

# THE CHARTERED INSTITUTE OF TAXATION

## APPLICATION AND PROFESSIONAL SKILLS

### Human Capital Taxes

**May 2023**

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TIME ALLOWED

3 HOURS 30 MINUTES

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- 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 2022/23 legislation (including rates and allowances) continues to apply for 2023/24 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 Taxadv, an international firm which provides support to employers of globally mobile employees. You report to Jay Turner, a Director in your UK firm. She has received an email (**EXHIBIT A**) from Lesley Cobbler, who is a Senior Tax Manager in your Canadian office.

A client of the Canadian office, Havarn CA Ltd, has asked for advice on the implications of employing a UK national who is currently resident in the UK. They have also asked for advice on the implications of carrying out a UK-based project they are about to bid for.

The following exhibits are provided to assist you:

**EXHIBIT A:** Email from Lesley Cobbler to Jay Turner

**EXHIBIT B:** Report prepared by Lesley Cobbler to Havarn CA Ltd

**EXHIBIT C:** Email exchange between Jacky Grayson, HR Director, and Jason Blackman, Head of Engineering at Havarn CA Ltd

**EXHIBIT D:** Meeting notes regarding the proposal for a UK project

**EXHIBIT E:** Pre-seen information

You should assume an exchange rate of £1 = CAD\$ 1.7 and that the OECD model treaty applies to all countries mentioned.

**Requirement:**

**Prepare a draft report for Lesley Cobbler advising on the compliance obligations for Havarn CA Ltd given (a) the proposed employment of a UK national and (b) the UK project, should they be successful in their bid. You should include recommendations on alternative ways by which Havarn CA Ltd may achieve their objectives.**

## EXHIBIT A

### Email from Lesley Cobbler to Jay Turner

To: Jay Turner, Taxadv UK Ltd  
From: Lesley Cobbler, Taxadv Canada Ltd  
Date: 26 April 2023

Re: Havarn CA Ltd

Dear Jay

I hope you are keeping well. Could you please assist us with the following issue for one of our longstanding clients, Havarn CA Ltd?

They manufacture and service large hydraulic lifting machinery for the industrial market. To date, they have done this mostly in Canada and the US. I attach some background information on Havarn CA Ltd (**EXHIBIT E**).

Experienced hydraulic engineers are hard to find and they've recently been in discussions with an engineer in the UK, Tony Farrell. He's a UK national and he lives in the UK with his partner and three young children. They would really like to make him a job offer and he seems keen to work for them. However, before they go any further, they have asked for some advice about employing someone who will be living in the UK.

Havarn CA Ltd has two core activities:

- 1) Manufacturing hydraulic lifting machinery and component parts.
- 2) Carrying out the regular servicing on hydraulic lifting machinery.

To do any maintenance, the machine has to be shut down for the service period, which is usually two to three months. The engineer will order parts and arrange delivery to the customer's location prior to the shutdown. These machines are generally far too large to be moved away for maintenance, so the servicing is done at the customer's premises. The engineer will then go to the customer's location for the whole shutdown period until the service is complete and the machine goes back into operation.

Havarn CA Ltd foresees that Mr Farrell will be a valuable resource for new design ideas and testing. He will also carry out servicing contracts in Canada and the US. He will be able to do some of the preparations from home in the UK. He will make some short business trips to the customer's location while preparing for the service shutdown period. He may need to go to Havarn CA Ltd's offices during this period as well. He will then be at the customer's location for the shutdown period, with a week-long home leave trip part way through. He will return to the UK after the shutdown period to complete the servicing reports from home. He will then repeat the process for the next servicing project.

I have attached a copy of my report to Havarn CA Ltd on the issues from the Canadian side on them employing Mr Farrell (**EXHIBIT B**). I have also included emails between Havarn CA Ltd's Head of HR and their Head of Engineering, which detail the remuneration package they are thinking of offering (**EXHIBIT C**). I would very much appreciate it if you could prepare a report on the UK issues involved in employing Mr Farrell, which I can send on to the company.

For your information, there is a UK company in the Havarn Group, Milvarn UK Ltd. They only carry out servicing contracts in the UK and Europe. They do not manufacture. They have offered to employ Mr Farrell if it facilitates any compliance issues for the Canadian company. However, Havarn CA Ltd would prefer to employ Mr Farrell themselves if they can.

You should also know that there is a potential project arising in the UK in 2025, which Havarn CA Ltd are keen to bid on. It is another reason why they are keen to hire Mr Farrell and have a UK-based engineer. The potential customer has indicated that Havarn CA Ltd would be front-runners in the bid process, except they are concerned that Havarn CA Ltd does not have a UK base. Milvarn UK Ltd may therefore also have to become involved in this bid as described in the attached meeting note (**EXHIBIT D**).

