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EMPLOYMENT TAXES VOICE

Issue 9 – April 2024

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Welcome from the Chair

Some good news on simplification and fairness but there's still more to do!

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Welcome to this ninth edition of Employment Taxes Voice. The CIOT Employment Taxes Committee has been very busy over the last year addressing matters relating to everything from the Construction Industry Scheme to (the abolition of) the pensions lifetime allowance, via occupational health in the workplace and Off-Payroll Working. But I want to frame my introductory remarks to this edition of ETV around the path to simplification and to fairness on the Employment Taxes roadmap (well mine anyway!).

It was a sad day for me when section 347 of the Finance (No 2) Act 2023 was passed into law. You may (or may not) recall that section 347(1) of the Act states, bluntly, that "*the Office of Tax Simplification is abolished*"! The obvious question then being where this left the impetus to simplify and improve our tax legislation / administration given that the OTS had very much been in the vanguard on this. However, reading HMRC's "Simplification Update – January 2024" it seems that all may not be lost. The Update includes not one, but two, employment taxes initiatives. Firstly, a new, simplified process for employees to claim tax relief for unreimbursed expenses (details to follow). And, secondly, a new digitised process to report and pay tax and Class 1A NICs on all BIKs via employer payroll – this will not be implemented until April 2026 and whilst it will be mandatory, close consultation is promised with stakeholders to ensure the design is optimised. I am encouraged by these initiatives - both rely on harnessing the power of IT which must surely be the right way forward as regards streamlining process and saving time/costs for employees, employers and HMRC alike. This said, moving to mandatory payrolling of BIKs won't be without its challenges and Steve Wade and Dalbir Kathuria explore what this will mean for employers in more detail on pages 8 to 10.

But, aside from tax administration, HMRC might have added another simplification measure as well, and one which I very much welcome. This is the introduction of an exemption from the Construction Industry Scheme (CIS) for payments made by landlords to tenants for building work undertaken further to their lease agreement. This will be effected by new regulation 20A of the CIS Regulations (from 6 April 2024) on which the government previously consulted. I believe this will significantly reduce the CIS administrative burden presently involved when building work is undertaken and this approach is one which the CIOT has very much supported. Lee Knight and Susan Ball have more to say on this in their article on the CIS on pages 17 to 23.

And on the theme of simplification there was of course the more recent and key announcement in the Budget concerning a new regime to tax foreign income and gains with effect from 6 April 2025. This will move away from the long-established building blocks of domicile and the remittance basis to a regime which is based on a prior qualifying period of ten years of non-UK residence and with no restriction on funds being received in the UK. We don't yet have all the details, but Eleanor Meredith discusses what the government have said so far on pages 5 to 7.

Moving from simplification to fairness, the CIOT was pleased that the government decided to act in response to the representations that we (and others) made some time back concerning the amount of tax due in a settlement under the Off-Payroll Working (OPW) rules where a worker engaged via an intermediary (typically a PSC) is mis-categorised as self-employed rather than employed. This is effectively *Demibourne* v2.0, ie the equivalent of regulations 72E-G of the PAYE Regulations which apply in direct engagement situations. It will mean that businesses involved in OPW settlements get credit for taxes paid by the worker/PSC so that both sides then pay their fair share to HMRC, no more and no less.

But fairness isn't always about the need for new legislation. Sometimes it's about the correct interpretation of what's already on the statute book. A topical example which the CIOT raised with HMRC is where an employee is provided with an electric car by their employer and is reimbursed for the cost of charging it at home. HMRC's guidance (at EIM 23900) previously said that where there was private use then such reimbursement was taxable and subject to Class 1 NIC. But following the CIOT's representations concerning the correct interpretation of section 239(2), ITEPA 2003 – which exempts payments to employees made in connection with company cars (and noting that electricity isn't (yet) a fuel for section 149 purposes) – HMRC agreed to revisit their interpretation and the guidance was subsequently updated to reflect the CIOT's view that no tax/NIC charge arises in these circumstances. I should add that technical and policy matters concerning employee expenses and benefits are discussed regularly with HMRC via the Employment Payroll Group, and in this respect the CIOT is very pleased to see that an Expenses & Benefits sub-group has recently been established to work through a number of other points that have been raised.

However, there is a key challenge which still very much remains to be resolved. This is the fundamental issue of employment status for tax (and NIC) purposes. We keenly await the Supreme Court's decision in *Revenue and Customs v Professional Game Match Officials Ltd* and very much hope that the Court will provide helpful guidance on how properly to apply the "mutuality of obligation" test in deciding whether or not an engagement is employment or self-employment for tax purposes. And we also have the recent FTT decision in *Atholl House Productions Ltd v Revenue And Customs* which is the IR35 case relating to Kaye Adams and her work with the BBC which went all the way up to the Court of Appeal, who then remitted it back to the lower courts to re-decide the case based on the correct application of the three classic tests set out in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance*. In a 74-page judgement the FTT found the matter very finely balanced but decided, once again, in favour of Kaye Adams. However, in my view the amount of time and effort involved surely illustrates the need for a statutory definition, or at least a framework, governing what we mean by "employment" for tax purposes.

Space does not permit me to cover all the great work done by the Committee over the last year in relation to, for example, the CIOT's Budget representations, responding to the consultation on tackling abuse in the umbrella company market, addressing the role of tax incentives in promoting occupational health, considering potential improvements to SAYE schemes / SIPs and reviewing the detailed legislation abolishing the pensions lifetime allowance. But, as I said at the beginning, it's certainly been a very busy year – and, with the prospect of new ideas and initiatives being proposed ahead of the forthcoming General Election, the next year is likely to be pretty busy too!

Finally, to say many thanks to all those who have contributed articles to this edition of Employment Taxes Voice and indeed to all those who have been involved with the Employment Taxes Committee over the last year. I hope you find the articles interesting and if you would like to get involved with the work that we do please let me know.

Reform of non-domicile status

Eleanor Meredith discusses the government's recent proposals to abolish non-domicile status

It was announced at the Budget on 6 March 2024 that the tax advantages currently associated with non-domiciled status for income tax and capitals gains tax would be abolished from 6 April 2025. This brief article summarises what we know as of now and in particular some of the concerns that may arise for employers seconding individuals to the UK.

Background to reform

The significance of domicile in the context of income tax reporting, dating back to 1799, is almost as old as income tax itself, but there has been considerable pressure to review it over the last 20 years, with major reforms in 2008 and 2017. These had eroded some of the tax benefits, by limiting the period over which income and capital gains tax benefits associated with non-domiciled status can be claimed, and by charging longer-term UK tax residents to access them.

The non-domiciled regime had been heavily criticised, as it depends on where taxpayers were born, where their parents were domiciled at the time of their birth, and taxpayers' intentions regarding their settled pattern of living: as such, it can be difficult to determine objectively. Press coverage suggesting that those domiciled outside the UK were not paying their 'fair share' of tax has only intensified the lobbying to move to a more modern, subjective system of taxation for expatriate employees (and others) who come to the UK with the intention of not staying in the UK permanently.

What do the proposals say?

The policy has been badged as tax simplification, because the proposals centre on the taxpayer's pattern of UK tax residence and abolish the concept of domicile as a relevant factor in terms of tax status.
Individuals not UK tax resident in the previous ten years will be eligible for an exemption on their foreign i.e. non-UK income and capital gains, for a fixed period. The exemption will apply regardless of whether the foreign income and/or gains are remitted to the UK. The new regime will be known as the foreign income and gains (FIG) regime.

The fixed period will comprise the first four UK tax years for which the individuals are UK tax resident (subject to separate rules for overseas workdays relief - see below). Once that period is over, individuals will only be eligible for further relief if they are not resident in the UK for a period of at least ten UK tax years.
The current system of overseas workdays relief that benefits employees who are considered non-UK domiciled is to be retained and will be reformed, but no details have been released apart from the period for which it is expected to apply, which is for the first three tax years of UK tax residence. It has also been confirmed that from 2025/26 the relief will not be conditional on income from employment being retained outside the UK.

