

Answer-to-Question-_1_

To: Frederica

Subject: Daniel's UK tax residency position

Part 1

An individual's UK tax residency position is determined using the statutory residence test (SRT). The SRT consists of the automatic overseas tests, the automatic UK tests and the sufficient ties tests, which are hierarchical and apply in that order.

A person is automatically overseas resident if:

- i. they were resident in the UK for at least 1 of the previous 3 tax years and spend less than 16 days in the UK in this tax year;
- ii. they were not resident in the UK for any of the previous 3 tax years and spend less than 46 days in the UK in this tax year; or
- iii. they work sufficient hours overseas with no significant break from overseas work, and spend less than 91 days in the UK in the tax year, of which fewer than 31 days are work days.

'Sufficient hours' means a day in which at least 3 hours of work took place. A 'significant break' from overseas work is a period of at least 31 days in which a person would have worked overseas, but didn't due to for example annual leave, sick leave or parental leave.

A person is automatically UK resident if:

- i. they spend at least 183 days in the UK in the tax year;
- ii. they have a UK home; or
- iii. they work full time in the UK.

A person has a UK home if there is a period of 91 consecutive days (of which at least 30 fall in the tax year) in which a person has a home in the UK available to them, and either does not have a home overseas, or does have a home overseas but spends less than 30 days there in the tax year.

A person works full time in the UK if there is a 365 day period in which they work sufficient hours in the UK with no significant break from UK

work, at least 75% of the days in which sufficient hours are worked take place in the UK, and at least 1 of these days is in the tax year.

If a person is not automatically overseas or UK resident, the number of sufficient ties they have to the UK are used to determine if they are UK resident. The number of sufficient ties required depends on whether they were resident in the UK for any of the previous 3 tax years and the number of days they spend in the UK in this tax year.

In the tax year 24/25, whilst Daniel spent 80 days in the UK, 28 of these days were spent in hospital in the UK. A sudden or life threatening illness or injury, such as Daniel's skiing injury, is an example of an exceptional circumstance for SRT purposes. If a person spends days in the UK due to exceptional circumstances, a maximum of 60 days do not count as spent in the UK for SRT purposes. As such, Daniel is only considered to have spent 42 days in the UK in the 24/25 tax year.

Daniel fails the automatic overseas tests as he was tax resident in the UK for one of the previous 3 tax years (being 22/23) and has spent more than 16 days in the UK in this tax year.

Daniel fails the first automatic UK test as he spent less than 183 days in the UK.

Whilst Daniel has a UK home available to him for a 91 day period, he also has a home in Spain in which he spent more than 31 days in 24/25, so he fails the UK home test.

Daniel does not work full time in the UK as he only worked 5 days in the UK in the tax year, meaning he had a significant break from UK work.

Therefore we need to consider the sufficient ties tests. As Daniel was resident in the UK in one of the previous 3 tax years, and spent more than 15 days in the UK but less than 45, he needs at least 4 ties to be UK resident.

Accommodation tie - Daniel fails this tie. Whilst he has a UK accommodation available to him, he has not spent at least 1 night there in the tax year.

Work tie - Daniel fails this tie as he does not work in the UK for at least 40 days in the tax year.

Family tie - Daniels' two children do not create a family tie as they are over the age of 18. Frederica is also not UK tax resident for similar reasons to Daniel (i.e. not enough sufficient ties), despite working 45 days in the UK such that she passes the work tie. As such, Daniel will fail this tie.

90 day tie - Daniel passes this tie as he spent more than 90 days in the UK in one of the previous 2 tax years, being 22/23.

Country tie - Daniel fails this tie as the UK is not the country in which he has spent the most nights in the UK in the tax year.

Daniel only has one sufficient tie with the UK in 24/25, and as such he is not UK resident.

Part 2

If Daniel is UK resident under the SRT for 24/25, he is potentially dual resident in both Spain and the UK. As Spain and the UK have a DTA in place which is in line with the OECD model, Article 4 acts as a tie breaker in determining which country he will be resident in.

Under Article 4, a dual resident person is deemed to be resident in the country in which they have permanent home. As Daniel does have a permanent home in both the UK and Spain (despite not using the UK home), he will be resident in the country in which his personal and economic relations are closer. This is not clear for Daniel, as he doesn't work in the UK or have business interests in the UK, but he does have close family in the UK and retains an interest in English literature.

