

The Chartered Institute of Taxation

Advanced Technical

Human Capital Taxes

May 2023

Suggested solutions

ANSWER 1

Joining bonus

A payment to induce someone to take up employment is taxable as earnings at the point of payment, even if the employment has not started. Big Ltd will have to register Amy as a new starter on their payroll in June 2023.

Big Ltd will need to use a BR tax code and deduct tax at 20% from the payment, as they are aware that this is a second job. The amount payable will be £40,000 (£200,000 x 20%).

This will result in an underpayment, which Amy should resolve via self-assessment.

The payments will also be subject to NICs as follows:

Class 1 Primary NIC (deducted from the amount paid to Amy)

Band		Liability	
PT+	£0 to £1,048	£1,048 x 0%	£0
PT-UEL	£1,048 to £4,189	£3,141 x 13.25%	£416
UEL+	£4,189+	£195,811 x 3.25%	£6,364
Total			<u>£6,800</u>

Class 1 Secondary NIC (borne by Big Ltd)

Band		Liability	
ST	£0 to £758	£758 x 0%	£0
ST+	£758.00+	£199,242 x 15.05% =	£29,986
Total			<u>£29,986</u>

House Sale

If an employee is relocating to undertake a role and the employer pays qualifying relocation expenses, there is no income tax or NIC charge on the first £8,000. Any excess will be taxable on the employee.

For the exemption to apply, the employee's existing main residence must not be within a reasonable commuting distance of the new job location. Amy is to relocate from London to Leeds which would meet this condition.

The £7,000 legal fees in disposing of her old home qualifies under s279 ITEPA 2003 and can be reimbursed tax and NIC free.

If Amy chooses not to take up the job, then she will not be entitled to any tax-free payments for relocating.

School fees

On the assumption that the fees are reimbursed to Amy, this is a pecuniary liability and does not qualify as a relocation expense. It is subject to tax and Class 1 NIC, reportable via the payroll, in September 2023.

The amount payable will be £2,000 (£10,000 x 20%). This will result in an underpayment which Amy must resolve via Self Assessment.

Class 1 Primary NIC

Band		Liability	
PT+	£0 to £1,048	£1,048 x 0%	£0
PT-UEL	£1,048 to £4,189	£3,141 x 13.25%	£416
UEL+	£4,189+	£5,811 x 3.25%	£189
Total			<u>£604</u>

Class 1 Secondary NIC

Band		Liability	
ST	£0 to £758	£758 x 0%	£0
ST+	£758.00+	£9,242 x 15.05% =	£1,391
Total			£1,391

Hotel and Travel costs for Amy

These would qualify as temporary living accommodation costs under s281 ITEPA 2003. Both could be paid tax and NIC free. However, she has already used £7,000 of the £8,000 exemption and only £1,000 can be paid tax free.

Any excess will be reported on P11D and be subject to Class 1A NIC. This will result in an Income Tax liability of £2,700 (£6,000 x 45%) for Amy which she will need to include in her 2022/23 self-assessment tax return. and £903 (£6000 x 15.05%) of NIC for Big Ltd.

MARKING GUIDE

TOPIC	MARKS
Explanation of tax position on joining bonus	½
Confirmation of tax code to use	½
Tax payable	½
National Insurance position	1
Self-Assessment	½
Relocation exemption: Reasonable distance condition	½
Application of conditions to Amy	½
Limiting to £8,000 total	½
School fees – Income Tax	1
School fees - National insurance	1
Travel/legal fees and hotel qualifying relocation expenses	1
Only £1,000 of exemption remaining	½
Excess reported on P11D and subject to Class 1A NIC	1
Tax and Class 1A NIC payable	1
TOTAL	10

ANSWER 2

Requirement 1

A refund will be due to Michelle and Beth to the extent that they are entitled to a credit for the overseas tax paid. Subject to the availability of any relief under an applicable double tax treaty, the foreign tax credit (FTC) is limited to the lower of the amount of the foreign tax and the UK tax due on the same income.

