TaxTalk

Simplifying the complexities of Tax

June 2023

PKF

pkf-l.com

TaxTalk: June 2023

Personal Tax

Overseas relief: how to make the most of it 2

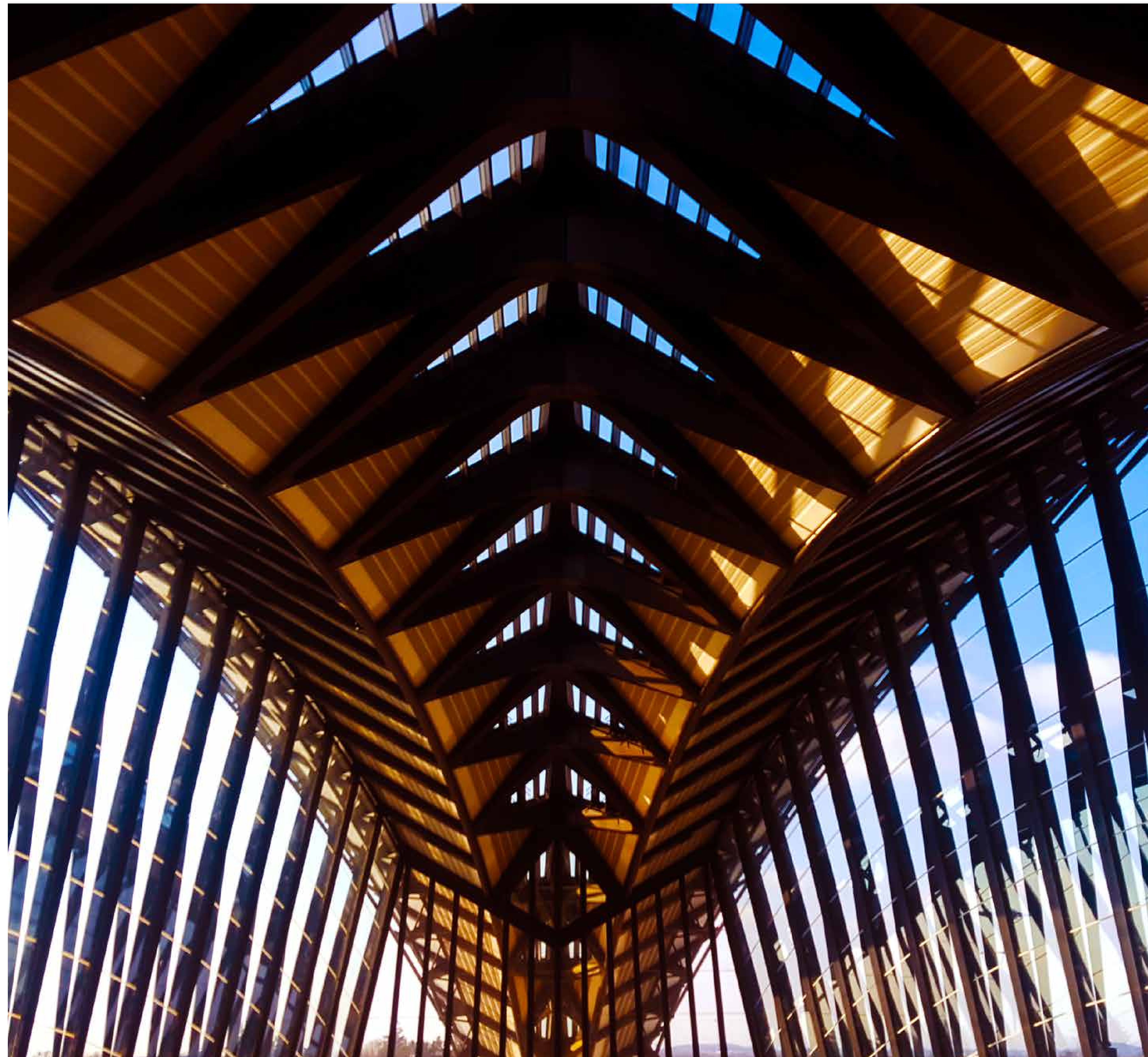
Personal Tax

Mixed membership partnerships: beware the complex rules 4

Employment Tax

Company cars: back with a difference 7

About PKF 10



Overseas relief: how to make the most of it

Whether you are a famous sports star or just someone who works abroad a lot, you could save large sums with this relief if you qualify.

