The rise of social media

OMB | Personal tax



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Jon Elphick explains the best ways to manage tax planning for internet influencers

Key Points

What is the issue?

A media influencer will usually be (but does not have to be) an individual person who has set up a social media profile on his or her own account. The influencer will usually be paid a fee for using their social media account to endorse a specific product or service.

What does it mean to me?

Where an influencer uses their social media account to generate income, the activity will be considered as a trade for UK tax purposes.

What can I take away?

If the influencer can demonstrate that they are carrying out a genuine trade of endorsing products via social media, then it may be appropriate for them to set up an image rights company.

February 2019 celebrated the 15 year anniversary of the launch of Facebook, a US based social media and social networking service that initially launched online before being developed into a mobile application. It is estimated that by its 15th anniversary, Facebook had more than 2.3 billion active users each month. Since the launch of Facebook, other social media platforms have been developed, including (amongst others) YouTube and Instagram, which boast estimated users of 1.9 billion and 1 billion respectively.

The ‘influencers’

The value and reach of social media platforms have become significant. Celebrities use their social media accounts to provide regular pictures and videos of their day to day lives, with the intention of allowing their fans to feel closer to the celebrity and making the celebrity more relatable (and therefore more popular) to the general public. This helps to sell merchandise, as well as increasing demand to see the celebrity perform in their respective profession.

Celebrities also use their social media accounts to promote their own brands of clothing, beauty products, fragrances, etc., as well as endorsing other brands within the pictures or videos they post. This form of advertising can have a significant reach – the 15 most popular celebrities on Instagram, for example, have between 100 and 180 million followers, thereby providing brands with an opportunity to

expose their products to a large number of potential customers.
In addition to celebrities, ‘influencers’ are also using their social media exposure as a means of earning income. ‘Influencers’ are essentially bloggers, who initially created blogs to provide their comments on matters such as fashion, travel, beauty and fitness, among other things. Followers of these bloggers become influenced by the opinion of the writer, and will often use the products or services that are recommended in the posts. Brands are now turning to influencers to help promote their products, paying substantial sums for the influencer to post pictures or videos of themselves using specific products or services and providing positive comments for their followers.

How are influencers taxed?

An influencer will usually be (but does not have to be) an individual person who has set up a social media profile on his or her own account. Where an influencer uses their social media account to generate income, the activity will be considered as a trade for UK tax purposes.

A UK resident sole trader will be subject to UK income taxes on the profits of their trade. UK tax will be applied at the individual’s marginal rates of up to 45%, depending on the level of profits made by the sole trade. National Insurance contributions will also be due under Class 2 (at £3 per week) and Class 4 (at 9% on profits exceeding £8,632, falling to 2% on profits exceeding £50,000). Such a trade is likely to be a highly profitable activity, as there should not be significant overheads incurred by an individual maintaining a social media account of their own, and so the tax liabilities incurred by an influencer may be substantial.

Tax planning for influencers

Depending on how the arrangements with specific brand owners are set up, the influencer will usually be paid a fee for using their social media account to endorse a specific product or service. This is effectively the same as an image rights arrangement, whereby a professional athlete would be paid an image rights fee for commercially endorsing a specific product. This raises a question as to whether an image rights company (IRC) may provide an effective tax planning tool for influencers.

An IRC can be set up in the UK or overseas. The suitability of its location will depend on a number of factors, including the residence of the influencer, their domicile and where the underlying commercial activity of the company will be undertaken. Assuming the influencer is UK resident and domiciled, the UK is likely to be the more appropriate location for the company.

A UK resident company is subject to UK corporation tax on the global profits of its trade. UK companies are currently subject to corporation tax at a rate of 19%. The influencer will be subject to additional taxes to the extent that they are paid a salary from the company, or if they receive dividends. However, using the company will provide some important benefits, such as the ability to roll up ‘excess’ profits in the company, and the limitation of personal liability.

Are IRCs accepted?

Whilst it is noted that HMRC have vigorously cracked down on image rights arrangements since the late 2000s, there are important differences between influencers and professional athletes. There are also recent case law developments, plus HMRC’s updated ‘manuals’ that provide useful guidance for effective tax planning.

The most important difference between an influencer and a professional footballer is that whilst an influencer is self-employed and carrying out their own independent trade, the footballer will be an employee of a football club and will be paid, predominantly, to provide professional services as an athlete. An influencer’s profile is built purely on their image, reputation and activity, as opposed to an athlete who uses their existing profile to generate secondary income from endorsing products.

HMRC’s main grievance with image rights arrangements historically is that image rights payments are disguised employment remuneration, rather than payment for separate (commercial endorsement) services carried out by the footballers. Without any such employment contract in place (and ignoring any potential IR35 issues), it cannot be argued that the income being earned by the influencer represented employment income, rather than endorsement income.
Whilst the recent case of *Hull City AFC (Tigers) v HMRC* [2019] UKFTT 227 resulted in success for HMRC at the First-tier Tribunal (a success, it should be noted, that was based on the disguised employment income argument), the underlying technical arguments debated in the tribunal provide interesting guidance for advisers.

Firstly, the tribunal agreed with an argument put forward by HMRC that it was necessary to look at the substance of the sums that were paid, rather than their form. In other words, whilst the payments were ‘formed’ as image rights payments, the underlying detail and circumstances surrounding the agreement of the contract, payment of the sums and the actual performance of the contract were necessary. Whilst the argument favoured HMRC in this case, it can be assumed that where a bona fide image rights arrangement is in place, and the individual influencer clearly performs the necessary functions to fulfil the contract, then the ‘substance’ of the arrangement would justify a genuine image rights payment.

Secondly, the tribunal outlined in its findings that Hull City AFC did not have a clear intention of commercially exploiting the rights it obtained, that it had no clear evidence of how the rights were valued, and that the players’ rights had never been commercially exploited. Again, these are damning findings, but they do indicate that if Hull had been able to demonstrate that they had a clear plan to exploit the rights, had valued the rights correctly and had actually exploited the rights commercially, then the tribunal may have determined that genuine image rights arrangements did exist.

Key considerations

If the influencer can demonstrate that they are carrying out a genuine trade of endorsing products via social media, then it may be appropriate for them to set up an IRC.

When establishing an IRC, the influencer will need to consider how to transfer their existing activity into the company. HMRC’s manuals consider that where an individual can demonstrate an existing trade, then the transfer of an image right can represent the transfer of goodwill as a going concern. Such a transfer may be eligible for roll over relief, and so an initial charge to tax on the transfer could be avoided.

UK companies will provide a limitation of liability for the influencer, and so the influencer can gain personal protection from any legal action taken by, or damages sought from, the brand owners or any other third party. This may in itself be sufficient motivation for the influencer to establish an IRC.

There may be significant tax advantages to be obtained by retaining profits within the IRC, or potentially establishing a holding company to accumulate excess revenues from the IRC without paying them to the influencer. For example, a holding company may be able to act as a pension (or in conjunction with a company pension scheme) to provide future income to the influencer when they decide to retire.

Parting thoughts

Despite historic pressure from HMRC, and their recent success in the FTT, the appropriate use of image rights arrangements remains a useful tax planning tool. For influencers, their ability to generate income via social media has been developed by their personal profile being synonymous with online blogs, reviews and endorsements. They are known purely for that activity and so any endorsement earnings they generate cannot have derived from anything else. From the author’s perspective, influencers appear to be the perfect clients to establish an IRC.