

# THE CHARTERED INSTITUTE OF TAXATION

## APPLICATION AND PROFESSIONAL SKILLS

### Human Capital Taxes

**November 2021**

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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.
- 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 a tax manager in Bootle, Baker & Co, a firm of Chartered Tax Advisers. You report to Rachel Bootle, the Managing Partner in your firm. She has received a letter (**EXHIBIT A**) from Sara Qureshi who is the Finance Director at your client MGB Style Ltd, a clothing retailer.

For the last three years MGB Style Ltd has paid Ordinateur Ltd to assist with the development and upkeep of their website and app. The MGB Style Ltd board of directors has agreed that these tasks should be brought in-house. Accordingly, negotiations have started with the owner of Ordinateur Ltd.

Sara has asked your firm to recommend whether MGB Style Ltd should acquire the shares or the trade and assets of Ordinateur Ltd.

The following exhibits are provided to assist you:

**EXHIBIT A:** Letter from Sara Qureshi

**EXHIBIT B:** Email from George Barnes

**EXHIBIT C:** Extracts from the financial due diligence report on Ordinateur Ltd

**EXHIBIT D:** Pre-seen information

You should assume that the UK/France Double Tax Treaty follows the OECD Model Treaty.

**Requirement:**

**Prepare a draft report to Sara Qureshi recommending how MGB Style Ltd should proceed in relation to Ordinateur Ltd.**

Continued

**EXHIBIT A**

Letter from Sara Qureshi

Rachel Bootle  
Bootle, Baker & Co  
25 Uppingham Road  
Leicester  
LE5 3TB

Sara Qureshi  
MGB Style Ltd  
10 Knightthorpe Road  
Loughborough  
LE11 4JP

29 October 2021

Dear Rachel

Re: Acquisition of Ordinateur Ltd

As we discussed briefly yesterday, we are in negotiations to purchase Ordinateur Ltd. They are an IT consulting company located in Loughborough.

The MGB Style Ltd board of directors considers online shopping to be the key source of future growth for the company. As a result, it is a priority for us to have a strong in-house team rather than rely on external service providers.

We have used the Ordinateur Ltd team to develop our website and mobile shopping app for the last three years. We are happy with their work and they have a good understanding of our company.

Ordinateur Ltd's owner is Ordinateur SA, a large IT consultancy company listed on the Bourse de Paris stock exchange. Their expansion into the UK market with Ordinateur Ltd has not been as successful as they would have liked and 60% of their revenue currently comes from MGB Style Ltd.

Ordinateur SA have agreed to sell us the Ordinateur Ltd business for £1 million. We have yet to agree whether we will structure the acquisition as a share purchase or a trade and asset purchase (we would only acquire the tangible and intangible assets and leave the debtors, creditors and cash). Either way, the price will remain the same.

Following the acquisition the staff of Ordinateur Ltd will continue to sell their services to other customers as at present. We have been assured that they do not have any existing contracts with organisations who are direct competitors to MGB Style Ltd.

Please find enclosed an email (**EXHIBIT B**) from our HR Director. He recently had a meeting with the Ordinateur Ltd Managing Director to gather some information on the employees.

Please also find enclosed extracts from an independent financial due diligence report on Ordinateur Ltd (**EXHIBIT C**). This also contains the latest set of accounts prepared by Ordinateur Ltd.

Please can you review all the information and let me know if there are any tax issues we should be considering. I would be especially interested in your opinion on whether we should purchase the shares of Ordinateur Ltd or seek to buy the trade and assets.

Yours sincerely

Sara

Continued

## **EXHIBIT B**

### Email from George Barnes

From: george.barnes@MGBstyle.co.uk  
To: sara.queshi@MGBstyle.co.uk  
Date: 25 October 2021  
Subject: Ordinateur Ltd People Matters

Hi Sara

Hope you are well. I have just got back from my meeting at Ordinateur Ltd and thought I would share my notes. There were a few surprises!

As we discussed last week, if we buy the trade and assets of Ordinateur Ltd we would bring all the employees across to MGB Style Ltd under the TUPE regulations. They would become our employees but we would have to give them the same terms and conditions as they have right now.

Let me know if you would like to discuss.

Regards

George

### Notes from HR due diligence meeting with Ordinateur Ltd – 25 October 2021

#### Employees

Managing Director and Principal Developer - Francois Du Plessis  
Junior Developers - Jenny Smith, Vinesh Bhatia, Rita Brown  
Office Manager - Chris River

#### Core remuneration items for all staff

Annual salary  
Company car  
Share Option Scheme – see notes below

#### Contractual work location

The contractual work location for all employees is the Ordinateur Ltd office in Loughborough. However, it is not uncommon for Chris River to be the only occupant as all the developers spend time at other client sites.

Francois Du Plessis has an unofficial working from home arrangement. His family home is in the South of France. He flies to and from France each week at his own expense. He usually works from home in France every Thursday and Friday. All other employees live near Loughborough.

#### Payroll management

Chris Rivers runs the payroll in the UK and also prepares the annual forms P11D for the company cars. He has not had any involvement with the share option scheme administration to date and says he doubts anything has been sent to HMRC so far.

