 4

- 1) As regards compulsory coverage, subject to the provisions of paragraphs 2 to 5 and Articles 5 to 7, where a person works as an employed or self-employed person in the territory of one Party, that person shall be subject only to the legislation of that Party. Where a person is subject only to the legislation of the United Kingdom in accordance with the provisions of this paragraph, that legislation shall apply to that person as if that person were ordinarily resident in the United Kingdom.
- 2) As regards compulsory coverage, subject to the provisions of paragraph 1 of Article 5, where a person works as an employed person in the territory of both Parties and would otherwise be subject to the legislation of both Parties for the same period, that person shall be subject only to the legislation of the Party in whose territory that person is ordinarily resident.
- 3) As regards compulsory coverage, where a person is ordinarily resident in the territory of one Party and works as a self-employed person in the territory of both Parties and in case that person would otherwise be subject to the legislation of both Parties for the same period, that person shall be subject only to the legislation of the Party in whose territory that person is ordinarily resident.
- 4) As regards compulsory coverage, subject to the provisions of paragraphs 1 and 2 of Article 5, where a person works as an employed person in the territory of one Party and as a self-employed person in the territory of the other Party and in case that person would otherwise be subject to the legislation of both Parties for the same period, that person shall be subject only to the legislation of the Party in whose territory that person is ordinarily resident.
- 5) A person who is receiving benefits under Japanese laws and regulations on account of sickness, injury or pregnancy for any period while that person is in Jersey or Guernsey, shall be excepted from liability to pay a contribution in respect of that period, other than as an employed or self-employed person, under the legislation of Jersey or Guernsey.

Article 5

- 1) As regards compulsory coverage, subject to the provisions of Articles 6 and 7, where a person who is insured under the legislation of one Party, and employed by an employer with a place of business in the territory of that Party, is sent by that employer, either from the territory of that Party, or from a third country, to work in the territory of the other Party, that person shall be subject only to the legislation of the former Party as if that person were working in the territory of that Party, provided that the period of such detachment is not expected to exceed five years.
- 2) As regards compulsory coverage, where a person insured under the legislation of one Party, who ordinarily works as a self-employed person in the territory of that Party, works only in the territory of the other Party, that person shall be subject only to the legislation of the former Party as if that person were working in the territory of that Party, provided that the period of the self-employment in the territory of the other Party is not expected to exceed five years.
- 3) Where, by virtue of the provisions of paragraph 1 or 2, a person works as an employed or self-employed person in the territory of one Party while remaining subject only to the legislation of the other Party, that person shall not be entitled to pay contributions voluntarily under the legislation of the former Party, unless such voluntary payments are made under the legislation of that former Party with respect to voluntary payment of contributions only by those aged sixty or over.
- 4) For the purposes of this Article, "insured" means,
 - (a) in relation to Japan, that, immediately before the commencement of the period of detachment or self-employment in the United Kingdom, contributions have been paid by, or in respect of, or are payable by, or in respect of, the person concerned, or exemption from liability for contributions has been granted to, or in respect of, the person concerned, and
 - (b) in relation to the United Kingdom, that, immediately before the commencement of the period of detachment or self-employment in Japan, contributions have been paid by, or in respect of,

End of Question

4. You are a tax manager in a firm of Chartered Tax Advisers. Your client, Gorman & Rajani LLP, is a large professional partnership, which commenced in business on 1 April 2018 and has a 31 March year-end. You have received the following email from Francis Lee, their Managing Partner.

To: Susan Smith
From: Francis Lee, Managing Partner – Gorman & Rajani LLP
Subject: Gorman & Rajani LLP – HMRC Review
Date: 16 October 2020

Hi Susan

I am hoping you can help!

We were recently contacted by HMRC who said that they wish to investigate whether the Salaried Member legislation applies to us. They indicated that this review will be based on our first year in business which ended on 31 March 2019.

In advance of HMRC's visit, I would be grateful if you would review the likelihood of HMRC challenging whether any of our partners will be considered salaried members and, if relevant, the potential liabilities arising to Gorman & Rajani LLP as a result.

To help you with your analysis, I would draw your attention to the following:

- 1) Gorman & Rajani LLP has 170 members split into three groups: Leadership, Divisional Heads and Junior Members (all individuals).
- 2) Under the LLP agreement, the members are required to delegate the running of the LLP to a board of management consisting of those LLP members in the Leadership group. The Leadership group is responsible for key decisions concerning the LLP's future direction, including acquisitions and disposals, budgeting and forecasting, investments, and future partner admissions.
- 3) The Divisional Heads have a high degree of autonomy over the running of their business lines, including marketing spend and new employee hires, subject to the overall guidelines and budgets laid down by the Leadership group.
- 4) All three groups receive a combination of drawings and discretionary profit allocations with the following total amounts paid to each group in the year to 31 March 2019:

<u>Group</u>	<u>Number of members</u>	<u>Drawings (total per group)</u> (£'000)	<u>Discretionary allocations (total per group)</u> (£'000)
Leadership	5	1,250	250
Divisional Heads	15	3,000	900
Junior Members	150	15,000	5,250

All members received at least £100,000.

