Tolley® Exam Training

CTA ADVANCED TECHNICAL PAPER

HUMAN CAPITAL

PRE REVISION QUESTION BANK

FA 2019

May and November 2020 Sittings

PQ726
CTA

Tolley® Tax intelligence from LexisNexis®

INTRODUCTION

This Pre Revision Question Bank for the Advanced Technical Human Capital paper contains 15 exam standard questions (all with answers updated to Finance Act 2019).

Using this question bank

All the CTA exams, with the exception of the Awareness paper, are **3¼ hours** in length. The initial 15 minutes are pre examination reading time and during this time you are permitted to read the question paper and the legislation and **annotate the question paper** but will not be allowed to write in the answer folder. Calculators may be used during this period. There will be an announcement at the end of the fifteen minutes reading time after which you may start writing in the answer folder.

During the 3 hour writing period we recommend you initially **allocate 1.7 minutes per mark** to allow time for a final review stage at the end of each question.

10 mark question = 17 minutes
15 mark question = 25 minutes
20 mark question = 34 minutes

You should attempt each question as if you were in the real exam. Try to **avoid just reading the answers** to **questions** – it is all too easy to nod as you read our answer saying "yes I know that point, yes I understand that advice given" – the test is would you have actually put those points in your answer? You won't find this out unless you **write the answers out** yourself.

Writing "proper" answers also gives you a good idea of how long an exam standard answer will take you to write.

Reviewing your answers

It is essential to read through your answer when you have finished writing it. We thought it might be useful at this stage to pass on some tips about how to review your answers effectively – **before** you look at our model answer.

Remember the first thing the marker will do is read your answer through as a whole – what overall impression are you giving of your ability? Have you put the marker in a good mood as soon as they see your script or are they going to be dreading marking what you have handed in? You want those red ticks to be flowing freely onto your page!

Key **presentation considerations** include spacing your answer out, cross referencing your workings and using subheadings and short paragraphs in written answers.

You may be able to make some small corrections at this review stage – you may find you have missed out a vital word such as "not" or you may at this stage think of another point or two to add while reading your answer. This approach could increase your marks much more effectively than carrying on with the point you were making before you stopped to do this final review.

Perhaps consider giving your answer to somebody else (even a non-tax person) to read. If they can understand the points you are trying to make, your communication skills are fine. Remember that you are writing letters / memos etc for someone else to read, so look at your work from the viewpoint of the reader. Would the reader pay money for your advice?

Reviewing the model answer

In the advanced technical papers it is quite likely that there is no single right answer. The model answer is only one possible solution. You may well have included valid points which are not included in the model answer. Review critically both your answer and the model answer. Are there points in the model answer which you could have included in your answer to get extra marks? Are there points you have included which, with the benefit of hindsight, you should have left out?

CONTENTS

QUESTIONS

CTA EXAMINATIONS

2020

TAX TABLES

INCOME TAX - RATES AND THRESHOLDS

	2019/20	2018/19
Rates	%	%
Starting rate for savings income only	0	0
Basic rate for non-savings and savings income only	20	20
Higher rate for non-savings and savings income only	40	40
Additional and trust rate for non-savings and savings income	45	45
Dividend ordinary rate	7.5	7.5
Dividend upper rate	32.5	32.5
Dividend additional rate and trust rate for dividends	38.1	38.1
Thresholds	£	£
Savings income starting rate band	1 – 5,000	1 – 5,000
Basic rate band	1 – 37,500	1 – 34,500
Higher rate band	37,501 – 150,000	34,501– 150,000
Dividend allowance	2,000	2,000
Personal Savings Allowance		
- Taxpayer with basic rate income	1,000	1,000
- Taxpayer with higher rate income	500	500
- Taxpayer with additional rate income	Nil	Nil
Standard rate band for trusts	1,000	1,000
Scottish Tax Rates(1)	%	%
Starter rate	19	19
Scottish basic rate	20	20
Intermediate rate	21	21
Higher rate	41	41
Top rate	46	46
Scottish Tax Thresholds(1)	£	£
Starter rate	1 – 2,049	1 – 2,000
Scottish basic rate	2,050 – 12,444	2,001 – 12,150
Intermediate rate	12,445 – 30,930	12,151 – 31,580
Higher rate	30,931 – 150,000	31,581 – 150,000
Top rate	150,000 +	150,000 +

INCOME TAX - RELIEFS

	2019/20	2018/19
	£	£
Personal allowance(2)	12,500	11,850
Married couple's allowance(3)	8,915	8,695
- Maximum income before abatement of relief - £1 for £2	29,600	28,900
- Minimum allowance	3,450	3,360
Transferable Tax allowance for married couples and civil partners(4)	1,250	1,190
Blind person's allowance	2,450	2,390
Enterprise investment scheme relief limit(5)	1,000,000	1,000,000
Venture capital trust relief limit	200,000	200,000
Seed enterprise investment scheme relief limit	100,000	100,000
Social investment relief	1,000,000	1,000,000

Notes (1) Scottish taxpayers pay Scottish income tax on non-savings income.

(2) The personal allowance of any individual with adjusted net income above £100,000 is reduced by £1 for every £2 of adjusted net income above the £100,000 limit.

(3) Only available where at least one partner was born before 6 April 1935. Relief restricted to 10%.

(4) The recipient must not be liable to tax above the basic rate. The recipient is eligible for a tax reduction of 20% of the transferred amount.

(5) From 6.4.18, the limit is £2 million, where over £1 million is invested in knowledge intensive companies.

CTA EXAMINATIONS

2020

TAX TABLES

ISA limits	**2019/20**	**2018/19**
Maximum subscription:	£	£
'Adult' ISAs	20,000	20,000
Junior ISAs	4,368	4,260

Pension contributions

	Annual allowance[(1)]	**Lifetime allowance**	**Minimum pension age**
	£	£	
2018/19	40,000	1,030,000	55
2019/20	40,000	1,055,000	55

Basic amount qualifying for tax relief £3,600

Notes (1) The annual allowance is tapered by £1 for every £2 of adjusted income above £150,000 for individuals with threshold income above £110,000. It cannot be reduced below £10,000.

Employer Supported Childcare

Exemption – basic rate taxpayer[(1)]	£55 per week	£55 per week

Notes (1) For schemes joined on or after 6 April 2011 the exempt childcare amounts for higher and additional rate taxpayers (based on the employer's earning assessment only) are £28 and £25 respectively.

ITEPA mileage rates

Car or van[(1)]	First 10,000 business miles	45p
	Additional business miles	25p
Motorcycles		24p
Bicycles		20p
Passenger payments		5p

Notes (1) For NIC purposes, a rate of 45p applies irrespective of mileage.

INCOME TAX - CHARGES

Child benefit charge	**Withdrawal rate**
Adjusted net income >£50,000	1% of benefit per £100 of income between £50,000 and £60,000
Adjusted net income >£60,000	Full child benefit amount assessable in that tax year

INCOME TAX - BENEFITS

Car benefits

Emissions	**2019/20[(1)]**	**2018/19[(1)]**
0 – 50 g/km	16%	13%
51 – 75 g/km	19%	16%
76 – 94 g/km	22%	19%
95 g/km or more	23% + 1% for every additional whole 5g/km above threshold	20% + 1% for every additional whole 5g/km above threshold
165 g/km or more	37%	
180g/km or more		37%

Fuel benefit base figure	**2019/20**	**2018/19**
	£24,100	£23,400

Notes (1) 4% supplement for diesel cars excluding those that meet the Real Driving Emissions Step 2 (RDE2) standard.

CTA EXAMINATIONS

2020

TAX TABLES

Van benefits	**2019/20**	**2018/19**
	£	£
No CO_2 emissions	2,058	1,340
CO_2 emissions > 0g/km	3,430	3,350
Fuel benefit for vans	655	633

	2019/20	**2018/19**
Official rate of interest	2.5%	2.5%

INCOME TAX - SIMPLIFICATION MEASURES

Allowances

	2019/20	**2018/19**
	£	£
'Rent-a-room' limit	7,500	7,500
Property allowance/Trading allowance	1,000	1,000

Flat Rate Expenses for Unincorporated Businesses

Motoring expenses	First 10,000 business miles		45p per mile
	Additional business miles		25p per mile
Business use of home	25 – 50 hours use		£10 per month
	51 – 100 hours use		£18 per month
	101+ hours use		£26 per month
Private use of business premises	No of persons living there:	1	£350 per month
		2	£500 per month
		3+	£650 per month

Cash Basis for Unincorporated Businesses	£
Turnover threshold to join scheme	150,000
Turnover threshold to leave scheme	300,000

CAPITAL ALLOWANCES

Annual investment allowance for plant and machinery (AIA)(1)	100%
WDA on plant and machinery in main pool(2)	18%
WDA on plant and machinery in special rate pool(3)(4)	6%
WDA on patent rights and know-how	25%
WDA on structures and buildings (SBA) (5)	2%

Notes (1) On first £1,000,000 of investment in plant & machinery (not cars) from 1 January 2019 to 31 December 2020 (£200,000 before 31 December 2018 & from 1 January 2021).

(2) The main pool rate applies to cars with CO_2 emissions of not more than 110 g/km (130 g/km for expenditure incurred before 1 April 2018).

(3) The special pool rate applies to cars with CO_2 emissions greater than 110 g/km (130 g/km for expenditure incurred before 1 April 2018).

(4) The special pool rate was 8% prior to 6 April 2019 (1 April 2019 for companies).

(5) The 2% rate applies to expenditure from 29 October 2018 on new qualifying non-residential structures and buildings on a straight-line basis.

100% First year allowances available to all businesses

1) New energy saving plant and machinery, and water efficient plant and machinery (until April 2020).
2) Capital expenditure incurred by a person on research and development.
3) New zero-emission goods vehicles (until April 2021).
4) New cars registered before 31 March 2021 if the car either emits not more than 50 g/km of CO_2 (75g/km before 1 April 2018) or it is electrically propelled.
5) Electric vehicle charging points expenditure incurred from 23 November 2016 until April 2023.

CTA EXAMINATIONS

2020

TAX TABLES

NATIONAL INSURANCE CONTRIBUTIONS

Class 1 limits	2019/20			2018/19		
	Annual	Monthly	Weekly	Annual	Monthly	Weekly
	£	£	£	£	£	£
Lower earnings limit (LEL)	6,136	512	118	6,032	503	116
Primary threshold (PT)/ Secondary threshold (ST)	8,632	719	166	8,424	702	162
Upper earnings limit (UEL)/ Upper secondary threshold for under 21 (UST)(1)/ Apprentice upper secondary threshold for under 25 (AUST)(2)	50,000	4,167	962	46,350	3,863	892

	2019/20	2018/19
Class 1 primary contribution rates		
Earnings between PT and UEL	12%	12%
Earnings above UEL	2%	2%
Class 1 secondary contribution rates		
Earnings above ST (1)(2)	13.8%	13.8%

Notes (1) Rate of secondary NICs for employees < age 21 on earnings between ST&UST is 0%.
(2) Rate of secondary NICs for apprentices < age 25 on earnings between ST&AUST is 0%.

	2019/20	2018/19
Employment allowance		
Per year, per employer	£3,000	£3,000
Class 1A contributions	13.8%	13.8%
Class 1B contributions	13.8%	13.8%
Class 2 contributions		
Normal rate	£3.00 pw	£2.95 pw
Small profits threshold	£6,365 pa	£6,205 pa
Class 3 contributions	£15.00 pw	£14.65 pw
Class 4 contributions		
Annual lower profits limit (LPL)	£8,632	£8,424
Annual upper profits limit (UPL)	£50,000	£46,350
Percentage rate between LPL and UPL	9%	9%
Percentage rate above UPL	2%	2%

OTHER PAYROLL INFORMATION

Statutory maternity/adoption pay — First 6 weeks @ 90% of AWE
Next 33 weeks @ the lower of £148.68 and 90% of AWE

Statutory shared parental pay /paternity pay — For each qualifying week, the lower of 90% of AWE and £148.68

Student Loan — Plan 1: 9% of earnings exceeding £1,577 per month
Plan 2: 9% of earnings exceeding £2,143 per month

Postgraduate Loan — 6% of earnings exceeding £1,750 per month

National living/minimum wage (April 2019 onwards)

Category of Worker	Rate per hour	Category of Worker	Rate per hour
Workers aged 25 and over	£8.21	18–20 year olds	£6.15
21–24 year olds	£7.70	16–17 year olds	£4.35
		Apprentices	£3.90

CTA EXAMINATIONS

2020

TAX TABLES

CAPITAL GAINS TAX

	2019/20	**2018/19**
Annual exempt amount for individuals	£12,000	£11,700

CGT rates for individuals, trusts and estates

Gains qualifying for entrepreneurs' relief/investors' relief	10%	10%
Gains for individuals falling within remaining basic rate band(1)	10%	10%
Gains for individuals exceeding basic rate band and gains for trusts and estates(2)	20%	20%

Notes (1) The rate is 18% if the gain is in respect of a residential property
(2) The rate is 28% if the gain is in respect of a residential property

Entrepreneurs' relief and Investors' relief(1)	**2019/20**	**2018/19**
Relevant gains (lifetime maximum)	£10 million	£10 million

Notes (1) The first claims for investors' relief can be made in 2019/20.

Retail Prices Index

	Jan	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
1982	–	–	79.44	81.04	81.62	81.85	81.88	81.90	81.85	82.26	82.66	82.51
1983	82.61	82.97	83.12	84.28	84.64	84.84	85.30	85.68	86.06	86.36	86.67	86.89
1984	86.84	87.20	87.48	88.64	88.97	89.20	89.10	89.94	90.11	90.67	90.95	90.87
1985	91.20	91.94	92.80	94.78	95.21	95.41	95.23	95.49	95.44	95.59	95.92	96.05
1986	96.25	96.60	96.73	97.67	97.85	97.79	97.52	97.82	98.30	98.45	99.29	99.62
1987	100.0	100.4	100.6	101.8	101.9	101.9	101.8	102.1	102.4	102.9	103.4	103.3
1988	103.3	103.7	104.1	105.8	106.2	106.6	106.7	107.9	108.4	109.5	110.0	110.3
1989	111.0	111.8	112.3	114.3	115.0	115.4	115.5	115.8	116.6	117.5	118.5	118.8
1990	119.5	120.2	121.4	125.1	126.2	126.7	126.8	128.1	129.3	130.3	130.0	129.9
1991	130.2	130.9	131.4	133.1	133.5	134.1	133.8	134.1	134.6	135.1	135.6	135.7
1992	135.6	136.3	136.7	138.8	139.3	139.3	138.8	138.9	139.4	139.9	139.7	139.2
1993	137.9	138.8	139.3	140.6	141.1	141.0	140.7	141.3	141.9	141.8	141.6	141.9
1994	141.3	142.1	142.5	144.2	144.7	144.7	144.0	144.7	145.0	145.2	145.3	146.0
1995	146.0	146.9	147.5	149.0	149.6	149.8	149.1	149.9	150.6	149.8	149.8	150.7
1996	150.2	150.9	151.5	152.6	152.9	153.0	152.4	153.1	153.8	153.8	153.9	154.4
1997	154.4	155.0	155.4	156.3	156.9	157.5	157.5	158.5	159.3	159.5	159.6	160.0
1998	159.5	160.3	160.8	162.6	163.5	163.4	163.0	163.7	164.4	164.5	164.4	164.4
1999	163.4	163.7	164.1	165.2	165.6	165.6	165.1	165.5	166.2	166.5	166.7	167.3
2000	166.6	167.5	168.4	170.1	170.7	171.1	170.5	170.5	171.7	171.6	172.1	172.2
2001	171.1	172.0	172.2	173.1	174.2	174.4	173.3	174.0	174.6	174.3	173.6	173.4
2002	173.3	173.8	174.5	175.7	176.2	176.2	175.9	176.4	177.6	177.9	178.2	178.5
2003	178.4	179.3	179.9	181.2	181.5	181.3	181.3	181.6	182.5	182.6	182.7	183.5
2004	183.1	183.8	184.6	185.7	186.5	186.8	186.8	187.4	188.1	188.6	189.0	189.9
2005	188.9	189.6	190.5	191.6	192.0	192.2	192.2	192.6	193.1	193.3	193.6	194.1
2006	193.4	194.2	195.0	196.5	197.7	198.5	198.5	199.2	200.1	200.4	201.1	202.7
2007	201.6	203.1	204.4	205.4	206.2	207.3	206.1	207.3	208.0	208.9	209.7	210.9
2008	209.8	211.4	212.1	214.0	215.1	216.8	216.5	217.2	218.4	217.7	216.0	212.9
2009	210.1	211.4	211.3	211.5	212.8	213.4	213.4	214.4	215.3	216.0	216.6	218.0
2010	217.9	219.2	220.7	222.8	223.6	224.1	223.6	224.5	225.3	225.8	226.8	228.4
2011	229.0	231.3	232.5	234.4	235.2	235.2	234.7	236.1	237.9	238.0	238.5	239.4
2012	238.0	239.9	240.8	242.5	242.4	241.8	242.1	243.0	244.2	245.6	245.6	246.8
2013	245.8	247.6	248.7	249.5	250.0	249.7	249.7	251.0	251.9	251.9	252.1	253.4
2014	252.6	254.2	254.8	255.7	255.9	256.3	256.0	257.0	257.6	257.7	257.1	257.5
2015	255.4	256.7	257.1	258.0	258.5	258.9	258.6	259.8	259.6	259.5	259.8	260.6
2016	258.8	260.0	261.1	261.4	262.1	263.1	263.4	264.4	264.9	264.8	265.5	267.1
2017	265.5	268.4	269.3	270.6	271.7	272.3	272.9	274.7	275.1	275.3	275.8	278.1

CTA EXAMINATIONS

2020

TAX TABLES

Lease percentage table

Years	Percentage	Years	Percentage	Years	Percentage	Years	Percentage
50+	100.000	37	93.497	24	79.622	11	50.038
49	99.657	36	92.761	23	78.055	10	46.695
48	99.289	35	91.981	22	76.399	9	43.154
47	98.902	34	91.156	21	74.635	8	39.399
46	98.490	33	90.280	20	72.770	7	35.414
45	98.059	32	89.354	19	70.791	6	31.195
44	97.595	31	88.371	18	68.697	5	26.722
43	97.107	30	87.330	17	66.470	4	21.983
42	96.593	29	86.226	16	64.116	3	16.959
41	96.041	28	85.053	15	61.617	2	11.629
40	95.457	27	83.816	14	58.971	1	5.983
39	94.842	26	82.496	13	56.167	0	0.000
38	94.189	25	81.100	12	53.191		

CORPORATION TAX

Financial year	**2019**	**2018**	**2017**
Main rate	19%	19%	19%

EU definition of small and medium sized enterprises	Small (2)	Medium (2)	Extended definition for R&D expenditure
Employees(1)	< 50	< 250	<500
Turnover(1)	≤ €10m	≤ €50m	≤ €100m
Balance sheet assets(1)	≤ €10m	≤ €43m	≤ €86m

Notes (1) Must meet employees criteria and either turnover or balance sheet assets criteria.
(2) Thresholds apply for transfer pricing and distributions received by small companies.

