

THE CHARTERED INSTITUTE OF TAXATION

APPLICATION AND PROFESSIONAL SKILLS

Human Capital Taxes

May 2021

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.
- Except as set out below or indicated by additional information in the question, you may assume that 2020/21 legislation (including rates and allowances) continues to apply for 2021/22 and future years.

1) You MUST assume that the UK remains within the European Union.

2) You MUST ignore all temporary Covid related legislation including furlough, grants, loans and the reductions in VAT and SDLT rates.

Except in relation to points 1) and 2) above, 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 Tem Finlanda an assistant manager in a firm of Chartered Tax Advisers.

Your client is Rance Grey Ltd, a privately owned business providing marketing campaigns and social media services to a range of businesses in the UK, US and Australia. It has a UK subsidiary, Rance Grey Motor Media Ltd, which has historically run media campaigns for the motor sport industry and which has been loss making for several years.

You and your firm's tax partner, Cody McAmella, recently met with Jinny Barbayas the HR Director of Rance Grey Ltd. Jinny explained that Rance Grey Motor Media Ltd will cease trading and be dissolved. Some employees will be transferred to Rance Grey Ltd and five employees will be made redundant. Additional information on the plans (**EXHIBIT A**) has been provided by Jinny. Cody has also had a telephone conversation with Freya Archibald, the Group Finance Director, (**EXHIBIT C**) regarding the redundancy plans and the finances of both businesses.

Cody has asked for you to prepare a draft report on the redundancy plans for her review.

The following exhibits are provided to assist you:

- EXHIBIT A:** Email from Jinny Barbayas to Cody McAmella
- EXHIBIT B:** Proposed Termination Arrangements
- EXHIBIT C:** Notes of telephone conversation between Cody McAmella and Freya Archibald
- EXHIBIT D:** Email from Freya Archibald to Cody McAmella
- EXHIBIT E:** Pre-seen information

Requirement:

Prepare a draft report to Jinny and Freya, for Cody's review, discussing and making recommendations in relation to the redundancy plans.

Continued

Continuation

EXHIBIT A

Email from Jinny Barbayas to Cody McAmella

To: Cody McAmella
From: Jinny Barbayas
Date: 3 May 2021
Subject: Redundancies

Dear Cody

It was good to see you and Tem on Friday.

As discussed, sadly we're having to make redundant our five most senior and long-serving employees.

Another five employees have already left the business as they have found employment elsewhere. The remaining 10 will be employed by Rance Grey Ltd from 1 September 2021.

Attached are our plans for the redundancy arrangements in Rance Grey Motor Media Ltd (**EXHIBIT B**). My initial plans are to pay the various items separately (option 1) but as the total payment is £50,000 I'm wondering whether it would be simpler to pay a bonus (option 2). I've added what I think is the tax and NIC treatment for each of the options.

We've been lucky that we haven't needed to make anyone redundant at Rance Grey Ltd since the business started in 1994. I last looked at redundancies 12 years ago whilst at my former employer so I would appreciate your review of the summary please.

Thanks for your help and I look forward to hearing from you.

Best wishes

Jinny Barbayas
HR Director

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EXHIBIT B

Proposed Termination Arrangements

Working papers prepared by Jinny Barbayas – May 2021

Current Package

The five employees being made redundant are all on annual salaries of £65,000 and are monthly paid. These salaries are after a 5% salary sacrifice each employee makes in return for employer contributions to our defined contribution pension plan. The employees being made redundant are:

<u>Employees</u>	<u>Start Date</u>	<u>Age</u>
Bill	1 January 2004	57
Harry	15 February 2004	56
Oliver	10 January 2004	52
Rebecca	13 March 2004	55
Eleanor	27 February 2004	51

Their contracts provide for three months' notice and do not include a right to make a payment in lieu of notice. Contracts do not include any entitlement to a payment on termination.

Whilst we have not formally carried out a selection process we have involved all employees in discussions about the plans for the business closure.

Option 1 splits out the component items whereas option 2 is a lump sum.

Timetable

<u>Actions</u>	<u>Expected Timetable</u>
Formal notice to be given to employees (three months)	1 December 2021
Employees expected to finish client facing activity	By 19 December 2021
Employees on annual holiday over Christmas period	20 December 2021 to 4 January 2022
Finish administration and close office	4 to 14 January 2022
Payroll cut-off date for data to payroll team	15 January 2022
Garden leave	15 to 31 January 2022
Date of redundancy	31 January 2022
Payment to be made in payroll	31 January 2022

Proposed Termination Packages

Option 1

<u>Item</u>	<u>Amount</u> £	<u>Tax & NIC</u>	<u>Notes</u>
February salary paid in lieu of notice for February 2022 (non-contractual). £65,000/12	5,416	Tax and NIC free	
Enhanced Redundancy Pay (non-contractual)	20,000	Included in £30,000 exemption, Tax and NIC free	1
Additional termination payment	24,084	Tax and NIC due	2
Restrictive Covenant	500	Tax and NIC free	3
Total	<u>50,000</u>		