#### Share Option Scheme

The share option scheme is administered by the Ordinateur SA French head office team. It is a relatively new scheme set up under French legislation. No UK tax review has been done of the scheme and no HMRC notifications or reporting has been undertaken.

The first options were granted on 2 June 2020 and vested on 1 June 2021. Each of the five Ordinateur Ltd employees was granted options over 100 shares in Ordinateur SA with a discounted option price of £1 per share. On 1 June 2021 each of the shares was worth £10. All employees exercised their options immediately.

A further option grant took place on 2 June 2021. This is scheduled to vest on 1 June 2022, however Ordinateur SA have agreed that they will accelerate the vesting if the transaction goes ahead to allow a clean break with the employees.

#### Contractors

There is one contractor: Brad Flowers. He is a mobile application development specialist who has been working with the team for the last 12 months. He operates through Flowers Ltd in which he is the sole director and shareholder. His company is paid a day rate of £1,000 plus VAT for any day on which he is engaged.

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**EXHIBIT C**Extracts from the financial due diligence report on Ordinateur LtdBackground

Ordinateur Ltd was incorporated on 1 January 2018 as a wholly owned subsidiary of Ordinateur SA. It provides IT consultancy services to the retail industry.

Current Trade

60% of Ordinateur Ltd's annual revenue is generated from a contract with MGB Style Ltd under which it maintains and develops their online shopping platforms. The remainder of its revenue is generated from a variety of non-recurring consultancy projects with other retailers.

Ordinateur Ltd has made a small profit in each of the past three financial years. It is again expected to make a small profit overall for the year ending 31 December 2021.

Tax Matters

All Corporation Tax and VAT returns have been filed within the statutory deadlines. There are no open HMRC enquiries.

Ordinateur Ltd opted to tax their freehold property on acquisition. There has been no qualifying expenditure for structure and buildings allowances since its purchase.

Company Assets and Liabilities

Tangible and intangible assets have been valued as follows:

	£
Freehold property	750,000
Company cars	150,000
Employee laptops	15,000
Other office equipment	50,000
Goodwill	<u>35,000</u>
	1,000,000

The freehold property originally cost £750,000 when it was purchased by Ordinateur Ltd three years ago. There are also trade creditors of £50,000.

Ordinateur Ltd - Income statement for the year ended 31 December 2020

	£
Turnover	900,000
Cost of sales	<u>(250,000)</u>
Gross Profit	650,000
Administrative Expenses	(50,000)
Employment Costs	(450,000)
Other expenses	<u>(100,000)</u>
Profit/(loss) before tax	<u>50,000</u>

Ordinateur Ltd - Balance sheet at 31 December 2020

	£	£
Fixed Assets		
Freehold property	750,000	
Plant and machinery	<u>250,000</u>	
		1,000,000
Current Assets		
Debtors	40,000	
Cash at bank	<u>180,000</u>	
		220,000
Current Liabilities		
Creditors		(50,000)
Long term liabilities		
Mortgage		<u>(170,000)</u>
Net Assets		<u>£1,000,000</u>
Represented by:		£
Share capital		800,000
Profit and loss b/w/d		150,000
Profit for the year		<u>50,000</u>
		<u>£1,000,000</u>

Continued

**EXHIBIT D**

Pre-seen information

Client

MGB Style Ltd.

The company was set up in 1990 to sell clothing through a shop in Leicester. Over the years it has expanded into properties in Birmingham, Nottingham and Northampton. Since 2013 it has also had an online retail presence with a website and mobile app.

The head office and main distribution centre is in Loughborough. All properties are freeholds and owned by MGB Style Ltd.

Ownership

90% of the shares are owned by Malcolm Barnes, the founder of the company.

The remaining 10% are owned by Malcolm's brother, George Barnes.

The directors of the company are:

Malcolm Barnes – Managing Director

George Barnes – HR Director

Sara Qureshi – Finance Director

Employees

MGB Style Ltd has 65 employees. 40 are shop based with the remaining 25 working at the Loughborough premises.

Remuneration items

Annual salary

Employee of the month voucher scheme

Staff discount

VAT

The company was registered for VAT on 1 July 1990 with registration number: 123987456.

No options to tax have been made.

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Financial

The company prepares its accounts to 30 June each year and draft accounts for the year ended 30 June 2021 show the following:

Income statement for the year ended 30 June 2021

	£	£
Sales		15,100,000
Cost of sales		<u>(9,300,000)</u>
Gross profit		5,800,000
Other income:		
Bank interest		50,500
Expenditure:		
Director's remuneration	500,000	
Employment costs	3,750,000	
Other administration costs	<u>425,000</u>	
		<u>(4,675,000)</u>
Net profit		<u>£1,175,500</u>

Director's remuneration and employment costs include employer's National Insurance contributions and company pension contributions.

Balance sheet at 30 June 2021

	£	£
Fixed Assets		
Freehold property	7,500,000	
Plant and machinery	<u>900,000</u>	
		8,400,000
Current Assets		
Stock	5,050,000	
Debtors	1,330,000	
Cash at bank	<u>2,500,500</u>	
		8,880,500
Creditors		<u>(8,700,000)</u>
Net Assets		<u>8,580,500</u>
Represented by:		
Share capital		1,000
Profit and loss b/w/d		7,404,000
Profit for the year		<u>1,175,500</u>
		<u>£8,580,500</u>