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Application and Interaction

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Date of Examination

Tick box if you have answered in accordance with Scots Law

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Instructions

Your script will be scanned electronically. Failure to comply with these instructions may lead to your paper not being marked. You must:

- Complete the details on this page and on the answer pages using BLACK or BLUE ballpoint pen only.
- Write on one side of the page.
- Not write in the margin areas indicated.
- If you have used additional pages, please add your candidate number and the question number to these pages.
- Do not put blank pages into the envelope at the end of the exam.

Please do all of the above before the end of the examination.

| | Tick question attempted | For use by examiner only |
|---|-------------------------|--------------------------|
| 1 | | |
| 2 | | |
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| 4 | ✓ | |
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| FORMAT & STYLE OF ANSWER | MAXIMUM MARKS | MARKS AWARDED |
|---|---------------|---------------|
| <p>The answer is set out in the format demanded. Thus, if it is a letter, it will be properly set out as a letter with addresses, date, "Dear X" and conclude "Yours sincerely" etc. If it is a report, it will give some indication as to what it is about and who it is for.</p> | 1 | |
| <p>The report or letter should contain an introduction setting out the terms of reference, information being relied on etc. It should also contain a summary of the key findings and recommendations.</p> | 2 | |
| <p>The body of the letter or report should be laid out in a clear way with appropriate headings so that the reader can navigate around it easily and spot the key areas without reading the entire document to try to find a discussion of, for example, income tax on some employment related shares.</p> | 1 | |
| <p>The answer "flows" so that a logical chain of thought presented to the reader rather than a series of random comments (which may nevertheless be technically correct).</p> | 1 | |
| <p>The style of writing should be appropriate to what is being produced. For example, a report to a client or lay person (which will always be the main element of a question) should not contain large numbers of legislative references whereas a technical note to the tax partner should. Technical advice should be conveyed in style appropriate to the reader.</p> | 2 | |
| <p>RELEVANCE OF ANSWER</p> | | |
| <p>The answer does not contain large amounts of irrelevant material which would only serve to confuse a client.</p> | 2 | |
| <p>Technical knowledge (which will be rewarded through the technical marks and should not affect the awarding of these marks) has been directly applied to the specific circumstances of the reader and has this resulted in an answer tailored to their circumstances.</p> | 3 | |
| <p>The question(s) posed has/have been answered.</p> | 2 | |
| <p>PROVISION OF ADVICE</p> | | |
| <p>The report gives advice. This means that where possible it should come off the fence and suggest the best option rather than simply giving a list of unweighted possibilities which fail to give the client an answer to their real problem: what should I do?</p> | 4 | |
| <p>Advice should include relevant and appropriate planning for the future.</p> | 2 | |
| <p>Advice should be commercial. This means that candidates should consider the bigger picture rather than narrowly focussing on saving tax.</p> | 2 | |
| <p>TOTAL HIGHER SKILLS AND PRESENTATIONAL MARKS</p> | 22 | |

1) REPORT

To: Karen Jackson

From: Charles Dunn

Date: 8 November 2017

~~Subject~~

This report has been prepared in response to your (Karen Jackson) queries in the recent meeting with me (Charles Dunn) in relation to Fresh Air Ltd's reporting requirements in the UK.

The report is split into 3 sections, as follows:

- Section 1 ~~A~~ - Jennifer Green
- Section 2 ~~B~~ - Inbounds from Air Frais SAEL
- Section 3 - The launch event

Once you have had a chance to digest the information provided, we would be happy to set up a meeting to discuss this further.

Executive Summary

- Jennifer Green should remain subject to UK national insurance, in order to do so the company will need to apply for a portable document A1 to keep her within UK scope, please refer to section 1, part b for further information.
- A disclosure should be made to HMRC in respect of Jennifer Green as there is undeclared PAYE of approximately £20,000 relating to the travel and accommodation allowance she received.
- The apartment should be rented and arranged for by the company to reduce the NIC liability.
- Further detail is needed on the nature of the UK duties of the individuals coming from France, we would suggest for now a short term business visitor agreement is put in place.
- The launch event could create a taxable benefit for the individuals, we recommend a PAYE settlement agreement is put in place.

Section 1 - Jennifer Green.

We understand that Jennifer has been working in France and other European countries over an ~~increased~~ increasing amount of time in recent years. The first section of this report is designed to cover the ~~impact~~ income tax and national insurance implications of her working pattern.

a) Residence and domicile.

In order to assess Jennifer's liability to UK income tax, we first need to consider UK residence and domicile position.

Domicile relates to her long term intentions, on the basis that she usually resides in the UK and her home and family are in the UK, I will assume she is UK domiciled.