The next factor to consider will be where his habitual abode is. He doesn't spend any time in his UK home which suggests that this is Spain, but he still only spent 95 days in his Spanish home in the tax year. However, this is likely to determine that he is resident in Spain.

If this is not enough evidence for the tax authorities, a mutual

agreement procedure will take place between HMRC and the Spanish tax authorities where they will decide where Daniel is resident.

Part 3

A UK resident individual is subject to UK tax on their worldwide income and gains on an arising basis i.e. in the period in which they arise.

As Daniel was non-UK resident in 23/24, his income and gains would not have been subject to UK tax, unless they were derived from activities or assets in the UK. If AI-5 is a UK listed company, then the dividends received and capital gain generated would have been subject to UK tax in 23/24 on an arising basis.

As Daniel was previously UK resident (e.g. in 22/23) and was non-resident for one year only (23/24), then in 24/25 he would be deemed as a temporary non-resident individual due to his one year period of non-residence.

Answer to Question 2

Memorandum

To: The Board of Solaris Future SA

Subject: Expansion into the UK

Part 1

A company is tax resident in the UK if it is incorporated in the UK or if it is centrally managed and controlled (CMC) in the UK.

CMC is a concept based on case law such as *De Beers Consolidated Mines vs Howe*. CMC is determined to be where the highest level of management of a company takes place. This is deemed to be where the strategic decisions of the company take place, which is typically in the board meetings, such that CMC is deemed to be where the board meetings take place. However, the location of the board meetings alone does not determine CMC. If a number of the directors are not physically present in the board meetings (i.e. are dialling in), then it may be that they are exercising CMC from wherever they are located. Furthermore, if decisions of the company are actually made elsewhere and merely 'rubber stamped' in the board meetings, then CMC is deemed to take place where the decisions are actually made.

A company can also be subject to UK corporation tax (CT) if it operates in the UK through a permanent establishment (PE). A company has a UK PE if it either has a fixed place of business in the UK, or has an agent in the UK who has and habitually exercises the authority to do business on behalf of the company.

A fixed place of business includes a place of management, a branch, an office, a factory and a workshop, amongst others. A fixed place of business does not create a PE if the activities that take place there are of a preparatory or auxiliary nature. This is broadly where the activities are merely the storage, display or delivery of goods owned by the company.

An agent does not create a PE if they are doing preparatory or auxiliary services, or if they are habitually exercising authority to do business on behalf of the company, but are doing this as part of the agent's ordinary course of business i.e. it is an independent agent who does this for other companies.

If a UK PE is created, the UK PE is subject to the normal CT rules regarding deadlines, filings and preparation of returns. The PE is required to register for CT purposes with HMRC. The PE is taxed in the

UK as if it is a sepearte enterprise to the company itself, such that any transactions between the company and the PE are subjet to the UK transfer pricing rules.

Under the current structure, Solaris does not operate through a UK PE and is not UK tax resident, such that it is not subject to UK tax.

Under option 1, Solaris will not create a PE in teh UK. This is becuae the office premises in London will be let on a short-term basis such that it is not a 'fixed' place of business. As the staff based in the UK will not be negotioating or concluding sales to UK custoemrs, then they are not habitually exercsiing authority to do business on behalf of Solaris, such that they do not create a PE as agents.

Solaris holds some board meetings in teh UK, which creates a potential risk of being UK resident. However, as the majority of the board meetings will be held in Spain and the major strategic decisions will be signed off in Spain, then Solaris should remian non-UK resident.

Under option 2, Solaris UK Ltd (SUK) will be tax resident in theUk due to being incoproated in the UK. SUK will therefore be subject to UK CT on its worldwide income and gains. Given that there are some Spanish directors on SUK's baord, there is a risk of CMC being in Spain. It is imprtant that the baord meetings continue to be held int eh UK and that the Spanish directors are present at the meetings to mitiagate this risk. It is alos important that the strategic decions are made in the meetings themselves (or by the UK directors generally), rather than the board meetings being used to rubber stamp deciosns made in Spain.

To the extent that teh Spanish tax authoriteis deem SUK to be resident in Spain, the tax treaty between the UK adn Spain contains a tie brekaer clause to determine residency. This will mean a mutual agreeemnt procuedure (MAP) will take place between the two tax authorities to determine SUK's residency. One factor they will look at is place of effective management (POEM). This is similar to CMC but looks at where the day to day management deciosnsa re made raterh than the stratgic decions. Provided that the UK management team make the daily deciosn of the company, then SUK should be UK residernt.