The FTC and earnings are:

	<u>Beth</u>		<u>Michelle</u>	
	£	£	£	£
Total Income		205,000		220,000
Foreign sourced		<u>74,000</u>		<u>59,000</u>
UK sourced		131,000		161,000
UK tax on UK sourced only:				
Personal allowances (Note N1)	0	0	0	0
20% band	37,700	7,540	37,700	7,540
40% band	93,300	37,320	112,300	44,920
45% band			<u>11,000</u>	<u>4,950</u>
	<u>131,000</u>		<u>161,000</u>	
UK tax due on UK sources only (1)		44,860		57,410
Total UK tax due before foreign tax credit (2)		<u>77,210</u>		<u>83,960</u>
UK tax due on foreign sources (2-1) (A)		<u>32,350</u>		<u>26,550</u>
Foreign tax paid in 2022/23 (B)		37,500		19,470
FTC is the lower of A and B	A	<u>32,350</u>	B	<u>19,470</u>
Amount not recovered/waivered (only if using A)		<u>£(5,150)</u>		<u>£0</u>

Note N1 – Beth and Michelle are not entitled to personal allowances as income exceeds threshold of £125,140.

Michelle will not have any loan waived so the distribution to participators is not relevant.

As the FTC is less than the overseas tax, a loan balance for Beth will remain outstanding. If the balance was waived this would be earnings liable to PAYE/NIC. Given Holdings Ltd's desire to protect their employees, the waiver should be grossed-up for income tax and NIC. The waiver is reportable on the P11D but Class 1 NIC is due via the payroll as additional pay.

The gross-up for Beth's payroll should be as follows:

	£
Gross-up needed	5,150
Gross-up for tax and NIC $£5,150 \times (45+3.25)/(100-45-3.25)$	4,802
Cost to company:	
Total as above	9,952
Employer's NIC @ 15.05%	<u>1,498</u>
Total	<u>£ 11,449</u>

The waived amount should be entered on Beth's P11D but with the amount recovered through PAYE also included so the net amount on her P11D is zero.

Requirement 2

A beneficial loan can generate a taxable beneficial interest charge for employees when loans made by reason of employment to the employee or their family members, exceed £10,000 and when the loan has no interest payable or a low interest rate.

An average balance is calculated using the amounts outstanding at the beginning and end of the year. HMRC's official interest rate is applied to obtain the P11D benefit. Where a loan is made within the year, the average calculation starts from the date the loan was made and interest is pro-rated.

An employee can elect for a calculation of beneficial interest on a strict daily basis if the result is lower but HMRC can insist it is used. This is unlikely unless the difference is significant.

Loans to an employee's household staff are ignored.

Expense advances can be ignored where below £1,000, for business expenses, and claims are regularly submitted for and the loan is used within six months.

Beth's Loans

The loan to Beth's housekeeper is ignored but the loan to her husband has to be considered.

Michelle's Loans

Michelle is a director and a participator as she owns more than 5% of a close company. When a loan is made to a participator, if the loan remains outstanding beyond nine months from the end of the accounting period, s.455 tax is charged at 33.75% of the loan. This is due at the same date as normal corporation tax.

The s.455 tax can be refunded 9 months after the accounting period in which the loan is repaid or written off. If any of the loan is written-off it is treated as a distribution to the participator.

£16,500 overseas tax for Michelle was paid in December 2022. Corporation tax is usually due nine months and 1 day from the end of the accounting period so if this amount is not repaid by 30 September 2023, s.455 tax of £5,568.75 is due. Ideally the repayment from Michelle's tax return needs to be received by 31 December 2023 otherwise the corporation tax would not be repaid until October 2025. It is recommended that Michelle's 2022/23 tax return is submitted as soon as possible to avoid or mitigate the corporation tax charge.

P11D 2022/23 Entries

	<u>Beth</u> £	<u>Michelle</u> £
15 March 2022 home repair loan	40,000	
1 May 2021 Season ticket loan	2,250	
1 June 2021 Husband's loan	4,600	
Balance of loans on 5 April 2022	46,850	0
Loans made in year (excluding exempt):		
1 May 2022 Season ticket loan	3,500	
1 October 2022 Loan for apartment deposit		
12 December 2022 & 31 March 2023 Loans for overseas tax	37,500	19,470
Repayments made in year:		
31 October 2022	(20,000)	
31 January 2023	(15,000)	
15 April 2022	(2,250)	
Balance of loan at the end of the year	£50,600	£19,470