The proposals also include transitional reliefs:

- Non-UK domiciled individuals who lose access to the remittance basis on 6 April 2025 and who are not eligible for the new four-year FIG exemption regime, will enjoy a temporary 50% reduction in the personal foreign income subject to tax in 2025-26.
- Current non-UK domiciles who are not deemed UK domiciled for tax purposes and have claimed the remittance basis will be eligible to rebase their capital assets to 5 April 2019 levels for disposals that take place after 5 April 2025.

- UK resident individuals who have paid tax on the remittance basis will be able to remit foreign income and gains that arose before 6 April 2025 to the UK at a rate of 12% under a new Temporary Repatriation Facility in the tax years 2025-26 and 2026-27.
- While the government is removing protections on non-resident trusts for all new FIG that arises within them after 6 April 2025, FIG that arose in protected non-resident trusts before 6 April 2025 will not be taxed unless distributions or benefits are paid to UK residents who have been here for more than four years.

Inheritance tax will also move from a domicile-based to a residence-based regime following a government consultation. To provide some certainty, the government has announced that the treatment of non-UK assets settled into a trust by a non-UK domiciled settlor before 6 April 2025 will not change, so such assets will remain outside the scope of UK inheritance tax.

What do we not know so far?

The proposals so far released are at a very high level, and there is considerable uncertainty attached, not least because the proposals are due to come into force after the next General Election. Although the election date remains uncertain, it will be before 6 April 2025, and so the detail of the reform, even to the extent that it is known, may be subject to change. However, regardless of the government in power in 2025/26, it seems unlikely that reform will be delayed, or that a more generous regime than that currently outlined will ultimately apply. The timetable is ambitious, but there is likely to be political pressure to achieve it either way, given both the Conservatives and Labour have now expressed a desire to change the current policy on non-domiciled status.

Much of the detail has yet to be confirmed. For example, will foreign income and gains be defined in the same way as relevant foreign income currently, or will other foreign income (such as chargeable event gains on non-UK life assurance policies) be included? It was confirmed that a taxpayer leaving the UK after only one year of tax residence, being non-resident in years 2 and 3 and then returning to the UK for year 4 may be eligible for the FIG election in that fourth year, but the announcement did not mention whether the FIG exemption might be available after a longer gap. Based on the announcement, it would be assumed that in this scenario a 10-year gap would be needed to restart the FIG clock, but this was not specifically addressed.

What will concern employers?

In many ways, the simplification will be welcome, especially as the 2017 reforms placed emphasis on where an individual was born and deem someone who had made a permanent home outside the UK for the longer term to be domiciled for income tax and capital gains tax due to being born here, if UK tax resident. The proposals would help to remove this potential anomaly, which can currently catch out HR teams looking to second individuals to the UK.

In addition, the current regime of overseas workdays' relief is very complex because of its interaction with the remittance basis and the mixed fund rules, and this complexity makes it uncertain, because relief can so easily be lost if the wrong type of money is inadvertently remitted to the UK. A system of relief that allows funds to be brought to the UK and spent or invested here, thereby generating other UK tax revenue (such as VAT), is more practical and sensible, as well as being something that most practitioners have been pressing for over some years.

The prospect of change, though, may be alarming to non-domiciled employees currently in the UK and is likely to increase the complexity of tax return reporting for any individuals remaining in the UK beyond the initial four years of UK tax residence. So, employers may want to consider more support with tax return reporting and/or UK tax liabilities that could not have been anticipated when any UK assignment was being planned. The proposed four-year FIG regime is quite short and might be viewed as ungenerous compared to other countries, although there is (presently at least) no charge proposed to access it.

Finally, because it is such a longstanding concept, non-domicile status is embedded in much of the income tax legislation and thought will need to be given to the implications of its removal. For instance, the ‘home leave’ provisions, which allow employers to fund travel to the home country and back to the UK for employees and their families tax-free in most cases is predicated on the employee concerned being non-domiciled. No comment has so far been made as to whether some similar form of relief may be retained under the FIG regime, and certainly this relief is widely used, both in the context of expatriates assigned to the UK and non-resident directors coming here to perform their duties.

Final thoughts

As with most reforms of the tax system, the devil is likely to be in the detail and we look forward to the release of further commentary and draft legislation. Compared with the timeframe utilised in earlier reforms of non-domiciled status, and the introduction of the Statutory Residence Test the timeframe looks tight and may allow for limited consultations. Whatever else happens, the next 12 months are likely to be interesting times but it’s clear that the non-domicile rules which have been with us from 1799 have now reached their expiration date!

Eleanor Meredith

Eleanor has been a director in Deloitte’s Tax Policy Group since June 2016, specialising in Global Employer Services and providing technical support to that part of Deloitte’s UK tax practice.

The end of Forms P11D – what does this really mean for employers?

Steve Wade and Dalbir Kathuria discuss the government's proposals to mandate the payrolling of BIKs

On 16 January 2024, HMRC announced the mandatory *"reporting and paying of Income Tax and Class 1A National Insurance Contributions (NICs) on benefits in kind via payroll software from April 2026".*

Under the current system, where employers provide benefits to their employees, they have the option of either submitting Forms P11D annually by the 6 July following the end of the tax year or alternatively, agreeing with HMRC to formally payroll benefits in kind. By payrolling benefits in kind, the benefits are taxed through PAYE and whilst Forms P11D do not need to be submitted to HMRC, employers must still submit Form P11D(b) which declares the amount of Class 1A NIC due to HMRC and inform employees of the amount of the benefits payrolled.

From April 2026, however, this will change, and employers must payroll benefits in kind. This will be good news for some, as it will mark the end of preparing Forms P11D which for many employers can be a cumbersome task. However, whilst in the long term these changes should result in efficiencies and simplification, in the short term, they do present a number of challenges for employers, their agents (including tax agents and payroll agents), benefit vendors and HMRC. As this is such a significant change for which those affected should start to prepare now. Waiting for all the details to be published is likely to be too late for some employers to be ready in time. What's more employers who are already payrolling benefits should not be lulled into a false sense of security. They will also probably need to make some changes to their systems to fulfil all the reporting requirements.

What does this change mean for employers?

Data management

The ability to meet the requirement to payroll benefits in kind will vary across employers. The biggest challenge facing employers is likely to be whether they are able to acquire the benefits data in a timely fashion to meet the monthly, or even weekly, payroll reporting. Employers will need to ensure that they have robust processes to collate the required data from all their relevant sources and benefit suppliers to enable timely reporting. Furthermore, where the operation of payroll is outsourced to a payroll bureau they will need to review how the data flows to that bureau: will all data be collated by the employer or will any data flow directly to the bureau? Whatever the scenario this will require careful planning and ownership, to ensure the right data flows through at the right time.

Timeframe

The question most employers are asking themselves is, whether the current mandatory deadline of 6 April 2026 allows sufficient time to enable them to prepare for this change? Whilst April 2026 is some two years away, it is probably too soon to allow full and robust testing of new payroll software by software developers and the subsequent integration by employers of any new systems required to provide the benefits data either monthly or weekly. Will this cause some employers to considering moving from weekly payrolls?

Though in essence the ask is straightforward, what HMRC appears to have overlooked is that the degree to which UK employers are ready for this change varies significantly. Depending on the size of the organisation, the sector, and the employer profile in terms of employee incentivisation, organisational readiness will vary from one employer to another.

Whilst simplification in the long term is one of the objectives HMRC is trying to achieve, it is likely that in the short to medium term, we will see a greater number of payroll adjustments to the payroll. One area where this is particularly likely is with respect to globally mobile employees. As an example, for this population their workdays are determined after the year end. Transitioning to payrolling benefits in kind in real time may require calculation of workdays on a cumulative monthly basis – however, the question is how employers implement this as it is likely to be impractical to do so. When a S690 determination is in place payroll is calculated on an estimate of the taxable percentage of the earnings. For NIC purposes, will this need to be trued up via payroll or only via the form P11D(b)? For tax the true up could continue to be via the employee's self-assessment tax return.

Cost impact for employers

There is likely to be a material cost impact for employers, especially where their current payroll software may not be configured to payroll benefits in kind. In fact, this should be one of the key factors employers should be assessing now, as potentially payroll software may need to be upgraded or the employer may even need to consider changing payroll supplier. The latter is not only costly but time consuming, and if required, employers should consider moving vendor ahead of April 2026 to enable new processes to bed in.

