

# THE CHARTERED INSTITUTE OF TAXATION

## ADVANCED TECHNICAL

### Human Capital Taxes

**May 2021**

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TIME ALLOWED

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3 HOURS 30 MINUTES

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- 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.
- Except as set out below or indicated by additional information in the question, you may assume that 2020/21 legislation (including rates and allowances) continues to apply for 2021/22 and future years.

1) You **MUST** assume that the UK remains within the European Union.

2) You **MUST** ignore all temporary Covid related legislation including furlough, grants, loans and the reductions in VAT and SDLT rates.

Except in relation to points 1) and 2) above, 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. Hoora BV is a Dutch limited company, which manufactures hearing equipment in the Netherlands. It has recently purchased all of the shares of a UK company, Plasio Ltd, for £2.2 million. After the purchase of Plasio Ltd, Hoora BV is worth €38 million. It has fixed assets of €20.2 million and current assets of €500,000. Hoora BV employs 233 full-time staff and does not have any other subsidiaries.

Plasio Ltd was incorporated in the UK in 2018 and prior to its purchase by Hoora BV, it had two equal and otherwise unrelated shareholders: John Red and David Yellow. The company makes specialist hearing aids using 3D printing technology. It employs 12 full-time staff and three part-time staff, who each work for 25 hours per week. Hoora BV plans to continue to operate the company in the same way and accordingly all staff have been retained on the same terms. John and David are still directors and continue to work full-time as General Manager and Head of Design respectively.

Hoora BV plans to introduce a Dutch tax approved share scheme for six key employees, including John and David as they feel it is important to retain these two individuals. There are two possibilities under Dutch law:

- 1) The first scheme allows the company to award an employee free ordinary shares up to a set limit with no Dutch tax or social security due at the time of the award. If the employee leaves the company, the shares are forfeited and there are restrictions on the shares such that the employee cannot sell or otherwise dispose of them apart from in the circumstances described below:
  - (a) If the company is bought out within five years, the employee can either sell their shares to the purchaser or exchange their shares for shares in the purchasing company.
  - (b) If Hoora BV floats on the stock market within five years, the employee will exchange their shares for shares in the new public limited company.
  - (c) If Hoora BV is not purchased by a third party and does not undergo a flotation within the five-year period, the employee can sell the shares back to the company at their current market value or retain them in anticipation of a future purchase or flotation.
- 2) The second possible scheme is a share option scheme. Hoora BV could award options up to a set limit. The number of options would have to be calculated, but the value would be based on the current market value of Hoora BV shares. The options would vest after five years, although if the company is bought or floats on the stock exchange before then, the employees can exercise their options at that time. There are no Dutch tax charges on grant, vesting or exercise, only on the sale of the shares acquired.

The monetary value received by the employees would be expected to be similar under either scheme, perhaps in the region of €280,000 each.

In the Netherlands, any sale or deemed disposal under either scheme, would incur a Capital Gains Tax charge at 20% on the total current value but the gain can be deferred if there is an exchange of shares. As the shares are in a Dutch company, John and David would also be liable to this Dutch Capital Gains Tax charge under domestic Dutch law.

**Requirement:**

**Explain how the Dutch share schemes will be treated in the UK suggesting any amendments or alternatives which could improve the position. (20)**

**An exchange rate of €1.16 to £1 should be used.**

**An extract from the UK/Netherlands Double Tax Treaty is provided.**

Continued

1. Continuation

UK Netherlands Double Tax Treaty 2008

Article 13 Capital Gains

1. Gains derived by a resident of a Contracting State from the alienation of immovable property referred to in Article 6 of this Convention and situated in the other Contracting State may be taxed in that other State.
2. Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State, including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise) may be taxed in that other State.
3. Gains derived by a resident of a Contracting State from the alienation of ships or aircraft operated in international traffic or movable property pertaining to the operation of such ships or aircraft, shall be taxable only in that State.
4. Gains derived by a resident of a Contracting State from the alienation of shares, other than shares which are traded on a recognised stock exchange, or other comparable interests deriving more than 75 per cent of their value directly or indirectly from immovable property situated in the other Contracting State, other than immovable property in which that company or the holders of those interests carry on their business, may be taxed in that other Contracting State. However, such gains shall be taxable only in the first-mentioned State where:
  - a) the resident owned less than 50 per cent of the shares or other comparable interests prior to the first alienation;
  - b) the gains are derived in the course of a corporate reorganisation, amalgamation, division or similar transaction; or
  - c) the resident is a pension scheme, provided that the gains are not derived from the carrying on of a business, directly or indirectly, by that pension scheme.
5. Gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4 of this Article, shall be taxable only in the Contracting State of which the alienator is a resident.
6. Notwithstanding the provisions of paragraph 5 of this Article, a Contracting State may, in accordance with its laws, levy tax on gains derived by an individual who is a resident of the other Contracting State from the alienation or deemed alienation of shares or other rights in a company which, under the laws of the first-mentioned Contracting State, is a resident of that State, and from the alienation or deemed alienation of part of the rights attached to the said shares or other rights, if that individual, either alone or with other connected individuals according to the laws of that State, directly or indirectly holds at least 20 per cent of the issued capital of a particular class of shares in that company. This provision shall apply only if the individual who derives the gains has been a resident of the first-mentioned State at any time during the ten year period preceding the year in which the gains are derived and provided that, at the time he became a resident of the other Contracting State, the above-mentioned conditions regarding ownership in the said company were satisfied.

