

THE CHARTERED INSTITUTE OF TAXATION

APPLICATION AND PROFESSIONAL SKILLS

Human Capital Taxes

November 2022

TIME ALLOWED

3 HOURS 30 MINUTES

- In order to secure a pass in this exam, you will be required to demonstrate competence in each of three skills.

You will be assessed across your answer as a whole for Structure. A pass or fail grade will be awarded.

You will be assessed for competence in a number of broad topics for the following skills:

- Identification and Application
- Relevant Advice and Substantiated Conclusions

For each topic for each of these two skills, a grade will be awarded. The grades for those topics will be weighted and averaged to produce a final grade for each skill of 0, 1, 2, 3 or 4. A grade of 3 or 4 is required to demonstrate competence.

- 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 in the question, you may assume that 2021/22 legislation (including rates and allowances) continues to apply for 2022/23 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.

You are a tax manager in AZA LLP, a firm of Chartered Tax Advisers. Your manager, Jasmin Patil, has received an email (**EXHIBIT A**) from Claire Swan, Head of Tax, at your client RDJ Pharmaceuticals UK Ltd.

RDJ Pharmaceuticals UK Ltd specialises in the research and development of vaccines for rare diseases. It is a wholly owned subsidiary of RDJ Pharmaceuticals Inc, a US company.

Claire Swan has received a standard letter from HMRC enquiring about the implementation of the off-payroll working rules. Claire would like to know what impact it may have for the company, how she should respond to it and has requested recommendations on how to proceed going forward.

Jasmin has asked you to prepare a draft report to RDJ Pharmaceuticals UK Ltd.

The following exhibits are provided to assist you:

EXHIBIT A: Email from Claire Swan

EXHIBIT B: Email from Peter Wong

EXHIBIT C: Output from HMRC's Check of Employment Status Tool (CEST) for Peter Wong

EXHIBIT D: Pre-seen information

Requirement:

Prepare a draft report to Claire Swan, for review by Jasmin Patil recommending any actions RDJ Pharmaceuticals UK Ltd should take following receipt of the letter from HMRC.

Continued

EXHIBIT A

Email from Claire Swan

From: Claire.Swan@RDJ.co.uk
To: Jasmin.Patil@AZALLP.co.uk
Date: 29 October 2022
Subject: HMRC review into off-payroll working

Dear Jasmin

We have just received what seems to be a standard letter from HMRC saying that if we have contractors we should have been applying the off-payroll working rules since April 2021. HMRC has asked us to provide the information about our contractors including any 'status determination statements' by 15 January 2023.

We use a number of contractors / self-employed individuals who provide services to us from time to time, but we have not previously considered the off-payroll working rules as we thought the rules did not apply to us. Having looked at the information leaflet HMRC provided, we are particularly worried about one of our consultants Peter Wong. In fact, as suggested, we used HMRC's Check of Employment Status tool (**EXHIBIT C**) which provided us with the outcome that Peter's employment status for tax purposes is undetermined. We have attached the inputs we used, perhaps you could review. Please let us know any key areas of concern, how we should respond and identify any potential exposure in the worst case scenario.

Peter initially commenced work with us as a part-time consultant from 1 May 2019 under an engagement between his company (Peter Wong Services Ltd) and us. He has great connections with leading research institutions and this is incredibly useful for prioritising and accelerating our pipeline. We understand Peter's company was providing services to other organisations at that time. However, we have ramped up our activities on our own pipeline over the last 18 months and Peter started to increase his time commitment to us from early April 2021 under the same terms but at an increased daily rate.

He works from home most of the time, but the nature of his work does mean he needs to come into the lab from time to time as well as attend meetings with research institutions and regulatory bodies. He has the use of a company laptop and email; this is purely for security and confidentiality in accordance with our policies.

Recently our Head of Research and Development, Jane Brown, has been taken ill and could be off work for an extended period. We have been in discussions with RDJ Pharmaceuticals Inc about seconding someone from the US to cover Jane's duties but this may be impractical in the near term due to the time it will take to get a work permit. We need to see if Peter can cover some of her duties including managerial responsibilities and reporting directly to the board. This change would take effect from November 2022. If Peter was to take on these extra responsibilities we would see this as a permanent change as we are expanding and would still need extra resource at this level when Jane returns.

Does this change anything for us and, if so what are our options and your recommendations going forwards?