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Continuation

Option 2

<u>Item</u>	<u>Amount</u>	<u>Tax & NIC</u>	<u>Notes</u>
Termination Bonus	£50,000	£30,000 tax and NIC free Balance taxable but no NIC	4

Notes

- 1) We do not have a redundancy policy. As all five employees started within a few of months of each other and have very similar roles and levels of salary it seemed a “fair” amount to pay. We are not specifically paying statutory redundancy as the enhanced redundancy package more than covers what it would have been. We calculate statutory redundancy would have been around £10,000 per employee.
- 2) The additional termination pay reflects an extra amount that we want to pay to the employees. We don't have a formal bonus plan or objectives that the employees must meet, so this will be a flat amount for all employees. It isn't based on their years of service. We wanted to pay them an additional amount on top of their enhanced redundancy to round it up to £50,000.
- 3) The only restriction would be to ensure confidentiality.
- 4) We wonder whether it would be simpler to have a total bonus of £50,000 which would be paid to the employees at the end of their employment. This would reflect their service to the business and their hard work over the years. It would also cover the restriction to ensure confidentiality.
- 5) Our private medical scheme costs us £1,200 per year per employee and under both options we will allow employees to stay in the company scheme until 30 June 2022.
- 6) All employees (apart from Bill) are fit and healthy and tell us that they would wish to continue working in similar professions so will be actively seeking new roles. They have all committed that they will remain to close-down the business.
- 7) Sadly, Bill suffered a stroke a few months ago. We have continued to pay him full pay whilst off sick but I have just heard that he will suffer long-term disabilities and will not be able to perform his job going forward. Whilst he is in the list of redundancies, he would not have been able to continue to work due to his disabilities.
- 8) Employees are offered a car allowance of £6,500 per year or a company car. Harry and Oliver have company cars whereas all other employees chose the cash option. The details of the cars included on the 2020/21 P11D forms are as follows:

	<u>Harry</u>	<u>Oliver</u>
Available from:	06/04/2020	06/04/2020
Available to:	05/04/2021	05/04/2021
Car benefit	£12,210	£5,600
Fuel benefit	£zero	£zero
- 9) Harry and Oliver want to buy their cars from us. We are happy with this, perhaps we will sell at a slight discount.

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Continuation

EXHIBIT C

Notes of telephone conversation between Cody McAmella and Freya Archibald

Date: 3 May 2021

Subject: Company cessation

Freya called further to my meeting with Jinny on 30 April 2021.

She shared with me the reasons Rance Grey Motor Media Ltd was now being wound-down:

- 1) Rance Grey Motor Media Ltd was managed by Rance's brother Grange Toms until early 2018.
- 2) The brothers fell out about how the business was run with Rance wanting Grange to make changes to help improve profits.
- 3) They could not agree so Grange left the business in April 2018 to start up his own rival agency.
- 4) Unfortunately, Grange had some excellent client relationships and he was able to take many clients and staff with him.
- 5) The business has struggled since and now it is agreed that the business is no longer viable.
- 6) Rance Grey Motor Media Ltd will cease trading and cessation accounts will be drawn up from 1 January 2021 to 31 March 2022.
- 7) Some junior staff can be hired by Rance Grey Ltd and will be offered new contracts of employment.
- 8) The remaining assets in the business are office and IT equipment which will be transferred to Rance Grey Ltd.
- 9) The company will be dissolved after cessation. A small amount of stock will remain which will be transferred to Rance Grey Ltd.
- 10) The last project will end in December 2021 and we are expecting income for this in March 2022

Freya will send me the latest projected profit figures for both Rance Grey Motor Media Ltd and Rance Grey Ltd plus brought forward loss figures. They haven't previously taken any relief for Rance Grey Motor Media Ltd's losses as they had hoped it would become profitable. Freya asked whether there was any merit to paying the termination payments from Rance Grey Ltd to avoid further increasing the losses in Rance Grey Motor Media Ltd.

Freya was interested in whether there were any good reasons to accelerate or delay the redundancy payments. She said December was a quiet month so perhaps they could close everything down so everyone could finish before the Christmas break.

Cody McAmella

Continued

Continuation

EXHIBIT D

Email from Freya Archibald to Cody McAmella

To: Cody McAmella
From: Freya Archibald
Date: 3 May 2021
Subject: Further to our call

Hi Cody

Further to our call, please find below the latest figures for Rance Grey Ltd and Rance Grey Motor Media Ltd plus details of historic losses for your kind attention.