Part 2

The UK unallowable purpose (UP) rules are one of the rules used to restrict the amount of interest which is deductible in a UK tax resident company's CT return.

Broadly, a UP is where the loan advanced does not have a commercial purpose i.e. one of the main purposes of the loan provided is to obtain a UK tax advantage. A UK tax advantage is obtained where there is reduced income subject to tax in the UK, which in the context of a loan, is typically where the UK resident company receives deductions for interest expenses.

The portion of the loan which covers SUK's acquisition of an office, plant and machinery, and working capital requirements appears to be a commercial purpose as it is helping SUK to establish itself in the UK. As such, interest on this portion of the loan should be deductible.

However, the portion of the loan used to fund SUK's acquisition of a stake in SR. This is because the loan is being provided by Solaris to SUK, for SUK to purchase a share of a 100% subsidiary of Solaris. Whilst the £30m would be used by SR to support its commercial objectives, there is no reason why Solaris couldn't provide the £30m to SR directly through a loan or as an equity subscription.

As a result of the loan, SUK will have a tax-deductible interest expense of £1.35m per year, which effectively reduces the UK tax liability if SUK by $£1.35m \times 25\% = £337,500$.

There appears to be no commercial objective to providing the loan to SUK to then subscribe for equity in SR, rather than Solaris doing it itself. This suggests that the main reason for providing the loan is to obtain a UK tax advantage through an excess interest deduction in SUK.

As such, this portion of the loan is likely to have a UP, such that the £1.35m of interest deducted in the CT computation of SUK should be disallowed by HMRC.

Part 3

The UK does not levy withholding tax (WHT) on dividend payments made by UK resident companies, such that any dividends paid by SUK to Solaris will not be subject to UK WHT.

It may be the case that Spanish WHT is due on dividend payments received by SUK from its stake in Solaris Research SA (SR). However, given that there UK and Spain double tax agreement (DTA) is in line with the OECD model, the dividend WHT will be limited.

Under Article 10 of the DTA, dividend WHT is limited to 5% to the extent the recipient/beneficial owner directly holds at least 25% of the shares in the paying company.

Given that SUK only holds 5% of SR, the dividend WHT will be restricted to 15%, such that SR will be required to withhold tax of 15% on the gross amount of dividend it pays to SUK.

Answer to Question 4

Part 1

The UK controlled foreign companies (CFC) rules are a piece of anti-avoidance legislation designed to prevent companies from artificially diverting profits out of the UK tax net to low tax jurisdictions.

A foreign company is controlled by a UK person (or company) if the UK parent owns more than 50% of the shares, voting rights, or rights to assets on winding up of the company, or if the UK parent owns more than 40% of the shares, voting rights, or rights to assets on winding up of the company, and another person owns more than 40% but less than 55%.

A CFC charge works by apportioning the profits of the CFC to the UK parent (based on the ownership %) such that the UK resident parent is subject to UK corporation tax (CT) on the profits of the CFC.

However, only the profits of the CFC which pass through one of the 5 gateways are subject to a CFC charge:

1. Profits attributable to UK activities - this *prima facie* applies to all CFCs and subject profits to a CFC charge which arise as a result of UK activities by the CFC.
2. Non-trading finance profits - charges profits which arise from non-trading finance activities such as investing excess cash on behalf of the group.
3. Trading finance profits - charges trading profits from finance activities such as acting as a treasury company for the group.
4. Captive insurance - applies to profits from insurance business.
5. Solo consolidation - generally applies to banks but applies to companies whose accounts are not consolidated with the rest of the group.

Prior to looking at the gateways, there are 5 exemptions that can exempt the CFC from giving rise to a CFC charge:

1. Exempt period exemption - exempts the first 12 months of profits in which the CFC is first subject to the CFC rules, provided that actions are taken to ensure that no CFC charge arises in future periods.
2. Tax exemption - exempts CFCs which are subject to foreign tax which is at least 75% of the equivalent UK tax, based on UK CT principles.
3. Low profits exemption - exempts CFCs with profits of less than £50k, or less than £500k to the extent that less than £50k is non-trading income.
4. Low profit margins exemption - exempts CFCs with profit margins of less than 10% of operating expenditure.
5. Excluded territories exemption - exempts CFCs resident in one of the territories on HMRC's excluded territories list.

Part 2 and 3

Zurich R+D SA, Eire Trading Ltd and Dutchco BV are all wholly owned subsidiaries of London Holdco plc (LH), such that they are controlled in the UK and are therefore CFCs.