VALUE ADDED TAX

	Standard rate	**VAT fraction**
From 4.1.11	20%	1/6

Limits	**From 1.4.19**	**From 1.4.18**
Annual registration limit	£85,000	£85,000
De-registration limit	£83,000	£83,000

Thresholds	**Cash accounting**	**Annual accounting**
Turnover threshold to join scheme	£1,350,000	£1,350,000
Turnover threshold to leave scheme	£1,600,000	£1,600,000

OTHER INDIRECT TAXES

	2019/20	**2018/19**
Insurance premium tax(1)		
Standard rate	12%	12%
Higher rate	20%	20%

Tobacco products duty	**From 29.10.18**	**Until 28.10.18**
Cigarettes	16.5% x retail price + £228.29 (or £293.95 (2)) per thousand cigarettes	16.5% x retail price + £217.23 (or £280.15 (2)) per thousand cigarettes
Cigars	£284.76 per kg	£270.96 per kg
Hand-rolling tobacco	£234.65 per kg	£221.18 per kg
Other smoking/chewing tobacco	£125.20 per kg	£119.13 per kg
Tobacco for heating from 1 July 2019	£234.65 per kg	N/A

Notes (1) Premium is tax inclusive (3/28 for 12% rate and 1/6 for 20% rate).
(2) The £293.95/£280.15 per thousand cigarettes is a minimum excise duty (if higher than the first calculation).

CTA EXAMINATIONS

2020

TAX TABLES

INHERITANCE TAX

Death rate	40%[1]	**Lifetime rate**	20%

Notes (1) 36% rate applies where 10% or more of the deceased person's net chargeable estate is left to charity.

Nil rate bands

6 April 1996 – 5 April 1997	£200,000	6 April 2003 – 5 April 2004	£255,000
6 April 1997 – 5 April 1998	£215,000	6 April 2004 – 5 April 2005	£263,000
6 April 1998 – 5 April 1999	£223,000	6 April 2005 – 5 April 2006	£275,000
6 April 1999 – 5 April 2000	£231,000	6 April 2006 – 5 April 2007	£285,000
6 April 2000 – 5 April 2001	£234,000	6 April 2007 – 5 April 2008	£300,000
6 April 2001 – 5 April 2002	£242,000	6 April 2008 – 5 April 2009	£312,000
6 April 2002 – 5 April 2003	£250,000	6 April 2009 – 5 April 2021	£325,000

Residence nil rate bands[2]

6 April 2017 – 5 April 2018	£100,000	6 April 2019 – 5 April 2020	£150,000
6 April 2018 – 5 April 2019	£125,000	6 April 2020 – 5 April 2021	£175,000

Notes (2) An additional nil rate band is available where a main residence is passed on death to a direct descendant. Tapered withdrawal for estates > £2million.

Taper relief		
Death within 3 years of gift		Nil%
Between 3 and 4 years		20%
Between 4 and 5 years		40%
Between 5 and 6 years		60%
Between 6 and 7 years		80%
Quick Succession relief		
Period between transfers less than one year		100%
Between 1 and 2 years		80%
Between 2 and 3 years		60%
Between 3 and 4 years		40%
Between 4 and 5 years		20%
Lifetime exemptions		
Annual exemption		£3,000
Small gifts		£250
Wedding gifts	Child	£5,000
	Grandchild or remoter issue or other party to marriage	£2,500
	Other	£1,000

ANNUAL TAX ON ENVELOPED DWELLINGS (ATED)

Residential property value	From 1.4.19	From 1.4.18
>£0.5m - ≤ 1m	£3,650	£3,600
> £1m - ≤ 2m	£7,400	£7,250
> £2m – ≤ 5m	£24,800	£24,250
> £5m – ≤ 10m	£57,900	£56,550
> £10m – ≤ 20m	£116,100	£113,400
> £20m	£232,350	£226,950

STAMP DUTY/SDRT

Stamp duty[1]	- On shares transferred by physical stock transfer form	0.5%
Stamp duty reserve tax[1]	- On agreements to transfer shares[2]	0.5%
	- On shares transferred to depositary receipt schemes	1.5%

Notes (1) Does not apply to UK securities traded on a recognised growth market (eg AIM).
(2) Does not apply to units in UK unit trust schemes or shares in UK OEICS bought from fund managers.

CTA EXAMINATIONS

2020

TAX TABLES

STAMP DUTY LAND TAX

Stamp Duty Land Tax on purchase price / lease premium / transfer value – England & NI

Basic Rate %[(1)(2)(3)]	Higher Rate %[(1)(2)]	Residential[(1)(2)(3)]	Non-Residential
0	3	£0 - £125,000	£0 - £150,000
2	5	£125,001 - £250,000	£150,001 - £250,000
5	8	£250,001 - £925,000	£250,001 +
10	13	£925,001 - £1,500,000	N/A
12	15	£1,500,001 +	N/A

Notes (1) The basic rates are increased by 3% where the purchase is of an additional residential property for individuals (see column 2 for the rates that apply). Companies and trusts pay the additional 3% on all purchases of residential properties, subject to note 2 below.

(2) Companies pay 15% on purchases of residential property valued > £500,000.

(3) First-time buyers purchasing a single dwelling as their only or main residence on or after 22.11.17 may benefit from a reduced rate. (This includes qualifying shared ownership properties.) SDLT will not be due on properties up to £300,000. For homes up to £500,000, SDLT will be payable on £200,000 at 5%. Homes bought for more than £500,000 will incur the rates as per column 1 of the table above.

New leases – Stamp Duty Land Tax on lease rentals – England & NI

Rate (%)	Net present value of rent	
	Residential	**Non-residential**
Zero	Up to £125,000	Up to £150,000
1%	Excess over £125,000	£150,001-£5m
2%		Over £5m

Land and Buildings Transaction Tax (LBTT) on purchase price – Scotland

Basic Rate %[(1)(2)(3)]	Residential	Rate %[(1)(4)]	Non-Residential
0	up to £145,000	0	£0 - £150,000
2	£145,001 - £250,000	1	£150,001 - £250,000
5	£250,001 - £325,000	5	£250,001 +
10	£325,001 - £750,000		
12	£750,001 +		

Notes (1) Rates are charged on the portion of consideration that falls in each band. The same tax is payable for a premium granted for a land transaction, except for residential leases which are generally exempt. Special rules apply to a premium for non-residential property where the rent exceeds £1,000 a year.

(2) An additional amount of tax equal to 4% (for effective dates on or after 25 January 2019) of the relevant consideration applies broadly to purchases of an additional dwelling by individuals and trusts (over which the beneficiary has substantial rights) and to purchases of a dwelling by certain businesses, companies and other trusts. Where the effective date is on or after 25 January 2019 but the contract was entered into prior to 12 December 2018, the 3% (prior) rate will apply.

(3) For contracts entered into after 8 February 2018, where the effective date of the transaction is on or after 30 June 2018, there is a relief for first-time buyers where a 0% rate is applied to the first £175,000 of the purchase consideration.

(4) These rates apply where the effective date is on or after 25 January 2019. Prior to this date the 0% band was the same, £150,001-£350,000 was 3%, £350,001+ was 4.5%.

New leases – Land and Buildings Transaction Tax (LBTT) on lease rentals - Scotland

Rate (%)	Net present value of rent[(1)]
	Non-residential
Zero	Up to £150,000
1%	£150,001+

Note (1) Residential leases are generally exempt

QUESTIONS

1. You work in the tax department of a firm of Chartered Accountants. Your manager, Jack White, receives an email on 18 November 2020 from Keith Silver. He is the Payroll Manager at your client, Thissop Ltd and he has some queries relating to some apparent payroll irregularities which occurred in 2019/20.

Your manager forwards the email to you. It reads as follows:

“To: jackwhite@taxrus.com
From: ks@thissop.co.uk
Date: 18 November 2020
Subject: Urgent: PAYE issues

Hi Jack

Thissop Ltd encountered some financial and operating difficulties in 2019/20, including losing a number of our payroll staff. This has forced me to leave most of the payroll activity to Josh, our payroll and administration apprentice.

I have only recently had the opportunity to review his work and have found the following:

1 A number of late deductions of tax and NIC were paid to HMRC via PAYE during the year. The late payments occurred in respect of the May, August, September, November and December pay periods in 2019 and also the February 2020 pay period. All the returns were, however, submitted on time.

2 It looks as though we haven’t reported the five directors’ bonuses paid in December 2019 on their P60s. This has only come to light because HMRC opened an enquiry into the return of Steve Simons, our Managing Director, and Steve has contacted me to let me know that they’ve spotted the error regarding his missing bonus. Josh says he realised they were missing but didn’t know what to do about it, so he just left them out. We haven’t paid the tax or NIC for the bonuses over to HMRC yet as we’re having a bit of a cashflow crisis. At this stage I don’t think we’ll be able to make the payments until January 2022.

I know we will have to pay interest on the late payments, but can you get back to me regarding our exposure to penalties for these matters?

Can you also let me know what Josh should have done when he spotted the omission? It will be a good learning experience for him.

Thanks in advance for your response.

Keith”

Requirement:

Draft a response for Jack to Keith’s email. (10)

2. Transcoastal Freight Ltd (TFL) is a small coastal freight operator based in Southampton. It has recently started to sell its services into French ports. This expansion means that more crew members are needed. One of the new crew members recruited is a French deckhand, Pascal.

Pascal arrives in the UK on 28 April 2020 in order to take up duty on 1 May 2020. His base will be the Southampton freight depot and he will be required to form part of the crew four days a week to assorted destinations around the UK and French coasts as required by the freight manager.

The freight manager forecasts that Pascal will form part of the crew making a voyage to France three times a month, always leaving on one day and returning on the next day.

Pascal is domiciled in France and has only ever visited the UK for a week or so in total, in the past ten years. On 28 April 2020 he buys a small dilapidated property close to Southampton. He is giving up the lease on his apartment in Lille on 31 May 2020. He intends to spend all his available time off work for the next year or so, renovating his new home in the UK. He is entitled to four weeks' annual leave, which he will take in a single block over Christmas. His place on all voyages during that period will be assigned to another crew member.

Requirement:

1) Explain whether TFL should deduct tax under PAYE on the whole of Pascal's earnings or just on the earnings relating to the days he spends on voyages to UK ports.

2) Discuss whether the split year rules apply to Pascal's residence position.

You are not required to comment on National Insurance Contributions. (15)

3. Ayushi Sharma works for an HI International plc (HII), an aerospace company. She joined the company as part of their graduate intake on 1 July 2019. Between leaving University and starting work at HII she worked increased hours at the job she'd previously had on a part-time basis at a local multiplex cinema. The 'student loan deductions' box had been ticked on her P45 from the cinema. Ayushi has confirmed that her student loan was taken out in September 2015.

   Her starting salary at HII is £22,000 and the company pays for her private medical insurance at a yearly premium of £600, a benefit which it payrolls. She received a 'welcome payment' of £800 with her first salary payment. She is paid monthly.

   In September 2019, she complains to the payroll department because she had money deducted from her July pay as a student loan deduction, and she did not think she earned enough for that to happen. She thought HII had noticed their mistake when no deduction was made in August but would like to know when she will get a refund of the money deducted in July.

   Requirement:

   Draft a response for HII to send to Ayushi addressing her complaint. (10)

4. You (Simon Robart) have received an urgent email from Dennis Wyatt, one of the directors at Samphire Ltd. Samphire Ltd is a recently established company which has engaged your firm to advise it on all tax and compliance matters.

To: Simon.robart@taxfirm.co.uk
From: Dennis.wyatt@samphire.co.uk
Date: 9 April 2020
Subject: PAYE and placed workers

Dear Simon

As you know, our company has recently been set up as a facilities management agency. We aim to provide a comprehensive service to help clients fill staff vacancies, cover temporary roles and provide facilities management services generally for short-term or long-term projects.

You have already helped us with advice on setting up a PAYE scheme in respect of our directors and the staff we have taken on to man the office. My understanding was that we would have to deduct tax and national insurance from the workers that we find to fulfil clients' requirements, but I am now not clear about whether and for whom we should be doing that. A few of the people we have placed with clients have refused to fill in starter questionnaires saying that our PAYE scheme won't apply to them.

The people who have refused to complete the PAYE starter questionnaire are:

- Alison Eddowes: we placed her with a local hotel for 5 days as a temporary receptionist.
- Dermot Flynn: he is a close-up magician we have provided to a local theme park as they wanted someone to entertain the queues. His contract is for 3 months.
- Dilnott Ltd: who provided ten workers to be stewards at the 4-day beer festival this week.
- Mohammed Khalid: an IT specialist engaged to install wi-fi and point-of-sale facilities for the beer festival.

In each case we have a contract with our client to find a person to fit their requirements. We find the appropriate worker(s), invoice the client for their services and pay the workers/ the provider of workers ourselves.

Can you please explain how we decide which workers we should bring into our PAYE scheme and why? Do we have to tell HMRC about those workers we do not deduct tax and NIC from?

Kind regards

Dennis Wyatt

Requirement:

Reply to the email from Dennis Wyatt. (15)

5. A new non-executive director is being appointed to the main board of Bigelow plc. The HR team are planning to meet with your tax partner to discuss whether the non-executive director will be liable to UK tax and national insurance contributions. In advance of the meeting, they have provided the following facts about the director:

1 He is a non-UK national.

2 He holds a contract with Bigelow plc, a UK incorporated company.

3 He is tax resident in a country that taxes worldwide income and does not have either a double tax treaty or a reciprocal social security agreement with the UK.

4 He currently holds no other UK directorships, but has done so in the past five years. He has not previously been UK tax resident.

5 He will attend Board meetings and other committee meetings in Bigelow plc's London office, and will also travel to other parts of the UK and overseas locations as required.

6 He is expected to spend 15 days in the UK in 2020, 39 days in 2021, and around 55 days per year thereafter.

7 The director will pay his own air fares to the UK; all other costs will be picked up directly by Bigelow plc.

Requirement:

Prepare a briefing note for your tax partner dealing with the queries raised by the HR team. (15)

6. Your firm is the tax adviser to Aeratech Ltd (AUK). AUK has always traded from within the UK, but recently decided to take advantage of new trading opportunities by setting up a subsidiary in Yeswain, Aeratech Yeswain Ltd (AY).

AY is going to need short-term support from the UK based workforce of AUK. AUK is prepared to offer some of its UK based employees secondments to AY in Yeswain. Whilst in Yeswain, these staff will help train the staff of AY. After the secondments, the staff will return to their UK duties.

AUK has approached your firm to ask for your advice about how to explain to their staff the UK tax implications of these secondments.

The proposals are:

1 Staff will be seconded to AY for 18 months at a time. Start dates for each secondment will be 1 January or 1 July.

2 Seconded staff will work full-time for AY in Yeswain, have no UK duties and will be paid in Yeswain Dollars (Y$) by AY.