Communicating this change to employees and cash flow impact on employees

Alongside the above cost and disruption, employers will need to explain the changes to their employees. The impact on employees will vary depending on whether they are UK employees or on international assignment. Employers will need to ensure that the impact for the various employee groups is carefully considered and communicated in a clear manner. That said, as some of the detail of the proposed changes have yet to be published (e.g. how accommodation benefits/loan benefits will be payrolled), employers will need to monitor the progress of the consultation, to ensure this information is shared with employees when the details become available.

For some employees there may also be a cash flow disadvantage for the year starting April 2026 due to 2026/27 PAYE notice of coding adjustments collecting tax on benefits for earlier years whilst the tax and NIC on current year benefits is being collected through payroll.

Summary

At the time of writing, the mandatory payrolling of benefits is due to take effect from 6 April 2026, however, it is unlikely that this is the last we hear of this. We await further clarity from HMRC over the coming weeks and months as to how this will impact accommodation and loan benefits, internationally mobile employees and many other points of detail. Has HMRC been too eager in mandating this change and as the difficulties are explored will the case for a soft landing become irresistible and the start date delayed? Time will tell but for now, many employers will have a sizeable task at hand in order to meet the current 6 April 2026 deadline.

Steve Wade

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Dalbir Kathuria

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Electric cars, car allowance drivers and double cab pick ups

Peter Moroz gives his annual update on some of the developments in tax complexities relating to cars and vans

Charging electric cars at home vs. paying mileage allowances

Company cars

After much lobbying by the CIOT, HMRC have finally relented on their position and now agree with us on the law concerning reimbursements for home charging of company Electric Vehicles (EV):

The updated HMRC guidance at EIM23900 now states the following in relation to company cars used for business and private mileage:

The exemption under s.239(2) ITEPA 2003 means there is no separate charge to tax under the benefits code where an employer reimburses an employee for the cost of electricity to charge their company car at home. Employers will need to ensure that the reimbursement made towards the cost of the electricity is solely for the company car.
The little sting in the tail is the requirement for the employer to be able to show that reimbursement relates solely to the company car, but there are increasingly technological solutions to help them do so with apps linked to home chargers showing the actual usage.

Elsewhere in HMRC guidance, it gives the Advisory Electric Rate (AER) which can be used to reimburse business mileage in relation to a company EV; this is currently 9ppm.

9ppm is still a bit mean, especially as the cost of charging at motorway services can be as high as 19ppm. Also, paying by reference to mileage seems now to be a hugely tax inefficient way of reimbursing costs of charging. I have seen some companies who want to reimburse a "fair amount" in respect of business mileage who are paying 9ppm tax free plus a taxable top up of a further 6ppm for business mileage to ensure drivers are not losing out. Instead, they could put in place a mechanism to reimburse 100% of charging cost and it would all be tax free. If they didn't want to be that generous, they could then require a contribution from the driver towards private mileage. It would still produce savings.

Private Cars

In contrast to the above reimbursing home electricity costs for a private car is still a taxable benefit. So, paying a reimbursement by reference to business mileage can make more sense as the current rate is 45ppm for the first 10,000 miles. The Employment income Manual deals with this as follows:

If by reference to mileage, AMAP rules apply for business miles travelled. Any amounts in excess of AMAP rates would be taxable. If less than AMAPs rates, employee may claim appropriate amount of tax relief under MAR for business miles. If a flat-rate amount is paid it is taxed as earnings.

VAT recovery on charging electric cars at home

The question of VAT recovery by an employer who reimburses home electricity costs is still in limbo and there has been no movement from HMRC since January 2022 when they withdrew their previous guidance (which said there was no VAT recovery) to say that they were thinking about it:

Motoring expenses (VAT Notice 700/64)8.4.1 Electricity paid for by employees

We are considering the situation where an employee is reimbursed by the employer for the actual cost of electricity used in charging an electric vehicle for business purposes.

This is to determine what evidence can be practicably provided, to allow the employer to claim the related VAT, subject to the normal input tax rules.

8.4.2 Simplification measures

We are also considering other simplification measures that may reduce administrative burdens in terms of accounting for VAT on private use.

When I last contacted HMRC in March 2024, I was assured that they are still thinking about it!

Car allowance drivers and business mileage

Moving on from company EVs to car allowance drivers in general. Following the outcome of the Willmott Dixon case last year, every employer who paid car allowances to drivers who drove business mileage can make a claim for a refund of National Insurance contributions provided they fit into the criteria in the below.

The fact pattern in many companies is similar. A company pays a car allowance. This may be as an alternative to a company car. It is often treated differently from salary when it comes to pay rises. It is typically set by reference to the grade of the employee such that more senior employees are entitled to a bigger car allowance.

In return for the car allowance, the employee is required to have an appropriate car available for business travel and to service / maintain and insure it for business travel. There may or may not be an additional payment by the employer for fuel costs. Many companies use the HMRC Advisory Fuel Rates for company cars to determine the rate of payment for business travel, but they can pay whatever they like. Some provide fuel cards.

The issue at hand, in broad terms, is that when an employer pays a mileage rate for business travel of less than 45ppm, but also pays a car allowance, then part of the car allowance could be regarded as free from National Insurance (NI) to the extent that the total payment for business mileage does not exceed 45ppm.

Because of the Willmott Dixon case which I am proud to say I advised on, the Courts agreed that a claim can be made to HMRC going back to the previous 6 tax years for the refund of National Insurance.

As an illustration, if an employer had 100 drivers who drove 10,000 business mileage pa each and were paid 10ppm, then, depending on the car allowance, the potential refund claim for employer's NI is £289,800.

A more detailed explanation is given in the Tax Adviser Article I wrote last September.

In October 2023, HMRC included a section in their Employer Bulletin about how to make NI corrections via RTI. Whilst I agree with HMRC that it should be possible to make such amendments if you are still in the same tax year, it appears that the software often used, and the mechanisms suggested by HMRC are impractical once the tax year has ended and the final FPS has been submitted. The only practical mechanism is to apply for a refund of NI directly.

We are not talking about just a refund of secondary NI, but also primary NI paid by the employee.

Also, it is not just a question of claiming a refund for past years, but reducing the NI on car allowances going forward. This involves having a payroll wage type whereby the car allowance can be split on the payroll so that part is paid taxable but NI free and the rest is taxed and subjected to NI.

Given that the employee can also make a claim for tax relief up to 45ppm, you might also be wondering whether a part of the car allowance can be paid tax free too, to save the employee the effort of putting a claim on form P87. However, I would advise against this, as HMRC may then argue that the Optional Remuneration OpRA rules apply. If OpRA applies this would then mean that there is no tax relief (nor NI relief)! Such an argument is in my opinion nonsensical, as OpRA was never intended to be triggered by an employer's view on whether or not a payment should be subject to PAYE, but nonetheless HMRC have raised this issue in some instances.

When is a van not a van?

In a tax case involving Coca Cola a few years ago, VW Kombi and Vauxhall Vivaro vans were adjudged by the Courts to be classified as cars for BIK purposes. These looked like vans to most observers, but the issue was in the definition of a van in tax law. S 115 ITEPA 2003 defines a van in terms of being a "goods vehicle" of under a specified weight. A "goods vehicle" is a vehicle of a *construction primarily suited* for the conveyance of goods. If it is not a van or a motorcycle, then it is a car.

The Courts considered the words in italics in great detail and decided that because of the way the vehicles in questions were constructed; there was a point in the manufacturing process where the finished product could have either been a people carrier or a goods vehicle. Therefore, because of the common elements in the manufacturing process they did not meet the primarily suited test and so the "goods vehicle" definition did not apply. They were therefore cars.

Cars have a taxable BIK of Retail Price x CO_2%

Vans have a BIK of £3,960, i.e. a lot less than what it would be if they were classified as cars.

On 12 February 2024, HMRC decided to announce that the same logic should apply to Double Cab Pick up trucks which they had previously said would be regarded as vans. This meant that from July 2024, they would be taxed as cars and the BIK would increase massively (subject to an element of grandfathering).