2022/23 P11D entries	<u>Beth</u> <u>£</u>	<u>Michelle</u> <u>£</u>
Average loans outstanding		
(Balance at start of year + balance at end)/2	48,725	9,735
P11D Entry Beneficial loan interest @ 2%	975	195
Adjustments:		
Michelle's loan apportioned from 1/12/22 x 4/12		65
Less: Interest charged on loan to Beth's husband x 1.75%	(80)	
	<hr/>	<hr/>
Beneficial loan interest	<u>£895</u>	<u>£65</u>

Strict basis for Beth's loans

As Beth's loan is significant, the strict position should also be checked:

<u>From</u>	<u>Days</u>	<u>Balance</u> <u>£</u>	<u>Interest @</u> <u>2% p/a</u> <u>£</u>
06 April 2022	9	46,850	23
15 April 2022	16	44,600	39
01 May 2022	183	48,100	482
31 October 2022	42	28,100	65
12 December 2022	50	50,600	139
31 January 2023	59	35,600	115
31 March 2023	6	50,600	17
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Total days	365		£880
Less interest on husband's loan			(80)
Strict benefit			<u>£800</u>

The strict basis is lower than the average by £95 and so the strict basis should be used.

Holdings Ltd should report £800 for Beth and £65 for Michelle respectively on their P11Ds. These are due by 5 July 2023. Holdings Ltd could pay the tax by making a reimbursement through the payroll. This would have to be grossed-up for income tax and NIC. Holdings Ltd should report them on P11D, paying Class 1A NIC which is due by 19 July 2023 or 22 July 2023 if paid electronically.

MARKING GUIDE

TOPIC	MARKS
<u>Requirement 1</u>	
Explanation of waiver being liable to tax and gross-up needed for tax equalisation	1
Calculation of effective rates of tax UK and overseas	1
Calculation of amount of refund due to employer	0.5
Calculation of FTC available and loan waiver	2
Calculation of gross-up for tax and NIC at correct rates	1.5
Confirmation that Michelle does not have a dividend distribution	0.5
Confirmation that amounts liable to employer NIC	0.5
Subtotal Marks	7
<u>Requirement 2</u>	
Loans exceeding £10,000 in total	0.5
Inclusion of loans to family members	0.5
Exclusion of loans relating to household staff	0.5
Expenses advances do not need to be included as balance Less £1,000, for business expenses and regularly claimed through expenses	1
Average balance to be used (or from when loan started) or strict basis can be used	0.5
Identification of Michelle as a participator	0.5
Corporation tax charge if loan o/s for more than 9 months	0.5
Adjustment to CT when loan repaid	0.5
Amount written-off treated as distribution	0.5
Advice that CT would arise	0.5
Identification that CT would fall into 2024 and recommendation that TR prepared asap	1
Calculation of loan balance at start and end of year	1
Calculation of beneficial loan interest	1
Apportionment of interest for loans part way through the year	0.5
Deduction of interest charged	0.5
Calculation of strict interest basis Beth	2
Confirming amounts to enter on P11D	1
Advising of P11D filing deadline	0.5
Subtotal marks	13
Total	20

ANSWER 3

Social security

Pierre will be working both in the UK and the EU. The guiding principle on social security coordination between the UK and EU under the Trade and Cooperation Agreement (TCA) is that individuals should only be subject to social security legislation in one state (Article SSC.10).

Pierre is a covered person as he has historically been subject to the social security legislation of France.

Pierre is expected to carry out his work in multiple EU states as well as the UK, therefore Article SSC.12 should be considered.

Pierre is a resident of France; however, he is not performing a substantial part of his activity in France as he is expected to perform less than 25% of his duties there.

As DesGlaz Ltd is a UK registered company with place of business in the UK and the role will be Pierre's only employment, Pierre will be subject to the UK's legislation on social security (i.e., Class 1 NIC) on his remuneration.

An approach should be made to the French authorities to confirm the position who will then ask HMRC to issue a certificate of continuing liability to certify the position. The position should be monitored regularly as French duties may increase to the point that they could be considered significant, and Pierre could then be subject to French social security legislation and not UK.

If social security obligations were to be moved to France, an obligation would arise for DezGlas Ltd to pay contributions (including employer contributions) to the French authorities similar to any other French employer under SSC.14 of the TCA.