3 All benefits and expenses of the Yeswain secondment, as listed below, will be arranged and paid for by AY.

4 Expenses of travel will include the costs of travel between the UK and Yeswain at the start and end of the 18 month secondment and also one trip per month between the UK and Yeswain, either for seconded staff or their relatives.

5 Yeswain has no public health system, so private medical insurance will be provided throughout the secondment.

6 A rented apartment will be provided for the use of each seconded employee and their family throughout the secondment.

7 It is anticipated that employees owning homes in the UK may wish to know the UK tax implications of any disposal of the property while they are on secondment.

8 AUK has confirmed that all staff to be seconded are currently classified as resident within the UK and have been for some time. They are all domiciled within the UK.

9 Yeswain is situated outside the EEA. It has no UK double tax treaty and no reciprocal social security agreement with the UK.

Requirement:

Draft a guide for use by the Human Resources department of Aeratech Ltd on the UK personal tax and National Insurance implications of the proposed overseas secondments. (20)

7. Patrick England is the Managing Director and majority shareholder of Fibrotech Ltd, a technology company based in the Republic of Ireland.

A decision has recently been taken to develop Fibrotech Ltd's activities within the UK. Fibrotech's Sales Manager Kieran Clarke, will accordingly relocate to London to oversee the initial phase of this project. This is expected to take between 18 months and two years.

It is likely that additional support and sales staff will be seconded to the UK from Head Office in the Republic of Ireland for short periods while the London office is being established. Some employees will be seconded to the UK for 2 months; others will be seconded to the UK for 4 months.

Although Kieran Clarke will spend most of his time in the UK, he will also spend at least 2 months each year visiting customers in Europe. This is not anticipated to include any time in the Republic of Ireland.

Patrick England is in London to meet a potential UK client next week. While he is here, he will visit your office for a meeting with your Tax Partner to discuss any UK income tax and national insurance issues arising for Fibrotech Ltd from the various secondments. Your Tax Partner has therefore requested that you provide him with some briefing notes for him to read prior to the meeting.

An extract of the UK/Ireland DTA is attached.

Requirement:

Prepare the appropriate briefing notes in advance of your Tax Partner's forthcoming meeting with Patrick England. (20)

<u>EXTRACT FROM UK / IRELAND DOUBLE TAXATION AGREEMENT</u>

<u>ARTICLE 4</u>
<u>Fiscal Domicile</u>

(1) For the purposes of this Convention, the term "resident of a Contracting State" means, subject to the provisions of paragraphs (2) and (3) of this Article, any person who, under the law of that State, is liable to taxation therein by reason of his domicile, residence, place of management or any other criterion of a similar nature; the term does not include any individual who is liable to tax in that Contracting State only if he derives income from sources therein. The terms "resident of the United Kingdom" and "resident of the Republic of Ireland" shall be construed accordingly.

(2) Where by reason of the provisions of paragraph (1) of this Article an individual is a resident of both Contracting States, then his status shall be determined in accordance with the following rules:

(a) he shall be deemed to be a resident 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 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 has not a permanent home available to him in either Contracting State, he shall be deemed to be a resident of the Contracting State in which he has a habitual abode;

(c) if he has a habitual abode in both Contracting States or in neither of them, he shall be deemed to be a resident 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.

ARTICLE 15
Employments

(1) Subject to the provisions of Article 17 and 18, 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.

(2) Notwithstanding the provisions of paragraph (1) of this Article, 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 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 or a fixed base which the employer has in the other State.

(3) In relation to remuneration of a director of a company derived from the company the preceding provisions of this Article shall apply as if the remuneration were remuneration of an employee in respect of an employment and as if references to "employer" were references to the company.

8. Knowle plc is the UK head of a travel agency group. It currently has subsidiaries in five European companies. It is considering setting up a new business in Portugal and has asked the UK marketing director, Selwyn, to move to Lisbon to open a new office on 6 April 2020. As he is not sure how well this will turn out, Selwyn has agreed the following with Knowle plc:

- Selwyn's wife will accompany him, but his two children will remain in the UK at university
- Knowle plc will provide accommodation for Selwyn and his wife in Lisbon, but Selwyn will be responsible for any tax payable in respect of this
- The family will retain their home in the UK as one of the sons still lives at home, and Selwyn will stay there as and when he returns to the UK
- Selwyn will make frequent work trips to the UK, for around one week per month. All travel connected with these UK will be paid for by Knowle plc
- Selwyn's UK trips will enable him to update the board on Knowle's progress in Portugal, and also to keep in touch with his UK-based team who will still report to him

Selwyn is UK domiciled.

An extract from the Double Taxation Agreement between the UK and Portugal is set out below.

Requirement:

Advise Knowle plc on the UK income tax and social security implications of the arrangements agreed with Selwyn. There is no need to consider tax equalisation.
(15)

EXTRACT FROM UK / PORTUGAL DOUBLE TAXATION AGREEMENT

ARTICLE 4

Residence

(1) For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the law of that State, is liable to taxation therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and the terms "resident of the United Kingdom" and "resident of Portugal" shall be construed accordingly.

(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 in accordance with the following rules:

(a) He shall be deemed to be a resident 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 of the Contracting State with which his personal and economic relations are closest (centre of vital interests);

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

(c) If he has a habitual abode in both Contracting States or in neither of them, he shall be deemed to be a resident 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.

9. You are a tax manager with OJAA Tax Consultants and you firm acts for BreakOut Ltd. BreakOut Ltd was recently set up by Harry Markham, a serial entrepreneur with experience in the leisure industry. BreakOut Ltd operates a virtual reality escape room centre which Harry expects to be very successful. Currently there are 100,000 £1 ordinary shares in issue, all of which are held by Harry. To ensure growth, he wishes to incentivise the full-time director, Daisy Lord, by offering her 5,000 newly issued £1 ordinary shares. The shares are not subject to restrictions and their current market value for tax purposes is estimated at £5 per share. Harry hopes to sell the company to a leisure chain in about three years' time when the shares may be worth £15 each.

Harry has discussed three alternatives with you:

1 Daisy would be offered the shares immediately at a price of £2.50 per share and the company would make a loan to Daisy to subscribe for the shares. The loan would be interest-free and would be repayable when the shares are sold.

2 Daisy would be granted an option to purchase the shares at £5 each. The option would only be exercisable if there is to be a sale of the company. This would be achieved by the option agreement providing that they could be exercised either on an actual sale of the company, or by Board resolution immediately before a sale if the Board believed that such a sale was likely to take place.

3 Daisy would be granted an option on the same terms as in 2) above, except that it would be a qualifying Enterprise Management Incentives option.

Harry would like your advice on the tax implications of the alternative methods of providing an incentive to Daisy and information on any reporting obligations.

Requirement:

Write a draft letter to Harry Markham for your tax partner to review, advising on the tax implications for the company and for Daisy of the alternative methods of providing an incentive, and explaining the company's reporting obligations. (20)

10. You are a tax manager in OJAA Tax Consultants and your firm acts for Crabtree Ltd, which trades as a builders' merchant. In recent years Crabtree Ltd has also developed a plant hire business which has been treated as a separate trade for Corporation Tax purposes. The plant hire business has not been successful and it was decided to close the business in three weeks' time on 31 May 2020. This will result in the manager responsible for the plant hire business (Gordon, aged 53) being made redundant.

    Gordon has an annual salary of £36,000. His redundancy package includes a statutory redundancy payment of £2,500 plus an additional payment of £2,500 under the company's redundancy scheme. Gordon's contract of employment entitles him to three months' notice of termination of his employment. On closure of the plant hire business the company is considering whether to:

    1 Summarily terminate Gordon's employment and pay £9,000 in lieu of notice, or

    2 Give three months' notice of termination and pay his salary for June to August in the normal way but advise Gordon that his services will not be required after closure of the plant hire business.

    In addition, the company will make a non-contractual payment of £30,000 by way of compensation for loss of employment. The company has no established practice of making such payments apart from the redundancy scheme.

    The company will also pay £2,000 into the company's registered pension scheme for Gordon.

    The company has asked for comprehensive advice on how each payment will be treated for Income Tax purposes and regarding the resulting PAYE liabilities and reporting responsibilities.

    Requirement:

    Prepare a briefing note for your tax partner, Owen James, detailing:

    1) The Income Tax and National Insurance implications of the proposed payments to Gordon, including both alternatives 1) and 2) for the payment in respect of Gordon's notice period. (12)

    2) The relief available for Corporation Tax purposes for each payment. (3)

    Total (15)

11. On 20 April 2019, Bestrest Hotels UK Ltd recruits Nikolas to become the general manager of its new Cambridge hotel. Nikolas (now 42) previously managed the Bestrest Hotel group's flagship Cypriot hotel in Paphos. Nikolas's salary in his new post is £75,000 a year and he has no other UK income.

Nikolas has been contributing to an occupational pension scheme set up locally by Bestrest Hotels (Cyprus) Ltd at a rate of 5% of his salary and wishes to continue to do so whilst working in the UK. Whilst working in Cyprus, his contributions to the scheme were deductible against Cypriot tax.

Bestrest Hotels UK Ltd has indicated it is willing to make matching employer contributions to the Cypriot pension fund instead of to its own UK occupational pension scheme, provided that such contributions are deductible for corporation tax purposes.

Requirement:

Explain:

1) **If Nikolas will be entitled to UK tax relief in respect of his pension contributions to the Cypriot scheme;**

2) **Whether Bestrest Hotels UK Ltd will be entitled to a corporation tax deduction in respect of the employer's contributions it makes to that scheme in respect of Nikolas; and**

3) **How the annual and lifetime allowance rules apply to Nikolas.**

Total (15)

12. Barbary Ltd is an unlisted events management company, which has recently set up a new office in Bristol with a view to expanding its operations into the South-West and South Wales. It has transferred Stephanie, a member of the existing senior leadership team, to the Bristol office to lead the expansion.

In order to motivate Stephanie to make a success of the expansion, on 5 July 2019 the company awards her with 2,000 £1 Class B shares in the company ('B' class shares entitle the holder to dividends at 50% of the dividend rate declared for ordinary £1 Class A shares and carry no voting rights). The company has its shares valued at the beginning of July 2019 as:

Class of shares	Value per share
	£
Class A	6.20
Class B	3.00

If Stephanie succeeds in building the Bristol business so that it achieves turnover and net profit above a set level, she will be entitled to convert her Class B shares into ordinary £1 Class A shares. If she achieves that target within three years of the Bristol office opening, she will also have the option to acquire a further 500 ordinary £1 Class A shares at their July 2019 value of £6.20 each.

Stephanie is very good in her new role and achieves the target levels of turnover and net profit for the new business by 30 November 2021. At that time, the value of the company's shares is as follows:

Class of shares	Value per share
	£
Class A	9.00
Class B	4.25

Stephanie's Class B shares are duly converted to Class A shares on 30 November 2021.

As the targets are met within three years of the opening of the Bristol office, on 30 November, Stephanie is awarded the option to acquire 500 ordinary £1 Class A shares at £6.20 each. She exercises that option on 1 July 2022, when the shares are worth £11.50 each. She expects to hold the shares for at least two years before selling them.

Requirement:

Explain:

1) **How Stephanie will be taxed on her share-based remuneration; and** (8)

2) **What the company's reporting obligations are and the penalties that will apply if those obligations are not met.** (7)

Total (15)

13. You receive a telephone call from Phoebe Parker, the HR Director of Canefero Industries plc. A copy of the telephone attendance note is set out below:

"Client: Canefero Industries plc

Attendees: Phoebe Parker (HR Director, Canefero) and Ann Adviser

Date: 6 November 2020

Subject: New company location – Hull

Canefero are a large bread and cake manufacturer. Their head office is in Leeds but they are about to open a new manufacturing and distribution site just outside Hull.

Phoebe is responsible for staffing the new site. Most workers are employed locally but some of her team have agreed to travel to the new site for at least part of the week to assist with training and provide on the ground HR support.

There is no desire for her team to be out of pocket and so it is proposed to pay all expenses associated with the trips to Hull.

Details are as follows:

1 Stan lives in Leeds and is based in the Leeds office. He will travel to Hull for three days a week for the next three months. He will stay overnight as it is anticipated days will be long. His remaining two days a week will be spent at home (although occasionally he will go to the Leeds office for meetings). He is to be fully reimbursed his hotel expenses and travel costs.

2 Julie also lives in Leeds. She works four days a week, previously at the Leeds office, but has agreed that going forward indefinitely, she will spend two of these days each week in Hull. She will be reimbursed all costs of travel to and from Hull.

3 Jason works only at client sites as a merchandiser for Canefero. He is provided with a company car and with fuel. He must reimburse all private mileage fuel. His official base is Leeds and it is usual for him to treat his trips to client sites as business mileage. Going forward, his base is going to switch to Hull as many of his clients are based near there and it will give credibility to the new location, although he will still live in Leeds. It is anticipated that he will call into Hull office most mornings to collect the samples/products he needs. It has been agreed that he can still treat his journeys from his home to client sites via the Hull location as business mileage.

Phoebe is calling into the office tomorrow for a meeting on this."

Requirement:

Prepare notes for tomorrow's meeting on the tax and NIC consequences of the proposals. (10)

14. You are the group tax manager for Sporket Group Ltd, the parent company of a group of UK companies working in the advertising sector. Fran Wiltshire, the finance director of Sporket (Markets) Ltd, which is a marketing agency in the group, has sent you an email in relation to a freelancer the company has been using.

"To:	gtm@sporketgroup.com
From:	Franwiltshire@sporketmarkets.co.uk
Date:	12 August 2020
Subject:	Simon Jetson

Hi Tim,

I hope you are able to help me with a query I have.

Simon Jetson is a graphic designer who has been working on a project for one of our main clients, under the direction of the director in charge of the client account, for the last two months.

He has been and will continue to be working almost exclusively for us for the duration of the project, which is likely to last for at least another four months. He does have some other clients which he may work for if there are periods when we have nothing for him to do.

He works at our premises using our equipment. He is paid at an agreed hourly rate for the work, provided it meets with the account director's approval.

When we first took Simon Jetson on, he insisted that he was self-employed so we have been paying his invoices on this basis. However, I've since read something about the problems of incorrectly treating someone as self-employed.

Can you help? Thanks.

Fran"

Requirement:

Reply to Fran's email explaining whether, based on the facts, Simon is being correctly treated as self-employed, and if not, what the consequences of this are likely to be. (15)

15. Echo (UK) Ltd has recently been incorporated in the UK to carry out insurance business. It is a subsidiary of EQO, a company incorporated in Ecuador. Rafael Moreno has been appointed as the finance director of Echo (UK) Ltd and has asked to meet with you to discuss various issues affecting the taxation of employees who will be working in the United Kingdom.

    It is intended that a significant number of employees will be transferred or seconded from Ecuador to the UK. They will be working in the United Kingdom for periods of between three months and five years. They will be provided with accommodation at the company's expense and paid a daily allowance to cover subsistence and other costs. Some of these employees will rotate between the UK and Ecuador working for four weeks in each location.

    Some of these employees will be entitled to bring their families with them and the company intends to pay for the families' travel at the beginning and end of the assignments and also for three return journeys home each year for vacation.

    EQO is a quoted company on the Ecuadorian Stock Market and it has granted options over shares to various of the Group's senior employees including some of those who will be assigned to the UK. Further options are likely to be granted in the future.

    Mr Moreno has advised you that EQO traditionally pays large bonuses to its senior employees and would wish to keep these outside the charge to UK tax and National Insurance. As a general rule, the Group would not wish employees to be disadvantaged by the assignment and understands that this may be achieved through tax equalisation, a concept he has asked you to explain. He has also asked if payment of remuneration through a non-UK company will avoid having to account for PAYE and National Insurance.

    There is no double taxation or social security convention between the United Kingdom and Ecuador.

    Requirement:

    Make notes of the matters that you would discuss with Mr Moreno. (20)

ANSWERS

1. THISSOP LTD

To: ks@thissop.co.uk
From: jackwhite@taxrus.com
Date: 18 November 2020
Subject: Urgent: PAYE issues

Hi Keith

Thank you for your email.

Please find below my response to your queries:

1) Penalties

Penalties for late payment of tax and NIC

The first late payment for the May pay period was the first default in the tax year, so can be ignored for penalty purposes.

The company will be charged a penalty of 1% of the amounts paid late for the second, third and fourth defaults (August, September and November).

For the fifth and sixth defaults (December and February) there will be a penalty equal to 2% of the amounts paid late (including the directors' bonuses).

You do not mention how late the payments reported for August, September, November and December were. If any amount remains unpaid six months after it was due to be paid there is an additional penalty of 5% of the outstanding amount.

In addition, if the company does not pay the tax and NIC in respect of the bonus payments until January 2022, the payments will be more than 12 months late and so there will be a further 5% penalty (making 10% in total, in addition to the original default penalties) charged on the outstanding amount. All penalties are in addition to the late payment interest charges. If you cannot pay sooner, consideration should be given to approaching HMRC to request that payment be paid over monthly instalments. There is also the possibility of a short deferral period. If HMRC agree to the request (known as an agreed 'time to pay' (TTP) arrangement), interest will still accrue but you will not be charged any late payment penalties which would have accrued after the arrangement is in place provided any terms set down by HMRC are complied with.

