Chartered Institute of Taxation
Excellence in Taxation

The Chartered Tax Adviser Examination

May 2019

Human Capital Taxes

Advanced Technical Paper

TIME ALLOWED – 3 ¼ HOURS

- The first 15 minutes is designated as reading time. During this time you may read your question paper and legislation, annotate your question paper and use your calculator. You are not permitted to write in the answer booklet. The Presiding Officer will inform you when you can start writing.
- You should answer all **SIX** questions.
- Start each answer on a fresh page and do not write in the margins.
- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Marks are specifically allocated for presentation.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should tick the appropriate box on the front of each answer booklet.
- Unless otherwise indicated by the provision of additional table information, you may assume that 2018/19 rates and allowances continue to apply for 2019/20 and future years. Candidates referring to actual or pending rates and allowances for 2019/20 and future years will not be penalised.

1. You work as a tax manager in a firm of Chartered Tax Advisers. Your client, Memsie plc, is hiring a new Head of Business Strategy who will be based in their London office. Memsie plc is a multinational group, headquartered in the UK.

Sharon Liu, who has been successful at interview stage, currently works for the Canadian subsidiary and is Canadian resident and domiciled. She would need to relocate to the UK to take up the new role and would become UK resident from the start of her employment. Sharon is concerned about the higher cost of living in the UK. She has no sources of income other than her employment income.

The Head of Human Resources, Malcolm Stratton, has identified two alternative packages which could be offered to Sharon and he would like advice as to which should be offered:

1) Package A: employment on local terms from the outset, or
2) Package B: a tax equalised assignment for an initial two year period.

Under Package B, during the tax equalised period, Sharon's salary would be paid from the Canadian payroll, subject to a hypothetical tax and social security withholding at a combined rate of 30%. A certificate of coverage would be obtained for that period.

Malcolm has experience of tax equalisation and modified payroll but has found it to be expensive and complex. Malcolm has told you that cost is a key concern for the company. Before he decides on which package to offer Sharon, he has asked you to model the costs of both packages using a representative gross salary of £250,000 and comment on the administration aspects of each package. The Canadian payroll team have confirmed that the Canadian employer social security due on the salary of £250,000 is £25,000 per annum.

Malcolm would also like to hear any suggestions which might work well for both Sharon and the company.

Requirement:

Write an email to Malcolm Stratton advising on which package should be offered to Sharon. (15)

2. You are Alan Jones, an Employment Tax specialist in a large firm of accountants. You have just received a call from a colleague in the Corporate Finance team, Frank Carpenter, who requires some assistance with a due diligence exercise.

Frank has provided you with the following facts, which he obtained during a phone call with the company accountant at the target business, Piggiebank Ltd:

1) Between 6 April 2017 and 5 April 2019 the Finance Director, who is not a shareholder, has drawn £1,000 a month from the company without deduction of PAYE or Class 1 NIC. These amounts have been classed as loans by the company. However, the Finance Director's P11Ds have not included any beneficial loan entries and just show company car and medical benefits. The Finance Director is paid a salary of £60,000 per annum which is subject to PAYE and Class 1 NIC via the payroll. It is expected that when the business is sold, the Finance Director will receive a substantial bonus and will use the proceeds from this to repay the loan.

2) The Marketing Director's wife was paid £100 per week from 6 April 2017 up to 5 April 2019, without any PAYE or Class 1 NIC deductions. She did not undertake any work for the business. The Marketing Director is paid a salary of £80,000 per annum which is subject to PAYE and Class 1 NIC via the payroll.

3) There is a yacht shown in the accounts, which was purchased new for £650,000 on 6 April 2017 for the purposes of client entertaining. However, no clients have actually been entertained on the yacht. The only use has been by the Managing Director and his family, who have used it for five weeks each year for holidays. The running costs of the yacht are £24,000 per annum. The Managing Director receives a salary of £200,000 per annum which is subject to PAYE and Class 1 NIC via the payroll. No benefit in relation to the yacht has been declared on his P11D.

Your colleague wants to understand if there are any potential PAYE and National Insurance issues arising in relation to the above.

Requirement:

Prepare an email to Frank Carpenter advising on any PAYE and National Insurance issues in relation to the three points identified by him. (15)

3. You are the employment taxes specialist in a large accountancy firm. You have received the following email from the HR Director at Longbentons Ltd, who have been a client of your firm for many years.

