THE CHARTERED INSTITUTE OF TAXATION

APPLICATION AND PROFESSIONAL SKILLS

Taxation of Individuals

November 2023

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 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 a small firm of Chartered Tax Advisers. You have recently met with a new client, Stefan Richter.

Stefan is a German national who arrived in the UK in September 2020. He is employed in London. He owns shares in a German company, Kremet GmbH, and jointly owns his former family home in Leipzig with his brother, Lukas. Lukas pays Stefan rent in return for the exclusive occupation of the property.

Stefan and Lukas have agreed that Lukas will buy out Stefan from the property in Leipzig. In addition, Stefan has decided that he will sell his shares in Kremet GmbH. He would like to use the proceeds from both transactions to make additional pension contributions.

The following exhibits are provided to assist you:

EXHIBIT A: Notes of your meeting with Stefan

EXHIBIT B: Prior year UK tax calculations

EXHIBIT C: Extracts from the UK-Germany Double Taxation Convention

EXHIBIT D: Pre-seen information

Requirement:

Write a letter to Stefan advising on how he should optimise his UK tax position given his circumstances and proposals, including recommendations for any actions he should take.

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EXHIBIT A

Notes of your meeting with Stefan

Date: 31 October 2023

Stefan arrived in the UK on 1 September 2020 and he works full-time for a corporate bank in London. Upon arrival in the UK, he stayed in rented accommodation before buying a property on 1 February 2021.

He met with me to seek tax advice on the sale of his share of a property in Leipzig, and of his shares in Kremet GmbH, to fund additional pension contributions in a tax-efficient manner.

He explained that the Leipzig property was inherited in equal shares by him and his brother, Lukas, from their late father on 1 November 2007. At that time, both Stefan and Lukas lived together in the property. They continued to do so until 1 March 2010, when Stefan moved out for a job opportunity elsewhere in Germany as an investment manager in Frankfurt. It was impractical for Stefan to continue living in Leipzig for the role, so he lived in rented accommodation in Frankfurt until he moved to the UK. He was occasionally required to travel to the UK as part of this role, though not for more than 10 workdays a year.

When Stefan left Leipzig, the brothers agreed that Lukas would pay Stefan rent in return for exclusive use of the property, although Lukas felt it was unfair that he had to pay money to Stefan as a result of Stefan's decision to leave their home town.

Lukas has since married and he has a young child, Jonas. He would like to buy Stefan out, and the brothers have agreed this will happen as soon as practicable. However, Lukas has insisted that the amount he pays is discounted to reflect the rent he has paid Stefan to date, having never been comfortable with the rental arrangement between them.

Stefan has reluctantly agreed, but only to maintain cordial relations between him and his brother's family. In particular, Stefan is keen not to be cut off from his only nephew. He is very fond of Jonas and makes a point of returning to Leipzig twice a year to see him. As Stefan does not have children himself, he explained that he would want Jonas to be the sole beneficiary of his estate when he dies.

Stefan says that the current market value of the property in Leipzig is estimated to be 487,500 Euros (£406,250). However, he has agreed to accept just 180,000 Euros (£150,000) from Lukas in return for transferring his share of the property to Lukas.

Stefan also explained to me that he would like to sell his shares in Kremet GmbH. Kremet GmbH is a German company which makes parts for diesel and petrol engines. Stefan believes that the future is in electric cars, so he is not optimistic about the future value of his investment. In addition, he says that the high marginal rates of tax he is paying on the dividend income in the UK make the investment "not worthwhile".

Stefan advised that the current market value of the shares is 45 Euros (£37.50) per share.

With the funds from the sale of his shareholding and the property in Leipzig, Stefan would like to make additional pension contributions, as he says this will be tax-efficient.

Stefan has both German and UK pension schemes. The UK pension is with his UK employer. He and his employer each contribute 5% of his gross salary into that scheme under a net pay arrangement (and have done so since Stefan's arrival in the UK). He has asked whether it would be better from a UK tax perspective to make the additional contributions into his German or his UK pension scheme, or into both.

Since 2020/21, Stefan has filed his Self Assessment tax returns himself, reporting his overseas income on the arising basis. He provided me with copies of his Self Assessment tax calculations for 2020/21 to 2022/23 (**EXHIBIT B**).

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Stefan said that he does not have a long-term intention to remain in the UK and that at some point he will return to live in Germany. Stefan was not familiar with the remittance basis of taxation and is curious to know if it would be beneficial for him. He confirmed that he has not remitted any of his overseas income to the UK. The cumulated funds are held in a German savings account.

Stefan provided the following information for me to use in modelling his estimated UK tax position for 2023/24:

	£
Employment income for 2023/24	110,000
Rental income from Lukas since 6 April 2023	7,000
Foreign savings interest for 2023/24	500
Kremet GmbH dividends received since 6 April 2023	2,500

Stefan advised that the rate of German tax on the rental income and dividends is 15%. No German tax is payable on the foreign savings interest or on the sale of the Leipzig property.