Following intense lobbying by farmers and the auto industry, HMRC reversed their position less than a week later and said the law would be changed to the effect that double cab pick ups would continue to be taxed as vans, not cars. It is good to see common sense prevailing.

Peter Moroz

Peter Moroz is Chairman of Innovation & sits on the CIOT Employment Tax Technical Committee. Innovation are specialists on all aspects of Cars; Tax & Mileage Tracking including change management / communication strategy, and project implementations.

HMRC’s focus on umbrellas companies

Rob Woodward discusses the employment tax matters to consider when engaging with umbrella companies

Since the introduction of the off-payroll working rules for medium and larger-sized businesses in April 2021 (April 2017 for the public sector), there has also been a greater focus on the labour supply chain more generally, not just those engaged through personal service companies (colloquially known as IR35).

In particular, one area of focus is the use of umbrella companies and how businesses engage with them for the supply of workers. While this encompasses employment rights as well as tax, and HMRC have also paid greater attention regarding National Minimum Wage compliance, here we look at employment taxes and what businesses need to consider when engaging with umbrella companies.

HMRC Guidance

In late 2023 HMRC published guidance on the responsibilities of businesses working with umbrella companies, available at https://www.gov.uk/guidance/responsibilities-for-employment-businesses-working-with-umbrella-companies.

The key takeaway from the guidance was that businesses must identify the entities in their labour supply chain, understand how workers are being engaged and paid as well as assess and reduce any risks of non-compliance. These checks should be regular, reasonable and proportionate for their business.

Naming and shaming

Another area where HMRC has been increasing their attention on the umbrella company market is through their publication of named tax avoidance schemes, promoters of tax avoidance schemes and enablers of tax avoidance schemes (https://www.gov.uk/government/publications/named-tax-avoidance-schemes-promoters-enablers-and-suppliers/current-list-of-named-tax-avoidance-schemes-promoters-enablers-and-suppliers). Given that the majority of recent entries have been umbrella companies the appearance of a current / recent supplier on this list (or a business associated with them) should prompt a business to undertake further enquiries.

Consultation

In the light of HMRC's concerns in relation to non-compliance by certain umbrella companies, last year the Government consulted on how tighter regulation could assist in reducing tax avoidance and the exploitation of workers’ rights. The consultation has now closed, and its outcome and potential next steps are due to be announced on Tax Administration and Maintenance Day 2024 (18 April). Whilst a number of key issues were raised about the way that employment agencies use umbrella companies, it's also important to recognise that genuine / compliant umbrella companies do play a useful role in the labour market. Therefore, a blanket prohibition or regulation that would make them redundant, would not be good for businesses at a time when the need for flexible labour and cost management has never been greater.

The consultation posed over sixty questions but essentially the key ideas put forward were:

1. Mandating due diligence by either the employment agency or end user client,

2. Transfer of any tax and NIC unpaid by the umbrella company to the employment agency or end user client, and/or

3. Worker payrolls to be operated by the employment agency where an umbrella company is used.

It should be noted that, notwithstanding a suggestion made in the consultation document, many umbrella companies already seek accreditation by industry bodies because they recognise the commercial benefits; indeed, a significant part of the labour supply market already expects that an umbrella company has some accreditation. By formally recognising accreditation, perhaps through an existing trade body or even a new scheme operated by the Employment Agency Standards Inspectorate, HMRC compliance activity could then be better focused on the non-accredited umbrella companies. It would also give employment agencies and end user companies a clear quality indicator.

Managing risk

Pending the Government's response to the consultation, businesses using agency workers should step up their supplier diligence to protect themselves from the potential implications of using workers connected to unscrupulous umbrella companies. In anticipation of any potential changes, which are likely to address at least some of these issues, ten key warning signs that should be heeded are set out below.

1. Workers are promised increased net pay if they work through that umbrella.

The only way that a worker can be paid more by an umbrella company is if that umbrella charges less (its margin) or if it isn't fulfilling its tax obligations properly. If it's the former, questions should be asked on how it can provide the same level of service, compliantly, than similar businesses. If the latter, then clearly there's a more fundamental problem.

2. The worker has no choice but to work through certain umbrellas.

This may be because the engager or agency has undertaken an assessment of suppliers and only wants workers who are able to work via their preferred supplier. But it also might be that the agency or their consultants are receiving a cash incentive for placing that worker through that particular umbrella and do so without undertaking proper due diligence which would be more worrying.

3. Payslips are incomprehensible.

Unless the business engaging with the agency/umbrella company can clearly understand the link between what they pay, and the amount workers receive after PAYE/NIC and any other deductions then they should be concerned. Especially if the payslip shows unusually low levels of tax/NIC or different categories of taxable/non-taxable pay that cannot be explained.

4. The workers are employed by one entity but paid by another.

Why are they being paid by someone who isn't their employer? This might be indicative of a tax avoidance scheme or of historic compliance issues.

5. Employees can claim expenses tax free without the need to keep comprehensive records.

There are limited circumstances now where umbrella employees can claim tax free expenses. All of these require records to be kept and checked, at least periodically, by the employer so any umbrella claiming that tax free expenses can be paid without records being kept is likely to be operating non-compliantly.

6. The umbrella company website has no real detail to it, no contact names, numbers or address.

It might indicate a new or very small business or just one that isn't very good with managing its own web presence but any business that employs people might be expected to have some substance behind it including contact details, some background on the senior management, their history and experience and maybe even useful documents and FAQs. If this information is not available, then the position should be challenged.

7. **The umbrella management/directors/shareholders have been involved in similar businesses that no longer trade.**

A quick and free search at Companies House will provide a list of the shareholders and directors as well as their prior records. If that shows a long list of short-lived businesses or the information contradicts what they are saying or showing on their website, more questions should be asked.

8. **The umbrella claims to employ 1,000's of workers but operates from a private address, an office above a corner shop or only lists a registered office.**

Not every business needs a flagship head office but do their business premises support what they are saying about their business?

9. **The umbrella holds no form of industry accreditation such as FCSA or Professional Passport.**

If they have been trading for any length of time and reached any reasonable size, an umbrella business without some form of independent accreditation should raise alarm bells.

10. **Only vague answers are given in response to anything other than basic questions.**

It is highly unlikely that an experienced umbrella hasn't been asked a particular question about their business and operations many times before. If they can't answer the questions easily and quickly or refuse to answer the questions or provide supporting information when asked politely, engagement with them should be seriously reconsidered.

In short, businesses should make sure they know who they are engaging with before dealing with a particular agency / umbrella. The direction of travel is towards greater regulation and as shown with other reforms such as IR35, that is likely to mean a greater burden on engaging parties. Getting ready for those changes ahead of time not only assists with current compliance requirements but is prudent to build in some "future-proofing".

Finally, it should also be noted that besides the employment tax implications of getting it wrong, which may increase if debt transfer proposals are enacted, all businesses have an obligation to know who is in their supply chains under other obligations namely the Criminal Finance Act 2017.

Rob Woodward

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Construction Industry Scheme

Lee Knight and Susan Ball from RSM UK discuss the Construction Industry Scheme – back to basics, problem areas, and changes from 6 April 2024

What is the Construction Industry Scheme?

The Construction Industry Scheme (CIS) is a tax withholding and reporting scheme that applies to payments made from contractors to subcontractors under construction contracts.

The primary CIS legislation is within Sections 57 to 77, and Schedules 11 and 12, of Finance Act 2004 (FA2004). The secondary CIS legislation is in the Income Tax (Construction Industry Scheme) Regulations 2005 (SI2005/2045).

The CIS operates in relation to tax months with a tax month running from the sixth of one month to the fifth of the next.

A construction contract is a legally binding agreement, under which one person (the subcontractor) carries out, or provides labour for, construction operations, to another person (the contractor). A contract of employment is not a construction contract.

Where a single contract includes some services that relate to construction operations and others which do not, then all payments under that contract are caught by CIS, even those payments that are for non-construction work. This is known as the ‘mixed contract’ rule.

