# THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2016

# PAPER 2.09 – UNITED KINGDOM OPTION

## ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

TIME ALLOWED – 3¼ HOURS

You should answer **FIVE** out of the nine questions: **BOTH** questions from Part A; **ONE** question from Part B; and **TWO** questions from Part C.

Part A questions are worth 25 marks each. Part B questions are worth 20 marks. Part C questions are worth 15 marks each.

You should aim to spend approximately half of your exam time answering Part A, and the remaining half answering Parts B and C. The amount of time you spend answering each question should correspond broadly to the number of marks available for that question.

Start each answer on a new page. If you are using the on-screen method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.

All workings should be made to the nearest month and Pound Sterling, unless the question requires otherwise.

Marks are specifically allocated for presentation.

## PART A

**You are required to answer BOTH questions from this Part.**

1. Wheels Ltd (Wheels) is a company which manufactures luxury cars, tax resident in the United Kingdom. Wheels' main market is the UK, but it has also entered into a significant deal with a distributor in Canada. The Canadian distributor is keen for at least some part of the car assembly process to be carried out in Canada, so that it can advertise this fact. Wheels has therefore agreed to set up a finishing plant and paint shop in Montreal. It has established a wholly owned Canadian limited liability company, Spokes, Inc. (Spokes), to conduct this work. Spokes is treated as a corporate entity for the purpose of UK and Canadian tax, and has taken a lease on premises.

   The management of Wheels expects Spokes to act as a sub-contractor for Wheels, i.e. Spokes will not acquire ownership of the cars from Wheels at any stage in the process, but will merely provide services to Wheels. Any parts or components which are to be delivered to the finishing plant will be purchased directly by Wheels and delivered to the facility in its name.

   The operations team at Wheels are keen to ensure that the quality on which their brand is valued is maintained, and wish to be involved in every stage of the process at Spokes. They are considering sending a number of UK operations staff over to Canada for a period, in order to "assist" with the work.

   The Finance Director (FD) of Wheels is aware that tax rates in Canada are significantly higher than in the UK, and is concerned that the activities of Spokes and the Wheels operations team may create a taxable presence for Wheels in Canada.

   **1) You are required to prepare a memo for the FD, analysing the activities undertaken in Canada, to determine whether a Canadian permanent establishment for Wheels could be created. You should assume that the double tax treaty between the UK and Canada follows the OECD Model. You should also advise the FD on how to mitigate any permanent establishment risk, particularly with regard to the location of employees.** (20)

   **2) For those employees who are to be sent from the UK to Canada on a temporary basis, you are required to provide a short memo noting the UK tax implications of their employment income, and expenses paid, during their time in Canada.** (5)

   Total (25)

2. Phelan is the Managing Director and majority shareholder in MediaX Ltd (MediaX), a digital media company incorporated and based in Dublin, in the Republic of Ireland. MediaX's board meets monthly, and all of the company's key strategic decisions are taken at these board meetings. The meetings are chaired by Phelan and attended, either in person or via telephone, by the company's five other directors. A decision has recently been taken to develop MediaX's activities within the United Kingdom, a market which has been identified as offering the potential for significant growth in the short to medium term.

Phelan and the company's Sales Director, Dermott, are to relocate to London to oversee the initial phase of this project. They plan to acquire an office in London and source secretarial and administrative support. It is envisaged that, if things develop as anticipated, a sales team will be hired within twelve months. In the interim period, both Phelan and Dermott will visit existing and potential UK customers, although neither will conclude contracts.

It is likely that staff will be seconded from the Dublin office for short periods of less than 60 days in any tax year, while the London office is being established.

Although Phelan and Dermott will spend much of their time in the UK, they also plan to spend at least eight weeks each year visiting customers in the Benelux region.

Business forecasts have been prepared which envisage break-even being achieved within two years.

Phelan has given much thought to MediaX's strategic level management over the period of his absence from Dublin, and does not wish to relinquish control of the company. He foresees chairing monthly board meetings either by phone or via video conference from London, or alternatively alternating board meetings between London and Dublin.

**Phelan has asked you to provide advice in answer to the following questions:**

1) **What is the risk of MediaX becoming UK resident?** (9)

2) **How will PAYE, National Insurance and overseas work day relief operate, in relation to Phelan and Dermott's salaries?** (3)

3) **What are the PAYE issues surrounding the short term secondment of the Dublin office employees?** (2)

4) **If the duration of the secondments was extended to 120 days, would the seconded employees be subject to UK income tax on their earnings?** (3)

5) **Are the envisaged activities likely to create a UK permanent establishment?** (5)

6) **From a tax perspective, should the UK business be carried on through a UK company?** (3)

Total (25)