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EXHIBIT B

Prior year UK tax calculations

2022/23

	£
Employment income	105,500
Foreign rental income	8,750
Foreign savings interest	420
Foreign dividends	4,020
Total income	118,690
Personal allowance	(3,225)
Taxable income	115,465
Tax thereon:	
£37,700 at 20%	7,540
£73,325 at 40%	29,330
£420 at 0%	-
£2,000 at 0%	-
£2,020 at 32.5%	656
Tax before reductions	37,526
Foreign tax credit	(1,560)
Tax after reductions	35,966

2021/22

	£
Employment income	93,995
Foreign rental income	9,105
Foreign savings interest	390
Foreign dividends	4,860
Total income	108,350
Personal allowance	(8,395)
Taxable income	99,955
£37,700 at 20%	7,540
£57,005 at 40%	22,802
£390 at 0%	-
£2,000 at 0%	-
£2,860 at 32.5%	929
Tax before reductions	31,271
Foreign tax credit	(1,705)
Tax after reductions	29,566

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2020/21

	£
Employment income	58,020
Foreign rental income	3,925
Foreign savings interest	350
Foreign dividends	3,650
Total income	65,945
Personal allowance	(12,500)
Taxable income	53,445
£37,500 at 20%	7,500
£11,945 at 40%	4,778
£350 at 0%	-
£2,000 at 0%	-
£1,650 at 32.5%	536
Tax before reductions	12,814
Foreign tax credit	(1,320)
Tax after reductions	11,494

Continued

EXHIBIT C

Extracts from the UK-Germany Double Taxation Convention

Article 6
Income from immovable property

1) Income derived by a resident of a Contracting State from immovable property (including income from agriculture or forestry) situated in the other Contracting State may be taxed in that other State.

2) The term “immovable property” shall have the meaning which it has under the law of the Contracting State in which the property in question is situated. The term shall in any case include property accessory to immovable property, livestock and equipment used in agriculture and forestry, rights to which the provisions of general law respecting landed property apply, usufruct of immovable property and rights to variable or fixed payments as consideration for the working of, or the right to work, mineral deposits, sources and other natural resources; ships and aircraft shall not be regarded as immovable property.

3) The provisions of paragraph 1 shall apply to income derived from the direct use, letting, or use in any other form of immovable property.

4) The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise.

Article 10
Dividends

1) Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

2) However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident and according to the laws of that State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed:

   a) 5 per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly at least 10 per cent of the capital of the company paying the dividends;

   b) 10 per cent of the gross amount of the dividends if the beneficial owner is a pension scheme;

   c) 15 per cent of the gross amount of the dividends in all other cases.

   The provisions of this paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid.

3) The term “dividends” as used in this Article means income from shares, “jouissance” shares or “jouissance” rights, mining shares, founders’ shares or other item which is subjected to the same taxation treatment as income from shares by the laws of the State of which the company making the distribution is a resident, and income from distributions on certificates of a German “Investmentvermögen”.

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4) The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State of which the company paying the dividends is a resident, through a permanent establishment situated therein and the holding in respect of which the dividends are paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.

5) Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company, except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

Article 14
Income from Employment

1) Subject to the provisions of Articles 15, 17, 18 and 19 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, 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 any twelve month period commencing or ending 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 which the employer has in the other State.

3) Notwithstanding the preceding provisions of this Article, remuneration derived by a resident of a Contracting State in respect of an employment exercised aboard a ship or a aircraft operated in international traffic shall be taxable only in that state.

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Article 17
Pensions, Annuities and Similar Payments

1) […], pensions, other similar remuneration or annuities arising in a Contracting State and paid to a resident of the other Contracting State, shall be taxable only in that other State.

2) Notwithstanding the provisions of paragraph 1, payments which are made in accordance with the social insurance legislation of a Contracting State shall be taxable only in that State.

3) Notwithstanding the provisions of paragraph 1, such a pension, similar remuneration or annuity arising in a Contracting State which is attributable in whole or in part to contributions which, for more than 15 years in that State,

a) did not form part of the taxable income from employment, or
b) were tax-deductible, or
c) were tax-relieved in some other way

shall be taxable only in that State. This paragraph shall not apply if that State does not effectively tax the pension, other similar remuneration or annuity, or if the tax relief was clawed back for any reason, or if the 15 year condition is fulfilled in both Contracting States.

4) Notwithstanding the provisions of paragraph 1, recurrent or non-recurrent payments made by one of the Contracting States or a political subdivision thereof to a resident of the other Contracting State as compensation for political persecution or for an injury or damage sustained as a result of war (including restitution payments) or of military or civil alternative service or of a crime, a vaccination or a similar event shall be taxable only in the first-mentioned State.

5) The term “annuities” means certain amounts payable periodically at stated times, for life or for a specified or ascertainable period of time, under an obligation to make the payments in return for adequate and full consideration in money or money’s worth.

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EXHIBIT D

Pre-seen information

Client name	Stefan Richter
Date of birth	4 June 1986
Place of birth	Leipzig, Germany
Marital status	Single
Children	None
Residence status	UK resident
Domicile	Germany
UK Will	No UK Will

Asset Schedule

32 Grove Road, London

This is Stefan's main residence. It was purchased on 1 February 2021 for £495,000. Stefan paid a 10% deposit and took out an interest-only mortgage for the remainder of the purchase price.

Klostergasse 45, Leipzig, Germany

This property is jointly owned with Stefan's brother, Lukas. Stefan owns 50% of the property. No debt is secured against the property.

The property was originally purchased by Stefan's parents in November 1984 for 20,000 Deutschmark (£5,400).

It was then inherited by Stefan and Lukas on 1 November 2007 when the market value of the property was 325,000 Euros (£270,833).

Kremet GmbH shares

The acquisition and disposal history for the shareholding is as follows:

Date	Number of shares bought/(sold)	Cost/proceeds per share
1 July 2008	1,000	£50
1 March 2010	2,000	£60
1 August 2015	(2,000)	£55

Other Assets

£20,000 held in a UK cash ISA.

50,000 Euros (£41,667) in a German savings account.