The services the CIS applies to are known as ‘construction operations’ which includes a wide range of work done to permanent or temporary buildings, structures, or to the land (such as site clearance and civil engineering works).

Payments made from contractors to subcontractors under construction contracts are known as contract payments.

For the CIS to apply the construction operations must be within the UK or UK territorial waters (extending twelve nautical miles from the high watermark). Overseas based contractors and subcontractors must consider registering for and (for contractors only) operating the CIS in relation to UK construction operations.

Note that the agency rules at Chapter 7 of Part 2 of ITEPA 2003 and the off-payroll working rules at Chapter 10 of Part 2 of ITEPA 2003 take priority over CIS. It is therefore vital that contractors consider these obligations, along with the obligation to consider the employment status of subcontractors engaged directly as individuals, before considering CIS.

Contractors can be liable for any CIS tax under-deducted from contract payments to subcontractors. If reasonable care has not been exercised HMRC are able to recover that CIS tax for up to six years from the end of the tax year it relates to, together with interest and penalties. While there is scope (under Regulation 9 SI2005/2045) to reduce such settlements with HMRC, this cannot be relied on and may not reduce the final settlement with HMRC to nil.

How is a contractor defined?

A contractor is a party to a construction contract which is either:

- Under S59(1)(a) FA 2004, a business which includes construction operations, such as a construction business or property developer. HMRC refers to these contractors as mainstream contractors; or

- Under S59(1)(l) FA 2004, a business that is not a mainstream contractor but whose cumulative VAT exclusive expenditure on construction operations within the previous twelve-month period exceeds £3,000,000. HMRC refers to these contractors as deemed contractors; or

- Under S59(1)(b) to (k) FA 2004, a type of other body (local authority, housing association etc) whose (with one exception where the deemed contractor threshold is irrelevant) cumulative VAT exclusive expenditure on construction operations within the previous twelve-month period exceeds £3,000,000. HMRC also refers to these contractors as deemed contractors; or

- Under S57(2) FA 2004 a subcontractor who engages other subcontractors to carry out construction work (FA04/S57(2)).

A householder having construction work undertaken on their own home is not a contractor in respect of these works.

The inclusion of deemed contractors means that non-construction businesses and certain other bodies whose expenditure on construction operations exceeds the deemed contractor threshold are within scope of the CIS.

Deemed contractors may have to operate the CIS immediately after the threshold is or is expected to be exceeded and so ongoing monitoring of expenditure on construction operations against the threshold is required.

For deemed contractors the requirement to register is subject to a discretionary ‘period of grace’ (to be agreed with HMRC) not exceeding 90 days.

Are there any relaxations to the rules for deemed contractors?

For a business treated as a deemed contractor under S59(1)(l) FA2004, Regulation 22 of SI2005/2045 (Regulation 22) might apply to certain payments it makes.

Under Regulation 22 a payment made under a construction contract is not regarded as a contract payment where it is made in respect of property used for the purpose of the business of either:

- the deemed contractor making the payment; or

- if the deemed contractor is a company, another company within the same group, or another company in which the business holds at least 50 per cent of the shares.

Regulation 22 exempts the payment not the contractor.

Regulation 22 cannot be applied where the property to which the construction operations relate is for sale or let or is held as an investment. However incidental use by another person is disregarded for the purpose of Regulation 22.

For landlords letting property to tenants, please note the changes regarding landlord to tenant payments highlight below.

Regulation 22 can only apply to a business treated as a deemed contractor under S59(1)(l) FA2004. It does not apply to other types of bodies (local authorities, housing associations etc) who are treated as deemed contractors under S59(1)(b) to (k) FA 2004.

For deemed contractors there is also a relaxation for small payments where a contract has a value not exceeding £1,000 (excluding VAT and after deducting materials) and certain other conditions are met. Contractors must apply in writing to HMRC to apply this relaxation and should not use the arrangement without HMRC approval.

What obligations do contractors have?

Contractors have several compliance obligations. They must:

1. Register as a contractor on time.

2. Consider the employment status of subcontractors engaged directly as individuals.

There is a requirement for the contractor to conduct a status assessment to determine whether the subcontractor has employment status.

A contract of employment is not a construction contract. If the status assessment shows that the subcontractor is employed by the contractor, then payments to them should be subject to income tax and NIC under PAYE. The CIS does not apply.

If the status assessment shows that the subcontractor is self-employed, then (subject to their services falling within the definition of construction operations) the contractor must apply the CIS rules.

3. Consider whether the agency provisions or IR35 regulations apply and take priority.

The agency provisions and off-payroll working (IR35) rules take priority over CIS and must be considered first.

If a payment is to be treated as employment income under either the agency provisions or the off-payroll working rules, then the CIS does not apply. If that is not the case, then (subject to the services falling within the definition of construction operations) the contractor must apply the CIS rules.

4. Identify whether the contract includes construction operations.

The legislative definition of construction operations is within S74 FA2004.

A contractor must consider whether the services performed by the subcontractor fall within the definition of construction operations.

The definition of construction operations includes a broad range of construction work. Examples include:

- constructing, altering, repairing, extending, or demolishing buildings or structures;

- constructing, altering, repairing, extending, or demolishing any works forming, or to form, part of the land (such as walls, roadworks, powerlines, electronic communications apparatus, and pipelines);

- installing systems of lighting, air-conditioning, ventilation, power supply, drainage, sanitation, water supply or fire protection, in any building or structure;

- internal cleaning of buildings and structures which is carried out during their construction, alteration, repair, extension or restoration; and

- painting or decorating the internal or external surfaces of any building or structure.

Operations which are an integral part of, or are preparatory to, or for rendering complete, other construction operations, are also regarded as construction operations. This is to ensure that activities which have the characteristic features of construction, but which are not specifically dealt with in the legislation, are also caught when undertaken as part of a wider project of construction. This can catch a variety of other services such as erecting and dismantling scaffolding, constructing site facilities, hiring plant with an operator, and certain traffic management activities.

Determining which operations constitute construction operations can be complex and the ‘mixed contract’ rule must also be considered. If a construction contract includes both construction operations and non-construction operations, then the contractor is required to apply CIS to all payments made under that contract.

For example, carpet fitting in isolation does not fall within the definition of construction operations, but if carpet fitting is undertaken under a single contract which includes other services falling within the definition of construction operations (such as painting and decorating), the payment for that carpet fitting will also be within the scope of the CIS.

Where construction operations are carried out partly within and partly outside UK territorial waters under a single contract, it is HMRC practice to treat all payments made under that contract as within CIS. This is relevant, for example, where a contractor engages a subcontractor to build a pipeline from an offshore installation outside UK territorial waters to a location in the UK.

5. Verify subcontractors.

The contractor must verify each subcontractor’s payment status online with HMRC at the correct time.

A contractor does not have to reverify a subcontractor if they last included that subcontractor on a CIS return in the current or two previous tax years.

Subcontractors will either be unregistered (contract payments require a 30 per cent deduction rate), registered for net payment status (contract payments require a 20 per cent deduction rate), or registered for gross payment status (contract payments can be paid without a CIS deduction).

6. Deduct CIS tax and pay it to HMRC and give a statement to the subcontractor.

Where a subcontractor does not have gross payment status the contractor must calculate the CIS tax due and deduct this from the payment before paying the subcontractor. They must then pay that tax to HMRC and provide the subcontractor with a statement showing the deduction made.

The direct cost to the subcontractor of materials, consumable stores, fuel (but not fuel for travelling), plant hire, and the cost to the subcontractor of manufacturing or prefabricating materials used, does not attract a CIS deduction.

Care needs to be taken by the contractor to ensure the CIS deduction is calculated correctly. If the cost of any items excluded from the CIS deduction are excessive or incorrect, HMRC can hold the contractor responsible for the under deducted CIS tax.

Materials costs can only be excluded where they represent the actual direct cost of materials to that subcontractor and specifically relate to the construction contract between the contractor and subcontractor under which the payment is being made. A ‘markup’ charged by the subcontractor on materials does not represent the actual cost of materials and should be subject to a CIS deduction.