- 5) Drawings are paid monthly in fixed equal instalments. Under the terms of the partnership agreement, members are not required to repay the sums once drawn.

Continued

4. Continuation

- 6) Discretionary allocations are reviewed annually and paid each year by 31 March. Junior Members received discretionary allocations of between 27% and 50% of their drawings based entirely on their personal performance. Leadership and Divisional Heads receive discretionary allocations based on profit share units which entitle them to a share of the profits of the partnership. Each profit share unit is allocated based on seniority of the member and personal/team performance. No member of either group received a discretionary profit allocation less than 30% of drawings.
- 7) All members are required to make a capital contribution equal to 10% of drawings.
- 8) All members are UK resident and domiciled and work in the UK. In addition, all have filed Self Assessment tax returns declaring the partnership profits and have paid Income Tax and Class 4 NIC for 2018/19.
- 9) We currently employ 500 support staff, who are all paid and subject to PAYE, Class 1 NIC and Apprenticeship Levy (our annual pay bill is more than £3 million) via a single PAYE reference.

I look forward to your response.

Kind regards

Francis

Requirement:

Write an email to Francis advising on any issues which may arise during HMRC's review and the extent of any costs relating to these issues. You are not required to comment on the penalty or interest position. (20)

5. You are Helena Trent, a payroll tax specialist in a small firm of accountants and tax advisers. You have received the email below from the Payroll Manager at one of your clients.

To: Helena Trent
From: Darren Goodge
Date: 1 November 2020
Subject: PAYE Coding for Gianluca

Hi Helena

I hope you are well. Could I ask you for some help with the issue below?

Gianluca is an Italian national who we took on under a local hire contract on 6 April 2020. He has received a number of PAYE coding notices since he joined us and he is unhappy about the level of his PAYE and NIC. I've copied below an extract of his email to me.

"...You told me that the PAYE amount was all about the "codes". You put me on a code of 1250L when I joined the company. This changed on my June payslip to 791L, which you said was probably because the car you gave me was included. It changed again on August's payslip to 90L M1 and again on October's to K309 M1. I am paying so much more PAYE now; it can't be right. Please put my code back to what it was in April.

I also do not understand why I am paying National Insurance. I have never paid this before. I have always paid in Italy. I still pay in Italy. I gave you a copy of my A1 certificate from before..."

To give you some background, Gianluca was on secondment to the UK with his previous employer. He didn't have a P45 when he joined us, so we did an expat starter checklist and he ticked box A "I intend to live in the UK for 183 days". Therefore, we gave him a code of 1250L and NI letter A. He's on a salary of £90,000 per year.

We sent off a P46 car at the end of April showing an annual P11D value of £4,590. The car was first provided on 15 April 2020.

Gianluca showed me his 2019/20 P11D, from his previous employer which he got in July. This showed a car worth £4,326 and a living accommodation benefit of £7,007. He told me he did his self-assessment tax return soon afterwards, which included the car, the living accommodation and also taxable travel costs of £2,133.

Could you advise us which is the correct code to operate for Gianluca? If we change it, how will it affect Gianluca's PAYE and will he get a refund?

Thanks

Darren

Requirement:

Write an email to Darren explaining the PAYE codes issued and the NI position, what corrections could be made and what difference it will make to the PAYE paid by Gianluca. (15)

6. You are Alex Smith, the employment tax specialist in an accountancy firm. Your colleague has asked you for assistance, having just had their annual catch up with Malcolm and Rachel Brown, directors of Tasty Wedge Ltd.

Malcolm and Rachel each own 50% of the shares in Tasty Wedge Ltd, which produces award winning specialist cheeses from its sole location in Devon and is highly profitable. The company was incorporated in 2005 and has no subsidiaries.

Many of the 20 current employees of Tasty Wedge Ltd have been with the business since the beginning and so Malcolm and Rachel regard it as a cooperative, even a family, rather than their business. All employees work full-time.

Malcolm and Rachel now want to travel the world together, as they have no children or other ties. They are keen to see the company continue to trade and thrive and would like to transfer their entire shareholding to these 20 employees.

Malcolm and Rachel need around £10,000 a month to fund their travels, but do not need a large lump sum on the transfer of the company so are happy for the consideration to be deferred and paid for out of future profits. The current full market value of the company is £1.5 million. They would be happy to sell the shares at a discount of 20% to the current full market value.

Malcolm and Rachel are keen that all existing employees can participate in owning the company, but know that some employees may have very little money. Therefore, they want to look at options that enable all employees to participate equally, if possible, and have been told that an Employee Ownership Trust may be appropriate, but they know very little about such things.

Requirement:

Write an email to Malcolm and Rachel explaining how they can achieve their aim of transferring the business to the existing employees. (15)