Overseas Workday Relief (OWR) gives certain individuals an opportunity to keep earnings related to work completed in a country other than the UK outside the scope of UK taxes. It's not available to everyone, but for certain non-UK domiciled people it can be quite lucrative.

To qualify for OWR you must:

- be a non-UK domiciled individual throughout the year
- be a UK tax resident following three consecutive years of non-UK residence
- elect to be taxed on the remittance basis
- have a UK employment where your duties are performed wholly or partly outside the UK
- have the proportion of your non-UK duties paid into an offshore qualifying bank account.

If you qualify for OWR, you can claim it for the first three tax years (including split-years) of UK tax residency. But the funds that are not liable to UK taxes must remain outside the UK and would be liable to UK taxes if remitted to the UK in that year, or a future year.

So OWR can give individuals who work outside the UK, for a UK employer, an opportunity to treat those specific earnings as foreign income not liable to UK taxes. This reduces tax liability and means they can receive a repayment of PAYE taxes if they've already been charged.

When claiming OWR it's essential to have accurate records to support the claim, as HMRC may ask for evidence of these. It can be a complicated area, so we would suggest taking professional advice and planning accordingly.

Take a famous footballer

In sport, we see this a lot with athletes moving to the UK for potentially short-term contracts, or for the first few years of their longer-term contracts.

Early this year Chelsea broke the record of the most expensive Premier League transfer of all time, taking Enzo Fernandez from Benfica for £106.8m.

It's understood he is earning around £315,000 per week. That's a staggering £16m per year. With the highest rate of income tax at 45%, you could estimate his UK income tax liability at over £7m.

Overseas relief: how to make the most of it

Assuming Fernandez qualifies for OWR in the current UK tax year (2023/24), it wouldn't be unrealistic to assume his non-UK related workdays could be around 15+%. If that's the case, claiming OWR could reduce his liability by around £1m.

What is a sporting workday?

But when it comes to sport, identifying a 'workday' might not be as simple as for those of us who are more office based. The standard definition for a workday, per the Statutory Residence Test (UK Tax Residency Guide), is a day in which you have completed three hours or more of work.

For sporting individuals, they are instead split into 'performance days' or 'training days'.
A performance day would mean taking part in a competition or being involved in public events.
A training day is considered as any day where you spend three hours or more in physical activity, which should contribute towards the performance of your sport. This could include practising your sport, or maintaining general fitness for your sport.

So a performance day for Fernandez would be playing a match, be that for Chelsea, Argentina, or any other team. And his training days could be general training and specific training camps, but also some of his days during 'winter break' if he was maintaining general fitness.

With Chelsea planning to return to the USA this summer for training and games, along with the various matches in Europe over recent years, it can be quite lucrative for players like Fernandez to consider available tax claims and planning opportunities in their first few years in the UK.

Is it an offside offence?

Although it may not stand up in the court of popular opinion, OWR can be sensible tax planning for international individuals coming to the UK. It can help to reduce UK tax exposure where the salary funds may not specifically be needed while in the UK and can be used in the future after their departure.

But OWR can be challenging when the employer, or club, will not pay a salary into an offshore bank account. Or when the individual will need access to the funds in the UK now, or in the future.

If you would like advice on any of the issues raised in this article, please contact Phil Clayton.

Phil Clayton
Senior Manager

+44 (0)20 7516 2412
pclayton@pkf-l.com

Mixed membership partnerships: beware the complex rules

We look at the pros and cons of having a corporate partner in the mix, and the additional care needed for their tax reporting.