For plant (scaffolding, cranes etc) it is only when the subcontractor hires the plant to carry out construction work for the contractor, that the cost (and any consumable items such as fuel needed for its operation) may be excluded from the contract payment. If the subcontractor owns the plant but includes a charge for this on their invoice to the contractor, this charge must be included as part of the contract payment.

Contractors must pay CIS tax deducted to HMRC within 14 days of the tax month end to which it relates if paying by post, or within 17 days of the tax month end if paying electronically.

The contractor must also provide a written statement to every subcontractor from whom a tax deduction has been made within 14 days of each tax month end. Contractors must include certain information in the statement but are otherwise free to decide on its style.

7. Submit monthly CIS Returns.

Contractors must send HMRC a monthly return which includes all payments made to subcontractors in that tax month. The return is due to HMRC within 14 days of the end of the tax month end it relates to.

The return must include details for the tax month of subcontractors paid, payments made, costs treated as materials, and tax deductions.

How does the CIS interact with the VAT domestic reverse charge for construction and building services?

The VAT domestic reverse charge (DRC) for building and construction services is a mechanism that can shift the responsibility for accounting for VAT from the supplier (subcontractor) to the recipient (contractor) in certain circumstances.

It applies to supplies of building and construction services where the services are reported (or should be reported) under the CIS. The services subject to the DRC align with services defined as 'construction operations' for CIS purposes. The DRC therefore interacts closely with the CIS.

CIS cannot be considered in isolation, it must be considered alongside the VAT DRC.

Are there any changes to the CIS rules from 6 April 2024?

From 6 April 2024, the compliance tests for subcontractors obtaining and retaining gross payment status (GPS) are stronger.

To obtain GPS the subcontractor must apply to HMRC and pass a business test, a turnover test, and a compliance test. As part of the compliance test, compliance with various tax obligations must have been met. Subcontractors granted GPS also have their tax compliance automatically checked by HMRC annually.

Prior to 6 April 2024 only compliance with direct taxes was considered but from 6 April 2024 subcontractors will also need to be compliant with VAT obligations to be granted or retain GPS.

In addition, from 6 April 2024:

- HMRC can now cancel GPS immediately if there are reasonable suspicions of fraud involving VAT, Corporation Tax, Income Tax, or PAYE.

- Telephone GPS applications will no longer be available apart from for those who are digitally exempt. Postal applications will remain available, but the longer-term plan is for digital applications only.

- The first review of a GPS holder's compliance history after obtaining GPS will now occur six months after application, followed by subsequent reviews at twelve-month intervals.

Another important change from 6 April 2024 is in relation to payments from landlords to tenants for construction operations. The wide scope of CIS means that it can extend to landlords making payments to tenants for construction operations.

Payments from landlords to tenants wholly for 'Category B' tenant fit out works provided as an inducement have historically been exempted from CIS as reverse premiums under Regulation 20 SI2005/2045. However, any other payments for construction operations from landlords to tenants (such as payments for 'Category A' landlord works) were caught. This could create CIS complications for both the landlord and the tenant.

To help address these complications, from 6 April 2024 a new regulation (Regulation 20A SI2005/2045) has been introduced. Under Regulation 20A a payment from a landlord to a tenant to complete construction work on a property occupied by the tenant is also not within the scope of CIS where all the following conditions are met:

- The payment is made by or on behalf of the landlord.
- The person receiving the payment is a tenant (if sub-let this includes a sub-tenant) or prospective tenant of the landlord.
- The payment is for construction operations agreed in connection with a lease or an enforceable agreement to enter into a lease.
- The tenant that occupies or will occupy the property will carry out the construction operations itself, or a third person will carry out the construction operations pursuant to a contract with the tenant.
- The payment is for construction operations relating to works intended primarily for the benefit and use of the tenant that occupies or will occupy the property under the lease.

Five common pitfalls and problems	
1	Not considering employment status, the agency provisions, and off-payroll working (IR35) rules in priority to CIS. These are contentious areas frequently targeted by HMRC.
2	Not identifying when the deemed contractor threshold is exceeded. Ongoing monitoring of expenditure on construction operations against the deemed contractor threshold is required.
3	Missing that a subcontractor is performing construction operations. The definition of construction operations broad and complex, and further complicated by the mixed contract rule.
4	Not applying CIS tax deductions to materials and plant hire costs that should have suffered a tax deduction.
5	Incorrectly applying or missing the VAT Domestic Reverse Charge (DRC) for construction services.

Conclusions

CIS can be complex and is a focus area for HMRC who check compliance with the scheme. There are several traps and pitfalls for the unwary and mistakes can be costly for both contractors and subcontractors. Being aware of the complexities and having robust procedures to facilitate compliance is crucial to avoid problems and potential settlements with HMRC.

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HM Revenue and Customs (HMRCs) National Minimum Wage Investigations: Understanding the Ins and Outs…

Vaneeta Khurana discusses National Minimum Wage investigations and common compliance errors

Over the last few months, there has been lots of media attention on the National Minimum Wage (NMW). This includes HMRC publishing it recent list of employers who have been publicly named for underpaying their employees in relation to historical investigations; a survey conducted by the Teachers Union Congress found that two out of five teaching staff worked 26 hours for 'free' each week, resulting in a combined 5.5m hours a year; the judgement of the employment tribunal in the case of Nexus Workforce Limited reminding us of the impact and effect of TUPE on NMW for companies who are seeking to acquire a business; and finally, HMRC's targeted compliance activity working through Regions in the UK and certain sectors including retail, manufacturing and the care sector.

The Minister for Enterprise, Markets and Small Business Kevin Hollinrake has been quoted in the media saying: '*Whilst not all minimum wage underpayments are intentional, the government has been clear that anyone entitled to be paid the minimum wage should receive it, and that enforcement action will be taken against employers who do not pay their staff correctly*'. The Independent Commissioner at the Low Pay Commission, Patricia Rice has also been quoted saying *'Since its introduction nearly twenty-five years ago, the national minimum wage has played a vital role in protecting the earnings of the lowest-paid workers in the UK. At a time when the cost-of-living is rising, it is more important than ever that these workers receive the pay to which they are entitled…'.*

Working culture has changed since COVID including hybrid working, remote working and HMRCs ability to forensically review and process large amounts of data means NMW compliance feels very different now to maybe five years ago, particularly around some of the tricky areas reviewed. So, what does an HMRC NMW investigation feel like and what are the typical risks we see emerging today?

What is the process of a HMRC NMW Investigation?

The majority of employers involved in an investigation will no doubt agree that it can feel like a long and protracted process, before arriving at a settlement position. The employer then needs to make good the underpayments to employees, which for many employers also involve a communication plan, and pay associated PAYE/NICs to HMRC, which needs be reported in a certain way by amending earlier year FPSs. Penalties of up to 200% of the underpayments can be levied, plus publicly being named.

The investigation is usually conducted by a Compliance Officer and begins with them sending a notice to employers indicating they have been selected for an investigation – this can be as a result of HMRC's targeted compliance activity, a re-visit to assesses what remedial action employers took in response to the previous investigation or instigated by a worker compliant. This notification typically requests specific records that employers are required by law to keep and offers a deadline for compliance.

The required records include salary payments, employee work hours, overtime, deductions, tips, bonuses and benefits-in-kind, contracts of employment, policy documents relating to flexible working, documented payroll controls / risk registers and evidence of any specific NMW checks all, of which are relevant in determining pay levels and the robustness of the controls in place.

Following the initial records review, the Compliance Officer will often interview a selection of employees. The interviewees may be chosen randomly or based on specific identified criteria. HMRC's aim behind conducting these interviews is to validate the information given in the documentation and to obtain a direct understanding of the working conditions and payment procedures from the employees' perspective. The Compliance Officer may ask for details about the employee's working hours, their understanding of their pay structure, and any overtime or additional work they do, and details of the messaging provided by their line managers. The information from these interviews is then cross-referenced with the records provided by the employer to ensure accuracy. This is where many employers trip up! The employee's responses to HMRC's questions can lead to the requests for more evidence, typically around working time and local practices which may not align with the company's policies. This additional administrative time to locate the requested records and provide evidence to respond to the employee's information can significantly lengthen the time an investigation can take to conclude. It is not unusual for an investigation to last for three or four years.

