<u>Question 1</u>

(1) All figures in £, so don't have to do foreign exchange translation.

Will look at each entity individually, then look at TL.

Note, given no entities

EL (5%)

Profit 3,000,000
Local tax 900,000
UK tax equivalent at 20% 600,000

Dividend not tax exempt, as not TE not SME and not from controlled company.

No credit for share of underlying tax on profit for dividend (900,000) as not 10% beneficial owner

Credit for WHT on dividend of £2,500

M

Profit 2,000,000

Local tax 300,000
UK tax equivalent at 20% 400,000

M is a branch, and not a separate legal entity to TL, and TL as a company based on the UK is taxable on its worldwide profits.

So M's profits are part of the consolidated profit for Tea Ltd (UK) TL of £500 million

Will receive credit for tax on profit of PE in poland, as has not made section 18A branch exemption election. Will get lower of credit between UK and Polish tax, being 300,000

LS (100%)

Profit 1,000,000
Local tax 300,000
UK tax equivalent at 20% 200,00

As a beneficial recipient (over 10% own, at 100%), get credit for full ULT of 300,000 on profit. Gets credit for lower of UK tax on relevant income and O/S tax, meaning credit will be for 200,000. Also gets credit for WHT of 20,000 on dividend.

Dividend tax exempt, as from from controlled company, no deduction, not part of tax avoidance scheme (Section 931). Also, part of dividend referable to preference shares should be

HCI

Profit 5,000,000

Local tax 900,000
UK tax equivalent at 20% 1,000,000 (51% is 510,000)
WHT is 30% on 1,000,000 (net dividend 950, plus WHT 50,000), being 300,000

As 51% owner, gets credit for underlying tax pro-rate on profits of 459,000 (900,000 x 51%) (gets foreign tax, as lower), and gets WHT of 50,000

Dividend tax exempt, as from from controlled company, no deduction, not part of tax avoidance scheme.

Thus, WHT is charged at 30%

Tea Ltd

Income 5,700,000

total tax at 20% 1,140,000

plus EL dividend of 50,000 taxed at 20% = 10,000

equals total UK tax at 1,150,000

less credits

Credits

EL WHT 2,500
M Tax 300,000
LS WHT 20,000
LS ULT 200,000 (UK tax equivalent lower)
HCI ULT 459,000 (lower of)
HCI WHT 300,000

total credit 1,281,500

Total UK tax less credits = 131,500 tax excess, no UK tax to pay

(2) Supply from TL to M (Poland, EU)

Goods

Place of supply, if goods leave UK, is UK, if goods arrive in UK is not UK.

Intra group dispatch inside EU, so providing VAT reg details given, zero rated.

Management services

Business to Business, place of supply is poland, VAT applied there.

Supply from TL to LS (Italy, EU)

Goods

Zero rated inside EU if Italian VAT registration details provided - intra group, deemed supply.

Management services

As B2B, place of recipient, being Italy.

Supply from TL to LS (Ruri, Non-EU)

Goods

Goods exported outside EU, place of supply is UK, but zero rated for VAT. Need good proof of export (eg bill of lading).

Management services

Services outside EU, but not to EU business, so place of supply UK, VAT fully chargeable.

(3) Disagree with the statement for several reasons.
One, dividend will not be exempt under current rules if a deduction is given in relevant territory. This is possible, and therefore would be taxed. Thus, in distinguishing a branch and sub on dividends, can't guarantee dividends received by company not taxed.
Two, law may change in the UK or the the O/S country, and given it could take to exit an investment (years), taxation of dividends should still be taken into account in choice branch/sub.
Three, branch exemption is hard to enter if PEs already have losses, so profits may be exempt, but exemption may not apply if too many losses. So tax still a factor.
Four, may not want PE exemption for WHT reasons under a relevant DTA eg may get lower
WHT rate if dividends subject to tax in UK that is a greater benefit in terms of cost.

Five, tax should still be a factor in branch vs sub choice because even if dividend and dividend exemption work, PE exemption arguably more complex to track, so sub better from this view.

Question 2

(1) Issue Does H establish a PE

There is likely to be a PE.