Mixed membership partnerships are subject to wide-ranging rules that allow HMRC re-allocate excess profit from the corporate partner to the individual partners for tax purposes.

So why have a corporate member in the partnership? One obvious reason is that the rates chargeable to tax for corporate and non-corporate members are very different. The Corporation Tax (CT) rate is currently 25% for companies with a profit over £250,000 (up from 19% in April), but is still only 19% for those with a lower profit. The rate is still very low compared to Income Tax (IT) applicable to individual partners, which starts at 20% but can be as high as 45%. What's more, individuals with trade income will be hit by Class 4 National Insurance, currently at the rate of 9% for income between £12,570 to £50,270 and 2% on the excess.

Another advantage of a hybrid structure is that it provides more flexibility on how individuals are remunerated and on the timing of extraction of profit from the company. This means more tax planning opportunities for minimising liability.

What are the tax planning opportunities?

Tax planning opportunities are available by deferring the payment of tax. This is a particular benefit where there's a need to retain cash in the corporate entity and delay the timing of its extraction from the business. Unlike an individual partner being taxed on their share of partnership profit, irrespective of whether or not it has been withdrawn from the partnership, the employees or the shareholders of the corporate entity will be charged to tax only on the eventual extraction of the company profit.

Comparison example

Tax on profit: individual vs corporate member (using current tax rates and assuming all the individual members are higher rate taxpayers).

Mixed Partnership		
Tax on	individual partner £	corporate partner £
Tax adjustmented profit	100,000	100,000
Income Tax at 40%	(40,000)	
Class 4 NIC at 2%	(2,000)	
Corporation Tax at 19%		(19,000)
Profit after tax	58,000	81,000
Effective rate of tax	42%	19%

So, there's definitely a cash flow advantage in having a corporate member and retaining the partnership profit by deferring payment of tax. This is important where cash is required for funding working capital or future capital injections to the LLP. But note that there will be a further charge to tax on the eventual extraction of profits.

Mixed membership partnership rules: when do they apply?

So, what are these rules about? The legislation was introduced on 6 April 2014 alongside the salaried member legislation (for more detail on the latter, see the November 2022 edition of Tax Talk).

It is for all UK partnerships, LLPs and foreign entities that are treated as partnerships for UK tax purposes, with 'mixed members' (a combination of individual and corporate members).
This legislation only applies when there are tax-motivated arrangements in place, between individual and corporate members, in allocating profits and losses in such a way that reduces the overall tax on their share of partnership profit.

Mixed membership partnerships: beware the complex rules

Broadly speaking, tax-motivated arrangements are those where partnership profits are allocated to a corporate partner in circumstances when the individual member receives the benefit from the allocation.

Not surprisingly, the rules are not restricted to profit-making partnerships. In a loss-making year of a partnership, the tax-motivated arrangement is made so that partnership losses are allocated to the individual partner(s), instead of the corporate member. This enables the individual partner(s) to access the reliefs from the loss allocations.

So it was to prevent this kind of tax avoidance that the mixed membership rules came into force in 2014.