What are the top three typical risks/ errors we see emerging today?

1) Deductions/ reductions that take pay below NMW and typically, this could be a salary sacrifice arrangement (including pension). A calculation is required every pay period to include the aggregated salary sacrifice amount across all arrangements, ensuring the pay does not fall below the NMW rate even if the employee voluntarily requests a larger salary sacrifice reduction to be applied.

2) Underpaid working time. Employers must be able to show the hours worked by employees and this must include all working time. This could include additional work before and after a worker's shift; rounding clock-in time to the nearest hour, half hour or five minutes, or unpaid travel time. These often come out from the interviews. 'Excess' hours has been in the spotlight for salaried employees – historically HMRC enforcement has concentrated on the employees who were paid by the hour, (time workers), typically time workers are paid closer to the NMW rates. However, currently HMRC's focus has shifted towards salaried employees, bringing middle earners with annual salaries of circa £40k to £50k into focus. There is an expectation that employers know and are able to evidence, how many additional or 'excess' hours their salaried employees work each week? How are they paid for those 'excess' hours? At what point in the year they are likely to hit the 'annual hours' stated in their contract? What is an 'Excess hours' calculation?

3) Identifying the correct worker category is fundamental. Each of the four worker categories have slightly different calculation requirements including how often the calculations need to be completed and, what pay elements should be included in the calculations.

Summary

It is a business's responsibility to prove that employees have been paid NMW. Employers should maintain accurate records of employee hours, bonuses, overtime, and every component factor of pay. Employers should have robust policies and training in place to ensure that policies are adhered to in practice in an employee interview situation. Regular internal investigations can help identify potential issues before they escalate. Special attention should be paid to sectors with a complex workforce. Finally, be aware of changes in the NMW rates and bands.

Vaneeta Khurana

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Non-Resident Directors – Tax and National Insurance – the challenges

Paul Tucker and Lee Muter discusses the PAYE and NIC liabilities of non-resident directors

In our article in Employment Taxes Voice last year, we highlighted some of the challenges in relation to UK resident Directors. This year we will be looking at topical challenges in relation to Non-resident Directors ("NR Directors").

As we highlighted last year, a director is regarded as an officeholder by HMRC. Payments in respect of director duties are liable to PAYE (tax and NI), but there are some exceptions and complications in relation to NR Directors.

Case study

We have adopted a slightly different approach with this article, and have used the case study below to illustrate some of the challenges and points to consider.

- Toon Limited is a UK subsidiary of a French company.
- The company has five directors
  - Keegan and Shearer – Executive Directors
    - Paid by Toon Limited;
    - UK residents; and
    - On the UK payroll and subject to UK PAYE (tax and NI).
  - Cole – Non-Executive Director
    - Fees paid by Toon Limited;
    - Resident in Germany;
    - Only provides director services; and
    - On the UK payroll and subjected to UK PAYE (tax and NI)
  - MacDonald – Non-Executive Director
    - Fees paid by Toon Limited;
    - Resident in Italy;
    - Provides director and consultancy services under one service agreement;
    - Consultancy services are all performed in Italy; and
    - Is not on the UK payroll
  - Ginola – Director of the French Company as well as Toon Limited
    - Paid by the French Company;
    - Resident in France;
    - Not on the UK payroll; and
    - Attends UK Board meetings in their role as a director of Toon Limited
- In the 2023/24 tax year there were four board meetings
  - Each lasted a day (and for the non-resident directors required no preparation or follow up, this assumption has been made to simplify the example);
  - All were held at the company premises in Newcastle;
  - All directors attended the meetings;

- The travel costs for Cole, MacDonald and Ginola were met by Toon Limited;
- All directors stayed overnight and had dinner in Newcastle the night before each meeting and settled the bill using the company credit card.
- No other subsistence costs were met.
- The non-resident directors travelled back to their home countries either immediately after the Board meeting or the following day.

Points to consider

1. Payroll – tax

a. Keegan, Shearer and Cole

They have been correctly included on the UK payroll and PAYE tax is being deducted from their salary/fees. Although Cole is not resident, the only service they provide is in respect of director duties. As a result they will not be eligible for a Short Term Business Visitors Agreement as they are legally employed by a UK resident employer and economically employed by that entity.
https://www.gov.uk/hmrc-internal-manuals/paye-manual/paye82000

b. MacDonald

They should be on the UK payroll and the amount attributable to the director duties performed in the UK should be subject to PAYE (tax). As some of the duties are performed overseas HMRC may agree to an apportionment of the fees paid, such that only those attributable to UK duties are subject to UK PAYE (tax). A request needs to be made to HMRC for a S690 ITEPA 2003 determination for an estimated apportionment to be applied, based on the percentage of time spent performing duties in the UK. Once agreement has been received from HMRC the estimated proportion should be subjected to UK PAYE (tax). https://www.gov.uk/hmrc-internal-manuals/paye-manual/paye81545

c. Ginola

Although they are not paid by the UK company, they are a director of the company and PAYE (tax) should be accounted for in relation to the proportion of their salary attributable to the director duties performed in the UK.
https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim40110
https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim77020

2. Payroll – NI

a. Keegan and Shearer

They have been correctly included on the UK payroll and PAYE NI is being accounted for in relation to their salary.

b. Cole, MacDonald and Ginola

Toon Limited should initially consider the European Council regulation covering the European Economic Area or Reciprocal Agreements. If after considering those there is a liability to UK NI, Toon Limited should then consider whether the administrative NI concession for non-resident directors applies.

As the directors are not resident in the UK and there are only four board meetings in 2023/24, they should be eligible for the non-resident directors concession, but only after considering the European Council Regulation covering the EEA

or reciprocal agreements with other countries first.
https://www.gov.uk/hmrc-internal-manuals/national-insurance-manual/nim12013

There will be no liability to Class 1 NI on earnings received if the director only attends board meeting in Great Britain and Ireland and:

- They attend a maximum of ten board meetings in a tax year; and
- Each visits lasts no more than two nights at a time; or
- If the director only attends one board meeting in a tax year, the visit lasts no more than two weeks.

3. Travel, accommodation and subsistence costs in relation to board meeting attendance.

HMRC will regard Newcastle as the directors' permanent workplace as all the board meetings are held there. This view is confirmed in their travel and subsistence guidance, Booklet 490 paragraph 3.12.
https://www.gov.uk/guidance/ordinary-commuting-and-private-travel-490-chapter-3#non-executive-directors

a. Travel costs of journeys to / from board meetings

Toon Limited is meeting the travel costs of the NR Directors, however they may not be taxable. Tax relief may be available under S373 to 375 ITEPA 2003. This applies in relation to travelling expenses for employees working, but not domiciled in the UK. Under this legislation, the travel costs from the country outside the UK in which the employee normally lives to any place in the UK where duties are performed, and the return journeys will not be taxable.

The rules are complex, and the following conditions must be met:

- The employee who is not domiciled in the UK:
- Receives earnings from an employment for duties performed in the UK; and
- An amount is included in the earnings in respect of the provision of travel facilities for a journey made by the employee or the reimbursement of expenses incurred by the employee on such a journey.
- The earnings are charged on receipt (the relief is not available against earnings charged on a remittance basis); and
- The journey ends within five years of the employees qualifying arrival in the UK.

There is no limit to the number of journeys that can be made, but an adjustment may be made if there is a dual purpose which would result in some of the cost being taxable.
https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim35030

The exemption only applies for journeys undertaken within a period of five years beginning with a date that is a qualifying arrival date. The arrival date is the date on which a person arrives in the UK to perform duties of an employment from which they receive earnings for the duties performed in the UK and either:

- They have not been in the UK for any purpose during the period of two years ending the day before that date; or
- They were not resident in the UK in either of the two years preceding the tax year in which that date falls.