If you have any questions or need any further information, please do not hesitate to contact me.

Kind regards

Lesley Cobbler  
Senior Tax Manager  
Taxadv Canada Ltd

## **EXHIBIT B**

### Report prepared by Lesley Cobbler to Havarn CA Ltd

### Employment tax and social security issues arising from their potential employment of Tony Farrell

#### Executive Summary

To the extent Mr Farrell works in Canada, Havarn CA Ltd ('the Company') will have to calculate and deduct Canadian tax and social security from the portion of the earnings related to days worked in Canada. There is no requirement to pay tax or social security contributions on the portion of earnings relating to work performed outside of Canada. However, all of the earnings will need to be reported on Form T4.

Mr Farrell will not be eligible to join the Company's pension and medical insurance plans.

Advice is needed from a UK tax specialist as to what is required to register the Company in the UK and file the necessary corporate returns. I can refer to my colleague in our UK office to obtain this advice.

#### Payroll in Canada

#### Withholding Tax

As a Canadian resident company, you are obliged to withhold wage tax deductions for any employee who is either

- 1) tax resident, or
- 2) working in Canada.

We must therefore determine if Mr Farrell will be tax resident in Canada. This will depend, firstly, on whether he establishes residential ties with Canada. Since Mr Farrell and his family will continue to live in the UK, he is not expected to have any residential ties with Canada.

For someone with no residential ties who enters Canada, one of the following would apply.

- 1) If they stay in Canada for 183 or more days in the year, they will be a resident of Canada for that year.
- 2) If they stay in Canada for fewer than 183 days in the tax year, they will be a non-resident of Canada for that year.

Therefore, Mr Farrell will be a resident of Canada, under Canadian domestic law, if and only if he exceeds 183 days in Canada in any calendar year. However, in that case, since he will not have a permanent home in Canada, we can apply Article 4(2)(a) of the Canada/UK Double Taxation Convention and claim treaty residence in the UK and treaty non-residence in Canada.

Therefore, Mr Farrell will not be tax resident in Canada and withholding tax is not due on income for working outside of Canada. It is still due, however, on his earnings for working in Canada. There can be no exemption under Art 15(2) Dependent Services of the Double Taxation Convention where the employer is a Canadian resident company.

However, the Company is still required to report all earnings on the annual year-end payroll record, Form T4. Therefore, you will still need to track total income on the Canadian payroll.

#### Social Security

There is a social security reciprocal agreement between Canada and the UK. Under Article 4(1), an individual is liable to social security in the country the work is performed. So, if he works in both countries, he is liable both in Canada and in the UK but only on the relevant portion of their earnings. Therefore, the individual will be liable to Canadian contributions on the earnings for days worked in Canada. He will then also be liable to UK contributions but only on the earnings for days worked in the UK. Since the employer contributions are always in the same jurisdiction as the employee contributions, you should expect to pay employer contributions in Canada and the UK.

Although only a portion of the earnings are liable to Canadian contributions, the liable amount is likely to exceed the earnings cap. Therefore, you should expect to pay the maximum possible contribution of CAD\$ 3,500 per annum. Mr Farrell will also have to pay a similar amount.

There is provision in the reciprocal agreement for a Canadian employee, who is on a temporary secondment to a UK company, to contribute solely to the Canadian system. Temporary is up to five years. This would not, however, apply in this case, since he is not being seconded and this is not a time-limited situation.

#### Other Issues

As a non-resident of Canada, Mr Farrell will not be eligible to join the Company's pension plan or be covered under the Company's medical and dental plan, even though he is an employee. Alternative arrangements will therefore be required.

## Corporate Registrations

In some other countries, the hiring of a local employee requires the Company to register in the other country's equivalent of the Corporate Registry. The Company may then also be obligated to operate a local payroll and register for any value-added type taxes. It would therefore be prudent to get confirmation of whether we need to make such registrations in the UK and what regular reporting obligations are subsequently required.

The above report is intended for the recipient only and is specific to the circumstances of the particular case. It is provided under the terms and conditions of our engagement letter with Havarn CA Ltd. No third party may rely on it without our consent. The report is based on current legislation and will not be updated to reflect future legislative changes unless requested.

Date: 20 April 2023

Continued

## EXHIBIT C

### Email exchange between Jacky Grayson, HR Director, and Jason Blackman, Head of Engineering at Havarn CA Ltd

Date: 20 April 2023  
From: Jason Blackman, Head of Engineering, Havarn CA Ltd  
To: Jacky Grayson, HR Director, Havarn CA Ltd  
Subject: Employment of Tony Farrell

Hi Jacky

I've had an open and honest discussion with Tony about the package he is receiving from his current employer. He appreciates that this situation is a bit different, but he is keen to join us and is willing to be flexible. He doesn't want to be worse off, though, and won't move for less money.