Tax Residence and Payroll Taxes

Under the Statutory Residence Test, Pierre is likely to pass the 2nd Automatic Overseas Test as he has not been tax resident in the UK for the previous 3 tax years and is expected to spend less than 46 days in the UK. As such, Pierre will only be subject to income tax on his UK sourced income which includes employment income that can be attributed to his UK duties.

As Pierre is tax resident in France, the tax treaty between the UK and France should be given consideration to confirm how double taxation can be relieved on his UK work duties.

Under Article 15, income arising on employment exercised in the UK will remain taxable in the UK. The exemption in paragraph 2 is unlikely to apply given DezGlas Ltd are a UK resident employer and the costs of the employment, at the very least those cost arising from UK work duties, will be borne in the UK.

Despite the position given under treaty, without agreement from HMRC, PAYE will be due on Pierre's full earnings. Given the nature of the work performed in the UK, it is unlikely that his UK workdays would be considered incidental.

DezGlas Ltd could apply for a Section 690 directive so that only a percentage of Pierre's remuneration is subject to PAYE based on anticipated UK work duties. This will reduce the PAYE that is deducted at source; potentially reducing it to nil if an application for 10% is made given then Pierre will be entitled to a full personal allowance as a national of an EEA state.

HMRC must confirm that they accept the application before it can be applied via the payroll. Furthermore, this will trigger a UK tax filing requirement for Pierre as the directive is only an estimate.

The provision of personal tax support will be considered a taxable benefit on Pierre.

The cost DezGlas Ltd incurs for the provision of the service, including VAT, will need to be reported on Form P11D and will be subject to employer only Class 1A NIC via form P11D(b).

An application could be made to include the benefit on a PAYE Settlement Agreement (PSA) so that DezGlas Ltd meet the tax on Pierre's behalf.

The deadline for setting up or amending a PSA is 5 July following the end of the tax year the benefit was provided.

If accepted the taxable value of the benefit will need to be reported on the PSA and grossed up at Pierre's expected marginal tax band. The benefit value and grossed up tax will be subject to employer only Class 1B NIC which will be due by 19 October following the end of the tax year (22 October if paying electronically).

MARKING GUIDE

TOPIC	MARKS
Identify that social security contributions when working across the EU and UK should only arise in one state	1
Confirm that Pierre is a Covered Person	1
Identify that the rules on working in two or more States will apply	1
Identify that Pierre will not perform a significant part of his duties in his State of Residence	1
Identify that as this is Pierre's only employment and DesGlaz Ltd is a UK registered company with place of business in the UK, then Pierre will be subject to UK NIC	1
Identify that a Portable Document A1 will need to be obtained	1
Identify that there is a risk that the position could change if French duties increase along with commentary on the implications	1
Likely to pass 2 nd Automatic Overseas Test and therefore non-UK tax resident	1
Subject to tax only on his UK sourced income	0.5
Identify that UK duties are unlikely to be considered incidental	0.5
Confirm that tax treaty will give UK the right to tax UK work duties	0.5
Exemption from UK tax under paragraph 2 will not apply	1
Subject to PAYE on his whole remuneration	0.5
Identify that a s690 application could be made to reduce PAYE liability	1
UK tax return requirement will automatically be created if included on a s690 directive	0.5
Point out that if directive reflects expected working pattern, likely that no PAYE would be due	0.5
Identify that preparation of tax return is a taxable benefit	0.5
Confirm what the taxable value and the reporting requirements	0.5
Identify that the benefit could be included on the PSA for administrative ease	0.5
Outline how the PSA and calculation will operate in practice, including deadlines	0.5
TOTAL	15

ANSWER 4

Requirement 1

Tax position

Anna's UK tax position is dependent on her tax residence position. As she is resident in both Germany and the UK, the Residence Article of the UK / German Double Tax Agreement (DTA) will need to be considered.

Considering each 'test' of the Article in order:

Anna will be resident only of the 'State' where she has a permanent home available to her. As she has a permanent home available to her in both Germany and the UK, consideration will need to be given to the next part of the test, i.e. an individual's personal and economic ties.