Relevant law

A permanent establishment (PE) is defined (Art 5 DTA) as either a:

1) Fixed place of business through which the RAB's business is carried on in whole or part by a dependent person; and/or

2) a dependant agent(economically/legally) who has, and habitually exercises the authority to, carry on the busines of RAB by concluding binding contracts on RAB's behalf in the main business.

If H's actiivities meet these definitions, it they will still not be a PE if the activities are prep or aux, or re agency, if the agent is independent and carrying out activities in ordinary course own business.

Re FPB, the OECD commentary to the DTA provides that a place may be 1) premises/facilities,
2) it may merely be at H's disposal, it is not necessary to have legal rights (rent) or it be exclusive use, and mere presence is not enough. Re fixed, it must be a separate and distinct place with a degree of permanence, re

Application

Here, applying the meaning of FPB, there is a place by virtue of the rented accommodation being provided by RAB having a room at his disposal for his work. Given this, there is a fixed place of business.

The office made available by JV partner may also constitute fixed place given it is at H's disposal. RAB's main activities are in the transport sector, and the UK project is significant. As sales director, H plays a direct part in the negotiation. He will be in the UK as the sales director. The activities are not P&A. The OECD guide state the decisive test is whether the activities are a significant part of the main business as a whole. as such his activities are not P&A.

Thus, he is carrying the business of RAB in the UK in the Fixed place.

Thus, there is a FPB PE.

In the alternative, if the activities are deemed to be those the JV, rather than RB, there may be an agency PE.

H has historically undertaken the negotiation process, and so has habitually exercised authority to negotiate contracts. As sales director for such projects, H has the authority to negotiate. He is in the UK to negotiate on behalf of RAB, via the JV. As an employee, H is a dependent agent (legally/economically - salary paid by RAB), and is not independent.

Fact that there for JV not affect that acting as RAB's agent, especially given JV not yet set up, and given he there to visit exiting and new customers generally for RAB.

Accordingly, there will be an agency PE, which will not be exempt as an independent agent or P and A.

Thus, RAB will be taxed for any income earned through the PE attributed under art 7 of the DTA. Sweden will have to provide tax credits for any tax paid by RAB in the UK on the attributed income.

Note - will likely be PE under UK rules as well given essentially same rules(CTA 10, s1141).

(2) Residence is determined by the statutory resident test (SRT)(FA 2013, Sched 45) for each tax year.

The SRT comprises three tests being, in order of priority - 1) automatic overseas tests, 2) automatic UK tests, 3) UK ties test (para 3).

Applying the automatic overseas test, the outcome will depend on if UK tax resident in the last 3 years, and if works full time abroad (full time 35 hour weeks outside UK). On the facts, he will arrive on 1 December 2016 until October/Nov 2017, so not automatic overseas under that test.

Facts unclear, but given works for Swedish resident company and having to bring his family, likely that not UK tax resident in any of last 3 prior tax years, so providing that works (3 hours work = work day), will not be tax resident if in UK for less than 91 days, providing only works 31 of those days.

However, he will probably fail this test in the tax year to April 2017, given he arrives in 1 December 2016, and work more than 91 days.

The automatic overseas test re being uk tax resident for 1 of the last 3 prior years is N/A.

Thus, unlikely to be non-resident under the automatic overseas test in year to April 2017, and correspondingly, given staying to October 2017, definitely unlikely meet this test for following tax year.

Turning to automatic UK test - there are 4 main tests. Applying here, will become UK resident once in UK for 183 days (May/June 2017) - split year may apply.

In the alternative, the second test is whether he has a home. Legal rights are irrelevant, merely has to be available for 91 days and used for one day (unless relative). The rented accommodation will constitute a home meeting the criteria and will be automatically UK resident once meets required days. Expect he has home in Sweden, based on fact family here and RAB thinks he busy enough that rented home required in UK, unlikely to spend time in Swedish home such that UK home test not met.

If this test not met, H will become resident once meets work day test.

If the automatic oversees, and UK tests not met, then sufficient ties tests apply. As an arriver, applying table in para 19 of SRT, once he stays past 120 days in year x, he will be resident if he has at least 2 ties - being family, home, work, UK etc. Also resident if 90 to 120 days with 3 ties. His family is in the UK, already discussed that has home in UK, and will be working in the UK - meaning has 3 ties. Accordingly, given he arrives 1 December 2016, he will be resident after 90 days with his 3 ties (he has more).