Jennifer is working outside the UK for 2-3 days per week, assuming she spends

the other 4-5 days in the UK, she would spend a minimum of 208 days in the UK. Therefore Jennifer would be automatically resident on the basis that she spends more than 183 days in the UK. If she doesn't meet this test, she would be resident under sufficient ties or her family and home are in the UK. AS a UK resident and domicile, Jennifer will remain UK taxable on her worldwide income and gains as they arise. All of her earnings should remain subject to ^{income tax} PAYE. ~~PAYE~~ via PAYE.

b) UK Social Security Position

Jennifer is spending some time working overseas, therefore ~~your French colleague~~ we do need to consider her position in relation to social security.

AS Jennifer is working ~~in several~~ across multiple EU states the EU regulations apply.

The EU regulations mean that a person

social security
 can't be liable to pay in more than one EU state at any one time.

Therefore, a person who pursues an activity as an employed person in two or more member states shall be subject to social security in:

- The member state of residence if they pursue a substantial part of their activity in that member state, or
- The member state in which their registered office of their employer is based if ^{they} do not meet the first conditions.

As Jennifer will remain UK resident and will still be working at least 40% of her time in the UK, this will count as a substantial part of her time. Therefore, Jennifer can remain within the UK social security rules.

As portable document A1 should be applied

for in the UK to keep her within the scope of UK ~~social~~ national insurance and outside the scope of French social security.

This should be applied for retrospectively to cover the period from which she started ~~contributing to French~~ working in France.

In addition, if Jennifer is spending more than 5% of her time in other EU States a multistate A1 can be applied for to cover each country. I note you mention she is working on expedition into other European countries.

Jennifer will therefore remain subject to UK tax and national insurance in full whilst she is working in France.

Collection of tax and NIC should ~~be~~ continue to be collected under ~~RTI~~ or real time information on a monthly basis.

c) Foreign Taxes Due

AS a result of Jennifer's ^{French} ~~UK~~ workdays, it is likely that taxes will be due in France.

It may be possible for France to exempt the income under the treaty, but we would need to refer you to French advisors for this advice. For the purposes of this report we will assume that France are taxing income relating to duties in France.

AS ~~£~~ Jennifer will remain resident in the UK, the UK will ~~also~~ retain the right to tax her income in full. Therefore with France taxing her French workdays, there will be the possibility that some of this income is being taxed twice.

Where there is double taxation, a credit can be claimed on Jennifer's UK tax return for the French taxes paid. ~~£~~ AS the French tax rate has ~~also~~ been confirmed at a

top rate of 20% whilst the UK will be a top rate of 40%. So for Jennifer, given her income levels then full relief should be available. This is because relief for foreign taxes is equal to the lower of the UK taxes paid on that income and the French tax paid on the same income. If this is a lower rate therefore the full credit would be available.

Normally, a tax credit is claimed via the tax return which can create cash flow issues for the individual as they have to wait in order to receive this. One option available would be to appreciate that your current idea is to ~~fill the~~ ~~gap~~ bridge this gap for Jennifer by means of a loan but this could create additional charges that I will come on to later.

The option to reduce the cash flow issues would be to set up what is called a 'net of foreign tax credit' scheme via payroll.

This means that the tax is calculated each month, after relief for foreign taxes, therefore reducing the cash flow burden on Jennifer.

This can be quite complicated so ~~that~~ we would happy to assist with this should you wish for us to do so.

d) Travel, Accommodation and Expenses.

Jennifer will be working in France for a period of 3 years for 2 to 3 days per week, this will mean that ^{the French office} ~~France~~ is a permanent workplace for her. A permanent workplace is one where you expect to work for longer than 24 months and more than 40% of your time.

The impact of a permanent workplace is that any ~~travel~~ commuting costs, accommodation and subsistence paid for by the employer will be taxable

in full for Jennifer. whereas, if ~~it~~ it was a temporary workplace these costs could be exempt. This might be a point to consider ~~who~~ if you send ~~it~~ manuals on assignment in future.

In terms of the historic position for Jennifer from January 2017, as a cash allowance was paid to ~~Jennie~~ Jennifer this should have been taxed in full and subject to class 1 NIC, ~~and should~~ The £4,000 a month should have been reported on the FPS on or before the date of payment and the tax and NIC paid by the normal payment dates of 19/22 following the month.

It is not too late to pay the correct tax and NIC on this amount for ~~November~~ October 2017. I would suggest a further FPS submitted and the amounts are paid.

In terms of the period from January 2017

10 September 2017, I would suggest a disclosure is made to HMRC to report the error.

I have calculated an estimate of the penalties in Appendix 1. Interest would run from the due dates of payment.