To: John Briggs
From: Neville Stott
Date: 14 April 2019
Subject: Site Closure

Dear John

As you know we have been discussing the re-organisation of the business for some time. The Board made the final decision last week to close the Norwich site within the next four months and move all manufacturing to the Ipswich site.

There are 20 staff at the Norwich site and we would like all of them to move to the Ipswich site. We have put together some suggestions of how Longbentons Ltd may ease the transition for the employees and I would like confirmation from you that these suggestions would be tax efficient. The Finance Director has already made it clear that there is no budget for the company to fund any tax or National Insurance costs for the staff.

A total of 15 staff live some way to the north of Norwich, which means they are about 60 miles from the Ipswich site and which will mean a round trip commute of around 90 minutes each way. The other five staff live to the south of Norwich around 20 miles from the Ipswich site and their journey would only take 35 minutes each way.

<u>Suggestion 1</u>
We provide a small bus from the Norwich site to the Ipswich site in the morning and evening. We can only do this for about 12 months as once the Norwich site is sold, there will be no parking facilities at this site.

Staff can then either take up Suggestion 2 below for a further year or take up Suggestion 3.

<u>Suggestion 2</u>
We provide a travel allowance of £10 per working day to help cover the additional travel costs. I understand we can do this for two years while Ipswich is a temporary workplace. Staff may take up this option for a short while until they relocate using the allowance under Suggestion 3.

<u>Suggestion 3</u>
We offer a relocation allowance of £5,000 to help with moving costs for employees who want to move closer to the Ipswich site. There is a very good school about eight miles from the Ipswich site. Some employees seem keen to move to within this school's catchment area.

<u>Suggestion 4</u>
Six of the employees to the north of Norwich live very close to each other and there is an idea that we could use a seven-seater MPV, which currently is sitting unused in the car pool. There are three years left on the lease hire and it would be good to make use of it. Could these employees do a car sharing arrangement using this vehicle?

<u>Suggestion 5</u>
One of the employees has asked if they can work from home. They have suggested installing a garden office and have asked if they can use the allowance under Suggestion 3 to help with the set-up costs.

Continued

3. Continuation

I would appreciate it if you could let me know which of the suggestions we can implement without creating additional tax and/or NIC costs for the employees or Longbentons Ltd.

Thanks and Kind Regards

Neville

Requirement:

Prepare an email to Neville Stott advising him on the suggestions he raises for the employees of the Norwich site. (20)

4. You work for a firm of Chartered Tax Advisers which provides tax advice to Oscar plc, a UK headquartered quoted company with a wholly owned subsidiary in Germany, Oscar GmbH. Delia, an employee of Oscar plc, commenced a two year secondment to Germany on 6 April 2019. As Delia is tax equalised on all employment and personal income, the company is concerned that the amount of time Delia is spending in the UK will impact on her UK tax liability and hence the cost for the business.

Delia had not lived or worked overseas prior to commencing her secondment. She is provided with an apartment in Germany. Throughout 2019/20, she is expected to return to the UK each month for four workdays a month. She also expects to spend two weeks in the UK during the summer and a further two weeks in the UK at Christmas. Her partner, with whom she was living prior to commencing her secondment, is remaining in the UK in the home they own jointly. Delia will stay in this home each time she returns to the UK.

Delia's annual remuneration package is as follows:

	£
Salary	40,000
Accommodation benefit (provided locally)	10,000
Private medical insurance benefit	2,000
Bonus	5,000

You understand from your German colleagues that Oscar GmbH is paying German withholding tax to the German tax authorities on all of Delia's cash remuneration under a shadow payroll. You have also been advised that the benefits in kind are taxable in Germany. The marginal rate of German tax is 20%.

Delia has a rental property in France in respect of which she earns profits of £5,000 per annum. This income is taxable in France at 15%. It is also taxable in Germany under domestic provisions.

Requirement:

Explain how Delia will be taxed in the UK during her secondment. You are not required to comment on social security. (15)

NOTE: Relevant extracts from the UK-Germany and UK-France Double Tax Treaties are provided.