Zurich R+D SA - further information is required to determine if this is exempt under the exempt period exemption, the low profits exemption, the low profit margin exemption or the tax exemption. However, Switzerland is not an excluded territory and is sometimes considered as a low tax jurisdiction, such that this could give rise to a CFC charge for LH. In any case, the profits of Zurich are generated from exploiting the IP of the group, which are excluded from a CFC charge under s371DJ, such that no CFC charge should arise.

Eire Trading Ltd - this is an exempt CFC under the low profits exemption as its profits are less than £500k.

Dutchco BV - this is an exempt CFC under the tax exemption, as the Dutch tax rate is more than the UK CT rate. This should be confirmed by preparing a tax computation for Dutchco in line with UK CT principles, to ensure that the tax payable in the Netherlands would be at least 75% of the equivalent UK tax. In any case, the Netherlands is an excluded territory such that it will be exempt under the excluded territories exemption.

Both Lux Finco SARL and Cayman Ventures Ltd are controlled from the UK on the basis that both its shareholders are UK resident.

Lux Finco SARL is an exempt CFC as Luxembourg is an excluded territory.

Cayman Ventures Ltd (CV) may be eligible for exemption under the exempt period exemption or low profit margin exemption, subject to further information. It is not eligible for exemption under the excluded territories exemption or low profits exemption (given its £1.6m of profits). It is unlikely to be eligible for the tax exemption as the Cayman Islands are typically considered as a low tax jurisdiction.

As such, we need to consider if the gateways apply to CV.

Trading finance profits, solo consolidation and captive insurance shouldn't apply given CV's activities.

The non-trading finance profits and profits from UK activities gateways should apply given that the profits fully arise from UK activities and

are non-trading finance profits. However, CV qualifies for the exemption for profits from qualifying loan relationships under s371ID of chapter 9 of Part 9A TIOPA 2010. Provided that LH makes a claim to HMRC, 75% of the profits of CV will be exempt from a CFC charge.

A CFC charge is not apportioned to a UK parent which owns less than 25% of the CFC. As LH owns 30%, it will be subject to a CFC charge.

75% of the profits are exempt, so the chargeable profits are $\pounds 1.6\text{m} \times 25\% = \pounds 400\text{k}$.

These are subject to UK CT of 25%: $\pounds 400\text{k} \times 25\% = \pounds 100\text{k}$. This is the total CFC charge.

30% of the CFC charge will be apportioned to LH: $30\% \times \pounds 100\text{k} = \pounds 30\text{k}$.

Therefore LH will be subject to a CFC charge of $\pounds 30\text{k}$ for the y/e 31 Dec, 2024. The CFC charge cannot be reduced by the use of b/f, c/f or group losses.

Answer to Question 9

Memorandum

To: Tax manager of AI Optima group

Subject: Diverted profits tax

Part 1 and 2

Diverted profits tax (DPT) was brought into UK legislation in 2015 and is designed to bring into the scope of UK tax profits which have been artificially diverted from the UK to low tax jurisdictions.

DPT is a separate tax from UK corporation tax and applies at a rate of 31% of the amount of diverted profits. Where a charging notice to DPT is issued, the DPT is due within 30 days after the day the notice was issued.

For DPT to apply, a number of conditions have to be met:

- i. the company is UK resident and has made a transaction or series of transactions with another person, and neither party is a small or medium sized enterprise;
- ii. the participation condition - one of the parties to the transaction was directly or indirectly participating in the management, control or capital of the other party, or the same party was directly or indirectly participating in the management, control or capital of both parties;
- iii. the transaction results in an effective tax mismatch outcome - the transaction results in a tax deductible expense or a reduction in taxable income for one party, and the resulting decrease in tax payable by that party is less than 80% of the resulting increase in tax payable for the other party; and
- iv. the insufficient economic substance condition - it is reasonable to assume that the transaction (or a person's involvement in the transaction) was designed to secure the resulting decrease in tax payable.

AI Optima's transaction structure falls into s86 *Avoidance of a UK Taxable Presence*. This brings it into the scope of DPT. As the group is a multinational group, it is unlikely to qualify as an SME.

This is because Optima (Ireland) Ltd (OI) is not UK resident, carries on a trade and does not have a UK PE, and it is reasonable to assume that the arrangement has been designed to avoid a PE in the UK such that there is no UK CT liability. The tax avoidance condition is met as this arrangement is in place with one of the main purposes being to avoid a charge to UK tax.