#### Package Comparison

He's currently on a basic salary of £90,000. He gets overtime at 1.5 times basic. He usually grosses between £104,000 and £110,000 per year.

He has international medical cover and a contributory pension of 8% employer / 3% employee. He has 30 days annual vacation including UK public holidays.

#### Locational split

I would think that Tony would spend around 80-85% of his working time in Canada or the US. The rest would be the UK. Obviously, that would change if we get the UK project.

#### UK Project

I had a meeting with Alan last week, just to explore the option of using Milvarn UK Ltd in the UK project, if we have to. The biggest hurdle is that the customer wants to deal with a UK registered company. Obviously Milvarn UK Ltd can't supply the machinery, so need us. Whereas we have the capability to do the whole project ourselves. If we did the project jointly, we'd supply the machines and supply some staff for the two servicing phases. Milvarn UK Ltd would supply some other staff and do the 10-year service contract. As you know, the 10-year service contract afterwards is what makes the real money. We risk handing the really lucrative part over to Milvarn UK Ltd and coming away with little or nothing.

I get the sense that they wish they'd found Tony themselves. They've offered to employ him, if it makes it easier, and lend him back to us. I do wonder though if we'd have to fight to get to use him. Would we have the control we need over when and where he works?

Can we try everything to employ Tony ourselves?

Thanks and best regards,

Jason

Date: 21 April 2023  
From: Jacky Grayson, HR Director, Havarn CA Ltd  
To: Jason Blackman, Head of Engineering, Havarn CA Ltd  
Subject: Re: Employment of Tony Farrell

Hi Jason

Thanks for your email yesterday. This is useful information for us.

I have been looking at how we might be able to employ a UK national, who continues to live in the UK, but will work this side of the Atlantic. I don't see why we can't do this, but on trying to fill in our standard employment contract and package template, it's raised a few questions.

#### Package Comparison

£90,000 is equivalent to around CAD\$153,000. This is slightly above the median for his role, which is CAD\$150,000, but I think that is OK given he is very experienced. We pay overtime at 1.25 times during the week and 2.0 times for weekends/public holidays. So overall, I think that would be comparable.

You say he has 30 days annual vacation, which includes UK public holidays. The Canadian standard is 25 days plus the 10 national and provincial public holidays.

Our employee benefits provider has confirmed that Tony cannot join the Canada Pension Plan or the Havarn CA Medical & Dental Plan, as he is not resident in Canada. He can be covered by the International Emergency Medical and Evacuation Plan, which we have for all internationally mobile employees. I suggest that we could increase his salary in respect of the fact that Tony would have to find his own pension and medical coverage from the UK. He seems prepared to do this.

Our normal pension contribution rate is 5% from both employer and employee, so I propose an uplift of 5% on basic salary for pension. I would think the medical insurance premium would be about £3,000. That would make his basic £97,500 or CAD\$165,750, which is right at the top of the range for his role.

I've input his place of work for now as his UK home address, pending advice to the contrary. Obviously, we'd fly him into Canada/USA. We fly local employees to customer locations most times. As it's long-haul international, it would be business class. When Canadian employees are working at customer sites, we'd normally allow a weekend home visit every three weeks. Given the distance, I suggest we offer one week every six, of which two days should come out of his annual vacation time, if you think that would work.

He'll be in a hotel or serviced apartment near to the customer, the same as other service engineers. He'll get our standard per diem of CAD\$90 when at customer's premises in Canada and USD\$70 when at a US location.

I've asked our advisers about employing Tony ourselves or if we need to do it through Milvarn UK Ltd.

Let me know what you think of the package.

Kind regards

Jacky

## EXHIBIT D

### Meeting notes regarding the proposal for a UK project

#### Note of internal meeting (held by video conference)

17 April 2023

#### Proposal for a UK project

Attendees: Jason Blackman, Head of Engineering, Havarn CA Ltd  
Alan Whitehead, Projects Director, Milvarn UK Ltd

#### Key Requirements:

- 1) Servicing of all the customer's existing lifting machinery, including non-Havarn products. To include the reinstatement of safety certificates on their existing machinery.

##### Phase 1 to commence 1 May 2025

Includes servicing of Havarn machinery. Expected date of re-commission of machinery 15 December 2025.

##### Phase 2 to commence 23 February 2026

Includes servicing of non-Havarn machinery. Expected date of re-commission of machinery 23 July 2026.

- 2) Customer needs to purchase two new large mobile lifting platforms.
- 3) Maintenance and servicing contract for 10 years from date Phase 2 completed.

#### Key points:

Customer has had a comprehensive health and safety audit. Some of their existing machinery needs a major overhaul to meet the latest regulations and has been shut down by the safety authorities. Machinery will need to be signed off by a certified engineer before it can be re-commissioned.