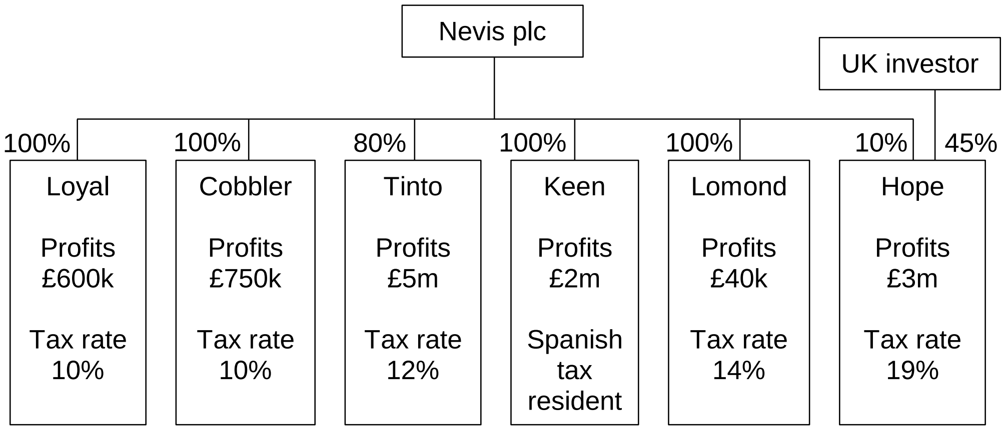
## PART B

**You are required to answer ONE question from this Part.**

3. Nevis plc (Nevis) is a company incorporated and tax resident in the United Kingdom. Nevis has shareholdings in a number of companies. The percentage of each shareholding is shown in the diagram below.

Nevis holds voting rights in each company, and a percentage entitlement to distribution income from that company, equal to its shareholding percentage.

The tax rates shown below are the effective tax rates for each entity on its profits to 31 March 2016.




Nevis acquired Loyal in July 2015 from a United States conglomerate, which had held the company for the previous five years. The management of Nevis intends this to be a long term investment for the group.

Cobbler runs a call centre function for the group. Its location was chosen for the availability of well trained and professional call centre operators. Cobbler's profits for the accounting period ending 31 March 2016 totalled £250,000, on operating expenditure of £3 million.

Tinto is the group finance company. Nevis provided Tinto with an injection of capital of £300 million two years ago, to allow it to provide loan funding to other group companies.

Keen is an established Spanish trading company which has benefited from a tax holiday on a portion of its profits in Spain for the last three years. The company was acquired three years ago by Nevis, and retained all members of its previous full management team. Keen is considered to be fully managed and controlled from Spain.

**You are required to prepare the Controlled Foreign Company (CFC) analysis for the Nevis Group for the accounting period ending 31 March 2016, explaining for each company whether its profits will be apportioned to Nevis under the UK Controlled Foreign Companies rules.** (20)

4. Edward is an Australian resident, who is currently employed by Benswick Pty Ltd (Benswick Pty). He is to be seconded to the United Kingdom to work for Benswick UK Ltd (Benswick UK) on a major infrastructure project. The assignment is forecast to last a period of three years, and to constitute full-time employment. It is expected that Edward's wife Jane and their children will accompany him on this assignment.

Edward and Jane both have significant investment income generated by their respective international portfolios of equities and bonds. These portfolios contain several UK assets generating UK dividend and interest income. In addition, Jane owns several Australian commercial properties generating substantial net income.

Neither Edward nor Jane have previously been UK resident, and their respective parents have always resided in Australia.

The dynamics of the project are in a state of flux and the company has pencilled in two possible dates for Edward's move to the UK:

- 1 March 2015; or
- 1 October 2016.

It is noted that, if the move is scheduled for 1 October 2016, it is possible that Edward will have to spend 40 days in the UK in May and June 2016 to undertake certain preliminary activities.

**Benswick Pty have asked you to provide advice regarding the following questions:**

1) **Will Edward be UK tax resident for 2014/15 if he is seconded to Benswick UK on 1 March 2015?** (3)

2) **How will Edward and Jane's income be taxed in the UK in 2016/17 if the assignment commences on 1 October 2016?** (9)

3) **How will Edward and Jane's income be taxed in 2016/17, if Edward spends 40 days in the UK in May and June 2016 attending to preliminary matters prior to moving to the UK on 1 October 2016?** (3)

4) **How will UK National Insurance be applied to Edward's salary.** (2)

The German subsidiary of Benswick Pty is involved in a similar project in Germany. It is possible that, in 2016/17, Edward will be required to work in Hamburg for one week per month while remaining based in the UK.

5) **Will Edward be subject to UK Income Tax on any salary paid in relation to his work in Germany?** (3)

Total (20)

## PART C

**You are required to answer TWO questions from this Part.**

5. Wendy, Inc. (Wendy), an import/export company headquartered in the United States, has recently purchased a British company, Peters Ltd (Peters), in order to expand its activities into the EU.