In cases where, under the laws of the first-mentioned State, an assessment has been issued to the individual in respect of the above-mentioned alienation deemed to have taken place at the time of his emigration from the first-mentioned State, the provisions of this paragraph shall apply only insofar as part of the assessment is still outstanding.
7. The provisions of paragraph 5 shall not affect the right of a Contracting State to levy according to its law a tax chargeable in respect of gains from the alienation of any property on a person who is, and has been at any time during the previous six fiscal years, a resident of that Contracting State or on a person who is a resident of that Contracting State at any time during the fiscal year in which the property is alienated.

**End of Question**

2. Plus Tard SARL is one of Europe's leading developers of nuclear power plants and has a branch in the UK (Plus Tard UK).

Plus Tard SARL has contracted with a UK utility company to build a new power plant for them at a cost of £50 million, in the North East of England, on land already owned by the utility company. The work involved will include site clearance and levelling, assembly of pre-fabricated units and systems installation (including electrics, water and sewage). The work will be carried out by the UK branch.

Due to a skills shortage and competing projects, Plus Tard UK needs to supplement its local UK employed workforce with UK agency workers to work as labourers. It also intends to bring additional workers to the UK from Romania who would come to the UK for a 200 day period, which falls in a single UK tax year. These workers will remain Romanian resident under domestic law and their families and main home would remain in Romania. They have previously worked for Plus Tard SARL on similar projects across Europe and have consequently built up knowledge of Plus Tard SARL's system and ways of working. Notwithstanding this, they will:

- 1) Work under the supervision, direction and control of Plus Tard UK employees.
- 2) Be paid on a day rate basis.
- 3) Not be required to remedy any mistakes in their own time.
- 4) Have no right of substitution and no right to refuse work.

Plus Tard SARL believes these individuals hold a special "freelance" tax status in Romania.

Finally, Plus Tard SARL will be engaging with a UK company, Briggs Plant Hire Ltd, for the hire of plant including scaffolding, bulldozers, boring machines and cranes together with associated labour.

**Requirement:**

**Explain the UK tax implications for Plus Tard UK of the contract with the utility company. You are NOT required to comment on Corporation Tax, VAT or social security. Extracts from the UK/Romania Double Tax Treaty are provided. (20)**

Continued

2. Continuation

Extracts from UK/Romania Double Tax Treaty

Article 3 General Definitions

1. In this Convention, unless the context otherwise requires:

(a) the term "United Kingdom" means Great Britain and Northern Ireland, including any area outside the territorial sea of the United Kingdom which in accordance with international law is or may hereafter be designated, under the laws of the United Kingdom concerning the Continental Shelf, as an area within which the rights of the United Kingdom with respect to the sea bed and sub-soil and their natural resources may be exercised;

(b) the term "Romania" means the territory of the Socialist Republic of Romania and the sea bed and sub-soil of the submarine areas beyond the territorial sea, over which Romania exercises sovereign rights, in accordance with international law and with its own law, for the purpose of exploration for and exploitation of the natural resources of such areas;

(c) the term "national" means: (i) in relation to the United Kingdom, any individual possessing the national status of citizen under the law of the United Kingdom by virtue of his connection with the United Kingdom and any legal person, association or other entity deriving its status as such from the law in force in the United Kingdom; (ii) in relation to the Socialist Republic of Romania, any individual having the citizenship of the Socialist Republic of Romania and any legal person or other entity created under the law in force in the Socialist Republic of Romania;

(d) the term "tax" means United Kingdom tax or Romanian tax, as the context requires;

(e) the terms "a Contracting State" and "the other Contracting State" mean the United Kingdom or Romania, as the context requires;

(f) the term "person" comprises an individual, a company and any other body of persons; (g) the term "company" means any body corporate, including a joint company (societate mixta) incorporated under Romanian law, or any entity which is treated as a body corporate for tax purposes;

(h) the terms "enterprise of a Contracting State" and "enterprise of the other Contracting State" mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State;

(i) the term "international traffic" means any transport by a ship or an aircraft or a railway or road vehicle operated by an enterprise which has its place of effective management in a Contracting State, except when such transport is made solely between places in the other Contracting State;

(j) the term "competent authority" means:

(i) in the case of the United Kingdom, the Commissioners of Inland Revenue or their authorised representative;  
(ii) in the case of Romania, the Minister of Finance or his authorised representative.