One consideration is that we would like to award share options to Peter personally under the proposed new share plan.

Peter's company has been invoicing us £12,500 per month (net of VAT), since January 2022. Prior to this in the 2021/22 tax year, he invoiced us the following amounts (net of VAT):

	£
April 2021	4,500
May 2021	5,000
June 2021	7,500
July 2021	8,000
August 2021	8,500
September 2021	10,000
October 2021	10,000
November 2021	11,000
December 2021	12,000

I have informed Peter and he has provided us with some more detail (attached) about tax payments he and his company have made (**EXHIBIT B**).

I look forward to hearing from you.

With kind regards

Claire

Continued

EXHIBIT BEmail from Peter Wong

From: Peter.Wong@RDJ.co.uk
 To: Claire.Swan@RDJ.co.uk
 Date: 3 November 2022
 Subject: HMRC letter

Dear Claire

Thank you for your note and I am so sorry to hear about Jane.

First of all, I am quite surprised that you are writing to me about tax changes that came into force over 18 months ago and hope HMRC will be reasonable. I trust this will not impact my or my company's cash-flow. My company initially entered into a consultancy arrangement to provide services with the expectation for me to commit a couple of days a week and I have always invoiced at the agreed daily rate.

I will happily cover for Jane and it would be good to discuss these arrangements. I really like working with the team and I think I can help support them with their development going forward. My commitment to RDJ Pharmaceuticals UK Ltd has increased over the last year or so and I have declined a number of opportunities with other clients in that time. If I do take on the extra duties RDJ Pharmaceuticals UK Ltd will be my only client and I will not be able to take on other work outside the organisation.

As requested, below are some details about my company. They are quite simple. I wholly own my consulting company, Peter Wong Services Ltd. My company has paid me a salary of £2,000 per month since May 2019 and dividends of £17,500 per quarter since April 2021. This is the only income I reported on my tax return for 2021/22. My accountant files my company's PAYE, Corporation Tax, VAT and personal tax returns and has provided the following:

	<u>Year Ended 30 April 2021</u>	<u>Year Ended 30 April 2022</u>
	£	£
Turnover	90,000	135,000
Expenses:		
Director's Remuneration including Employer NICs	26,098	26,092
Costs of travel to RDJ Pharmaceuticals UK Ltd (no travel to other clients)	750	1,200
Insurance	1,000	1,000
Stationary, printing costs and telephone costs (exclusively for RDJ work)	2,800	2,800
Profit before Corporation Tax	59,352	103,908
Corporation Tax	11,277	19,743
Dividends paid	44,000	70,000
Retained profits	4,075	14,165

I recently filed my company's accounts and Company Tax Return for the year to 30 April 2022 and my Self-Assessment Return for 2021/22 so I am up to date with all my tax returns. My accountant tells me I need to make a payment of around £17,000 on 31 January 2023 which consists of my remaining liability for 2021/22 and first payment on account for 2022/23. I have also made payments on account of £7,150 for 2021/22. My company needs to pay the Corporation Tax for the year to 30 April 2022 by 31 January 2023. Please let me know what you conclude from your review and what this means for my company and myself.

As you know, I like the flexibility of working through my own company but I am open to a discussion on reviewing any arrangements. I am also in the process of reviewing my company's insurance and if I take on the amended role from this month this will no longer be needed. I would also stop advertising for additional work and stop maintaining my own specialised equipment. I am hoping my costs will reduce going forward.

Lastly, thank the team for the invite to the Christmas party, I will of course be there. It will be great to be able to finally attend one of these events as I have heard a lot about previous years' functions.

Best wishes

Peter

Continued

EXHIBIT COutput from HMRC's Check of Employment Status Tool (CEST) for Peter WongQuestions and Answers provided