Customer will only engage with a UK registered supplier.

Customer will not act as the importer.

Customer will provide office space and a workshop facility at their premises for the duration of Phases 1 and 2 up to July 2026.

#### Offer from Milvarn UK Ltd:

Milvarn UK Ltd could lead the bid and engage with the Customer, since Havarn CA Ltd is not a UK registered company and does not have VAT registrations.

Havarn CA Ltd will supply the new machinery and components required for servicing, since Milvarn UK Ltd is not a manufacturer of these.

Milvarn UK Ltd can supply some general servicing staff and carry out the 10 year servicing contract. However, they do not have enough specialist staff or a certified engineer to sign safety certificates. These will be supplied by Havarn CA Ltd.

#### Mobile Lifting Platform Details:

The FR 245 platform is the best fit for the customer and will not require any bespoke re-design or on-site alterations. The latest design improvements will be ready early 2024, so any teething problems will be ironed out in good time. The specialist engineers will also have had training and some experience of them by 2025.

Each platform costs CAD 5.9 million to manufacture. Havarn CA Ltd currently have room in their production schedule to manufacture one before the start of Phase 1. The second would be ready in the first quarter of 2026.

Staffing:

Phases 1 and 2 will each require:

- 1) One Project Manager, who will be the certified engineer. On site for the whole of each phase, plus pre-commencement visits to check components required for servicing existing machinery.
- 2) Three teams to work on a three shift system.

Each team should consist of two general servicing staff (from Milvarn UK Ltd) and one specialist staff (from Havarn CA Ltd).

No staff are required for delivery of the new platforms as these are supplied ready to go. As they are mobile platforms, they are not required to be installed or fitted into the customer's premises.

The customer would prefer a UK employee as project manager, if the UK company is leading. UK staff will probably not have much experience of the FR 245 model.

Havarn CA Ltd is hoping to recruit a UK-based hydraulic engineer onto their permanent staff. This engineer is certified. If this is successful, this individual could become the project manager/certified engineer. Milvarn UK Ltd would be prepared to hire the engineer with a view to servicing this project. They have offered to lend the engineer back to Havarn CA Ltd in the interim between now and the start of the project. This would enable the engineer to become familiar with Havarn CA Ltd's machinery before the UK project started.

## EXHIBIT E

### Pre-seen information

#### Client

Havarn CA Ltd

#### Business Description

The Havarn Group manufactures and services hydraulic lifting machinery in Europe and the Americas. The parent company, Havarn Inc, is a publicly owned company in the US, listed on the New York stock exchange. It was formed in 1994 and listed in 2002. It has 61 employees.

#### Group Structure

Havarn Inc has two wholly owned subsidiaries: Havarn CA Ltd and Milvarn UK Ltd.

Havarn CA Ltd is incorporated and tax resident in Canada. It has 106 employees. It has no overseas branches. It manufactures and services hydraulic lifting machinery in Canada, the USA, Central and Latin America.

Milvarn UK Ltd is incorporated in England and Wales and tax resident in the UK. It has 43 employees and is VAT registered. It services lifting machinery throughout Europe.

#### Board Directors of Havarn Ltd

Managing Director	Bill Green (Employee of Havarn Inc / US citizen)
HR Director	Jacky Grayson (Employee of Havarn CA Ltd / Canadian citizen)
Finance Director	Freya Redman (Employee of Havarn CA Ltd / Canadian citizen)
Manufacturing Director	Wayne Brown (Employee of Havarn CA Ltd / Canadian citizen)
Customer Director	Lisa Teal (Employee of Havarn CA Ltd / US citizen)

#### Profit Before Tax Year Ended 31 December 2022

	<u>Havarn CA Ltd</u>	
	<u>CAD\$</u>	<u>CAD\$</u>
Turnover		92,730,650
Non-trading Income		101,070
Less: Cost of sales		<u>(57,750,045)</u>
Gross Profit before taxation		35,081,675
Bank interest receivable		3,500
Expenditure		
Wages and salaries	10,105,000	
Depreciation expense	65,850	
Motor expenses	421,010	
Office expenses	<u>2,251,860</u>	
		<u>(12,843,720)</u>
Profit before taxation		<u>CAD\$ 22,241,455</u>

#### Balance Sheet at 31 December 2022

	<u>CAD\$</u>
	<u>Havarn CA Ltd</u>
Freehold property	2,400,000
Plant & machinery	14,800,500
Debtors/inventory	2,950,000
Bank current account	1,250,000
Bank deposit account	12,950,000
Less: creditors	<u>(3,185,000)</u>
	<u>CAD\$ 31,165,500</u>
Capital & Reserves	
Share capital	1,000
Profit 2022	22,241,455
Retained earnings	<u>89,230,45</u>
	<u>CAD\$ 31,165,500</u>