Penalties for errors

The bonuses should have been reported on the Full Payment Submissions (FPS) due on or before the date that the bonuses were paid. As Josh omitted them from the FPS, this is an error which attracts a penalty; the amount of which depends on whether the error was careless, deliberate but not concealed or deliberate and concealed.

No penalty will be charged if Josh took 'reasonable care' when preparing the FPS. I think you'll agree it is unlikely that this will be successfully argued on this occasion.

An error is treated as deliberate if an incorrect FPS was submitted knowingly and intentionally. An error is deliberate and concealed if an incorrect FPS was submitted knowingly and intentionally and active steps were taken to hide the error. It is likely that HMRC will accept that Josh made a deliberate but not concealed error.

The penalty is calculated as a percentage of HMRC's potential lost revenue, ie the extra tax and NIC due. The maximum penalty is 70% for a deliberate but not concealed inaccuracy (30% for a careless inaccuracy, and 100% for a deliberate and concealed inaccuracy).

The maximum penalty can be reduced for either a prompted or an unprompted disclosure.

It may still be open to you to make an unprompted disclosure in respect of the other directors' bonuses before HMRC discovers the error also applies to them. The minimum penalty for an unprompted disclosure is 20% when the error is deliberate but not concealed.

However, as HMRC have already discovered the error in Steve Simons' return, the company has missed the opportunity to make an unprompted disclosure in respect of that. The company should contact HMRC as soon as possible, if it hasn't already, to tell them about the error, ie make a prompted disclosure. This will mean giving HMRC reasonable help in calculating the additional liability and access to your records to check the amount due. This should result in a minimum penalty of 35%.

2) RTI obligations

If Josh had discovered the error before he submitted the next pay period's FPS, he should have corrected the error by using revised year to date figures on the next FPS. Alternatively, he could have submitted an additional FPS for the same pay period.

If he had discovered the error after a subsequent FPS was submitted, he should have used adjusted year to date figures on the next FPS.

As the error has been discovered after 19 April 2020, it should now be corrected by submitting an additional FPS. This should record the difference between what was originally reported, as paid to the directors, and the correct amount.

I hope this helpful. Just let me know if you have any other questions or need any assistance with rectifying these matters.

Kind regards

Jack

MARKING GUIDE

TOPIC	***MARKS***
Late payment penalties:	
Ignore 1st default	½
1% for next 3	½
2% for next 2	½
Include directors' bonuses	½
5% x 2 if > 12 months late	½
Consider applying for "time to pay"	½
Penalties for error:	
Should have been reported on FPS	½
No reasonable care taken	½
Deliberate	½
Deliberate but not concealed	½
% x PLR	½
Max penalty	½
Unprompted disclosure not available	*1*
Prompted disclosure	½
Min penalties	½
RTI obligations:	
Action if discovered before next period's FPS	½
Action if discovered after FPS submitted in same year	½
Action if discovered after the year end	½
Presentation and higher skills	½
TOTAL	***10***

2. TRANSCOASTAL FREIGHT LTD

1) <u>PAYE on whole of UK earnings</u>

The first step is to consider Pascal's residence under the statutory residence test for 2020/21. Although Pascal's work is performed onboard a vessel, due to the fact that most of the trips that he makes are not cross border trips, he will not be considered a 'relevant worker' under the statutory residence test.

Pascal's expected days outside the UK (when he will be outside the UK at midnight) are:

6 – 27 April	22
3 days/month on each French voyages (excl. December)	<u>30</u>
Total	<u>52</u>

He will therefore be present in the UK for 313 days, which means the automatic overseas tests are not met. As Pascal is present in the UK for more than 183 days, he will be regarded as resident in the UK for 2020/21 under the first automatic UK residence test.

Ordinarily, where an individual is UK resident for tax purposes, they are subject to tax on their worldwide employment income on a receipts basis. If, however, they are non-UK domiciled they can claim the remittance basis for their income and gains. If the individual has a continuous period of non-UK residence for three tax years out of the previous five, as is the case here, and they chose to use the remittance basis, overseas workday relief (OWR) will apply. The effect of OWR is that Pascal is only taxable on the receipts basis in respect of earnings for UK workdays. Earnings relating to non-UK workdays are taxable on the remittance basis, ie only taxed if Pascal brings those earnings to the UK, or otherwise uses or enjoys them here.

However, in determining what constitutes UK workdays and what constitutes overseas workdays, account has to be taken of the fact that Pascal's duties as a deckhand are performed onboard a vessel. Under a special rule applying to UK residents working onboard an aircraft or vessel under s.40 ITEPA 2003; if a voyage starts or ends in the UK, then all duties performed on that voyage are treated as being carried out in the UK. Given that all of Pascal's voyages start or finish in the UK, his duties as a deckhand on the French trips are treated as being UK duties.

As all of Pascal's duties, whether on voyages to a UK port or a French port, are treated as UK duties, all of Pascal's earnings are taxable on the receipts basis regardless of whether Pascal qualifies for OWR. Accordingly, TFL should deduct tax under PAYE in respect of the whole of his earnings.

2) <u>Consideration of split year rules</u>

As set out in (a) above, Pascal is resident in the UK for 2020/21. If however, he can claim split year treatment, he will only be treated as becoming UK resident (and as such subject to UK tax on his worldwide income) part way through the year, rather than for the whole of the tax year. This will not affect the taxation of his earnings from TFL (which we have determined are all subject to UK tax in any event). It may, however, be important in connection with any overseas income Pascal may have in 2020/21.

In order to qualify for split year treatment in 2020/21, Pascal needs to fall within one of the cases specified in the legislation.

The potentially relevant cases are Case 4 – starting to have an only home in the UK, Case 5 – starting full time work in the UK and Case 8 – starting to have a home in the UK. If more than one apply, priority is given to the case that gives the shortest "overseas part" of the tax year.

Case 4 would give a date of 31 May 2020, the day he ceases to have a home in France,and has his only home in the UK. Case 5 would give a UK residence starting date of 1 May 2020, the day Pascal commences work in the UK. Case 8 would give the date of 28 April 2020, being the date on which he acquires his UK home. The case which gives the shortest period of overseas residence is therefore Case 8.

For case 8 to apply, Pascal must:

- be non-UK resident in 2019/20. As he spends fewer than 46 days in the UK (the number of days applicable to an individual who has not previously been resident in the UK) he will be treated as automatically overseas resident under the statutory residence test and as such will satisfy this part of Case 8

- be UK resident in 2021/22. This is likely to be the case under the automatic residence test as he will spend more than 183 days in the UK

- have no home in the UK at the start of the 2020/21 tax year but does have one by the end of the tax year. He buys a property and moves in on 28 April 2020 and has no intention to sell it and so this test is likely to be met

- continue to have a home for the whole of the following tax year. There is no indication that this will not be the case, and

- prior to acquiring the UK home, he must not have sufficient ties to make him UK resident. In determining the number of permitted ties, the number of days in the ‘arrivers’ table for the sufficient ties is reduced in proportion to the number of whole months left in the tax year after that date; ie by 11/12. However, it is unnecessary in this case as Pascal has no ties prior to 28 April 2020

Given there is no reason to suppose Case 8 will not apply, the day from which Pascal will be treated as UK resident will therefore be 28 April 2020.

MARKING GUIDE

TOPIC	***MARKS***
Residence determined by statutory test	*½*
Not a relevant worker	*½*
Pascal is resident in UK (present for 313 days, or over 183 days)	*2*
Impact of residence on general tax position; ie worldwide income	*1*
Identify potential for OWR if non–UK domiciled where overseas income concerned	*2*
Place of work of duties on board a vessel	*2*
Conclude TFL should deduct tax under PAYE on all his earnings	*1*
Impact of split year treatment	*1*
Potentially applicable cases being case 4, 5 and 8	*2*
Identify that on facts case 8 gives shortest "overseas period"	*1½*
Consideration of application of case 8	*1½*
TOTAL	***15***

3. AYUSHI SHARMA

HI International's headed memo

Ms A Sharma
[Departmental address]

[Date]

Dear Ayushi

Re: Student loan deductions

In response to your recent complaint, I have looked into why a student loan deduction was taken from your July salary payment.

As your student loan was taken out after 1 September 2012, this is a 'Plan 2' loan. Repayments under a Plan 2 student loan must be deducted when you start earning at a rate of more than £25,725 a year.

As student loans deductions are worked out on a month by month basis, we have to consider each month in isolation, testing your pay for the month against 1/12th of the repayment threshold. 1/12th of £25,725 a year is £2,143 (rounded down).

In July, in addition to your normal salary payment of £1,833, you received your welcome payment of £800. As the payment relates to your employment with us, that £800 is taxable as earnings and is subject to Class 1 National Insurance Contributions (NIC). This is added to your normal pay to arrive at your total earnings for the month, making your total earnings for July £2,633.

Your student loan deductions are worked out using your pay for the month for Class 1 NIC purposes. This means we ignore the £50 which was added to your pay in respect of your health insurance benefit as this is subject to Class 1A NIC rather than Class 1 NIC.

The calculation of the student loan deduction is therefore as follows:

	£
Salary	1,833
Welcome payment	800
Total earnings for NIC purposes	2,633
Less 1/12 of £25,725 threshold	(2,143)
	490
Student loan deduction at 9%	44

This amount of £44 was deducted from your July pay.

Your pay in August did not include any earnings for Class 1 NIC purposes other than your salary of £1,833 which is below the monthly proportion of the student loan repayment threshold of £2,143. No student loan deductions were therefore due for August.

The money that the company deducts from pay in respect of student loans is paid over monthly to HMRC, who pass it on to the Student Loans Company. As your employer, we are not in a position to look at your whole student loan account to see whether any repayments are due. However, if you believe that over the course of the year we have deducted too much from your pay in student loan deductions, you can apply to the Student Loans Company for a refund once the tax year has ended on 5 April.

The total amount that we deduct from you in respect of your student loan for the year will be included in your end of year statement of earnings and deductions (P60).

Kind regards
[name]

MARKING GUIDE

TOPIC	***MARKS***
Identify Plan 2 and quote threshold	*1*
Use pay for Class 1 NIC purposes (ie ignore PMI)	*½*
PMI subject to Class 1A and is therefore disregarded	*1*
Calculation for each payday	*3*
Welcome payment is taxable and subject to Class 1 NIC	*1*
Explain that each month considered in isolation	*1*
Requests for refunds to be made to student loan company	*1*
Total amount of deductions for year will be on P60	*1*
Presentation and higher skills	*½*
TOTAL	***10***

4. SAMPHIRE LTD

To: Dennis.wyatt@samphire.co.uk
From: Simon.robart@taxfirm.co.uk
Date: 10 April 2020
Subject: PAYE and placed workers

Dear Dennis

You are right in thinking that you may have to deduct tax and national insurance from the workers you find to fulfil clients' requirements.

The usual case is that you have a contract with your client to provide them with a worker and you find a suitable individual to carry out work for the client. If you, your client or anyone else has a right of supervision, direction or control over the way in which that work is carried out, then, unless the worker you provide is provided to you by another employer, you should normally deduct tax and national insurance contributions (NICs) under PAYE.

There are some exceptions to the requirement to operate PAYE in respect of workers you provide to clients. You do not have to deduct tax and NICs under PAYE if the worker you provide is working:

- As a musician, actor or other entertainer
- As a fashion, photographic or artist's model
- In the worker's own home or at premises not controlled or managed by the client or prescribed by the nature of the services

As you are providing Dermot Flynn to the theme park to work as an entertainer, you do not have to deduct tax and NICs under PAYE from payments made to him.

In other cases, the key test is whether anyone has a right of supervision, direction or control over the way in which work is done by the person you provide to the client. This can be a tricky test to apply but HMRC interpret each leg of the test as meaning:

<u>Supervision</u>: watching or overseeing the work; checking that the work meets a required standard.

<u>Direction</u>: making sure the work is done in a certain way, by providing instructions, guidance or advice.

<u>Control</u>: telling the worker how they should do the work or having the power to move them from one job to another.

Only one leg of the test needs to be met (to any degree) to make payments to the individual subject to PAYE. It also does not matter <u>who</u> has the right of supervision, direction or control or whether they actually exercise that right. Unless it is obvious from the kind of work being carried out that supervision, direction and control would not be appropriate, you should therefore assume that the test is met and operate PAYE in respect of payments to the worker.

One example of the kind of work where supervision, direction and control would not be appropriate is where a worker has been engaged to apply specialist skills to deliver work which no-one in the client business would know how to supervise, direct or control. This would appear to apply to Mohammed Khalid's engagement and you need not deduct tax and NICs from payments made to him.

However, it would appear difficult to argue that the work done as a receptionist by Alison Eddowes is not subject to supervision, direction and control or consists of specialist skills. You should therefore deduct tax and NICs from any payment you make to her, as well as making secondary Class 1 NICs contributions in respect of her earnings. You should re-issue a starter checklist to her, explaining that PAYE does apply to her.

Finally, you do not have to operate PAYE in respect of particular payments where the workers you send to the client are actually provided to you by another employer, such as is the case with the 10 workers provided to you by Dilnott Ltd. In this case, Dilnott Ltd should be deducting tax and NICs from the payments it makes to those 10 workers. You can therefore pay Dilnott Ltd the full contracted amount.

Quarterly reporting requirements

As you provide workers to clients to carry out services for those clients, you will have to make a quarterly report to HMRC. This report is quite separate from, and in addition to, any PAYE reporting obligations.

Reports are due in respect of each tax quarter (ending 5 July, 5 October, 5 January and 5 April) and must be submitted within one month from the end of the tax quarter.

The report should contain details of any workers that you have provided to clients during the period, except those which you have paid under deduction of tax and NICs under PAYE. This means you would not need to include details in respect of Alison Eddowes as long as you have operated PAYE on her income paid to her by you.

It does not need to include payments made to:

- a musician, actor or other entertainer;
- a fashion, photographic or artist's model, or
- a worker working in their own home or at premises not controlled or managed by the client or prescribed by the nature of the services.

You do not therefore have to include details of Dermot Flynn or (probably) Mohammed Khalid.

In the report, you will have to identify all of the individual workers, so if, for example you do not know the names, addresses and National insurance numbers of the workers provided by Dillnott Ltd, you will have to ask Dilnott Ltd to supply that information.

The report also has to include, for each worker mentioned, the reason why you did not deduct tax and NICs under PAYE.

There are penalties that apply if you do not make the required reports or if you make them late.

Do let me know if you have any further queries.

Kind regards,

Simon

MARKING GUIDE

TOPIC	***MARKS***
Explain basic rule: worker provided to client, subject to Supervision, Direction or Control (SDC), then PAYE applies	*1*
Exception for entertainers etc. (full list) (eg Dermot Flynn)	*2*
Explain SDC (and that any element of SDC is enough to make agency provisions apply)	*3*
If no SDC then agency provisions do not apply – no PAYE obligation (eg Mohammed Khalid)	*1*
PAYE should be operated on payments to Alison Eddowes	*2*
If worker provided to agency by another employer (eg Dilnott Ltd), it would be that company who should operate PAYE, not Samphire Ltd	*1*
Quarterly reporting requirements:	
Quarterly report in addition to PAYE obligations (incl due dates)	*1*
To include details of all non-PAYE workers provided in quarter	*1*
Obtain details of workers provided by others	*½*
Exclusion for entertainers etc.	*½*
Need to say why PAYE not operated	*½*
Penalties	*½*
Presentation and higher skills	*1*
TOTAL	***15***

5. BIGELOW PLC

BRIEFING NOTE IN RELATION TO INCOME TAX AND NIC CONSEQUENCES OF NEW DIRECTOR APPOINTMENT

Income tax position

Company directors (including non-executive directors (NEDs)) are office-holders and payments made to them in relation to their directorships are considered to be earnings for UK tax purposes.

We are told the NED has not previously been UK tax resident and therefore as long as he spends less than 46 days in the UK in the tax year, he will be treated as non-UK tax resident. Directors who are not resident in the UK are taxable only on any earnings that relate to duties that they carry out in the UK. As such the NED will be subject to UK tax on a pro-rated amount of his income from Bigelow plc to reflect the number of UK workdays.

UK workdays, where the duties performed in the UK can be shown to be ‘merely incidental’ to a non-resident’s overseas duties can be disregarded. While there is no statutory definition of ‘incidental’ there is case law and HMRC guidance, and these indicate that it is the nature of the duties carried out which determines whether they are ‘incidental’ to overseas duties. The facts of each case will therefore need to be considered.

If the work done in the UK is subordinate or ancillary to that done overseas, the UK duties are ‘merely incidental’. On the other hand, if the work done in the UK is of the same kind as that done outside the UK it will not be ‘merely incidental’ (even if the UK visit is very short).

Duties carried on in the UK by a company director are hardly ever considered to be ‘merely incidental’. Subsequently, where a company director who normally works overseas is required to attend Board meetings in the UK, these duties are treated as more than ‘incidental’ to his overseas duties. Attendance at the committee meetings is also likely to represent a substantive duty.