Continued

4. Continuation

UK GERMANY DOUBLE TAX TREATY EXTRACT

Article 4

Residence

1) *For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management, place of incorporation or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority of a "Land" or a Contracting State. This term, however, does not include any person who is liable to tax in that Contracting State only if he derives income or capital gains from sources therein or capital situated therein.*

2) *Where by reason of the provisions of paragraph 1 an individual is a resident of both Contracting States, then his status shall be determined as follows:*

   a) *he shall be deemed to be a resident only of the Contracting State in which he has a permanent home available to him; if he has a permanent home available to him in both Contracting States, he shall be deemed to be a resident only of the Contracting State with which his personal and economic relations are closer (centre of vital interests);*

   b) *if the Contracting State in which he has his centre of vital interests cannot be determined, or if he does not have a permanent home available to him in either Contracting State, he shall be deemed to be a resident only of the Contracting State in which he has an habitual abode;*

   c) *if he has an habitual abode in both Contracting States or in neither of them, he shall be deemed to be a resident only of the Contracting State of which he is a national;*

   d) *if he is a national of both Contracting States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.*

3) *Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.*

4) *If the place of effective management of a shipping enterprise is aboard a ship, then it shall be deemed to be situated in the Contracting State in which the home harbour of the ship is situated.*

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.*

Continued

4. Continuation

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.*

Article 21

Other Income

1) *Items of income beneficially owned by a resident of a Contracting State, wherever arising, which are not dealt with in the foregoing Articles of this Convention shall be taxable only in that State.*

2) *Notwithstanding the provisions of paragraph 1, the following provisions shall apply with respect to income paid out of trusts or the estates of deceased persons in the course of administration:*

   Where such income is paid to a beneficiary who is a resident of Germany by trustees or personal representatives who are residents of the United Kingdom out of income received by those trustees or personal representatives which would, if those trustees or personal representatives had been residents of Germany, have fallen within other Articles of this Convention, the beneficiary shall be treated as having received an amount of the income received by the trustees or personal representatives corresponding to the income received by him and any tax paid by the trustees or personal representatives on that amount shall be treated as having been paid by the beneficiary.

3) *The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Article 6, if the recipient of such income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein and the right or property in respect of which the income is paid is effectively connected with such permanent establishment. In such case the provisions of Article 7 shall apply.*

4) *Where, by reason of a special relationship between the person referred to in paragraph 1 and some other person, or between both of them and some third person, the amount of the income referred to in paragraph 1 exceeds the amount (if any) which would have been agreed upon between them in the absence of such a relationship, the provisions of this Article shall apply only to the last mentioned amount. In such a case, the excess part of the income shall remain taxable according to the laws of each Contracting State, due regard being had to the other applicable provisions of this Convention.*

5) *No relief shall be available under this Article if it was the main purpose or one of the main purposes of any person concerned with the creation or assignment of the rights in respect of which the income is paid to take advantage of this Article by means of that creation or assignment.*

Continued

4. Continuation

UK FRANCE DOUBLE TAX TREATY EXTRACT

Article 6

Income from Immovable Property

1) *Income derived from immovable property (including income from agriculture or forestry) situated in a Contracting State may be taxed in that 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, aircraft and railway vehicles 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.*

5) *Where shares or other rights in a company, other legal person, partnership, trust or any similar body give an entitlement to enjoy immovable property situated in a Contracting State and held by that company, other legal person, partnership, trust or similar body, income derived from the direct use, letting, or use in any other form of that entitlement to enjoy, may be taxed in that State notwithstanding the provisions of Article 7.*

End of Question

5. You are the employment tax specialist in a large firm of business advisers. You have received an email from a colleague in the legal department.

To:	Alison Havers
From:	Jose Marchant
Date:	26 April 2019
Subject:	Termination Payment

Hi Alison

We have been asked to advise on a termination payment which is to be made to Steve Jones, an employee of Ecmo Ltd. Ecmo Ltd is the UK subsidiary of Ecmo SA, a Gabonese company, and has been a client for many years.

Steve joined Ecmo Ltd on 1 July 2007 and lived and worked in London until 1 May 2014 when he was seconded to Ecmo SA in Gabon. Due to a restructuring of the business, Steve will be made redundant on 31 July 2019 and notice will be given to him on 1 May 2019. His notice period is six months.

Whilst he has been on secondment, he has been not tax resident in the UK and tax resident in Gabon. He is not currently liable to UK National Insurance.

Two options are being debated by the company:

1) Terminate his secondment at the end of May and bring him back to the UK. His UK employment contract will then be terminated on 31 July.

2) Terminate the secondment and the employment contract together on 31 July, whilst still in Gabon.

Steve prefers Option 2 as he does not wish to return to the UK. The client believes he has been made a job offer by another Gabonese company, which would mean he would continue to live and work in Gabon. However, if Option 1 took place the Gabonese job offer would have to be withdrawn due to work permit restrictions, as Steve would not be allowed to return to Gabon.