Looking at Anna's personal ties: her mother lives in Germany, her social circle is in Germany, and she spends most of her non-work time in Germany including holidays with her son. Her son lives primarily in the UK, but this is because he is at boarding school and not in fact spending this time with Anna. He does spend one week of his holidays with Anna in the UK, which is less than the holiday time they spend together in Germany. Anna is registered to vote in Germany, has a German driver's licence and is a member of her church, and golf club in Germany. Therefore, Anna has stronger personal ties with Germany, when compared with the UK.

Anna's economic ties are balanced between the UK and Germany – she owns homes in both countries, but her other investments are in Germany. Her professional roles are with UK companies, but she spends substantial time carrying these roles out in Germany.

When looking at Anna's social and economic ties as a whole, it can be concluded that she has stronger ties with Germany during the 2022/23 tax year. Therefore, for 2022/23, she should be considered tax resident of Germany and non-resident of the UK under the provisions of the DTA.

Anna's UK tax position will now be determined on the relevant articles of the DTA.

SkinUK plc:

Considering the Employment Income Article of the DTA: whilst Anna will not spend more than 183 days in the UK in any twelve-month period starting or ending in 2022/23 (ignoring her domestic UK residence period), the costs of her employment with SkinUK plc are being borne by the UK company. Therefore, it will not be possible to exempt her UK duties. As a DTA non-resident of the UK, her UK workdays for SkinUK plc will be taxable in the UK.

ShinySkin UK Ltd:

Considering the Director's Income Article of the DTA: it will not be possible to exempt UK duties from UK income tax as this Article does not provide exclusive taxing rights to the state of residence (Germany). Therefore, as a DTA non-resident of the UK, Anna's UK workdays for ShinySkin UK Ltd will be taxable in the UK.

Tax withholding obligations:

Both companies are required to withhold PAYE tax as the companies have a place of business in the UK and Anna is a UK employee. A s690 ITEPA 2003 application can be made to HMRC by each company, to withhold on a reduced percentage of income based on UK workdays. This will help Anna's cash flow position if she makes payments on account in Germany.

Social security position

The provisions of the Trade & Cooperation Agreement 2021 will need to be considered to determine if SkinUK plc are required to withhold / pay UK NIC. These provisions take precedence over domestic rules.

As Anna works in more than one covered country for more than one employer (SkinUK plc and ShinySkin UK Ltd), she will be subject to the social security legislation of the country in which she is habitually resident if she carries out a substantial part of her work activity in that country. For this purpose, substantial means at least 25%. Therefore, German social security would be due on earnings from SkinUK plc and ShinySkin UK Ltd.

Social security withholding obligations:

Both entities would need to register in Germany to facilitate payment of German social security.

An application should be made to the German authorities for an A-1 certificate to confirm that SkinUK plc and ShinySkin UK Ltd do not need to withhold UK NIC.

Requirement 2

<u>PAYE tax reporting:</u>			
SkinUK plc			
UK workdays	60		
Total workdays	264		
UK workday %	22.73%		
Taxable income:			
<u>Item</u>	<u>Total (£)</u>	<u>Reportable (£)</u>	<u>Explanations</u>
Salary	210,000	47,727	Taxable based on UK workday percentage, and subject to monthly PAYE tax
Car allowance	14,400	3,273	
Hotels and subsistence	18,000	4,091	Taxable based on UK workday percentage; not exempt under s373 as resident in prior tax year; no temporary workplace relief as no permanent workplace elsewhere. Likely viewed as 'ordinary commuting'. Subject to grossed up PAYE tax on reimbursement
ShinySkin UK Ltd			
UK workdays	8		
Non UK workdays	16	Includes 12 preparatory days carried out in Germany	
UK workday %	33.33%		
Taxable income:			
<u>Item</u>	<u>Total (£)</u>	<u>Reportable (£)</u>	<u>Explanations</u>
Fees	50,000	16,667	Taxable based on UK workday percentage
Travel allowance	8,000	2,667	Taxable based on UK workday percentage; only paid when travelling to the UK
Airfare and accommodation	7,200	2,400	Taxable based on UK workday percentage; not exempt under s373 as resident in prior tax year; no temporary workplace relief as no permanent workplace elsewhere
<u>NIC reporting:</u>			
No UK NIC reporting requirement for either company if an A-1 has been issued by the German authorities.			