Where Board meetings take place at non-UK locations, income relating to attendance at these will not be subject to tax in the UK.

For other days spent in the UK, further information will be needed on the nature of the NED’s duties before we can conclude on whether they are incidental or not.

For 2020 and subsequent years, the NED will continue to be taxable in the UK on income from non-incidental UK duties. If however, his days in the UK rise to 183 or more or if he acquires a home in the UK or if he spends more than 45 days in the UK and also has other ties to the UK over and above his work, for example, family or accommodation, he could become UK tax resident. In this case he will be taxable in the UK on all his worldwide income, and as such, the position will need to be revisited if the facts change from those outlined.

Technically, Bigelow plc needs to account for PAYE and national insurance on all of the NED’s worldwide earnings with Bigelow. However, for 2020/21 (and subsequent years if the NED remains non-UK resident), it can apply to HMRC for a Section 690 payroll arrangement to allow it to withhold tax under PAYE from the appropriate proportion of fees that relate to UK duties only. In practice, this will involve undertaking a review before each tax year of the proportion of the NED’s duties that are expected to be undertaken in the UK and asking HMRC to confirm that it is appropriate to account for tax under PAYE only on this proportion.

The NED will then need to complete a UK self-assessment tax return to ensure that the correct amount of UK tax is paid.

The NED may also be subject to income tax on the fees in his country of residence and will need to claim relief against those taxes for the UK taxes paid. Because the country in which the NED is tax resident does not have a double tax treaty with the UK unilateral double tax relief only will be available in the UK.

<u>Travel and expenses</u>

Travel and associated expenses will not be subject to UK income tax provided the following conditions are met:

1 The NED is non-UK domiciled;

2 The amount is included in the earnings or the reimbursement of expenses incurred by the employee on such a journey

3 The earnings are charged on a receipts basis not a remittance basis

4 The journey meets the following conditions:

   – The journey ends on, or during the period of five years beginning with, a date that is a 'qualifying arrival date' (see below) in relation to the employee; and

   – The journey is made from the country outside the UK where the NED is normally resident to the place in the UK where the duties of the employment are performed (or back to the home country from the UK).

For these purposes, a date is a 'qualifying arrival date' if:

i. It is a date on which the person arrives in the UK to perform duties for which they receive taxable earnings; and

ii. The person has not been in the UK for two years prior to the arrival date for any purpose, <u>or</u> the person was not UK tax resident in the two tax years before the arrival date.

We would therefore need more information about the NED's previous presence/ residence status in the UK before we can be certain about the availability of this exemption.

If the exemption referred to above is not available, it is likely that all travel and associated expenses will be fully taxable in the UK. In general terms, where expenses for travel from home (or from another location which the NED is not attending on Bigelow plc business) to a 'permanent workplace' are reimbursed, the amount reimbursed will be fully taxable in the UK, and income tax and NIC will need to be accounted for via PAYE on the amounts reimbursed.

A place will be regarded as a permanent workplace unless the individual spends less than two years or, if more than two years, 40 per cent or more of his working time there. If the majority of meetings will be at the London office it appears likely that the London office will be treated as the NED's only 'permanent workplace' for these purposes. On this basis, travel to and from the London office would be treated for UK tax purposes as 'ordinary commuting'.

Where expenses for travel to the London office (and associated subsistence such as the cost of meals) are reimbursed, the amount reimbursed will be taxable in the UK, and income tax will need to be accounted for via PAYE. To ensure that the NED is not out of pocket, it will be necessary to gross-up the amounts paid to him. Where any expenses in relation to travel and subsistence for his attendance at the London office are met directly by Bigelow plc, these would be considered to be taxable benefits reportable on Form P11D at the end of the tax year.

The provision or reimbursement of travel and subsistence in respect of journeys to the other locations in the UK (provided there is no stop-over to undertake substantive duties in London) should be exempt from UK tax, to the extent that the NED would be able to claim relief for the same amount when calculating his taxable earnings. This means that no income tax is due on the amount and Bigelow plc would have no reporting requirements in respect of these expenses.

If the above travel and subsistence expenses are not exempt, they will be treated in the same way as the expenses relating to travel to the London office.

<u>NIC</u>

In the absence of a reciprocal agreement between the UK and the NED's country of ordinary residence, the normal rules are that the NED and Bigelow plc will pay UK social security contributions in respect of the UK-related element of fees and reimbursement of taxable expenses paid to the NED. (The usual 52 week exemption does not apply here as the NED is employed by a UK employer.)

There is a concessionary treatment where HMRC will not seek to charge NIC in respect of payments to a non-UK resident director of a UK registered company who is not otherwise within the scope of NIC where the director attends no more than ten Board meetings in a tax year and either there is a single trip not exceeding two weeks or several smaller trips with each visit to the UK to attend a board meeting lasting no more than two days.

It is not clear on the facts whether this concession would apply in the current circumstances, but it would be worth considering further.

MARKING GUIDE

TOPIC	***MARKS***
Residence for tax purposes	*1*
Incidental test and application to facts	*2*
PAYE in the absence of a s690 direction	*1*
Need for a tax return	*½*
Potential liability for tax in home country	*½*
Travel expenses rules	*3*
Travel expenses application	*3*
NIC rules	*2*
NIC application to facts	*2*
TOTAL	***15***

6. AERATECH LTD

EMPLOYEE GUIDE:

THE UK TAX IMPLICATIONS OF OVERSEAS SECONDMENTS OF AERATECH LTD (AUK) STAFF TO AERATECH YESWAIN LTD (AY)

<u>The UK Income Tax and National Insurance implications of being seconded overseas</u>

<u>Income Tax</u>

The liability to UK income tax in respect of the individual's income in a tax year (6 April-5 April) depends upon whether the individual is resident in the UK or not for tax purposes and whether the income derives from duties carried out in the UK or is overseas income.

Where an employee is tax resident in the UK, he is taxable on all worldwide earnings, regardless of where his duties are carries out. Where an employee is non-tax resident in the UK, he is only taxable on earnings which relate to duties carried out in the UK.

<u>Tax years before the tax year in which the secondment takes place</u>

As the employees are UK resident and domiciled, they will be liable for UK Income Tax on their worldwide income as it arises.

<u>Tax year in which the secondment takes place</u>

The UK tax legislation has a Statutory Residence Test (SRT) which determines the individual's residence status for the tax year.

In general, an individual's residence status is determined for a tax year as a whole. However, in certain circumstances, the legislation allows a 'split-year' treatment, whereby the tax year may be split into a UK part and an overseas part. The individual will be treated as UK resident in the UK part of the tax year and non-UK resident during the overseas part of the tax year.

The application of these rules will differ depending upon whether the secondment starts on 1 January or 1 July. We shall consider each of these in turn.

1. <u>18-month secondment starting on 1 January</u>

This secondment will span three different tax years and we will consider each in turn.

For the tax year in which the secondment starts, the employee will be treated as UK resident under the automatic residence test. This is because the employee will have been present in the UK for at least 183 days. The employee will also be UK resident because he works full-time in the UK, and because he has a home in the UK (however only one test needs to be satisfied in order to be UK resident).

In the second tax year the employee will be treated as non-UK resident because he will satisfy the 'work abroad' rules. Broadly the 'work abroad' condition is met where:

a) The individual works abroad for an average of at least 35 hours a week for the whole of the tax year;

b) He has no 'significant breaks' in that overseas work (being 31 days or more without an overseas workday); and

c) He is present in the UK for fewer than 91 days in the tax year of which fewer than 31 days are spent working in the UK.

In the third tax year the employee will regain UK residence status. This is because he will again satisfy at least one of the following; the 183 day test, the UK work test and the home test. It is likely that many returning employees will, in fact, satisfy all three.

The split-year rules allow the years of departure and return to be split into UK and overseas parts if certain conditions are satisfied. The conditions are described in the legislation as split-year 'Cases'.

Under Case 1, the year of departure is split when:

- The employee satisfies the 'overseas work criteria' between the date of departure and the end of the tax year; and

- The employee is non-UK resident in the following year under the 'work abroad' rules

The 'overseas work criteria' are broadly as outlined above, ie the employee works abroad for an average of at least 35 hours a week, and his days spent in the UK are less than the permitted limits (being 90 days of which fewer than 31 days are spent working). These limits are scaled down in the year of departure.

Where the Case 1 conditions are met, the employee will be UK resident up to the date he starts working overseas and non-UK resident from his first overseas workday.

On completion of the secondment, the tax year of return can be split under Case 6. This Case applies to employees returning to the UK after a period of overseas work.

Case 6 applies where:

- The individual is non-resident in the previous year under the 'work abroad' rules (as outlined above);

- The individual was UK resident in at least one of the five tax years prior to his return; and

- The employee satisfies the 'overseas work criteria' between the start of the tax year and his final overseas workday.

Where the Case 6 conditions are met, the employee will resume UK residence from the day after their final overseas workday.

Consequently, if the 18-month secondment starts on 1 January, the employee will be non-UK resident throughout the period of secondment (being from the date of the first overseas workday until the overseas secondment finishes).

This would mean that, during the period of the secondment, the employee will only pay UK Income Tax on his UK income. All employment income and expenses paid whilst on secondment will be foreign income (being income paid in return for duties performed outside the UK). This foreign income would not be taxable in the UK.

2. <u>18-month secondment starting on 1 July</u>

A secondment starting on 1 July 2020 will last until 31 December 2021. It is assumed that on his return the employee will resume full-time work in the UK and again occupy a home in the UK.

This secondment spans two tax years. In neither of those tax years will the employee be automatically resident overseas because he will spend more than 15 days in the

UK, he will exceed the permitted UK days and workdays and will not work sufficient hours outside the UK for the whole of the tax year.

In both tax years the employee will remain resident in the UK. This is because he will satisfy either the home test or the UK work test.

The home test is satisfied if in a period of 91 days (30 of which must fall into the tax year) you have a home in which you spend at least 30 days living in, without an overseas home (or if you do have an overseas home, you spend no more than 30 days in the overseas home during the tax year).

If the employees leave the UK on 1 July, they have (presumably) been living in their UK home for at least 30 days in a 91 day period without an overseas home. This would be 30 days during the 3 months from 6 April to 1 July.

When the employee returns to the UK at the end of December 2020, they will once again presumably live in their home in the UK for at least 30 days in a 91 day period (during the 3 months from 1 January to 5 April) without an overseas home, so will likely be UK resident in this tax year (2021/22) too.

The UK work test is satisfied if there is a 365 day period during which the employee works full-time and any part of that 365 day period falls into the tax year under consideration.

Where employees leave the UK on 1 July, they have (presumably) been working for at least 365 days full-time in the UK, with the last few months of that 365 day period falling into the 2020/21 tax year.

When the employees return to the UK in December 2021, they will once again take up their full-time UK duties (with the expectation of continuing for a further 365 days) upon their return. December 2021 falls into the 2021/22 tax year.

Split-year treatment will not be available. Case 1 will not apply because the employee will not be non-UK resident in the following year (2021/22 in this instance) under the ‘work abroad’ rules. This is because the UK days/workdays will exceed the permitted limits and the overseas work does not extend to the whole of the tax year, as explained above.

Consequently, the employee will remain resident in the UK throughout the 18-month period of the secondment. As a result, income from the employment with AY will be subject to Income Tax in the UK. If the income is also taxable in Yeswain, unilateral double tax relief may be available. This reduces the UK Income Tax liability by the lower of the UK and the foreign tax paid on the income.

<u>Benefits and employment expenses</u>

Certain benefits and employment expenses may be exempt from UK tax or a deduction may be claimed, depending on the residence status of the employee (any deductions described below can only be set against earnings that are taxable in the UK and cannot reduce them below zero).

These include:

- Because the secondment lasts for less than two years, unless individuals are recruited specifically for the secondment (so it represents substantially the whole of their employment), the overseas location will be treated as a temporary workplace. As such, the payment or reimbursement of expenses relating to travel and subsistence, including accommodation, will not constitute a taxable benefit

(Please note that even if the temporary workplace rules do not apply, costs of travel to and from a location at the beginning and end of a secondment are deductible for tax purposes or (if paid for or reimbursed by an employer do not constitute a taxable benefit) where duties are performed wholly outside the UK.)

- Overseas medical expenses and medical insurance paid for by the employer are not a taxable benefit
- Costs of journeys to and from the overseas location by a spouse, civil partner or minor child do not give rise to a taxable benefit as long as:
  - The employer pays or reimburses the cost of the travel
  - The employee is abroad for at least 60 consecutive days
  - Journeys are restricted to two return journeys by the same person in a tax year

AY intends to pay for one return visit per month for either employees or their relatives. Up to two journeys per tax year by relatives can therefore be tax free but only if made by a spouse, civil partner or minor child of the employee (not by relatives in general). Any other journeys paid for by AY would be taxable as a benefit on the employee if the employee is being treated as tax resident in the UK at the time that the journey takes place.

<u>The UK tax implications of selling the UK property whilst abroad</u>

The UK CGT treatment of the disposal of an individual's private residence will depend on whether the disposal took place in a UK resident or non-resident period.

If the owner is treated as UK resident at the time of disposal, the gain is the difference between sales proceeds and total costs of acquisition.

Principal private residence relief (PPR) will exempt any gains which arise during periods when the individual occupied the property as his only or main residence. Therefore, gains arising during periods of absence will be taxable.

However, certain periods of absence can be classified as 'deemed occupation'. For example, the last 18 months of ownership are always treated as deemed occupation as long as the property has ever been the taxpayer's main residence. Deemed occupation also includes any period of absence, no matter how long, during which the individual was employed abroad. This particular period needs to be preceded and followed by actual occupation of the property.

If a property is sold without the employee returning to the property, there may be a Capital Gains Tax liability. However, the requirement to reoccupy the property after a period of absence does not apply where an individual who has worked abroad is unable to resume occupation because the terms of his employment require him to work elsewhere. It may therefore still be possible that any period of absence would be covered by the deemed occupation rules and that no gain would be taxable.

Should the deemed occupation rules not apply, any gain relating to any period the property was let to a third party tenant may also be partly or fully exempt under the letting relief rules up to a maximum of a £40,000 exemption.

If an asset disposal takes place in a non-resident period, whether in a tax year in which the individual is non-UK resident or the 'overseas part' of a split tax year, the resulting gain is not ordinarily chargeable to UK CGT. However, a gain on a non-resident's disposal of residential property is chargeable under the Non-Resident CGT (NRCGT) rules. In this case the gain is normally calculated by assuming that its acquisition cost is the value of the property at 6 April 2015. Any gains payable to HMRC would be due 30 days from completion declared by a NRCGT return due on the same day.

PPR relief would be available for the final 18 months of ownership but would only otherwise be available for periods in tax years after April 2015 if the individual or their spouse/civil partner spent at least 90 midnights in the property in the tax year.

As the employees will return to the UK before a full five years non residence is up however, the full capital gain on the property calculated using historical cost rather than the value at 5 April 2015 will become payable on 31 January in the year after the employee returns to the UK. Any tax on the NRCGT gains calculated and paid whilst they were away, will be able to be offset against this liability.

<u>National Insurance</u>

As Yeswain has no reciprocal social security arrangement with the UK, for the first 52 contribution weeks of any overseas employment the employee and employer will usually remain liable to Class 1 National Insurance primary and secondary contributions.

This depends on meeting three conditions:

1 AY having a place of business in the UK

2 The employee being ordinarily resident in the UK for NIC purposes (broadly meaning habitually present in the UK); and

3 The employee being resident in the UK immediately before the secondment began.

Travel expenses relating to the overseas employment and the provision of medical insurance whilst abroad are excluded from the Class 1A National Insurance charge for employers.

MARKING GUIDE

TOPIC	***MARKS***
Tax depends on residence (explain basic rule)	*1*
Explain concept of SRT and split years	*1*
Secondments starting 1 January (explain position for all 3 tax years)	*6*
Secondments starting 1 July (explain position for both tax years)	*4*
Benefits and expenses	*2*
CGT position on sale of property	*3*
NIC	*2*
Presentation and Higher Skills	*1*
TOTAL	***20***

7. FIBROTECH LTD

NOTES FOR TAX PARTNER RE: EMPLOYEE SECONDMENTS

PAYE issues for Fibrotech Ltd

Fibrotech Ltd will be required to operate PAYE if it has a taxable presence in the UK. As the clear intention is to create a London office, a PAYE scheme should be set up and operated from the outset.

Kieran Clarke (KC) – income tax issues

KC will become resident in the UK under the SRT (by virtue of either the 183 day test or the full-time work test). He will be UK resident for the tax year in which he starts working in the UK, with split year treatment available, most probably under Case 5 which would mean that the UK part of the split year would start with his first UK workday. He will remain domiciled in the ROI, and therefore as a non-domiciled UK resident will be able to choose between using the arising and remittance bases.