In summary, his is likely resident for year end April 2017, and for part of year end april 2018 – as not leaving until October/November 2017 and will meet tests for that period.

Given he is likely dual tax resident, his income will be subject to double taxation. He can get treaty tie break with the Swedish/UK DTA under article 4, and or likely to get credit on UK tax unilaterally for any swedish tax paid on his income (credit for lower of UK tax or Swedish tax).

Also, RAB may do salary equalisation, where they ensure after tax income equals what it would be without any double tax.

Re the tax year beginning in April 2017.

Question 3

(1) Transfer pricing (TP) rules aim to prevent connected parties (CP) from entering transactions non-arm's length pricing (NALP) to gain a UK tax advantage.

Under the transfer pricing rules in TIOPA, TP applies to financing arrangements, being debt issued by one company to another.

Under these rules deductions for interest, falling under these arrangements, will be denied for tax purposes.

In determining whether a company is denied deductions for excess deductions, you look at whether in the absence of a special relationship (TP relationship of control), the loan would be made at all, the interest, and amount and other terms. Relevant to this is whether the borrower is too thinly capitalised.

Each case is on the facts case by case, but HMRC have formerly provided guidance that if income: interest coverage is above £3:£1 and/or the debt-equity ratio is more than 1:1, the company is likely too thinly capitalised, and any deductions for related debt over this amount would be denied.

The TP rules apply here - not SME, not dormant.

All figures are in £ and the year to 31 March 2016.

Applying the law here, the TP rules apply as one company, US Inc (US), issued debt of £15 million to ABC (A), and US owns A 100%, so there is a special relationship or relationship of control.

ABC has interest deductions of £6million, attributable to £30 million third party loan (750) and US loan debt to equity is 1:1, but Interest to income coverage is negative, as in interest costs are greater than total turnover, leading to 8million loss before tax.

Also, Financing costs are not what third party charge. bank is charging 2.5% finance costs (750000/30,000,000), while US is 30% (4,500,000/15,000,000), and pref shares are 15%. External debt far too low, internal debt far too high.

It appears ABC is too thinly capitalised and some deductions will be denied.

Before pay, seek an advance price agreement with HMRC, where can agreed to interest costs. Binding on HMRC. Must apply in writing (see SP 2/10 for guidance).

Note, lender (US and bank) if excess deductions denied, are allowed compensating adjustment, so not WHT deducted at source in the UK. Have to make claim.

(2) US loan

There will be WHT on the loan to payments from A to US, but will be limited under the US/UK DTA, which states that, as A is beneficially owned by US, the UK will not charge WHT on interest paid by ABC.

Preference shares

There will be no WHT on the payments made under the preference shares, as they are deemed to be dividends from WHT in the UK.

Bank

Residence of bank unclear, but if Bank in UK, which reasonable given the assets purchased in the UK, then will not be WHT on payment of interest by A to bank.

Note

Any WHT paid is likely to be recoverable as a tax credit in the UK if UK taxpayer.

(3) The rules are that there is no WHT on interest paid between associated companies provided the interest is at ALP, consistent with the 4 freedoms.

Thus, providing this is the case, the effect on US if it was a resident of the EU in that there would be no WHT on the loans providing the meet the OECD APL transfer pricing guidelines.

<u>Question 5</u>

Introduction

The Diverted Profits Tax (DPT) applies from 1 April 2015 and introduced by the FA 2015 to prevent companies from artificially diverting profits from trading in the UK. It represents a major exception

The SPV in Jersey may be subject to the DPT. DPT is charged at 25% on diverted profits (DP), with a 3% charge added for days over 6 months late payment. DPT will not be charged unless a relevant notice is issued by Her Majesty Revenue and Customs (HRMC), however there is a duty to report if a company considers it is liable to DPT.

DP arises if a 1) UK resident company (UKRC) or a UK permanent establishment (UKPE)of a non-resident UK company (NRUKC) diverts profits from the UK or 2) a NUKRC avoids a UKPE (explain detail further below).