2. As regards the application of this Convention by a Contracting State any term not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that Contracting State relating to the taxes which are the subject of this Convention.

Continued

2. Continuation

Article 4 Fiscal Domicile

1. For the purposes of this Convention, the term "resident of a Contracting State" means, subject to the provisions of paragraphs 2 and 3 of this Article, any person who, under the law of that State, is liable to taxation there by reason of his domicile, residence, place of management or any other criterion of a similar nature. The terms "resident of the United Kingdom" and "resident of Romania" shall be construed accordingly.

2. Where by reason of the provisions of paragraph 1 of this Article an individual is a resident of both Contracting States, then his status shall be determined in accordance with the following rules:

(a) he shall be deemed to be a resident of the Contracting State in which he has a permanent home available to him. If he has a permanent home available to him in both Contracting States, he shall be deemed to be a resident of the Contracting State with which his personal and economic relations are closer (centre of vital interests);

(b) if the Contracting State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either Contracting State, he shall be deemed to be a resident of the Contracting State in which he has an habitual abode;

(c) if he has an habitual abode in both Contracting States or in neither of them, he shall be deemed to be a resident of the Contracting State of which he is a national (cetatean);

(d) if he is a national (cetatean) of both Contracting States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

3. Where by reason of the provisions of paragraph 1 of this Article a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident of the Contracting State in which its place of effective management is situated.

Article 16 Dependent Personal Services

1. Subject to the provisions of Articles 17, 19, 20, 21 and 22 salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1 of this Article, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:

(a) the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in the fiscal year concerned; and

(b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and

(c) the remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other State.

3. Notwithstanding the preceding provisions of this Article, remuneration in respect of an employment exercised aboard a ship, aircraft or railway or road vehicle in international traffic may be taxed in the Contracting State in which the place of effective management of the enterprise is situated.

**End of Question**

3. SSB Protect Inc is a US resident insurance broker with a representative office in the UK. The effect of this presence is that SSB Protect Inc has a place of business in the UK for PAYE purposes but is not liable to UK Corporation Tax on any part of its profits.

During the year ended 5 April 2021, the company had 150 employees (including directors) based in the UK. All are resident, domiciled and working in the UK and in the UK social security regime. Of these 150 employees, seven work in the Glasgow office and are Scottish taxpayers and the remainder live and work in London. The following tax rates apply to the employees:

- 1) 30 are basic rate taxpayers.
- 2) 68 are higher rate taxpayers.
- 3) 45 are additional rate taxpayers.
- 4) Seven are Scottish intermediate rate taxpayers.

During the year ended 5 April 2021, the following expenses and benefits were provided:

- 1) Employees were reimbursed for expenses incurred on client and supplier entertainment totalling £11,000 plus VAT.
- 2) £7,000 plus VAT was spent on working lunches. These lunches were attended by several of SSB Protect Inc's London based staff and held at restaurants close to its London office. The purpose of these meetings was to discuss business strategy.
- 3) Two annual functions were held:
  - (a) The Christmas party. All staff (except the seven employees in Glasgow) were invited to this event and it was attended by 80 employees including directors; of which 50% brought a spouse or family member as a guest. The total cost of the event (including any associated expense reimbursements) was £14,000 plus VAT.
  - (b) The Summer BBQ. This was an event held for all employees. 140 employees attended (no guests). The total cost of the event was £4,900 plus VAT.
- 4) Flowers for eight employees to celebrate the birth of a child; with each bouquet costing £50.
- 5) Christmas turkeys or hams for all employees with a total cost of £4,500.
- 6) Easter eggs for all employees with a total cost of £2,250.
- 7) Seasonal flu inoculations for all employees with a unit cost of £20.
- 8) Books of retail vouchers worth £50 each supplied as a prize to 12 "employee of the month" winners that tax year.

To the extent that any employment Income Tax or NIC liability arises in respect of the above, SSB Protect Inc intends to settle this via a PAYE Settlement Agreement.

**Requirement:**

- 1) **Explain the tax implications for the company of each of the benefits and expenses.**
- 2) **Prepare the calculation for the PAYE Settlement Agreement.**

(15)

4. Firesafex Ltd is a London based company, which installs and maintains fire extinguishers and fire safety equipment. The company has 119 employees, including 54 mobile engineers who carry out the installation and maintenance at customers' sites. Firesafex Ltd has a five-year bespoke agreement with HMRC for subsistence and laundry. The agreement was reached in April 2016 and provides for the following:

- 1) Bespoke subsistence rates of £7 for breakfast, £7 for lunch and £23 for evening meal.
- 2) A maximum of £25 per week for laundering uniforms.