MARKING GUIDE

TOPIC	MARKS
<u>Requirement 1:</u>	
Tax position dependent on residence: domestic resident in both countries: consider DTA Article 4	½
<ul style="list-style-type: none"> • Permanent accommodation • Centre of Vital Interests • Conclusion of tax position under DTA • Tax position for SkinUK plc employment • Tax position for ShinySkin UK Ltd Director role • Tax withholding – general requirement for both companies • s690 ITEPA 2003 • SkinUK plc – Appendix 4 position • ShinySkin UK Ltd – Appendix 4 position 	1 2½ ½ 1½ 1 1 ½ ½ ½
Social Security position: The Trade & Cooperation Agreement 2021 will need to be considered to determine the UK NIC position.	1
<ul style="list-style-type: none"> • Application to Anna's situation • • Social security withholding – both entities to register in Germany • A-1 certificates should be obtained 	2 1 ½
TOTAL	14
<u>Requirement 2:</u>	
Calculations:	
<u>SkinUK plc</u>	
<ul style="list-style-type: none"> • UK workday percentage • Taxable salary and narrative • Taxable car allowance and narrative • Taxable hotels / subsistence and narrative 	½ ½ ½ 1
<u>Shiny Skin UK Ltd</u>	
<ul style="list-style-type: none"> • UK workday percentage • Taxable fees and narrative • Taxable airfare, accommodation and narrative 	1 ½ 1
NIC reporting	1
TOTAL	6

ANSWER 5

Accommodation

If any property owned by an employer is made available for use as living accommodation by an employee a taxable benefit could arise.

If an employer provides an employee with accommodation which qualifies as 'job-related accommodation' under s.99 ITEPA 2003, this will be exempt from tax. To qualify the accommodation must be necessary to enable the employee to perform their duties properly or customary and to allow them to perform their duties better.

To qualify as 'necessary' for the performance of the job the employee would have to demonstrate that the occupation of the property is essential for the proper performance of their duties.

As Greig works fixed hours and is not required to provide cover outside these hours it is unlikely that the accommodation would be necessary for proper performance of his job. Additionally, his contract permits him to reside in the flat, it does not require him to do so.

Therefore, to qualify for the exemption Greig would need to demonstrate the accommodation is provided for 'better performance' of his duties and that it is customary to provide living accommodation to chefs.

Again, as he is not required to work outside his normal working hours it is unlikely that HMRC will accept he needs to live there for better performance of his job. HMRC provide a list of classes of employee who they accept can have customary living accommodation and whilst managers of public houses are listed, chefs are not.

It is therefore unlikely that HMRC will accept the accommodation is job related and it will be taxable.

The taxable value is as follows:

Annual value	£6,000
Additional yearly rent (£275,000 – £75,000) x 2%	<u>£4,000</u>
Taxable benefit	£10,000

As the property cost more than £75,000 there is an additional yearly benefit called additional yearly rent and as it was acquired more than 6 years before it was provided to Greig, the market value on first provision is used.

The taxable benefit of £10,000 should be reported on form P11D for 2022/23. Class 1A NIC of £1,505 (15.05% x £10,000) will be payable by PubDrinks Ltd and Greig will pay tax of £2,000 (20% x £10,000).

Running costs

a. Building Insurance

There is no benefit to Greig as the employer is insuring their property. This is therefore not taxable for Greig.

b. TV

The contract is in employer's name and paid for directly. Therefore the total cost of £600 should be reported on form P11D as a Class 1A NIC benefit. £90 (15.05% x £600) is payable by the company and Greig will pay tax of £120 (20% x £600).

c. Council Tax

As this expense is reimbursed to Greig it should have been taxed via payroll and subject to Income Tax and Class 1 NIC when each reimbursement was made. Tax on each payment for Greig would be £83 (£250 x 20% plus £250 x 13.25%). Employer NIC on each payment would be £38 (£250 x 15.05%) for Pubdrinks Ltd.

The PAYE position should be corrected by Pubdrinks Ltd by submitting an amended FPS with the correct year to date figures for Greig. An amended P60 should be given to Greig if he has already been provided with this.

d. Utilities

As the contract is in the name of the employer and paid for directly, the total value of £2,595 should be reported on form P11D and Class 1A NIC of £391 is payable by Pubdrinks Ltd (£2,595 x 15.05%). Greig will pay Income tax of £519 (£2,595 x 20%).

