Question 1 Script A

| | A | B | C | D | E | F | G |
|---|---|---|---|---|---|---|---|
| 1 | 1.1 (a) Corporation Tax Consequences | | | | | | |
| 2 | Corporation Tax Liabilities | | | | | | |
| 3 | | | | | | | |
| 4 | Notes: Tax Consequences | | | | | | |
| 5 | There are two alternative business structures being considered for the Tasland business, ie setting up as a permanent establishment (PE) of Savoury Ltd or incorporating the Tasland business.<br><br>Where the business is set up as a PE, it would be chargeable on corporation tax in UK. Where it is set up as an incorporated business in Tasland, it may depend on whether the business is centrally managed or controlled in UK. If it is, then it would be chargeable on UK corporation tax. However, if it is not, then it would be only taxable on Tasland's taxes unless it is a controlled foreign company (CFC).<br><br>Structure 1: Permanent Establishment<br>Where a permanent establishment is set up, the profits from Tasland business of Savoury Ltd would be treated as a trading income in Savoury Ltd. Therefore, as Savoury Ltd's business has estimated tax-adjusted trading lossesfor the year ending both 31 December 2019 and 2020, the trading losses could be relieved by the profits in the Tasland's business.<br><br>Under PE, it would be treated as a branch under the Savoury Ltd, and Savoury Ltd is a UK resident company. Therefore, it would be subject to worldwide profits. Normal capital allowances would also be available on the capital expenditure on plant and machinery.<br><br>For the four months ending 31 December 2019, the capital allowances would be time apportioned. It is calculated as follows: | | | | | | |

| 6 | | | CA 2019 | | CA2020 | | |
|---|---|---|---|---|---|---|---|
| 7 | | £ | £ | £ | £ | | |
| 8 | Purchase / TWDV b/f | 250,000 | | 172,333 | | | |
| 9 | AIA (200,000 * 4/12) | (66,667) | 66,667 | | | | |
| 10 | | 183,333 | | | | | |
| 11 | WDA @ 18% (*4/12) | (11,000) | 11,000 | (31,020) | 31,020 | | |
| 12 | TWDV c/f | 172,333 | | 141,313 | | | |
| 13 | | | | | | | |
| 14 | Total CA | | 77,667 | | 31,020 | | |
| 15 | | | | | | | |

Therefore, the taxable profits, if business is carried out under PE, would be as follows:

Four months ending 31 December 2019: £1 mil - £77,667 = 922,333
Y/e 31 December 2020 : £2 mil - £31,020 = £1,968,980

These profits would be taxable under UK corporation tax at the corporation tax rate of 19%, assuming it remains unchanged in the future years. However, double taxation relief (DTR) is available on the trading profits of PE, at the lower of UK corporation tax or Tasland's tax. It is clear that Tasland's corporation tax would be higher as the tax rules are identical but the tax rate is at 28%. Therefore, in this case, it is clear that there would be no UK corporation tax arising on the PE DTR is available on the UK corporation tax.

In addition, an exemption election could be made to exempt the profits of the PE from Uk corporation tax, however, this is an irrevocable election and it applies on all the branches in the future for Savoury Ltd, thus limiting tax planning opportunities. In addition, it is also not needed because there are no UK tax payable.

If under PE, as there are trading losses arising on the Savoury Ltd of £800,000 and £600,000 on 31 December 2019 and 2020 respectively, by setting up a PE, it would mean that losses could be offset by the profits in PE, thus this would give rise to a waste of the loss reliefs available in the future. Moreover, it is not tax efficient because the PE would then not only use up the losses arising on the Savoury Ltd, but it will also waste it's DTR.

The trading losses of four months ending 31 December 2019, amounting to £800,000 * 4/12 = £266,667 would be wasted to reduce the taxable profits of the PE in Tasland. Therefore, the four months ending 31 December 2019 profits would be reduced to £655,666. As for the year ending 31 December 2020, the trading profits would be reduced to £1,968,980 - £600,000 = £1,368,980.

As the DTR is available, then there would be no UK corporation tax arising. The UK corporation tax would therefore be £nil, and there would be unrelieved trading losses for Savoury Ltd to be carried forward agains tfuture trades of £800,000 + £600,000 - £266,667 - £600,000 = £533,333.

Tasland's tax would be as follows:
four months ending 31 December 2019: £922,333 * 28% = £258,253
y/e 31 December 2020: £1,968,980 * 28% = £551,314.

The use of £2.5 million of finance to set up the business in Tasland would give rise to no implications as there would be no interest charged issues.

Alternative 2
By incorporatiing the Tasland business as a Tasland-registered company, then there should be no UK corporation tax arising subject to the application of CFC rules. In this case, assumming that the Tasland company is centrally managed and controlled in Tasland, there would be no implications of UK corporation tax arising.