Harry, one of the mobile engineers, is the project manager on a contract to install equipment in a series of new hotels in the North West of England. The contract started on 1 October 2020 and is due to take three years to complete. Harry is expected to work full-time at different hotel sites across the area for the life of the project. His parents live in the North West so he is staying with them from Sunday night to Thursday night. He then returns home to London on Friday afternoon.

It was agreed that Harry would receive a fixed monthly subsistence allowance of £801.66 for the duration of the contract, which has been calculated as £37 per day x 260 days (which is the standard number of workdays per annum for HR purposes) per year / 12 months = £801.66 starting in October 2020. This allowance has been paid directly into his bank account and has not been included in the payroll system. Firesafex Ltd advised Harry that the amount was tax and NIC free.

Harry's expense claims have included a new pair of steel toe capped boots and a high-visibility vest with a Firesafex logo and a plain high-visibility winter coat for use on the building site. He has also claimed for five new polo shirts, which have the company logo embroidered on the front.

Harry also made a claim for two laundry receipts of £12.50 each for the first two weeks of October. Since then he has included a claim for a cash amount of 20 weeks x £25 on his expenses claim without including any receipts.

He also claimed £1,210 in mileage (2,689 miles @ 45p/mile) from his parents' house to the various hotel locations. He uses his mother's car.

Finally, Harry booked his weekly return train fares from London to the North West totalling £2,046 through a travel agent. Firesafex Ltd has paid the travel agent's invoice for the travel costs directly.

Harry earns a gross salary of £65,000 per year.

**Requirement:**

**Explain the amounts and liabilities to be reported to HMRC for 2020/21 and any changes required for future years. (15)**

5. Hotel California Ltd is a UK company, owned by its four directors who each have a 25% shareholding. The company operates 20 hotels, some of which have properties in the grounds, plus a chalet complex in the Scottish Highlands.

#### Hotels

Each hotel has a security guard, a night porter and a general manager. They stay at their hotel between their rostered shifts to be on call. Rooms at each site, which were once available to customers, are set aside for individual staff.

#### Properties in Hotel Grounds

There is a cottage in the grounds of their Grand Union Canal hotel which is occupied by the company's lock keeper who earns £15,000 per year. The company purchased it for £2,500 in 1963. It is currently valued at £70,000. The company pays for electric, gas, council tax and water rates of £1,200, £1,600, £960 and £240 per year respectively.

There is a fully furnished house in the grounds of their Berkshire hotel, which has been occupied by the Managing Director, Donagh Henley, since 1 February 2013. Donagh receives a salary of £220,000 per annum. The house cost £400,000 in May 2012, was valued at £550,000 when Donagh moved in, and is now valued at £1,250,000. Since 1 February 2013, the company has spent £40,000 on repairing the property and £100,000 furnishing it. Its gross rating value is £12,000. The company has paid the electric, gas, council tax and water rates of £2,800, £3,200, £3,400 and £940 per year respectively.

#### Chalets

The chalet complex comprises 30 self-catering chalets, available to customers, plus three spare chalets. Over the peak skiing season (October - April) the company employs 12 chalet maids who stay in the three spare chalets because it would be difficult for them to find suitable accommodation elsewhere due to the remoteness of the complex. Their only duties are to clean the chalets between guest stays.

The 33 chalets were built in 2001 at a total combined cost of £297,000 including fixtures and fittings. Their gross rating value is £500 each. The chalet maids pay for the running costs themselves.

All of the above are Hotel California Ltd employees. They are paid monthly via payroll, with Income Tax, National Insurance and pension deductions.

#### **Requirement:**

**Explain the relevant Income Tax and National Insurance rules and quantify any annual taxable values. (20)**

6. TOut Call Services Ltd, operates a call centre in Norwich.

It provides free private medical insurance for all employees and arranges for the local GP to undertake check-ups and administer flu jabs to all employees. It also provides every employee who is required to use a computer screen with a voucher for an eye test every two years, at the local opticians. Whilst the private medical cover is reported on P11Ds and form P11D(b), no reporting is done in respect of the GP check-ups, flu jabs or the eye tests.

It is considering a contribution towards spectacles as well as installing a pool or table tennis table in the staff canteen for all employees to use.

There is one employee who had tripped on some loose carpet in the office and fell down some stairs, badly injuring her left leg and right arm. The employee has received £3,000 of private treatment under the private medical insurance. However, she has also requested that the company pays for some specialist treatment that her doctor has suggested, which is not covered by the private medical insurance.

**Requirement:**

**Explain the reporting, tax and NIC treatment of the existing and proposed benefits. (10)**