There is no limit to the amount taxable as the accommodation is not job related.

Mobile Phone

The current treatment with payment subject to PAYE and Class 1 NIC via the payroll is correct.

$£100 \times 12 = £1,200$ is the taxable amount.

If the Company contracted with the provider directly, no benefit would arise as if an employer provides an employee with a mobile phone this is a tax exempt benefit even if the employer is paying for an employee's personal calls

	Item	Rate	Total for Period
A	Payment		£1,200
B	Grossed Up	$A \times 100/66.75$	£1,798
C	Class 1 Secondary on B	$B \times 15.05\%$	£270
D	Total Cost to Employer	$B + C$	£2,009
E	Potential saving for employer	$C \text{ less } A$	£809

It is therefore recommended that the arrangements are changed so that Pubdrinks Ltd contracts with the mobile phone provider directly which would save them £809, per annum.

MARKING GUIDE

TOPIC	MARKS
Accommodation exempt from tax under ITEPA s.99 if it qualifies as job related	½
Exempt if necessary for proper performance	1
Exempt if provided for better performance and customary	1
Consideration if accommodation necessary for Greig	1
Consideration if provided for better performance or customary	1
Conclusion accommodation taxable	½
Calculation of taxable benefit (annual value, additional yearly rent, use of market value)	2
Income Tax and Class 1A NIC due	1
Reportable on P11D	½
Building insurance not taxable	½
Treatment of Sky subscription	1
Council Tax taxable via payroll and subject to tax and NIC	1
Action Pubdrinks Ltd should take to correct	½
Treatment of utilities (Income Tax, Class 1A NIC and reporting on P11D)	½
Mobile phone – current treatment correct	½
Mobile phone – possible exemption and recommendation	1
Calculation of saving	1 ½
TOTAL	15

ANSWER 6

An option to acquire securities by reason of employment is an employment related security (ERS) under legislation (Part 7, ITEPA 2003).

By 6 July following the end of the tax year in which the option was granted (6 July 2019) her employer should have must registered with HMRC to make ERS returns and then filed a return reporting the grant of the option.

By 6 July in each subsequent tax year, the employer must make a further return reporting any reportable events in that tax year or a nil return if there were no such events. As well as the grant of options, the lapse, variation and exercise of options are reportable events. Mandy's exercise of her option would have been a chargeable event for her and should have been reported by 6 July 2022.

As there is a restriction (dividends and votes) on the shares that reduces their market value, the restricted securities legislation will apply which may create additional chargeable/reporting points.

In Mandy's case, as no elections were made, an additional chargeable event occurred when the dividend/voting restriction ceased. This must be reported on the ERS return by 6 July 2023.

As the disposal restriction doesn't affect market value, it doesn't fall within restricted securities legislation. The drag along provisions may or may not affect the market value of the shares and fall within the restricted securities legislation. However, assuming all shares of this class contain the same drag along restriction (which would be assumed), it is unlikely that the drag along restriction will be considered a chargeable event under s429, ITEPA 2003.

If Mandy sells her shares for more than their market value, this may be deemed a chargeable event. However, this is unlikely to apply on a sale of the company to a third party.

The shares can only be sold on a sale of the company. At the time of acquisition of the shares there is no mechanism outlined in which the shares can be exchanged for cash outside of a requirement to sell the shares back to the employer if they leave. The purpose of the scheme is stated to encourage growth in value of the company in anticipation of a future sale, but at the time of acquisition no purchasers have been identified and nothing has been agreed with relation to any potential sale so it is unlikely that this intention itself would constitute a mechanism to exchange the shares for cash.

The shares are therefore unlikely to be deemed to be a readily convertible asset ('RCA') given the shares, when acquired, cannot be exchanged for cash. It should be noted that the company buy back provision is unlikely to constitute a mechanism that HMRC would recognise as making the shares an RCA as in practice the company needs to be position legally to be able to buy back the shares so it cannot be taken as guaranteed at the point of acquisition.

It will be down to Mandy to report the taxable values for each chargeable event on their tax return via Self-Assessment. No PAYE or Class 1 NIC will be due.