The minimum penalties for late PAYE and NIC are £2,007, HMRC can levy additional penalties for careless errors. These can be up to 30% of tax and NIC due but will be reduced for an unprompted disclosure.

The total tax, class primary and secondary NIC due is £20,088.

An earlier year update can be made to correct 2016/17. Whilst an in year update to the FPS can be completed for 2017/18.

To the extent that you do not wish

for Jennifer to suffer the tax personally then the tax would need to be recalculated on a grossed up basis.

Looking for some of the expenses that this allowance was paid to cover may be deductible for tax purposes via Jennifer's self-assessment tax return. This would include flights to work overseas, as regardless of the length of the assignment, where:

- an employee is absent from the UK wholly and exclusively for the purposes of performing duties of employment.

- The duties can only be performed outside the UK

- The journey starts in the UK and returns to the UK.

Therefore, as Jennifer would meet these conditions and a deduction can be claimed on her tax return for the flights. It is important that receipts

are kept as records. This will have no impact for NIC purposes.

In addition, where her expenses include client entertaining a deduction can be taken for this provided it is not in relation to an allowable deduction for corporation tax purposes.

Looking forwards to the new package, I have a few comments on the taxation.

The flights ~~are~~ will be deductible as explained previously, therefore there are no reporting requirements required in respect of these expenses. I & recommend you keep all records in case of an enquiry from HMRC.

The accommodation provided to Jennifer will be a taxable benefit. However, it is ~~important that~~ it is provided will have no impact for national insurance purposes.

If Jennifer rents it and the company reimburses her, this will be a Class 1 national insurance liability. This means Jennifer will have to pay the NIC on the amount.

If the Jennifer arranges the accommodation and the Freshair directly pay it, this will still be a benefit for Class 1 NIC.

However, if the company arrange and pay for it then it will not be reportable via PAYE but just on her P112. It will then only be subject to Class 4 & 2 IA national insurance by the employee.

Class 1A national insurance is payable at 13.8%, the amount is calculated via the P11D(b) which needs to be submitted by 6 July following the tax year and the NIC paid by 22nd July. This gives an extension compared to paying via PAYE and means Jennifer won't have

any additional costs as a result.

✘ Paying for tax return support creates an additional taxable benefit, this amount should be reported on the P11D with ~~the~~ period class 1A NIC due on the amount. The VAT inclusive amount should be reported.

~~In addition, where additional to~~

e) Taxes paid by the employer

The fact that ~~the~~ Fresh Air Ltd will pay the additional taxes due on Jennifer's travel and accommodation costs means that the tax should be grossed up.

For example, for the accommodation, assuming £1,000 per month, this would create an additional cost for the company of:

$$12,000 \times 100/60 = £20,000$$

$$\text{Tax} = \del{£8,000} \quad £20,000 \times 40\% = £8,000.$$

Where tax is paid on behalf of an individual, the tax becomes a benefit. This creates a circular calculation which is what the gross up does. This is an additional cost to consider when covering the taxes. The tax will also be a benefit for Class 1A National Insurance.

f) Loan Benefit

Where a loan is provided to a director this can be a taxable benefit if it is interest free or exceeds £10,000.

Where this is the case the average amount is charged at the official rate of interest (3%) and taxed as a benefit on the individual's P11D. This amount will also be subject to Class 1A National Insurance by the company.

In addition where a close company makes a loan to a director who is working full time for the company then a charge

will occur to the company if the loan exceeds £5,000. This charge would be at $\approx 32.5\%$. It can be recovered where the loan is repaid, but is payable with the corporate tax return.

This is why a net of credit ~~the~~ scheme might be a preferable option to avoid the additional charges.

Section 2 - Air Fris S&L Staff

In general where an individual comes to the UK and there is a UK company ~~the~~ UK tax presence then the DAVE should be operated immediately.

However, there are exemptions available where the work performed is:

- incidental in nature
- There is a treaty exemption available.

For work to be incidental this could be training or reporting. It is unclear what the French employees were doing in the UK to determine whether those days are incidental or substantive.

If the days are incidental then there are no reporting requirements.

However, if they are substantive then we would consider the position under the UK/France ~~DB~~ Double taxation agreement.

The individuals income could be exempt under the treaty if:

- they are present for fewer than 183 days
- They are paid by an overseas employer
- The costs are not recharged to the UK.

From the information provided I would suggest that ~~they~~ the individuals in question would meet these conditions. However, treaty relief is not automatically available for PAYE and should first be ~~considered~~ reported for PAYE then ~~added~~ the exemption can be claimed via the tax return.

a) STBV Reporting

It is possible to reclaim PAYE via the
for individuals that are treaty exempt
if the company apply for ~~an~~ an
& STBV agreement with HMRC.