The mismatch condition is met as there is no tax being paid in the UK, but tax paid in Ireland of 12.5%, which is less than 80% of the UK CT rate of 25%.

The company (i.e. OI) has a duty to notify HMRC when it falls within the scope of DPT. The notification must be made in writing within 3 months beginning at the end of the accounting period to which the notification relates.

The notification must state the name of the company (the avoided PE) and a description and details of the transactions that took place, as well as stating whether the mismatch condition is met.

HMRC can give a preliminary notice if they believe that DPT should apply to OI. If HMRC do this, they must issue a charging notice to the company within 30 days of OI's reply to the preliminary notice if HMRC think DPT is payable.

Part 3

As OI is subject to tax in Ireland on its profits and also subject to DPT, it could be subject to double taxation. s100 of the DPT legislation deals with this.

Where double taxation has occurred, a 'just and reasonable' credit for the overseas tax is available against the DPT liability.

A credit is also available against DPT if a CFC charge has arisen as a result of OI's profits in Ireland. A CFC charge could arise as OI is not exempt under the tax exemption or excluded territories exemption, and is unlikely to have low profits in the UK due to the substantial sales.

Answer to Question 7

Part 1

The UK transfer pricing (TP) rules aim to mitigate lost revenue for HMRC arising as a result of transactions that are not on arm's length terms.

There is an exemption from the TP rules for SMEs. For these purposes, an SME is a company which employs less than 250 people, has an annual turnover of less than €50m, and/or has an annual balance sheet of less than €43m.

On this basis, Health Solutions Ltd (HUK) should be exempt from the TP rules on the basis that it has less than 250 employees and a balance sheet less than €43 on its balance sheet.

However, it will not be exempt from the TP rules on the basis that it is a wholly owned subsidiary of Health Solutions Inc (HINC), such that it is within HINC's control group, and HINC exceeds the SME exemption thresholds due to its consolidated revenues and balance sheet.

Part 2

R+D services - a markup to the services seems an appropriate TP method on the basis that the services could not be provided by a third-party, such that there is no comparable uncontrollable price (CUP) to benchmark against.

Accounting and payroll - a markup provided on these appears appropriate on that basis that these are low value add services that are not part of the core operations of the business. This could potentially be outsourced to a third-party, so a CUP may be available to benchmark against based on the price of those services by the third-party, which may be more appropriate.

Manufacturing services - a CUP is available based on the prices charged by the independent contract manufacturers, albeit the products are not exactly the same and the contractors are likely to be exposed to more risk. A CUP may be beneficial but on that basis will not be entirely accurate. A transactional split method is best used where the contribution made by the company is unique/valuable and for highly integrated operations. This therefore is an appropriate method given that Health Pvt Ltd has limited risks due to its integrated operations.

Part 3

An Advance Pricing Agreement (APA) is an agreement between HMRC and a company for the arm's length terms of an intragroup transaction. They assess businesses to determine the most appropriate TP method for complex transactions.

One key benefit of an APA is that they can prevent a Mutual Agreement Procedure (MAP) under a double tax treaty being required. A MAP in this context is where the two tax authorities affected by an intragroup

transaction engage with each other to agree an appropriate arm's length (AL) rate for the transaction. This can take time and require a lot of negotiation by tax authorities, which can result in delays for a business when trying to conduct their activities.

Another benefit of an APA is that it is a written agreement with HMRC that applies for a period of typically up to 5 years. This means that a business can have assurance that it will not be subject to a challenge by HMRC within the APA period for the transactions agreed under APA. This can also help with the forecasting for the business.

APAs also have a flexible scope that can be applied to various transactions and TP issues. For the HINC group, given the various complex transactions, an APA could be useful to ensure that the complexity does not lead to potential tax costs, on the basis that the transactions can be agreed with HMRC in advance.

Another benefit is that APAs can be unilateral, bilateral or multi-lateral. This means that the APA can potentially be agreed across multiple jurisdictions to prevent TP issues arising in other countries, such as China, India and Ireland for the HINC group.

A potential drawback is that an APA can be nullified or revoked, or penalties imposed on the company if the terms of the APA are not complied with, or if the assumptions used cease to be valid.

APAs can also take time to agree with HMRC (and other jurisdictions if relevant), providing a period of uncertainty for HINC. HMRC aims to complete the APA process within 18-21 months from the initial application.