There are two alternative redundancy packages:

<u>Option 1</u>

Redundancy per company policy	One month's base salary per full year of service
Statutory UK redundancy	£6,245, already included in redundancy figure above
Pay in lieu of notice	Three months' base salary

<u>Option 2</u>

Statutory Gabonese redundancy	1/5th of a month's assignment pay per month of Gabonese service
Damages	£15,000
Pay in lieu of notice	Three months' assignment salary

<u>Current pay package</u>

Base salary	£240,000
Assignment salary	£246,000 (paid instead of base salary whilst on assignment)

Continued

5. Continuation

The Gabon tax adviser has already advised, that under both options, tax will be due in Gabon. As Steve had spent more than five years in Gabon, the total termination package is liable to Gabonese tax and social security, even if it is paid after Steve has left Gabon or ceased Gabonese tax residence.

Gabonese tax and social security:

Option 1		Option 2	
	£		£
Tax	75,000	Tax	64,575
Employee's social security	14,000	Employee's social security	12,500
Employer's social security	14,000	Employer's social security	12,500

There is neither a double tax treaty nor a social security reciprocal agreement between the UK and Gabon.

It has also been confirmed that under Option 1, Steve will become UK tax resident for 2019/20. We expect that Steve will find work in the UK fairly easily and will therefore be an additional rate taxpayer in 2019/20.

Under Option 2, Steve will not become UK tax resident for 2019/20. He will remain Gabon tax resident, assuming he takes up the new job and continues to live in Gabon. He has no other UK taxable income.

Option 2 factors in Gabon employment law, which means Steve has more redundancy rights and consequently a higher redundancy package. It would therefore be our legal team's advice to go for Option 1. However, I would value your opinion as there may be tax and National Insurance implications, which we have not considered.

Requirement:

Write a memo to Jose Marchant explaining the UK Income Tax and National Insurance treatment of both packages and making any appropriate recommendations. (15)

6. You work in the Human Capital department of a medium-sized firm of accountants and you have just had a meeting with Alex Peters, the Compensation and Benefits Manager of Bugfix Ltd. Alex has recently been appointed and is concerned as to whether the company is dealing correctly with employee childcare.

Bugfix Ltd is a wholly UK-based company with about 200 employees. The share capital of Bugfix Ltd is wholly owned by its two directors, who are husband and wife.

At the meeting you established that:

1) Each director has received a cash allowance of £238.33 a month free of tax and NIC since April 2010, to help pay for a live-in nanny at their house to look after their two children.

2) Childcare vouchers are available to all employees. The number of participants per year and their marginal tax rate are as follows:

Tax year	Higher rate	Basic rate	Total
2010/11	5	10	15
2011/12	5	10	15
2012/13	7	13	20
2013/14	7	13	20
2014/15	9	15	24
2015/16	12	20	32
2016/17	12	20	32
2017/18	15	25	40
2018/19	15	30	45

The increase in participation over the years has been due to new employees joining the scheme. No employees have moved between tax bands over the years. All employees have always received £55 per week in vouchers and paid for these via a salary sacrifice arrangement. The employee benefits from the tax and employee's NIC saving on the amounts sacrificed and the employer saves secondary Class 1 NIC. The employer has in all cases agreed that the employee can keep all of their tax and NIC saving and in return the employer keeps all of the employer's NIC savings and so does not make a charge to the employees for running the scheme. There have been no new entrants to the scheme since September 2018.

All participants have other benefits and so a P11D is prepared for them. However, no amounts have been declared on them in respect of the childcare vouchers, nor included in the payroll for tax and NIC deduction purposes.

Five employees use the same children's nursery and have recently been having trouble with their provider, who is refusing to accept any more childcare vouchers. They have therefore contacted Alex requesting support with childcare at the company premises. There is some space available on site from where a workplace nursery could be run. Alex is considering this request but is unclear on the benefit in kind rules if they were to do this.

Alex is aware that all of the children are still of school age, but is nervous about whether the children of at least two of the employees qualify. These employees are divorced and the children live with the employee's partner but the employees still support the children financially.

It was agreed that you would write to Alex advising him on the childcare arrangements in place and on any planning that may be appropriate.

Requirement:

Draft a letter to Alex Peters advising him on the employer-provided childcare arrangements in place and on any appropriate planning. (20)