They are eligible if:

- Individuals are working in the UK from treaty countries with a competent employment income article
- Individuals a present for fewer than 183 days
- They are working for a UK branch of an overseas company
- They are not economically employed in the UK

They in addition if present for more than 60 days then need confirmation that costs are not recharged.

Under this scheme a report needs to be submitted to HMRC by 31 May

following the tax year. The information to be provided will depend on the number of days in the UK.

where the individuals are present for fewer than 30 days then HMRC will need just the names of the individuals.

The issue in this case would depend on the corporate structure, if the French Company becomes a branch of the UK then the treaty exemption will not apply. We need to consider this in further detail.

At this stage I would suggest you apply for an STBR report as it is likely that members of the French team might come to the UK on a regular basis.

it is important to track all visitors to

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UK in case HMRC ever enquire. It's good to ensure you are fully compliant.

~~HMRC~~ Tracking can be done via electronic passes, sign in books and other methods.

If no exemption applies then the individuals will be taxable immediately.

FOR EXAMINER
USE ONLY

Section 3 - Launch Event

In relation to the launch event you are due to have, I wanted to raise the issue of the costs you will incur.

As you may know, there is an annual limit of £150 per head for entertaining events. Any excess of this would be a taxable benefit for the individuals involved.

The way the limit works is that if you exceed the limit at an event the whole amount is taxable, you wouldn't just deduct the £150.

In respect to your two events, the dinner exceeds £150 per head. However

when budgeting I would suggest you consider reducing this to under £150 and then this could be your fully

exempt event.

The lunch would then be taxable but this works out as approximately £30 per head.

Cost for entertaining staff can be deemed impracticable to tax the individual or. Where this is the case, there is ~~some~~ a report called a PAYE settlement agreement. This can be used to pay the tax on costs that are minor, irregular or impracticable to collect the tax on.

Where the tax is paid by these means it has to be paid on grossed up basis

This means you work out whether the individuals are basic, higher or additional rate taxpayers and gross up on that basis.

Where the individual is a basic rate

taxpayer the amount is multiplied by $\frac{20}{80}$, then higher is $\frac{40}{60}$ and additional $\frac{45}{55}$. This gives the tax due.

Class 1B national insurance is then due at 13.8% on the value of the benefit plus the tax.

The PAYE settlement agreement must be agreed in advance of the event and then submitted by ~~the~~ 6 October following the tax year and the tax and Class 1B national insurance is then due by 22nd October.

This can be a really useful method of picking up extra costs to remain compliant. Should you need any help in applying please let us know.

Appendix 1

Travel and accommodation = £4,000

Tax and NIC each month:

$$\text{Tax: } 4,000 @ 40\% = 1,600$$

$$\text{Class 1 primary NIC: } 4,000 @ 2\% = 80$$

$$\text{Class 1 secondary NIC: } 4,000 @ 13.8\% = \underline{552}$$

2,232

January 2017 - default one = no penalty

$$\text{February 2017} \rightarrow 1\% = 1\% \times 2,232 = 223$$

$$\text{March 2017} \rightarrow 1\% = 1\% \times 2,232 = 223$$

April 2017 \rightarrow no penalty

$$\text{May 2017} \rightarrow 1\% = 223$$

$$\text{June 2017} \rightarrow 1\% = 223$$

$$\text{July 2017} \rightarrow 1\% = 223$$

$$\text{August 2017} \rightarrow 2\% = 446$$

$$\text{September 2017} \rightarrow 2\% = 446$$

2,007

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2) TO: Charles Dunn
 FROM: Ann Brown
 DATE: 18 November 2017
 SUBJECT: RE: Fresh Air Ltd.

Hi Charles

I have been working on the report for you which details the income tax and national insurance implications of the issues raised. I wanted to separately address some ethical and other tax issues that I believe are relevant.

In terms of taking on ~~at~~ Fresh Air Ltd, we need to check the terms of our ~~at~~ engagement letter. Consideration should be given to whether Fresh Air Ltd ~~owned~~ owned Air Fris ~~SAEL~~ when we undertook all of our risk procedures. If not we need to ~~do~~ complete again, to check we are covered for any work provided to the trench. If Fresh Air Ltd have the power to bind

Air & Francis SPRL then we may not need an additional engagement letter. However, it seems from the exchange of emails that the report will be shared with France.

If this is the case then we could consider an additional engagement letter with Air Francis SPRL. Either way if this happens then we need to consider meeting the client.