Although the conditions may appear very challenging, HMRC confirm in their guidance that for the second bullet an employee who does not become resident in the UK in the tax year in which they come to perform their duties in the UK may have a qualifying arrival date in each year they come.
https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim35060

As far as NI is concerned, if the travel costs are eligible for the relief under S373 to S375 ITEPA there should be no NI due

either; Para 5 Part VIII Social Security Regulations 2001.
https://www.gov.uk/hmrc-internal-manuals/national-insurance-manual/nim06410

b. Accommodation and dinner the night before each board meeting

These costs will be taxable in relation to all attendees. However, there may be no NI for the NR Directors if they have a certificate of continuing liability for National Insurance to be disapplied (also known as a “Certificate Of Coverage” or a PDA1). The Certificate of Coverage, from their home country, demonstrates that they are paying Social Security contributions in a jurisdiction other than the UK and exempts them from UK NI.

c. PSA or P11D

HMRC may be prepared to allow Toon Limited to include any taxable and NIable director travel and subsistence costs on a PAYE Settlement Agreement. If they do not, then P11Ds will be required. Class 1A NI will be due on the taxable benefits for directors who do not have a Certificate of Coverage.

Summary

The tax and NI treatment of non-resident directors can be very complicated. Employers should be aware of the make up of the Board, how they are remunerated, and the costs met in relation to attendance at Board meetings. They should then ensure the correct tax and NI treatment is adopted. As HMRC will have access to any information on directors via Companies House data, they are very able to ascertain very quickly via RTI submissions whether an employer has complied with their PAYE and NI obligations.

Lee Muter

Lee joined UNW in June 2010 as Employment Taxes Partner, immediately following a period leading the Human Capital team in the Newcastle and Scotland region for a Big 4 employer. A tax adviser for over 30 years, Lee is an experienced speaker and active locally from being involved in chairing a workshop on Employment Tax issues for the North East Branch of the CIOT, to providing innovative and entertaining seminars to clients and contacts. He also provides all UNW clients – large or small – with commercial, practical, and clear advice on all areas of employment taxes including salary sacrifice schemes (pensions and cars), Construction Industry Scheme, termination payment issues, off payroll workers (including IR35), HMRC employer compliance reviews, CJRS, NMW issues and employer expenses and benefits processes.

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Paul Tucker

Paul is part of UNW's Employment Tax team. He has extensive experience, having spent over 40 years working in tax, and advises clients on all aspects of employment tax and national insurance, providing practical and technical support. As well as being a Chartered Tax Adviser he is also a Vice Chair of the Chartered Institute of Taxation's Employment Taxes Committee.

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Termination Payments: the uncertainty of gaining certainty – HMRC changes to obtaining clearance

Sarah Hewson considers the challenges in obtaining certainty around termination payments.

The employment tax treatment of termination payments is often complex (more so following the introduction of the post-employment notice pay rules from 6 April 2018), with HMRC expecting each element of any termination payment to be separately considered to ensure the correct income tax and National Insurance ("NI") treatment is applied.

Whilst HMRC's guidance is comprehensive (https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim12800) the complexity of the rules, as well as understanding and assessing whether the conditions for various concessions and exemptions have been met, often leaves employers unsure of how to treat various items for income tax and NI purposes. For this reason, until recently HMRC committed to giving a binding answer relating to queries on certain termination cases, including those involving the disability and injury compensation exception, the foreign service exception and/or non-cash provisions (EIM12817). HMRC also previously committed to explaining how certain Statements of Practice and Extra Statutory Concessions operated in the context of a termination case (EIM12825).

However, in the February 2024 Employer Bulletin (https://www.gov.uk/government/publications/employer-bulletin-february-2024/february-2024-issue-of-the-employer-bulletin#termination-payments) HMRC announced that, as part of "*aligning its approach to the provision of advanced assurance on certain termination payment enquiries*", it will no longer give a binding answer on these cases and will instead now only issue guidance via the Non-statutory Clearance Service ("NCS") (https://www.gov.uk/guidance/non-statutory-clearance-service-guidance). HMRC's guidance, particularly EIM12820 (https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim12820), has been updated to reflect this change.

Aside from the fact any view given by HMRC will now only be guidance rather than a binding view, written advice via the NCS will only be given where certain criteria are met (albeit HMRC state in EIM12820 that it will "*not seek to retroactively impose any different result provided that an enquirer has acted in good faith and supplied all the necessary information*"). This includes the requirement for the person seeking clearance (e.g. an employer) to have fully read the relevant guidance or contacted the relevant helpline, to not have been able to find the information and genuinely be uncertain about how the legislation applies to their circumstances. As a result, if HMRC considers that the legislation and guidance are sufficiently clear, it is likely that any application made via the NCS will be unsuccessful.

Whilst not overtly stated, the suggestion is that the above changes have been made to streamline the process and reduce the resources needed by HMRC to provide such clearances. Whilst HMRC's resource constraints are well documented, this change is unlikely to be welcome news for employers, who often need to assess complex scenarios at pace to ensure the position can be properly documented (e.g. in a Settlement Agreement) and relevant amounts processed via the payroll on or before the date of payment.

It is not yet clear how long it may take HMRC to issue guidance under the NCS and in what circumstances an application may not be successful (albeit HMRC say this should usually be within 28 days unless the circumstances are complex). Given the limited timescales applying to many termination cases, there is a real risk that HMRC's view will not be issued ahead of the relevant payroll cut off date. Further, if an application is not successful but HMRC does not clearly state that they consider relevant conditions have not been met, this may leave employers in a difficult position. This is particularly topical given that, in the run up to this change, I understand there were a number of instances where HMRC considered the relevant payments did not fall into the disability and injury exception, which appears to reflect a narrower approach than they have taken hitherto.

Given the value of certain termination payments (particularly those in relation to injury and/or disability), if employers get the income tax/NI treatment wrong, this could lead to substantial liabilities (which an employer may be unable to collect from former employees), plus penalties and/or interest for employers. I envisage a number of circumstances where employers will need to take a view ahead of any payroll cut off date and manage this with the relevant (former) employee, and in this respect employers may be more likely to be cautious and subject amounts to income tax and/or NI via the payroll if there is any doubt on the matter.

All in all, whilst on the surface HMRC's change of approach on termination payments/clearances may seem fairly innocuous, employers should reflect on how they deal with more complex scenarios and where in any doubt seek professional advice with a view to ensuring the appropriate amounts of income tax and/or NI (if any) are withheld from the relevant payments.

Sarah Hewson

Having previously practised as a tax lawyer at an international law firm, Sarah moved away from law to specialise in employment taxes and is currently the UK Employment Tax Technical Lead at Vialto Partners. As well as feeding into technical tax consultations and policies, Sarah utilises her broad range of skills to advise clients on key employment tax related issues. Sarah has an active role in the CIOT/ATT, sitting on CIOT Council and various committees, including the Employment Tax Technical Committee, as well as being Chair of Membership & Branches. Sarah can be contacted at sarah.hewson@vialto.com.

Consultations and Submissions

CIOT Employment Taxes Committee – Public submissions - March 2023 to March 2024

Off-payroll working: calculation of PAYE liability in cases of non-compliance	20 June 2023
Construction Industry Scheme reform (Joint CIOT submission with Property Taxes Committee and Indirect Taxes Committee)	19 July 2023
Non-Discretionary Tax-Advantaged Share Schemes	29 August 2023
Tackling non-compliance in the umbrella company market	5 September 2023
Change to data HMRC collects from customers (Joint CIOT submission with Owner Managed Business Committee and Management of Taxes Committee)	12 September 2023
Abolishing the pensions lifetime allowance	15 September 2023
Taxation of Employee Ownership Trusts and Employee Benefit Trusts (Joint CIOT submission with Employee Ownership Trusts Working Group and Owner Managed Business Committee)	27 September 2023
House of Lords Economic Affairs Committee Finance Bill Sub-Committee - Draft Finance Bill 2023-24 (Joint CIOT submission with other Committees)	5 October 2023

Draft regulations: proposed amendments in respect of salary advances	6 October 2023
Occupational Health: Working Better	17 October 2023
Construction Industry Scheme (CIS) proposed amendments	8 January 2024
Calculating PAYE liabilities in cases of non-compliance for off-payroll working (IR35)	22 February 2024

Suggestions?

If you have any suggestions for further articles, please let us know:
technical@ciot.org.uk

To contact the Employment Taxes Committee Technical Officer, Matthew Brown, please email: mbrown@ciot.org.uk

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