Ordinarily, a UK resident is subject to tax on all earnings, regardless of where the work duties are performed. However, provided that KC has not been UK resident for three consecutive tax years in the five tax years before the year in which he takes up his post in London and he elects to be taxed on the remittance basis, he will be entitled to Overseas Workday Relief (OWR) for earnings in respect of duties performed abroad. OWR is available for a maximum of the year of arrival and the following two years; a total period of three years.

If OWR is available, earnings relating to the UK duties are taxed on the receipts basis, while earnings relating to non-UK duties are treated as 'foreign earnings' and are not taxable in the UK unless they are remitted to the UK.

OWR does not require dual contracts and applies where a remittance basis employee carries out both UK and non-UK duties under a single contract of employment. Total earnings from the employment will be apportioned on a just and reasonable basis which is likely to be by reference to UK and non-UK workdays in the tax year.

If KC's unremitted income and gains are less than £2,000 the remittance basis applies automatically and UK personal allowances are not lost. However, where they exceed £2,000, as is the case here, a claim will need to be made. This will result in a loss of his UK personal allowances. KC would therefore have to consider carefully how much of his earnings from his overseas duties he is likely to need or want to remit to the UK, and whether the tax saving on the earnings kept outside the UK is enough to compensate for the loss of the £12,500 personal allowance.

KC – PAYE issues

Even if OWR applies, Fibrotech Ltd should apply PAYE to the full amount of KC's earnings, which would lead to an over-deduction of tax. However, the company can make an application to HMRC for them to make a determination under s.690 ITEPA 2003. The company would then be able to apply PAYE only to the proportion of earnings that relate to UK duties. The earnings for non-UK duties would have to be remitted to a bank account outside the UK.

Fibrotech Ltd is responsible for deducting the tax due on its employees' earnings under PAYE and paying this over to HMRC. It can use commercial payroll software or outsource the function to a third-party payroll provider. Alternatively, it can use HMRC's 'Basic PAYE Tools' if it has no more than nine employees for whom PAYE should be applied.

For monthly-paid employees, PAYE deductions are typically made on a monthly basis with such deductions usually paid electronically to HMRC by the 22nd of the following month. However, if the total tax and NICs payable are less than £1,500 per month on average, the PAYE deductions can be paid to HMRC on a quarterly basis.

Kieran Clarke – NIC issues

As both the UK and ROI are EU member states, KC's NIC position will be determined by reference to the EU Regulations. Those rules operate to ensure that an individual can only be subject to the social security legislation of a single member state at any given time.

As KC is on a 'short assignment' (ie he is not expected to be in the UK for more than 24 months), he will remain in the ROI NI regime. He should apply for a Portable Document A1 from the ROI authorities which will exempt him from NIC in the UK during his secondment.

Other secondees

Where an individual works in the UK, any earnings paid are generally taxable in the UK, even if the individual is only working in the UK for a short period of time and remains non-UK resident. The earnings however may also be taxable in the individual's home country. If so, the home country should then give the individual relief for the UK tax paid.

However, it is possible to obtain an exemption from paying any UK tax if either:

1 The UK duties are incidental to the performance of the employee's overseas duties (unlikely to be the case here); or

2 The visitor claims exemption from UK tax under a Double Taxation Agreement (DTA). In this case the claim would be under Article 15 of the UK/ROI agreement.

Employees who are present in the UK for less than 60 days and remain contractually employed and on a foreign payroll are treated as employed by a foreign employer. So, if the additional staff members are seconded to the UK for fewer than 60 days, there should be no UK tax liability, provided they remain on the ROI payroll throughout their secondment.

However, if an employee is in the UK for between 60 and 183 days, full Treaty exemption from UK tax on employment income is only available where:

1 He remains contractually employed by the home country employer;

2 His remuneration is paid by an employer who is not resident in the UK; and

3 The remuneration is not borne by the UK, so not deductible in computing the profits of an enterprise chargeable to tax in the UK.

Therefore, if the London office bears the salary costs of the additional staff members, condition (2) would not be satisfied and the earnings would be subject to UK income tax.

Treaty exemption is normally claimed by the employee via the self-assessment return. However, such treaty exemption for earnings does not automatically absolve an employer from its obligation to apply PAYE on payments to employees working in the UK.

That obligation can, however, be removed if Fibrotech Ltd applies to HMRC for PAYE exemption under the Short Term Business Visitor ('STBV') rules.

A STBV Agreement can be obtained where:

- the employee is resident in a country with which the UK has a DTA covering employment income
- the employee is coming to work in the UK for a UK branch of an overseas company
- the employee is expecting to spend fewer than 183 days in the UK in a 12-month period, and
- the UK branch for which the employee will be working will not bear the remuneration costs (unless the employee is present in the UK for less than 60 days in which case this condition does not apply)

Obtaining a STBV Agreement will absolve Fibrotech Ltd from the obligation to make any PAYE deductions in respect of employees covered by the Agreement.

However, under an STBV Agreement, Fibrotech Ltd would still have certain reporting obligations to HMRC (which must be fulfilled by 31 May following the end of the tax year).

In all cases, HMRC require a list of individuals covered by the agreement plus further information, depending on the number of days the individuals spend in the UK:

- for employees present in the UK for fewer than 31 days there are no other reporting requirements
- for those here between 31 and 59 days, HMRC simply require confirmation that each short term business visitor remains contractually employed outside the UK and the 60 days do not form part of a longer period
- for employees present in the UK for between 60 and 90 days in the year, HMRC specify further additional information that the employer must submit for each short term business visitor
- for employees who are in the UK between 90 and 150 days in the year HMRC will require all of the above information plus a certificate confirming the employee's residence in the country from which they have been sent

It is likely to be advantageous to both the company and the visiting employees to enter into a SBTV agreement. The company will not have the compliance burden of operating PAYE in respect of the various short-term visitors and the employees themselves will not have to reclaim tax deducted under PAYE via the SA process.

MARKING GUIDE

TOPIC	***MARKS***
PAYE	*1*
KC:	
SRT and domicile	*1*
Split year treatment	*1*
OWR availability	*1*
Implications of OWR applying	*1*
Remittance basis	*1*
PAYE if OWR applies	*1*
PAYE practicalities	*2*
NIC for short assignment	*1*
Other secondees:	
Basic position	*1*
Exemption	*2*
Implications if < 60 days	*1*
Implications if 60 to 183 days	*1*
PAYE including STBV rules	*2*
STBV reporting requirements	*2*
Conclusion on SBTV agreement	*1*
TOTAL	***20***

8. KNOWLE PLC

The first thing to consider is Selwyn's UK tax residence position using the statutory residence test.

Selwyn is not automatically non-UK resident as he expects to spend more than 15 days in the UK and cannot satisfy the overseas work test as although it appears he will spend less than 91 days in the UK, he will spend more than 30 days working in the UK over the course of the tax year.

On the assumption that the assignment to Portugal will last at least until 5 April 2021, Selwyn will not be automatically UK resident, as he will not be spending 183 days in the UK during the tax year. He will also not be automatically UK resident under the 'home' test as, although he retains a home in the UK, he will also have a home in/near Lisbon where he expects to spend at least 30 days in the tax year. As Selwyn will not work full time in the UK in 2020/21, the third automatic UK test will not be passed either.

However, Selwyn will be UK resident under the 'sufficient ties test'. He has three ties to the UK.

1 An 'accommodation' tie - Selwyn has available accommodation in the UK (the family home) and will make use of it for at least one night in the year

2 A 'work' tie - it would seem that Selwyn will work for at least 3 hours on at least 40 days in the year in the UK

3 A '90-day' tie - he will have been present for at least 90 days in at least one of the previous two tax years

Selwyn will not have a 'family' tie as his wife will accompany him abroad and his children being at university, we assume are over 18.

Selwyn has been UK resident in at least one of the three previous tax years and will therefore be a 'leaver'. He will be UK resident under the sufficient ties test if he spends 46 days or more in the UK. As he will spend one week a month in the UK, averaging approximately 60 to 84 days, this will mean that Selwyn's UK residence is retained.

Selwyn is moving to live in a country with which the UK has a DTA. Selwyn is likely to be resident in Portugal as he is will be living and working in Lisbon for the majority of the year. He will therefore be dual resident.

Under the tie-breaker clause of the Treaty, Selwyn will be treated as resident only in the country in which he has a permanent home. If he has a permanent home in both countries, he is deemed to be a resident only of the State with which his personal and economic relations are closer (his "centre of vital interests").

If this cannot be determined, he will be deemed to be a resident only of the State in which he has a habitual abode. Otherwise he is resident in the State in which he is a national.

On the facts given, it is likely that Selwyn will be treated as resident only in the UK.

Selwyn's earnings will therefore be fully liable to UK tax. DTA exemption is unlikely to be available in Portugal given the number of days Selwyn will spend there and so Selwyn will also be liable to overseas tax in respect of his non-UK employment duties. Relief will be available against Selwyn's UK tax liability for the foreign tax paid.

Knowle plc has a tax presence in the UK and will therefore be required to apply PAYE to the full amount of Selwyn's earnings. It may also be required to deduct foreign tax and account for that tax to the overseas tax authority. In this case, advance DTR can be given through Selwyn's PAYE code under the 'net of foreign tax credit scheme'. Knowle plc should make an application to HMRC to use this scheme.

No taxable benefit will arise for Selwyn if his travel costs to and from Lisbon are borne by the employer (whether they relate to the start/end of the assignment or to business trips back to the UK). However, because the Lisbon office will be regarded as a permanent workplace, any accommodation or subsistence provided by Knowle plc in Portugal will be a taxable benefit. The exact tax treatment will depend on how the benefit is provided. For example, if Knowle plc reimburse Selwyn for his expenses, this will be treated as earnings and subject to PAYE. If Knowle plc provide the accommodation, it will be a benefit reportable on P11D and Selwyn will pay any tax directly through self-assessment.

National Insurance Contributions (NIC)

As both the UK and Portugal are EU member states, Selwyn's NIC position will be determined by reference to the EU Regulations. Those rules operate to ensure that an individual can only be subject to the social security legislation of a single member state at any given time.

Selwyn will be performing duties both in the UK and Portugal. In such a case, he will be within the social security regime of the country where he is habitually resident if he spends at least 25% of his working time there. If he spends less that that proportion of time working there, he will be covered by the social security provisions of the country where his employer has its registered office.

For NIC purposes, it is likely that Selwyn will remain resident in the UK as he is habitually resident in the UK and the centre of his vital interests are in the UK. There is no indication that the centre of his interests will move to Portugal.

If Selwyn spends 25% of his working time in the UK, he should continue to pay NICs in the UK. Even if it turns out he spends slightly less than 25% of his working time in the UK, the UK NIC system would still apply as Knowle plc has its registered office in the UK.

Knowle plc should apply to HMRC for a Portable Document A1, confirming that home country contributions will continue and ensuring that no Portuguese contributions will be due.

MARKING GUIDE

TOPIC	***MARKS***
Residence determined by SRT	*½*
Not automatically overseas resident	*1*
Not automatically UK resident	*1*
Sufficient ties test	*2*
Application of DTA and conclusion as to treaty residence	*2½*
UK tax on all earnings	*½*
Possibility of liability to Portuguese tax on Portuguese workdays – exemption in DT unlikely to apply	*1*
Knowle plc to apply PAYE – mention net of foreign tax scheme	*1*
Travel costs exempt	*1*
Accommodation taxable	*1½*
NIC: EU provisions apply	*½*
Work for same employer in 2 MS – country of hab. res if work >25%	*1*
If < 25%, country where employer has registered office	*½*
Conclusion – Selwyn still in UK system	*½*
Knowle plc to apply for PD A1	*½*
TOTAL	***15***

9. HARRY MARKHAM

OJAA Tax Consultants
[Address]

Mr H Markham
BreakOut Ltd
[Address]

[Date]

Dear Harry

As discussed, I am writing to set out the tax treatment of the three alternative methods of incentivising Daisy through the award of 5,000 shares in BreakOut Ltd. I have also outlined the company's reporting obligations.

<u>Registration and annual reports</u>

BreakOut Ltd must register any of the schemes it decides to use by completing an online annual report to HMRC for every tax year an employee holds shares, or options over shares, in the company. The return is due by 6 July following the end of the tax year. The report should include details of anything that has happened in connection with the shares or options. If nothing has happened, the company must submit a nil return. Penalties apply for failures to make annual reports.

<u>Outright share award of shares at a price of £2.50 per share</u>

Where employees are awarded shares in their employer's company, the market value of the shares less the amount the employee pays for them is immediately taxable as earnings, ie £5.00 - £2.50 = £2.50 x 5,000 = £12,500. If the shares are 'readily convertible assets' (RCAs), ie broadly if the shares are or are expected to be marketable, the company is also obliged to account for income tax under PAYE and to collect employee's Class 1 national insurance contributions (NICs) and pay over employer's Class 1 NICs in respect of this taxable amount. That is not the case here since there are no trading arrangements for the shares or any explicit understanding in existence at this time. As the tax is not recovered from Daisy via PAYE, she would have to pay this over to HMRC in line with the normal self-assessment deadlines (31 January following the end of the tax year in which the tax charge arises). NIC is not due.

With regard to the loan to Daisy to enable her to subscribe for the shares, as the loan would be interest-free the 'cash equivalent' of the loan, based on interest at the 'official rate' of 2.5% would normally constitute a benefit in kind to be declared on form P11D. However, where the loan is used to buy shares in a close company and the employee is either acquiring a material interest in the company (5% or more) or works full-time in the company, then no benefit arises and no P11D entries are required.

Daisy's gain on disposal, less the annual exempt amount (currently £12,000), would be taxable to capital gains tax. Depending on how long she will hold the shares for and assuming she will still retain at least 5% of the share capital, she should be entitled to entrepreneurs' relief, limiting the rate of capital gains tax to 10 per cent.

<u>Option to purchase the shares at £5 each if the company is sold</u>

No income tax charge arises on the grant of a share option. However, where an option is not granted under a tax-advantaged share option scheme, when the option is exercised, the market value of the shares less the option price (if any) is liable to income tax. The taxable amount of employment income assuming the shares would be worth £15 at the time of exercise would be £15 - £5 = £10 x 5,000 = £50,000.

As the option would be exercised in anticipation of the sale of the company, the shares would at that point be RCAs and the company would definitely be obliged to operate PAYE and account for employee and employer's Class 1 NICs.

BreakOut Ltd could consider including a clause in the option agreement requiring Daisy to pay the company's Class 1 employer's NIC liability. The amount of employer's NICs that Daisy pays as a result of such a clause will reduce her taxable employment income.

The company must include the employment income arising on exercise of the option (net of any employer's NIC paid by Daisy) in a Full Payment Submission (FPS) which it must send to HMRC on the earlier of the date it operates PAYE on the payment and the payment deadline for tax and NIC (ie 14 days after the end of the tax month in which the exercise takes place).

If there is insufficient salary being paid to Daisy to deduct the income tax due under PAYE from then she must 'make good', ie reimburse, the income tax due under PAYE to the company within 90 days after the end of the tax year in which the option is exercised. If Daisy does not do so, the amount of income tax paid by BreakOut Ltd via PAYE on her behalf must be entered on form P11D. Class 1 NICs are also payable. If Daisy then reimburses the income tax after the 90 day period has expired, and the income tax has been treated as a benefit, no further adjustment is able to be made.

In the event of an immediate sale of the company, the sale of the shares will be a disposal by the Daisy for CGT purposes, but assuming the base cost of the shares on acquisition (market value) and the sale price of the shares are the same, no capital gain would arise.

<u>EMI option to purchase the shares at £5 each if the company is sold</u>

As this is a tax-advantaged scheme there are additional reporting requirements for BreakOut Ltd. If it chooses to use an EMI scheme, the terms of the option will need to be in writing and BreakOut Ltd will need to register the scheme online with HMRC.

After HMRC have registered the scheme, they will provide a registration number and the grant of options must then be reported to HMRC within 92 days of the date of grant. BreakOut Ltd will also need to complete an annual report as described above.

No income tax charge arises on exercise of an EMI option if the option price is not less than the market value of the shares at the time of grant. As above, in the event of an immediate sale of the company, the sale of the shares will be a disposal for CGT purposes. Any gain will be calculated on any proceeds in excess of the exercise price.

<u>Corporation tax relief</u>

Corporation tax relief is available for employee share awards whether acquired outright, under a non tax-advantaged share option, or under a tax-advantaged share option scheme such as EMI.

Certain requirements must be met for BreakOut Ltd to qualify for corporation tax relief, one of which is that the company must not be under the control of another company. This is not in point of course in the case of an outright share award, and if an option were granted this will be exercisable immediately prior to sale and so relief should be available.

<u>Conclusion</u>

An outright award of shares will give Daisy the immediate benefits of share ownership. This is also the cheapest alternative for Daisy as she would be paying £12,500 for the shares plus would have taxable income of £12,500. However, she would need to fund the price and associated tax and would also be open to the risk that the share price might go down and/or a buyer is not found.

The grant of a non tax-advantaged option allows risk and cash flow to be managed until a deal is anticipated. However, it is not tax-efficient as Daisy will pay income tax on the whole of the commercial growth in value when the option is exercised and the company would incur substantial NIC costs.