For now, we should caveat that our advice only covers the Fresh Air Ltd and if they wish to share it then the advice can't be relied upon. Just to cover any notes at this stage.

In addition I have found some errors in the work that has been done by Fresh Air Ltd, they seem to have had a fairly relaxed attitude to compliance in the past. I have suggested that we assist with a disclosure in respect of the errors.

If they don't act on this then we may need to cease to act for them. We would need to advise them of this in writing, notify HMRC that we are ceasing to act but not of the reason and then inform any future advisors of this fact. Hopefully this will not be the case!

As they have seemed fairly relaxed, it ~~is~~ may be worth suggesting a full review of ~~their~~ ^{their} processes at this stage before they expand any further. This might be a conversation to have once they have reviewed the report as I don't want to overwhelm them at this stage.

From a corporation tax perspective as they now own the French company this could create transfer pricing issues when they are transferring goods and resources between each other. At this stage they are sending a director to work onsite so they should be recharging the costs

to the French company.

where they are providing ~~the~~ providing UK entertainment for ~~overseas staff~~ French staff they need to consider any transfer pricing implications as they don't seem to be charging the French company for this. Transfer pricing.

~~From a VAT perspective they do not create a VAT group etc~~

They should have submitted a stamp duty return on acquisition of the French shares. This would have been at 0.5% of the value and a return should have been submitted within 30 days. Penalties can apply for failure to do so.

As the company is close company, I have mentioned in the report that if they lend more £100k to a participant they could be subject to a s.455 charge. The amount they loan needs to be

considered carefully. A close company is when the company is run by 5 or few participators or directors, this is the case for Fresh Air Ltd as they only have 4 directors.

~~On purchase of an overseas company they could still be~~

~~UK~~ It seems as though they are relying on the French HR team rather than seeking a French tax advisor, I would therefore like to verify any French advice they receive as some of our advice may need to rely on this. This could create a risk.

The VAT paid ^{and the cost per} ~~entertainment~~ for the launch event will need to be considered. The costs for entertaining staff will be deductible, however the overseas employees are not staff. Therefore these costs are not allowed. In addition the VAT on staff entertaining can be recovered. Where the individuals are

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not staff, this can't be deducted.

~~A corporation tax could be credit~~

~~it may be possible to~~

let me know if you need anything
else.

Thank you

Ann.

FOR EXAMINER
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PLAN

REPORT TO KAREN JACKSON (FINANCE DIRECTOR)
FROM CHARLES ~~DONE~~ DUNN.

INTRO: purpose, income tax and NIC
implications of expansion

Executive summary

Section 1 - Jennifer Green

- a) residence + domicile - UK res, have stated that NR in France. (we have French advice)
- ≠ b) Treaty residence → can France exempt under the treaty.
- b) UK taxation - worldwide income and gains
- d) Foreign tax credit for double taxation
- e) workplace - temporary v. permanent
- f) Travel + expenses (future)
- directly paid → ~~no relief~~ class 1A
 - reimbursed → class 1
 - arranged by → class 1
 - flights → exempt for overseas travel

PLAN.

g) TRAVEL + expenses (historic)

- Cash allowance - taxable via PAYE

- interest and penalties.

- flights if receipts could be deducted.

~~h) Taxes reimbursed - gross up~~

h) NIC position → Appendix 7B.

i) Taxes reimbursed - gross up

Taxes paid - earnings for class 1 NIC.

Taxes loaned - taxable benefit plus 5.45%

↓ Other expenses paid to consider → ^{charge} for co.

entertaining would be deductible

tax return prep fee.

Net of credit scheme → claim FIC via payroll.

SECTION 2 - Air Force SARL Staff.

a) PAYE obligations - general

- incidental

- treaty relief.

b) STBR scheme set up in advance for future.

Corporation Tax: CT group → consider PLAN
group relief? If loss
making co...

Transfer pricing? costs not charged to
baseco co for staff stuff.

S.455 charge

VAT: Acquisition of French co. VAT group?

PLAN

c) If can't treaty exempt then taxable ✓

Section 3:

Event → will exceed the exemption amount for staff entertaining ✓

Can either reduce the costs to under the £150 per head allowance.

Include on PSA → Dinner is £153 per head so try and get that one down and then exempt that and tax the lunch
 → Gross up 20/80 40/60 45/55

EMAIL TO SENIOR MANAGER

Ethics: ~~the~~ takeover of new client? French Company. Are they included for the EL purposes? Do we need a fresh EL.

→ IS O/S/CS CO relying on our advice.

→ should understand who we are billing.

DISCLOSURE: will they act on it? What is attitude to tax? If not, advise them of implications and consider ceasing to act.