   While knowledgeable about customs duties, the Finance Director (FD) at Wendy is unfamiliar with VAT and has asked you to prepare a memo on any UK VAT implications for:

   - both Wendy and Peters, in respect of intra-group sales of goods between the two companies; and
   - transactions conducted by Peters with EU-based suppliers and customers.

   The FD is interested in both the potential cost of VAT to the business and its effect on cash flow.

   You should assume that Peters is a fully taxable VAT registered entity.

   **You are required to prepare the memo for the FD at Wendy.** (15)

6. Diamondia Ltd (Diamondia), a company resident in the United Kingdom, has been operating in Singapore since 1999 through a local branch, Gloriosa. Gloriosa's turnover is now in excess of £200 million per annum, with annual profits of around £20 million. The shareholders of Diamondia are developing a five year plan for an exit from the Singapore market, and expect that more value can be derived from the sale of their shareholdings if Gloriosa is incorporated into a Singapore limited liability company.

   Gloriosa is cash rich, and the shareholders would like to use the incorporation process to remit cash back to the UK. Gloriosa's assets are as follows:

   | Asset | Book Value (£m) | Open Market Value (£m) |
   |---|---|---|
   | Stock | 50 | 50 |
   | Debtors | 30 | 30 |
   | Warehouse | 20 | 40 |
   | Moveable Plant and Machinery | 10 | 8 |
   | Cash at Bank | 20 | 20 |
   | Goodwill | - | 100 |

   The shareholders propose that Gloriosa should issue shares with a value of £180 million to Diamondia and cash of £20 million on incorporation.

   **The shareholders have asked you to prepare a memorandum explaining the UK taxation implications of incorporating Gloriosa, along with any reporting requirements. In addition, the shareholders have specifically requested your advice on how further tax efficiencies can be obtained.** (15)

7. Pierre was born in France in 1964. He was seconded to the United Kingdom in 1990 by his employer and, although he has changed jobs several times, he has remained resident in London. Pierre feels settled at present, and has lived for several years in his current property which he and his wife jointly own. The property is ideally located, as it is a ten minute walk from the secondary school which Pierre's children attend. The family are bilingual, speaking both French and English fluently. However, they carry French passports only.

Pierre has recently received a substantial inheritance from his aunt Anouk, consisting of French real estate, works of art, bank accounts and a share portfolio.

**Pierre has sought your advice regarding the following questions:**

**1) What is Pierre's domicile status?** (7)

**2) How will the taxation of income and capital gains arising from the inherited assets be applied?** (5)

**3) How will UK Inheritance Tax be applied to Pierre's estate in the event of his death?** (3)

Total (15)

8. Miki is a very wealthy Japanese resident individual, and has contacted your firm regarding his forthcoming arrival in the United Kingdom. Miki's wealth comprises various assets including:

- significant cash deposits in various currencies;
- a very valuable, predominantly foreign, share portfolio;
- Japanese commercial real estate;
- Japanese residential property;
- works of art; and
- 20% of shares in a large Japanese group of trading companies.

Miki intends to fly into London on 1 July 2016 and stay in a hotel for two weeks, as a preliminary stage ahead of a move to London on 1 October 2016. Miki intends to acquire a London property while retaining his Japanese home, where he will spend some time each year.

While Miki is not coming to the UK primarily to work, he mentioned that it is possible that, at some point in the future, he might take up a part-time role with a Belgium company based in Ghent, which is owned by a former colleague. Although this role would be based in the UK, it is likely that Miki would spend a couple of days each week working in Ghent.

**Miki has asked you to explain how the statutory residence test will apply to his circumstances, and also to explain how he will be taxed in the UK as a non-domiciled taxpayer. In this regard, Miki also requests advice on what steps he should take to avoid remitting foreign income and gains to the UK.** (15)

9. Jasper, a Canadian resident, owns a large residential property portfolio in the United Kingdom. Most of the properties are held indirectly through SPV companies in low-tax jurisdictions; however, two very valuable properties which Jasper acquired many years ago are held personally. All of Jasper's UK properties are rented to third party tenants.

Many of Jasper's properties have been acquired using a combination of cash and mortgage finance. Jasper had previously been advised that this was tax efficient. The net rental income is subject to tax under the non-resident landlord scheme. Jasper regards the properties as long term investments, although on occasion he has made several disposals in cases where generous, unsolicited offers were made for newly acquired properties.

During a recent visit to London, Jasper met with an old friend who mentioned that the tax landscape for UK residential property had changed dramatically, particularly in the context of non-resident investors.

**Jasper has instructed your firm to provide an update, explaining how his portfolio is affected by these changes.**

**Jasper is particularly anxious to learn how future disposals of property will be taxed, and is concerned that, notwithstanding the introduction of the Annual Tax on Enveloped Dwellings (ATED) and Non-Resident Capital Gains Tax, there is a possibility that Her Majesty's Revenue and Customs (HMRC) may argue that future sales should be subject to income tax as constituting trading in nature.**

**You are not required to consider Stamp Duty.** (15)