The first charge applies if a UKRC or a UKPE enter a transaction with a connected party (as defined by TP rules, including control within 6 months of control event), where the transaction lacks economic substance (tax avoidance a main purpose and tax advantage not outweighed by non-tax financial benefit) and results in effective tax mismatch (profit reduction for UKRC/UKPR, and increase in taxable income for counter party that less than 80% of reduction (not referable to pension contribution/charity.

UK avoided PE if UKNRC has trade with connected party, and reasonable to assume avoiding UKPE and effective tax mismatch condition met or tax avoidance condition met.

Not apply if both SME or ETM relates to excepted LR.

Applying the rules to the SPV, the following comments can be made.

- Applying the para 80/81, a UKRC, York Ltd, would be entering an transaction with a connected party. The transaction, being to transfer the holding structure to Jersey, would lack economic substance because it would be mainly for the purpose of a UK tax advantage, especially given Jersey tax is 5% compared to UK corporate tax at 20%. There would be an ETM, given the taxable profit for York would fall, and the corresponding rise in income to SPV would be likely less than 80%. Neither would be SMEs, and other exceptions not triggered.

- applying the avoided PE would apply.

The SPV would be a NUKRC resident in Jersey. The entities it trades with regarding the UK are connected parties (all the subs). The invoicing and debt collection functions, and careful transfer pricing, means that designed to avoid PE. The difference in tax rates UK/jersey mean tax avoidance emanin aim, and neither are SMEs.

Conclusion

The DPT would likely apply, the UKRC/UKPE charge may apply to Y, while the UK avoided PE may apply to the SPV. DPT would be less like

Note also, that the GAAR is applicable, there will be no deduction, not APA.

Question 6

(1) Zeus (Z) is a UK incorporated company, and as such is UK tax resident (UKRC) pursuant to section 14 CTA 09.

Pursuant to section 18 CTA 09, Z, as a UKRC can become UK non-resident (UKNR) by transferring its operations to Luxembourg (Lux) in such a way that it also becomes tax resident in Lux under their local rules, and then operation the UK/Lux DTA residence tie-break in Art 4. Consistent with the OECD model DTA, Z can move become UKNR under Art 4 if it moves its place of effective management (POEM) to Lux, meaning then become UKNR under art 18.

OECD commentary defines POEM as place where key management and commercial decisions necessary for operation of business as a whole located. This is not the same as UK law test of central management and control, which is higher level of control (De Beers) (see HMRC SP 1/90 for guidance). Though moving the CM&C may mean that the POEM is moved as well.

Thus, to become UKNR in Lux, move POEM to Lux. here, this may mean moving all senior management to Lux, and relocating head office to Lux, and having all board of director meetings there.

It can also become UK non-resident through an act of Parliament (though unlikely, I know).

(2) There are numerous potential implications of movement to Lux.

There will be exit tax charges, which may be postponed (capital assets, IFAs (after 1 april 2002), or if not may enter payment plan with HMRC to pay of exit charges.

If not payment plan, and taxes not paid within 6 months, HMRC can issues notice within 3 years seeking payment from companies within same 75% group or from controlling director.

Z, as a company, deemed to stop trading in UK. Stock and plant (where claiming capital allowances) deemed sold at market value (MV) making trade income, derivatives/LF deemed sold/reacquired at fair value (non-trade income), capital assets & IFAs (after 1 april 2002) deemed sold and reacquired for MV making chargeable gains. All subject to corporation tax at 20%.

Gains on capital assets & IFAs (after 1 april 2002) can be postponed under section 857 CTA (IFA equivalent) if 1) trade assets used outside uk, 2) assets transferred to 75% sub, 3) from UKR parent, 4) both elect to claim postponement within 2 years. Stops being postponed if cease UKR parent or 75% sub, or sell assets within 6 years.

Note, unlikely to have to do international movements of capital report to HMRC, as any cross border movement below £100 million.

(3) Stock 5,000,000

Plant (book value 6mil, MV 3 mil) = - 3mill loss + capital charges of 3 mil = 0 to income

capital assets
building (cost 5mil, value 10mil)= 5,000,000 gain
Goodwill = sold 50 less 3 = 47 million gain
Investments subs (book 50mil, MV 50mil = 0 gain

Other intangibles - (sold/reacquired 100 mil) - no gain

total gain = 57 million taxable income at 20% corporate tax = £11,400,000