It should also be noted that assuming the employer is not under the control of an unlisted company, the shares on acquisition will be deductible for corporation tax. If they were not deductible, then this would have made the shares an RCA.

corporation tax relief will be available on:

- Exercise of the option on the amount constituting employment income
- Chargeable events when restrictions are lifted on the amount constituting employment income
- Costs of administering the scheme including necessary valuations

Corporation tax relief is not available in connection with setting up the scheme as this would be deemed capital.

Chargeable Event on Exercise

The amount subject treated as earnings was the market value less amount paid by Mandy:

Market value subject to restriction (10,000 x £4.50 * 75%)	£33,750
Less: paid by employee (10,000 x £1.00)	(£10,000)
Securities income	£23,750

As no elections were made, 25% of the unrestricted market value (UMV) was not taxed.

As Mandy worked overseas and was non-UK resident during part of the vesting period, relief from UK tax is available (Part 1, Chapter 5B, ITEPA 2003). This is defined as taxable specific income (TSI), which is Specific Income (SI) less Foreign Specific Income (FSI).

The relevant period is 1 October 2018 to 1 October 2021 (date option was acquired to earlier of vest or exercise): 36 months.

During this period, Mandy was non-UK resident for 24 months. Securities income arising during this period that did not relate to UK duties (i.e., 23 months) is FSI.

SI = £23,750

FSI = £23,750 x 23 / 36 = £15,174

TSI: £23,750 - £15,174 = £8,576 which should have been subject to tax and reported on Mandy's UK tax return for the 2021/22 tax year.

Chargeable Event on Lifting of Dividend/Voting Restriction

This was when the securities ceased to be restricted securities. The earnings are calculated as follows:

10,000 x £5 (market value) x the percentage of initial UMV that was not previously subject to tax (25%).

The relevant period for restricted securities is from the date of acquisition to the date of chargeable event.

From 31 December 2021 to 31 December 2022. Mandy was UK tax resident no relief was available.

£12,500 should have been subject to tax and reported on Mandy's UK tax return for the 2022/23 tax year.

On disposal of the shares, outside of any further chargeable events that may occur if the drag along provision is a restriction, Mandy may be subject to capital gains tax on her proceeds less her base cost. Her base cost is the amount she paid for the shares plus any amounts that have been subject to income tax as employment income.

MARKING GUIDE

TOPIC	MARKS
Reporting requirements	
Identify that acquisition of options and shares from an employment are caught as employment related securities	1
Requirement to register and file ERS returns along with general deadline	1
Identify that the shares are caught under the restricted securities legislation with reason	1
Identify each of the reporting/chargeable event dates for Mandy for the scenario concerned:	
Option granted – 6 July 2019	0.5
Option exercised – 6 July 2022	0.5
Restrictions lifted – 6 July 2023	0.5
Restriction of sale not caught under the restricted securities legislation	0.5
Drag along provision may not be considered a restriction if this applies to all other shares in the same class	0.5
Disposal may be caught under restricted securities legislation if restrictions still in place	0.5
Further chargeable and reportable event may occur if the shares are disposed of for higher than market value	0.5
Identifying that the shares are not an RCA with reason	2
Employer not required to operate and report PAYE and Class 1 NIC. Mandy will be required to self-assess the chargeable events via a tax return	0.5
Identify that if a corporation tax deduction is not available then the shares would be an RCA	0.5
Deductions available for corporation tax with examples	1
No relief from corporation tax will be available for costs associated with setting up the scheme	0.5
Comment on how and when the chargeable event on exercise will be taxed	1
Market value on exercise is £33,750	0.5
Less consideration paid by employee	0.5
Note that 25% of the UMV was not taxed	0.5
Identify that rules on IMEs need consideration and that the relevant period for options is grant to vest	1
Taxable specific income = SI - FSI	0.5
Only FSI relating to UK duties will be taxable	0.5
Identify that 1 month will be chargeable on a just and reasonable basis, also allow another reasonable metric if one is given	0.5
Taxable specific income is £8,576	0.5
Further chargeable event subject to tax when restrictions are lifted	0.5

Identify to use market value of £5 when restrictions lift	0.5
Only tax the percentage identified earlier that was not subject to tax (25%)	0.5
Identify that relevant period is different and subsequently there is no FSI	0.5
£12,500 is subject to tax on Mandy's tax return	0.5
Disposal may be subject to CGT	0.5
How cost basis will be determined	0.5
TOTAL	20