The EMI route, taking into account corporation tax relief and the absence of income tax charges and NIC costs, is clearly the most tax-efficient option, despite the additional initial reporting requirements. This may also be preferable to an outright award of shares in terms of incentive effect and would therefore be my recommendation.

I trust the above is helpful. If you have any queries or would like to discuss the alternatives further, please do not hesitate to contact me.

Kind regards

Yours sincerely

A Tax Manager

MARKING GUIDE

TOPIC	***MARKS***
Registration	*½*
Annual report (incl. nil returns)	*1*
Penalties	*½*
Option 1	
Charge to income tax as earnings	*1*
Consider RCA status and conclude no PAYE/NIC	*2*
No BIK on loan due to exception	*1*
Gain on disposal, with possibility of entrepreneur's relief	*1*
<u>Option 2</u>	
No charge on grant of options	*½*
Charge to income tax on MV on exercise	*1*
RCAs so PAYE/NIC payable	*1*
Pay employer's NIC	*1*
Include in FPS	*1*
Reimbursement of PAYE/application of 90 day rule	*1*
Treatment as BIK with Class 1 NIC if not reimbursed within deadline	*½*
No CGT on sale as acquisition at MV = sale price	*½*
<u>Option 3</u>	
Register scheme within 92 days and Report grant	*½*
No charge to tax on exercise of EMI option granted at MV	*1*
<u>Company:</u>	
CT relief	*1*
Control requirement	*1*
Conclusion – comparison of alternatives	*1*
Presentation and higher skills	*2*
TOTAL	***20***

10. CRABTREE LTD

BRIEFING NOTE

To: Owen James
From: A Tax Manager
Client: Crabtree Ltd
Date: 10 May 2020

1. Tax Implications of Proposed Termination Package

To determine the tax implications of the proposed package for Gordon it is first necessary to determine the nature of the payments comprised in that package.

Under general principles, amounts that constitute earnings will be taxable as earnings. Payments that are not related to the employment, that is, are neither part of the contract of employment nor a reward for services, cannot be taxed as earnings. However, if the payment can be classed as a redundancy payment or compensation for termination of employment, they will be governed by ITEPA 2003 s401.

Considering each of the elements in turn:

Pay In Lieu of Notice or Garden Leave

Gordon is contractually entitled to three months' notice but the company is considering whether to summarily terminate Gordon's employment following closure of the plant hire business or to give notice and advise him to take 'garden leave'. In both circumstances, the amount will be subject to income tax and Class 1 NIC.

If the company summarily terminates the employment, Gordon will be treated as receiving "Post Employment Notice Pay" equivalent to the basic salary he would have had if he had worked out his notice, ie £9,000. This amount will be subject to income tax and Class 1 NIC.

Alternatively, if the company gives three months' notice but gives Gordon 'garden leave' the employment does not terminate until the end of the notice period. The salary payments for those three months, whether paid monthly or in a lump sum, are liable to income tax as earnings, and NIC in the normal way through PAYE.

Contribution to pension scheme

Employer's contributions to a registered pension scheme are exempt from income tax.

Statutory redundancy payment

The Statutory redundancy payment of £2,500 is exempt from taxation as employment income and therefore comes within the scope of s401 ITEPA 2003. Under s.401 only the excess of termination payments (including any exempt statutory redundancy payments) over £30,000 is liable to income tax and, as the proposed payments are below £30,000, no tax is due. Class 1 National Insurance Contributions are only payable in respect of 'earnings' and therefore does not apply here.

Additional redundancy payment

The additional redundancy payment of £2,500 is within the terms of an established scheme. HMRC are therefore likely to accept that it is also a redundancy payment and as such is within the exemption within s401.

Additional payment of £30,000

If Gordon had a contractual entitlement to compensation on termination of his employment or this payment was expected or customary (which as the company has no established practice of making such payments it would not have been), as long as the additional payment of £30,000 is compensatory rather than 'in the nature of earnings' it will not be employment income.

There is always the danger that, as Gordon is not far from retirement age, HMRC will however re-categorise the payments to him as payments from an Employer Financed Retirement Benefit Scheme (EFRBS). If so, the payment will be fully taxable, and the £30,000 exemption will not be available. As the plant hire business is actually closing down and presumably, at 53, Gordon can show that he is intending to continue working this should be easy to dispute.

On the basis that the payment is not treated as a retirement payment, the position is governed by s401. As total payments under s401 (including the redundancy payments) amount to £35,000 and the exemption only extends to £30,000, the excess of £5,000 will be subject to income tax, accountable through PAYE. The whole amount of £35,000 will be exempt from NIC.

The company will need to report the payment in lieu of notice (or wages on a garden leave arrangement and the excess of £5,000 on a Full Payment Submission (FPS) under the Real Time Information (RTI) system. The FPS needs to show the taxable payments and the associated tax and NIC due. The due date for the tax and NIC is 14 days after the end of the tax month in which the payment is made, ie the 19th of the month, unless the company pays electronically in which case it has until the 22nd of the month to make the payment.

2. Corporation Tax Deductions

Relief for statutory redundancy payments is specifically provided by the legislation. Relief for payments in addition to redundancy, up to three times the statutory redundancy paid, is also allowable where a company ceases to carry on a trade or part of a trade.

The redundancy payments to Gordon will therefore be allowable.

If the company decides to pay Gordon three months' notice and pays this through his salary in the normal way it is merely meeting its contractual obligations and the payments will be allowable.

However, if the company decides to summarily terminate Gordon's contract of employment and make a payment in lieu of notice the payment is not in accordance with the company's contractual obligations but is in fact compensation for breach of contract and could be argued not to be allowable. The compensation payment to Gordon, however, is not a contractual obligation, and not arising from any such obligation and will likely be disallowable on general grounds, ie it is not wholly and exclusively for the purpose of the company's trade but for its end.

The rules for deductibility of company pension payments are also subject to the wholly and exclusively rule. If the payment was made under the terms of Gordon's contract of employment it would be allowable but otherwise it would not be allowable.

MARKING GUIDE

TOPIC	***MARKS***
Part 1:	
Treatment of redundancy payments generally	*1*
Contractual payments t/a earnings	*1*
Elements of the package:	
Treatment of PENP	*1*
Treatment of 'garden leave'	*1*
Treatment of contribution to Pension	*1*
Treatment of SRP	*1*
Treatment of additional SRP	*1*
Treatment of compensation	*1*
Application of £30,000 limit	*1*
PAYE on excess	*½*
Compensation not t/a earnings for NI purposes	*½*
EFRBS issue	*1*
RTI obligations for taxable payments	*1*
	12
Part 2:	
Deduction for statutory redundancy payment & additional SRP	*1*
Deduction for Garden Leave payment as contractual payment	*½*
Disallowance of compensation of breach of contract	*½*
General disallowance of payments on closure/ wholly & exclusively rule	*½*
Treatment of pension payment	*½*
	3
TOTAL	***15***

11. BESTREST HOTELS UK LTD

1) Employee's contributions

Nikolas will be able to claim tax relief in respect of his contributions to the Cypriot scheme, in the same way as if they were to a registered UK pension, if the scheme is a qualifying overseas pension scheme (QOPS) and Nikolas is eligible for migrant member relief (MMR).

To be a QOPS, the overseas pension scheme to which the contributions are made must either be established in an EU/EEA member state or be regulated and be recognised in the country in which it is established. It must also satisfy the tax recognition test, which essentially means it is open to residents in the country where it was set up, is registered with the local tax authority and tax relief against personal income tax is given on either, contributions to, or payments from, it.

As the Bestrest Hotels (Cyprus) Ltd occupational pension scheme was set up locally, Cyprus is a member of the EU and Nikolas has received tax relief for his contributions, the Cypriot pension scheme appears to meet these requirements.

The conditions for MMR to apply to Nikolas are that he must firstly be a 'relevant migrant member' which means he must:

- Have joined the overseas scheme at a time when he was not UK resident (UK resident in this context means he has arrived in the UK to live not 'tax resident')

- Been an existing member of the overseas scheme, having joined before he was UK tax resident

- Have been entitled to tax relief on contributions to the scheme immediately before coming to the UK

- Have been notified by the overseas scheme administrator and received confirmation by them, that information relating to benefit crystallisation events will be sent to HMRC.

For migrant member relief, the relevant migrant member must meet the following conditions:

- Have UK relevant earnings
- Be resident in the UK when the contributions are made
- Have notified the scheme administrator that he intends to claim MMR in the UK.

Nikolas is resident in the UK for 2019/20 as he will spend well more than 183 days here. It is possible that 2019/20 will be a split year, but this does not matter as he will only be seeking UK tax relief for the UK part of the year. His salary from Bestrest Hotels UK Ltd means that he will be in receipt of UK relevant earnings.

This means that he meets the virtually all the conditions above and can presumably arrange for the scheme administrator to issue the confirmation required to meet the fourth condition.

It therefore seems that all conditions are likely to be met to allow Nikolas to claim MMR in respect of his continuing contributions to the Cypriot pension scheme, so he will be able to claim tax relief.

2) <u>Employer's contributions</u>

Employer contributions to an employee's overseas pension scheme are deductible for corporation tax (CT) purposes in the same way as if the contributions were being made to a UK registered pension if the scheme is a qualifying overseas pension scheme (QOPS) and the employee in question is one who qualifies for migrant member relief (MMR).

In the case of Bestrest Hotels UK Ltd, it will be able to deduct the contributions made in respect of Nikolas, as and when made. This is because Nikolas can claim MMR and the contributions on his behalf are to a QOPS.

If for any reason the MMR or QOPS conditions are not satisfied, the company could refer to the relevant double taxation agreement (DTA) to see whether that allows it to obtain CT relief for contributions when they are actually made.

If the DTA does not provide for this, it may instead allow the company to claim a deduction for the contributions at the time that the overseas pension scheme eventually provides benefits to the employee.

3) <u>Annual and lifetime allowance</u>

The UK rules on the annual allowance and lifetime allowance apply to pension contributions qualifying for MMR in the same way as they apply to pension contributions to a UK registered pension scheme.

For 2019/20, the maximum annual allowance is £40,000 but this is tapered to a lower level for taxpayers with relevant earnings over £150,000. As Nikolas's pay is £75,000, he has the full £40,000 annual allowance available. His expected level of contributions is £3,750 (5% x £75,000), with an employer contribution at the same level, so at this level of contribution there will be no annual allowance charge.

The lifetime allowance is tested at a benefit crystallisation event, such as when lump sums are paid or pension payments are first made from the fund. As at 2019/20 the lifetime allowance stands at £1,055,000.

If, at the time of testing, the proportion of the pension fund that relates to accumulated contributions that have benefitted from UK tax relief is more than the lifetime allowance, a lifetime allowance charge arises on the excess.

Unless Nikolas's rate of pension saving increases dramatically, given his current age of 42, he is unlikely to have to worry about a lifetime allowance charge.

MARKING GUIDE

TOPIC	***MARKS***
1) Employee contributions	
Relief same as for UK registered pension scheme	*1*
Conditions to be met by overseas pension scheme	*1*
Conclusion on QOPS status	*½*
Conditions to be met by individual for MMR	*2*
Check that Nikolas meets the conditions	*1*
Check that Cypriot pension scheme sends confirmation on benefit crystallisation	*1*
Conclude that MMR will be available	*½*
2) Employer contributions	
Deductible if paid to QOPS where employee qualifies for MMR	*1*
In same way as if to UK registered pension scheme	*½*
If not, look to DTA	*½*
Failing that, relief may still be available but only when scheme provides benefits	*½*
3) Annual allowance and lifetime allowance	
AA/LTA apply to contributions as if to a registered pension scheme	*1*
AA is £40,000 for 2019/20 – no taper in Nikolas's case	*1*
Nikolas's contributions < £40,000, so no AA charge	*½*
LTA is £1,055,000	*½*
Only accumulated funds derived from UK-tax relieved (employer and employee) contributions count towards it. This will include currently relieved non-UK pension schemes as well as registered UK schemes.	*½*
Tested at benefit crystallisation event	*½*
If UK tax relieved part of pension pot> LTA, tax charges arise on excess	*½*
Current level of contributions and Nikolas's age make LTA charge unlikely	*1*
TOTAL	***15***

12. BARBARY LTD

1) How Stephanie will be taxed

2019/20

In July 2019, Stephanie is granted convertible shares. The grant of those shares is by reason of her employment, making them employment-related securities.

There is a tax charge arising on the share award on 5 July 2019. The taxable amount is the market value (MV) of the Class B shares less anything that Stephanie pays for them (nil). The future right to convert the shares is ignored. This produces an amount chargeable to tax as employment income on 5 July 2019 of:

2,000 x £3.00 = £6,000

The company is unlisted and there is no mention of any arrangements to enable Stephanie to sell her shares. As such the shares will not be regarded as readily convertible assets (RCAs) provided the company is not controlled by another company.

This means that the tax on the £6,000 will not be recovered through PAYE. Stephanie will have to include this amount in her self-assessment for the year. Also, as the shares are not RCAs they are not considered to be earnings for Class 1 National Insurance Contribution (NIC) purposes and so no primary or secondary Class 1 NIC will be due.

2021/22

On 30 November 2021, the Class B shares are converted into the more valuable Class A shares. This is a ‘chargeable event’ and triggers a further income tax charge on Stephanie.

That tax charge is calculated as follows:

		£
Market value of Class A shares immediately after conversion	2,000 x £9.00	18,000
Less: market value of Class B shares immediately before conversion	2,000 x £4.25	(8,500)
Taxable employment income		9,500

As the shares are not RCAs, this amount of taxable employment income is outside PAYE and Stephanie will have to include this amount in her self-assessment for the year. Class 1 NICs do not apply.

Also, on 30 November 2021, Stephanie acquires an option to acquire a further 500 Class A shares. There is no tax charge arising on the grant of a share option.

2022/23

When Stephanie exercises her share option on 1 July 2022, a tax charge arises on the difference between the market value of the shares on that date and the amount that Stephanie pays for them (the exercise price):

		£
Market value of Class A shares on 1 July 2022	500 x £11.50	5,750
Less: Exercise price	500 x £6.20	(3,100)
Taxable employment income		2,650

Once again, as the shares are not RCAs, this amount of taxable employment income is outside PAYE and Stephanie will have to include this amount in her self-assessment for the year. Class 1 NICs do not apply.

On sale of shares:

When Stephanie comes to sell the shares, any profit would be subject to capital gains tax (CGT). The base cost of the shares for CGT is the total of any amounts paid for the shares plus any amount charged to income tax in respect of their acquisition.

For the shares acquired in 2021, the CGT base cost is the amount charged to tax as employment income of £6,000 + £9,500 = £15,500.

For the shares acquired in 2022, the CGT base cost is the amount paid for the shares plus the amount charged to tax as employment income: £3,100 + £2,650 = £5,750.

2) Reporting obligations for Barbary Ltd

As the shares are not RCAs, this amount of taxable employment income is outside PAYE, so the company does not have to include anything on any RTI submission, nor on Stephanie's Form P11D.

Instead, the reporting requirements in respect of a non-tax advantaged share scheme apply. A non-tax advantaged share scheme is any arrangement, however tightly targeted or short-lived, under which an employer awards employment-related securities or grants options over employment-related securities, to employees.

The company must register online with HMRC that it is operating a non-tax-advantaged share scheme by 6 July following the end of the tax year in which the securities are first awarded, or options first granted.

The company must also submit an annual return by 6 July following the end of the tax year for that and all subsequent tax years, even if there is that is a nil return. HMRC provide a special template for such returns.

On the assumption that no other share-based remuneration is paid, returns required from Barbary Ltd would provide details of the following events:

Tax year	
2019/20	Issue of Class B convertible shares
2020/21	Nil return
2021/22	Conversion of Class B shares into Class A shares and grant of option over further Class A shares
2022/23	Exercise of option granted in Nov 2021

Barbary Ltd would continue to have to make annual returns showing details of any other share-based remuneration until it notifies HMRC that its non-tax advantaged share 'scheme' has ended. It would have to register afresh if it later made any further share awards or option grants.

If the employer is late in submitting an annual return, there is an automatic penalty of £100. If the return is still outstanding after three months, there is a further penalty of £300. A further penalty of £300 applies for returns that are six months late and returns which are nine or more months late can be subject to a penalty of up to £10 per day.

If a return is incorrect as a result of a material inaccuracy due to fraud or negligence, then a penalty of up to £5,000 applies.

MARKING GUIDE

TOPIC	***MARKS***
1) How Stephanie will be taxed	
Identify that these are convertible employment-related securities	*½*
Tax charge on value ignoring right to convert (£6,000)	*1*
Not RCAs so not PAYE or NIC	*1*
Conversion to A shares in Nov 2021= chargeable event	*½*
Calculation of tax charge	*1*
Still no PAYE or NIC	*½*
Grant of option in Nov 2021 – no tax charge	*1*
Exercise of option in July 2022 tax on MV – exercise price	*½*
Computation	*½*
Still no PAYE or NIC	*½*
Base cost for CGT	*1*
	8
2) Reporting obligations for Barbary Ltd	
Nothing on RTI submissions or P11D	*1*
Not a tax advantaged scheme	*½*
Company still have to register scheme with HMRC by 6 July 2020	*1*
Annual returns required by 6 July following end of each tax year	*1*
Events to report in 2019/20	*½*
Events to report in 2020/21	*½*
Events to report in 2021/22	*½*
Events to report in 2022/23	*½*
Obligation continues until HMRC notified scheme closed	*½*
Penalties	*1*
	7
TOTAL	***15***

13. CANEFERO

Reimbursement of travel expenses will not amount to a taxable benefit if they are simply a reimbursement of what would otherwise be a deductible expense in calculating taxable employment income.