<u>Projected Profit Before Tax</u>	<u>Year Ended 31 December 2021</u> <u>Rance Grey Ltd</u>		<u>1 January 2021 to 31 March 2022</u> <u>Rance Grey Motor Media Ltd</u>		<u>Notes</u>
	£	£	£	£	
Turnover		46,000,000		2,756,000	
Non-Trading Income		150,000		30,000	1
Less: Cost of sales		<u>(14,500,000)</u>		<u>(650,000)</u>	
Gross Profit		31,650,000		2,136,000	
Bank interest receivable		17,000		0	
Expenditure					
Wages and salaries	13,500,000		1,080,000		2
Depreciation expense	75,000		20,000		
Cash donations to charity	35,000		-		
Motor expenses	940,000		29,000		
Office expenses	<u>3,600,000</u>		<u>975,000</u>		
		<u>(18,150,000)</u>		<u>(2,104,000)</u>	
Profit before tax		<u>£13,517,000</u>		<u>£32,000</u>	

Notes

- 1) Rance Grey Motor Media Ltd received a small amount of property income; the property was sold in 2018 but rent was owed to us by a previous tenant and we received a small amount after an application to the tenant's liquidators.
- 2) Wages and salaries include an accrual for the expected redundancy costs.
- 3) Brought forward trading losses in Rance Grey Motor Media Ltd at 31 December 2020 are £320,000. These have arisen since 1 January 2016.

Do let me know if you have any additional questions and I look forward to receiving your recommendations.

Best regards
Freya

Continued

Continuation

EXHIBIT E

Pre-seen information

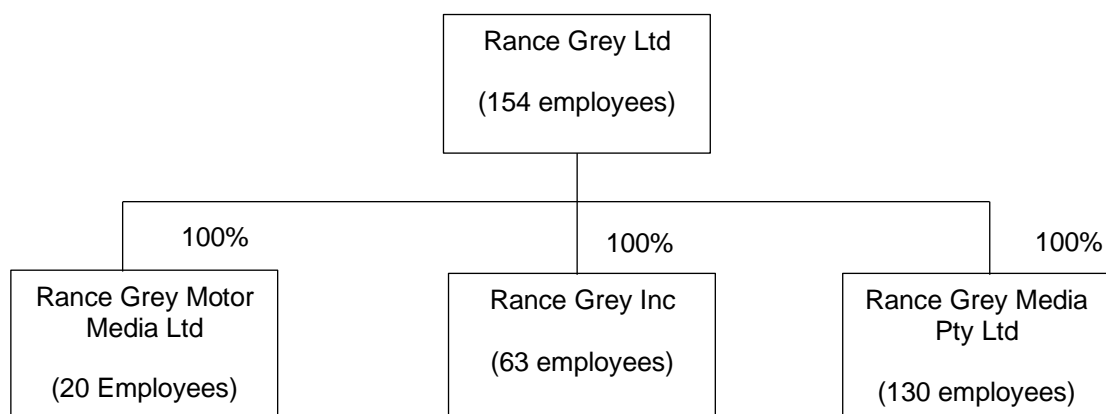
Clients

Rance Grey Ltd and Rance Grey Motor Media Ltd.

Business Description

Rance Grey Ltd is a privately owned digital advertising and media business providing campaigns and social media services to a range of businesses mainly in the UK, US and Australia. It was formed in 1994 and moved from traditional to online advertising and media in 2005.

Group Structure



Rance Grey Inc is incorporated and tax resident in the US.

Rance Grey Media Pty Ltd is incorporated and tax resident in Australia.

Company Ownership

Rance Grey Ltd has 200 ordinary shares of £1 held as follows:

	<u>Number of Shares</u>
Rance Toms	120
Amparo Grey	80

Directors

Managing Director	Rance Toms
Operations Director	Amparo Grey
HR Director	Jinny Barbayas
Finance Director	Freya Archibald

Pension Arrangements

Rance Grey Ltd and Rance Grey Motor Media Ltd each have a defined contribution company pension scheme. Employees may start to receive pension benefits at age 55.

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Continuation

Profit Before Tax Year Ended 31 December 2020

	<u>Rance Grey Ltd</u>		<u>Rance Grey Motor Media Ltd</u>	
	£	£	£	£
Turnover		37,729,650		1,936,490
Non-Trading Income		101,050		-
Less: Cost of sales		<u>(11,750,045)</u>		<u>(229,450)</u>
Gross Profit		26,080,655		1,707,040
Bank interest receivable		14,500		0
Expenditure				
Wages and salaries	12,105,000		880,000	
Depreciation expense	65,850		12,500	
Cash donations to charity	35,000		-	
Motor expenses	921,750		38,150	
Office expenses	<u>3,251,860</u>		<u>824,640</u>	
		<u>(16,379,460)</u>		<u>(1,755,290)</u>
Profit (Loss) before tax		<u>£9,715,695</u>		<u>£(48,250)</u>

Balance Sheets at 31 December 2020

	<u>Rance Grey Ltd</u>	<u>Rance Grey Motor Media Ltd</u>
	£	£
Freehold property	2,400,000	-
Plant & machinery	1,800,500	139,000
Debtors/inventory	850,000	39,000
Bank current account	1,250,000	175,500
Bank deposit account	2,950,000	340,500
Less: creditors	<u>(85,000)</u>	<u>(359,000)</u>
	<u>£9,165,500</u>	<u>£335,000</u>
Capital & Reserves		
Share capital	200	100
Profit & Loss	<u>9,165,300</u>	<u>334,900</u>
	<u>£9,165,500</u>	<u>£335,000</u>