What do you want to find out?	If the off-payroll working rules (IR35) apply to a contract
Who are you?	Hirer
Does the worker provide their services through a limited company, partnership or unincorporated association?	Yes
Has the worker already started working for your organisation?	Yes
Will the worker be an 'Office Holder'?	No
Has the worker ever sent a substitute to do this work?	No, it has not happened
Do you have the right to reject a substitute?	Yes
Has the worker paid another person to do a significant amount of this work?	No
Does your organisation have the right to move the worker from the task they originally agreed to do?	No, they would have to agree
Does your organisation have the right to decide how the work is done?	Not relevant, it is highly skilled work
Does your organisation have the right to decide the worker's working hours?	No, the work is based upon agreed deadlines
Does your organisation have the right to decide where the worker does the work?	No, some work has to be done in an agreed location and some can be the worker's choice
Will the worker have to buy equipment before your organisation pays them?	No
Will the worker have to fund any vehicle costs before your organisation pays them?	No
Will the worker have to buy materials before your organisation pays them?	No
Will the worker have to fund any other costs before your organisation pays them?	No
How will the worker be paid for this work?	An hourly, daily or weekly rate
If your organisation was not happy with the work, would the worker have to put it right?	Yes, unpaid but their only cost would be losing the opportunity to do other work
Will you provide the worker with paid-for corporate benefits?	No
Will the worker have any management responsibilities for your organisation?	No
How would the worker introduce themselves to your consumers or suppliers?	They are an independent worker acting on your behalf
Does this contract stop the worker from doing similar work for other organisations?	No
Is the worker required to ask permission to work for other organisations?	No
Are there any ownership rights relating to this contract?	Yes
Does the contract state the rights to this work belong to your organisation?	Yes
Has the worker had a previous contract with your organisation?	No
Is the current contract the first in a series of contracts agreed with your organisation?	No
Does the current contract allow for it to be extended?	Yes
Will this work take up the majority of the worker's available working time?	Yes
Has the worker done any self-employed work of a similar nature for other clients in the last 12 months?	Yes

Result: Unable to make a determination

Continued

EXHIBIT DPre-seen informationClient

RDJ Pharmaceuticals UK Ltd.

The company is a UK wholly owned subsidiary of RDJ Pharmaceuticals Inc, a US company listed on the New York Stock Exchange. The group develops and launches medicines and vaccines tackling rare diseases. It is headquartered in Pennsylvania, US. RDJ Pharmaceuticals UK Ltd is based in rented premises in Oxford and was set up for the European market.

RDJ Pharmaceuticals UK Ltd has 48 employees in the UK.

Ownership

20% of the shares of RDJ Pharmaceuticals Inc are either owned directly by employees and directors or subject to share options.

Financial Information

Its last three year's accounts show the following:

	<u>2019</u>	<u>2020</u>	<u>2021</u>
<u>RDJ Pharmaceuticals Inc</u>	£	£	£
Turnover	62,000,000	66,000,000	71,000,000
Cost of Sales	<u>(17,000,000)</u>	<u>(17,500,000)</u>	<u>(18,000,000)</u>
Gross Profit	45,000,000	48,500,000	53,000,000
Less: Employee costs	(24,000,000)	(26,000,000)	(30,000,000)
Less: other administrative costs	<u>(6,000,000)</u>	<u>(5,500,000)</u>	<u>(5,000,000)</u>
Net Profit	<u>15,000,000</u>	<u>16,000,000</u>	<u>18,000,000</u>
Number of Employees	320	340	400
<u>RDJ Pharmaceuticals UK Ltd</u>	£	£	£
Turnover	3,500,000	7,100,000	9,700,000
Cost of Sales	<u>(2,500,000)</u>	<u>(3,000,000)</u>	<u>(3,300,000)</u>
Gross Profit	1,000,000	4,100,000	6,400,000
Less: Employee costs	(2,400,000)	(2,800,000)	(3,200,000)
Less: other administrative costs	<u>(400,000)</u>	<u>(500,000)</u>	<u>(600,000)</u>
Net Profit	<u>(1,800,000)</u>	<u>800,000</u>	<u>2,600,000</u>
Number of Employees	34	40	44

Current Net Assets: £23,000,000

Exchange rate: £1 = €1.15

UK Employment Benefits offered

Private Medical Insurance – Cost £1,000 per employee per year.

Pension – 5% employee contribution, 3% employer contribution.

Holidays – 27 per year excluding bank holidays.

Life Insurance – Four times salary death in service, cost £20 per employee per month.

Stock Options – RDJ Pharmaceuticals Inc has an established share option plan and is in the process of setting up a subplan for selected UK based employees and consultants.

Corporation Tax

RDJ Pharmaceuticals UK Ltd is up to date with its Company Tax Returns and payment of Corporation Tax.

VAT

RDJ Pharmaceuticals UK Ltd is VAT registered and makes wholly taxable supplies.