Under both alternatives, Tasland's tax would be charged anyway. Therefore, it should not be under the consideration of whether to set up a business as a PE or a subsidiary.

Where the business is set up as a subsidiary, there would be no UK corporation tax arising. The profits from the subsidiary could then be remitted into the UK.

Dividends remitted to the UK do not suffer any corporation tax as it is a 100% subsidiary, and it is also not included under the augmented profits calculation.

However, the dividends that could be distributed are the distributable profits, ie the profits after tax charge from Tasland. This is calculated as follows:
£922,333 - £258,253 = £664,080
£1,968,980 - £551,314 = £1,417,666

In this case, when the dividends are remitted into the UK, there would be further witholding tax of 28% chargeable in Tasland. This witholding tax is however not relievable in any way from UK. In this case, the amount of profits available to Tasland would be further reduced to:
31 December 2019: 664,080 * 72% = £478,138
31 December 2020: 1,417,666 * 72% = £1,020,720

Even though the subsidiary set up is a CFC, there would be no CFC chargeable profits arising becasue Tasland's tax are much higher compared to UK tax.

However, there would be finance of £2.5 million required to set up the business in Tasland. Interest on loan would be 7% pa and the fiannce would be provided by Savoury Ltd. If Savoury Ltd is a large business, it would be charged under the thin capitalisation rules, and further information would be needed on whether there should be adjustments required under taxable total profits, which is needed if it is not at commercial price.

For the finance of £2.5 million, interest would be 7%, therefore this is an allowable deduction for the subsidiary, and reduces the trading profits being taxable in Tasland. The interest for 31 December 2019 would be £2.5mil * 7% * 4/12 = £58,333 whereas tfor the year ending 31 December 2020 it would be £2.5mil * 7% = £175,000. In this case, there would be reduced Tasland's corporation tax of £16,333 and £49,000 respectively under the subsidiary.

However, the allowable deduction would be a NTLR credit which is taxable in UK corporation tax, as it is an investment. Nevertheless, this NTLR could reduce the trading losses, thus no coporation tax in UK would arise still.

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20 (b) Tax Efficient Business Structure

21 It would be more worth it for Savoury Ltd to set up the company as a PE as there would be no UK corporation tax arising anyway because double taxation relief is available to reduce the UK corporation tax to £nil. Only the Tasland's tax are arising, in addition there would also be no witholding tax on the amount remitted from the Tasland's business to UK.

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23 (c) Further Information Needed

24 Information should be needed on whether there are any thin capitalisation rules in Tasland as in UK.

In addition, further information would be needed on:
- Whether any rules or implications in Tasland would arise by setting up a PE there
- Whether the PE would be treated as Tasland resident there.
- Whether there may be any future changes in the corporation tax and witholding tax in Tasland.

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26 1.2 Notes: UK Income Tax Implications

The UK statutory residence test needs to be used to identify whether the employees are UK resident or overseas resident on their secondment. They are all non-UK domiciled.

On the whole tax year of 2020/21, they would be under the secondment.
They did not spend less than 46 days in UK in that tax year, therefore they would not meet the overseas automatic test.

If they meet the full-time UK work test, they would be UK resident. The conditions for the test to be met are as follows:
- There is a 365 day period where all or part of which falls within the tax year when the employees work an average of 35 hours per week in the UK. This condition is met because they will work for 37 hours per week.

- Within the period, there would be no significant break of more than 30 days when they do not work in the UK. This is also met as they are spending annual holiday of four weeks in tasland, amounting to 4 * 7 = 28 days.

- Within the period, they work in UK more than 75% of their working days. This is very likely as they are only returning to Tasland one weekend per month.

- There is at least one day that falls into both the 365 day period and the tax year when they do more than 3 hours work in the UK. This condition would be met.

Therefore, the employees would be UK resident on 2020/21.

27 Split year rule will apply where they are working full time in UK. They would be deemed as UK resident starting from 1 january 2020. It would also apply on the time they end their secondment, ie their UK resident status would end at 30 June 2021.

Prior to 1 January 2020, there are 8 full months for the tax year of 2019/20. In this case, they would not meet both the automatic resident UK test and automatic overseas test. They should use the sufficient ties test instead. As there are 8 full months, provided if they meet 4 ties on the sufficient ties test, they would then be deemed UK resident for the whole tax year if they stay in UK for 46 * 8/12 = 31 days or above.

Where the employees are UK residents, they could choose to be taxed on their overseas income on arising basis or remittance basis.

The rent-free accomodation and their travelling costs would all be exempted from income tax in UK. There would also be no remittance basis issues arising on their employment income because they would be paid into UK bank account in strrling.

As for their spouses' visits, the trips would also be non-taxable from income tax in UK up to two return visits per person.

Where remittance basis claim is made, overseas income and gains would not be taxed (any income or gains from Tasland), however their personal allowance of £11,500 and annual exemption amount for gains of £11,300 would be lost.