Where deductible expenses are reimbursed, no tax consequences arise and no reporting by the employer or employee is required.

Sections 337 and 338 of ITEPA 2003 govern the position in relation to reimbursement of travel expenses. Essentially a deduction will be allowed if the expenses are:

1 Necessarily incurred in travelling in the performance of the duties of the employment; or

2 Attributable to the employee's necessary attendance at any place in the performance of the duties of employment.

However, this does not extend to the expenses of ordinary commuting, ie going to and coming from the normal permanent workplace from home.

Looking at each employee in turn:

<u>Stan</u>

Stan's permanent workplace is Leeds. Although he will travel to Hull on a regular basis, he will be doing so for a period of less than two years. As such it is regarded as a 'temporary workplace' and travel expenses and subsistence are deductible.

<u>Julie</u>

Although the placement is expected to exceed twenty four months, Hull could still be regarded as a temporary workplace, if Julie's time there is less than 40% of her working time. However, because she will be doing two out of four days, this exceeds 40%. Her journey from home to Hull would therefore be classed as ordinary commuting. If she is reimbursed for her travelling expenses as suggested, these would amount to earnings and would be subject to PAYE and Class 1 NICs. Consideration might be given to reducing her time to 40% or less to avoid this.

<u>Jason</u>

Jason's journeys to Hull will be regarded as ordinary commuting, although he could still get reimbursement for costs of driving from the Hull office to his clients. This is even if he just calls in briefly prior to moving onto a client. The consequence of this is that some of his work provided fuel will be used for private purposes. Unless he reimburses all of this, he will therefore suffer a fuel benefit charge, calculated by multiplying £23,400 by the appropriate percentage. The appropriate percentage cannot be calculated without further details of Jason's car. However, it will be between 9 and 37% which is a significant amount, and one which is likely to outweigh the level of reimbursement. The fuel benefit charge is reportable on the company's P11d and also attracts employer's Class 1A NIC. It would be much more effective for Jason not to be reimbursed for these miles. If however, this is not an option, the company could consider giving him a cash amount to cover his extra expense which would be subject to PAYE and NIC but, in all likelihood, would be more cost effective.

MARKING GUIDE

TOPIC	***MARKS***
Reimbursement of properly incurred expenses not a taxable benefit	*1*
Deductible expense not reportable and have no employment tax consequences	*1*
General principles that work-related travel expenses are deductible except ordinary commuting	*1*
Stan – identifying that there is a temporary workplace because less than 2 years	*1*
Julie – identifying Hull is not a temporary workplace because placement likely to last more than two year and spends more than 40% of her working time there	*1*
Julie – noting any reimbursed expense will be subject to PAYE and Class 1 NIC	*1*
Julie – recommending work pattern is looked at	*½*
Jason – identifying travelling to office even on way to a client site is ordinary commuting and not a deductible travel expense	*1*
Jason - impact that this gives rise to a fuel benefit charge and level of charge	*1*
Jason – reported on P11d and subject to employer's class 1A NIC	*1*
Jason - conclude should not be reimbursed and other ways of compensating him be explored	*½*
TOTAL	***10***

14. SIMON JETSON

To: Franwiltshire@sporketmarkets.co.uk
From: gtm@sporketgroup.com
Date: 12 August 2020
Subject: Simon Jetson

Dear Fran,

Thank you for your email concerning Simon Jetson (SJ).

You are correct to be concerned as this is a complex area. Definitively establishing SJ's status in relation to Sporket Ltd is essential, as the company could be exposed to liabilities if HMRC were to successfully challenge his self-employed status.

If SJ is in fact self-employed, working under a contract ***for*** service, we have been correctly paying him gross, with no deductions for income tax or NICs.

However, if SJ is instead found to be an employee of the company, working under a contract ***of*** service, we should have been, and should continue, to pay him through the PAYE system, deducting income tax and employee's NIC, as well as accounting to HMRC for employer's NIC.

There are also other liabilities to consider should he be considered as an employee, such as providing him with holiday and sick pay and enrolling him in our pension scheme.

When determining employment status, each case must be looked at on its own merits. There are a number of key factors, which I have set out below, which need to be considered. HMRC looks at the overall picture rather than any particular one factor.

Mutuality of obligation

This is a very important factor as an employer is under an obligation to provide work for their employee, and likewise an employee is under an obligation to carry out the work assigned to them. Where a worker has the right to decide whether to accept a particular assignment or not, then this is a strong indication of self-employment. Equally strong, from our point of view, is the fact that if there is no work for the worker to do then we do not use them, and therefore do not have to pay them. It is this flexible resource that makes freelancers attractive to us.

As SJ does work for other clients when we are unable to provide sufficient work, this is an indication of self-employment, but not likely to be a strong enough factor on its own to establish that there is no employment, particularly as he only searches for other work when we have nothing for him to do.

Control

If the worker is an employee they have less control over what, where and how they carry out their work. Theirs will be a master/servant relationship in relation to the company. Conversely a self-employed person is their own boss and they can please themselves largely when, where and how they will carry out the work. However just because a worker works our normal office hours on our premises does not automatically mean that they are under our control, it is more a matter of the nature of their work, who they report to and their level of autonomy.

Based on the information provided, I can see that SJ is under the direction of the director in charge of the client account. It is arguable therefore that SJ has more of a master/servant relationship than being his own boss, which would support the view that he is employed.

Provision of equipment

An employee is rarely expected to provide their own equipment, while a self-employed person is usually responsible for providing the necessary equipment to perform the work. However, in our industry where it is someone's knowledge or skills that are important the provision of equipment tends to be a minor issue. Therefore, simply using our equipment does not, on its own, indicate that SJ is an employee.

Substitution

The ability for a worker to send a substitute is an indicator of self-employment. This is because an employment contract, by contrast, is a personal contract and cannot be assigned. However, simply having a substitution clause in the contract does not automatically give self-employment status if the reality is a substitute is never sent, or if sent would not be acceptable to us for the work. We would not accept a substitute and would expect SJ to carry out his obligations personally, which is an indicator of employment status.

Financial risk

If there is financial risk, then this is an indication that someone is self-employed. If the worker can increase their profit by their own efficiency or if they must put matters right in their own time if work does not meet requirements (as we saw above), then these are financial risks just as much as a worker risking their own capital in taking on an engagement.

Presumably SJ would be responsible for any remedial work and must submit invoices before receiving payment, which would strongly indicate that he is self-employed.

Integration

Would the worker be considered by the outside world as being 'part and parcel' of the operation? This test becomes more important if the worker continues to work for us rather than simply on a particular project. If the worker has a title and is provided with administrative support, also such seemingly trivial matters such as being included in the telephone list and invited to staff functions, then this would all indicate employment. It is arguable that even someone engaged by the company for only a six month period can be considered an 'integral' part of the team, in which case SJ could be considered to be in the position of an employee.

Number of paymasters

If a worker has a number of customers, then this is a strong indication of self-employment because no one customer can have exclusivity. This is especially strong if the work is carried out concurrently for different customers. If a worker has only one employment at a time however, HMRC can argue that there is a series of different employments.

As well as the above factors it is very important to review any written terms and conditions to see how they reflect the relationship that is being established. What is written down in the contract or letter of terms must reflect the facts. For example, if the contract includes a substitution clause, then it must be accepted that a substitute would be used.

Conclusion

This is not a clear-cut case and we should ask SJ whether he is VAT registered and whether he has a standard contract or letter that he uses. If so, this should be reviewed to ensure that it clearly specifies that self-employment is the intended relationship, and that SJ accepts responsibility for his tax and national insurance contributions. Provided there is satisfactory paperwork that indicates SJ accepts responsibility then I would be confident continuing on the basis that he should be treated as self-employed.

HMRC status challenge

If, however, HMRC successfully challenges SJ's self-employment status and re-categorises him as an employee of the company, they will seek to recover the cost of the tax and NIC that should have been deducted under PAYE. This re-categorisation will treat the amount paid to SJ as the equivalent of his take home pay.

HMRC may seek to recover the tax and employee's and employer's NIC from us, as the engager, by way of a contract settlement. If that is not agreed, they will use a Regulation 80 determination.

If we can establish that, as an employer, we have taken 'reasonable care' to comply with the PAYE regulations, and the failure to deduct was due to an error made in good faith, HMRC would automatically try to recover amounts due from SJ himself first. Again, they could do this by way of a contract settlement or, if that cannot be agreed, by a Regulation 72 determination. A Regulation 72 determination can only be issued if a Regulation 80 determination has not already been made, so they could do this first, regardless of our position on reasonable care.

Whomever they seek to recover tax and NICs from, HMRC may also pursue interest and penalties.

At this stage, it would be advisable to review the contract documentation we have with SJ to ensure that we are in fact treating him correctly and document the findings accordingly.

I suggest that once you have had a chance to consider the contents of this email and collate the contract documentation, you contact me so we can discuss and agree how to take the matter forward.

Kind regards

Tim

MARKING GUIDE

TOPIC	***MARKS***
*Key differences in employer obligations between Contract **for** service and contract **of** service*	*2*
Determined by reference to facts of the case	*1*
Key factors – explanation and conclusion	*3½*
Written contract	*1*
Conclusion	*2*
Re-categorisation	*1*
Tax and NIC via PAYE	*1*
Determinations	*1½*
Interest & penalties	*1*
Presentation and higher skills	*1*
TOTAL	***15***

15. ECHO UK LTD

Residence and Domicile

The starting point is the need to determine the residence and domicile status of the employees.

As far as domicile is concerned, the transferred and seconded employees will only be regarded as UK domiciled if either:

- They were born in the UK, and at that time had a UK domicile of origin, had lost that domicile through a domicile of choice (presumably in Ecuador) and now become UK tax resident again; or

- They form a permanent intention to stay in the UK, cutting all ties with their previous country of domicile

Whilst it is probably the case that most employees will remain non-UK domiciled, the exact circumstances should be checked once the transferring and seconded individuals have been identified.

The UK has a Statutory Residence Test (SRT) to determine tax residence for individuals. The SRT determines whether a person is resident in the UK for a tax year by taking into account both the time spent in the UK and other 'ties' or connections an individual has to the UK.

There are three parts to the SRT: the 'automatic overseas test'; the 'automatic UK test'; and the 'sufficient ties test'.

An individual will be non-UK resident if they meet any of the automatic overseas tests. These tests look at and consider the number of days the individual is present in the UK (there is another test concerning full-time work outside the UK but this would obviously not be relevant to the individuals coming from Ecuador to work in the UK).

If none of the automatic overseas tests are met, an individual will be resident in the UK if they meet any of the automatic UK tests.

It is unlikely that the seconded employees will meet any of the automatic overseas residence tests as they will be working in the UK for periods of three months upwards. This is on the basis that the short secondments do not cross a tax year.

The employees that are on longer secondments (it is noted these will be up to five years in length) are likely to meet one of the 'automatic residence tests' as they are likely to be present in the UK for more than 183 days and/or have either their only home in the UK, or if they have kept their home in Ecuador, they spend no more than the permitted amount of time in it.

The position of the rotating employees may be more complex: it is likely they will spend between 46 and 182 days in the UK and as such the 'sufficient ties' test will need to be considered, looking at the ties of the individual such as family, accommodation, work and any previous presence in the UK.

If an employee comes to the UK part way through the UK tax year (which runs from 6 April) and is found to be UK resident under the rules, this will usually count for the whole tax year. Sometimes however, they may be eligible for 'split year' treatment for their tax residence, where they are treated as non-resident for the part of the year before their arrival in the UK. Similarly, a UK resident secondee leaving the UK to return to resume work at EQO in Ecuador can be treated as non-resident in the UK for the part of the tax year after departure.

Earnings

All employees are taxed in UK on earnings for duties performed in UK at the time that these earnings are received.

Employees who are both UK resident and domiciled are chargeable on all earnings regardless of where the work is performed or the earnings are paid.

If the employee is resident in the UK but is not UK domiciled, they can (by election) be taxed instead on a remittance basis in respect of any income arising outside the UK. If an employee on the remittance basis has a continuous period of non-UK residence lasting for three of the five previous tax years, they will qualify for Overseas Workday Relief (commonly known as OWR). OWR may be given for the first three years of residence in the UK. Under OWR earnings from duties performed outside the UK are only taxed in the UK if they are remitted (brought to) the UK. Earnings in relation to the contract for UK duties would be taxable in the UK on an arising (receipts) basis.

An election is required for the remittance basis each year unless total unremitted income and gains are less than £2,000 for the year. A side effect of claiming the remittance basis is that the employee would not be entitled to claim a UK personal allowance (the amount of annual income an individual can have before starting to pay tax, currently £12,500), or the annual exempt amount for capital gains (a similar allowance for gains currently standing at £12,000).

Employees who are not UK tax resident are taxable in the UK only for duties performed in the UK.

Travel expenses

In general, travel, accommodation and subsistence expenses will be free from tax if paid by the employer provided that the stay in the UK is intended to be temporary, ie less than 24 months under the temporary workplace rules. As soon as it is apparent that the period in the UK will exceed 24 months, such expenses will be taxable on the employee.

Even if the 24 months are exceeded, special rules apply to employer-funded travel expenses for non-domiciled employees, exempting them from a charge on travel expenses met by the employer between their normal home (if outside UK) and their UK place of employment for five years from their first arrival in UK.

Special rules also apply for the spouse, civil partner or minor child of a non-domiciled employee providing a similar exemption on the condition that the employee spends at least 60 continuous days in the UK, although this exemption only applies to two return trips per tax year.

Bonuses

The bonuses will follow the same pattern as for all other earnings. If they are in respect of duties performed in the UK, they will be taxable in the UK when received. This applies even if the payment is delayed until the employee has ceased to be resident in the UK.

Share options

The tax treatment of share option gains for internationally mobile employees involves statutory apportionment based on UK and non-UK workdays.

That apportionment means that part of the gain will be taxable on the arising basis, part on the remittance basis and part of the gain is non-taxable. In broad terms, the share option gain is treated as accruing evenly across the period between grant of the option and the date the option becomes capable of exercise. The portion of the gain that relates to workdays which give rise to earnings not chargeable to UK tax is ‘unchargeable foreign securities income’; the portion of the gain that relates to workdays which give rise to earnings charged in the UK on the remittance basis is ‘chargeable foreign securities income’ (and is itself taxed on the remittance basis). The remainder of the gain is taxed on the arising basis.

Apportionment can apply where an employee is given split year treatment for residency in a year.

As far as share option gains are concerned, the UK National Insurance (NIC) treatment is not aligned with the income tax treatment. Instead, income from employment related securities which is attributable to days when the employee is not within the charge to UK NI is disregarded and is not subject to UK NIC Contributions.

Tax equalisation

Tax equalisation is not a statutory concept, but an arrangement between the employer and the employee. It is the process by which the employer ensures that the employee is in the same net position as if he had not taken up the overseas assignment.

The employer deducts from the employee’s pay the amount that would have been due under home regime (hypothetical or ‘hypo’ tax) but pays over to local tax authorities where the seconded employee is working, the actual amount due under local tax laws, making up the difference if more, and can also pocket the difference if less.

The employee’s net earnings would be the amount after deduction of the hypo tax. As this is also the amount of their net earnings in the UK, the employer has to gross up that amount by reference to UK rates when working out how much to pay over to HMRC. A special modified PAYE scheme is available in tax equalisation cases.

National Insurance (NIC)

If the employee is assigned to the UK, a NIC liability will potentially arise for both employee and employer. If the employees are employed by Echo (UK) Ltd, NIC will be due on all of their remuneration from the UK company. However, if they were engaged by EQO and previously worked outside the UK, they will not be subject to UK NI for the first 12 months from their arrival in the UK, as their employer has a place of business outside the UK.

Paying through non-UK company

The use of a non-UK employer to pay salaries and bonuses will not escape PAYE. As the employees will be working for the UK company in its business, the UK company will be obliged to account for PAYE and NIC in respect of the amounts paid to the employee by the overseas employer.

MARKING GUIDE

TOPIC	***MARKS***
Domicile status of employees – overview of general rules	*1*
Residence status of employees – overview of general rules and application to employees	*4*
Tax impact if all UK	*1*
Non UK doms – remittance basis/ OWR	*2*
NR	*1*
Travel expenses and accommodation and subsistence	*2*
Bonus	*2*
Share options	*2*
Tax equalisation	*2*
NIC	*2*
Payment by overseas employer ineffective	*1*
TOTAL	***20***