The impact of the mixed partnership rules

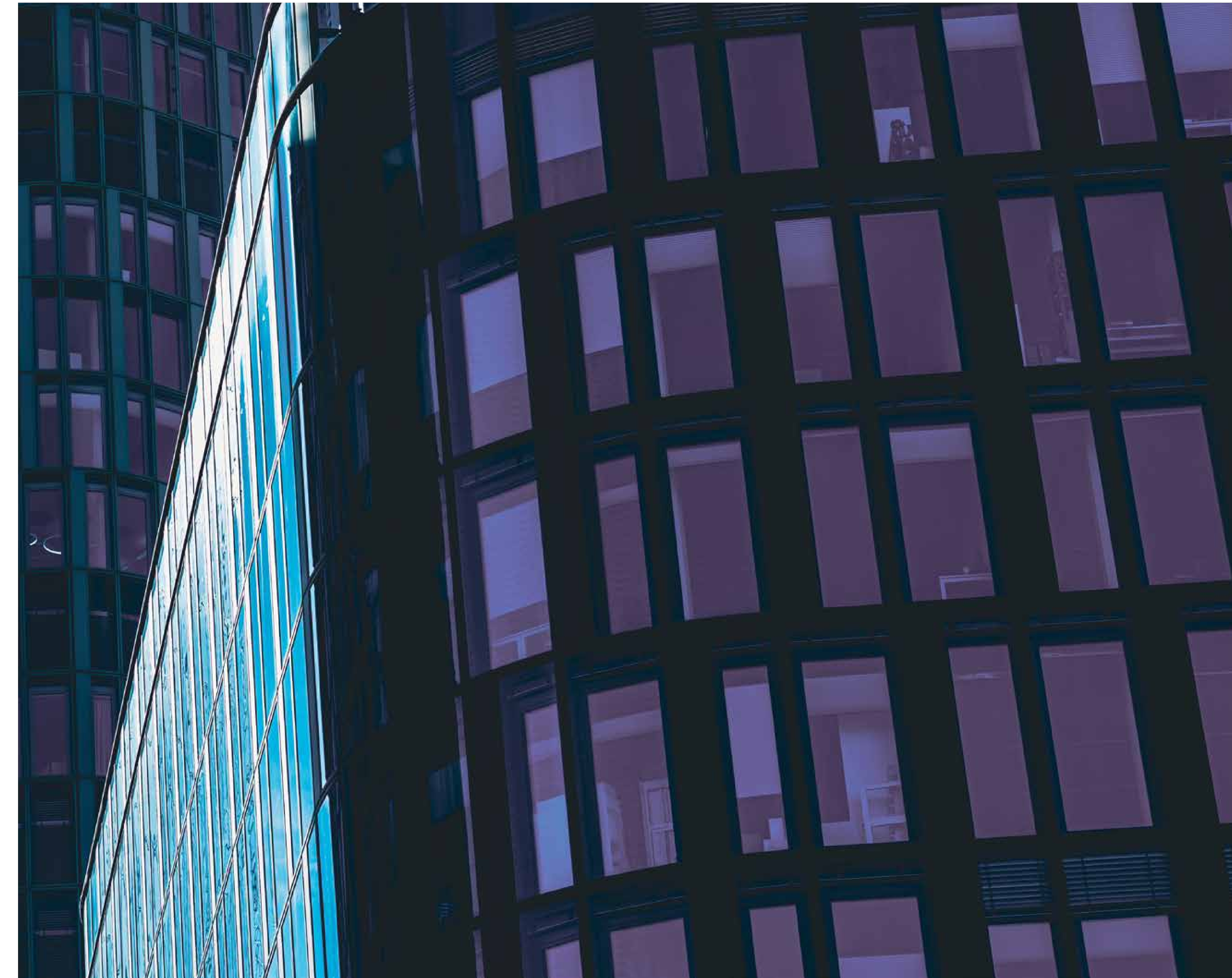
So, what are the implications? In a nutshell the provisions take partnerships back to the original position before any tax-motivated arrangements are made.

The rules affect excess profit allocation. The tax-motivated arrangements made to secure a tax advantage on the partnership profit allocation to the corporate member, above their genuine share of partnership profit acting at arm's length, will have to be reallocated to the individual partners.

As a result, the individual partners will have to pay Income Tax on the reallocated profit from a corporate member.

Equally, the corporate member will recognise a corresponding reduction in their taxable profits, and any distributions made to the company (with the tax-motivated arrangements) are ignored for tax purposes.

The overall tax impact from this excess profit allocation is that the rate of tax on a corporate member's profits that were originally allocated, and are now to be reallocated to an individual member, will be more than double: from as little as 19% for the corporate member to as high as 47% for the individual member.



Mixed membership partnerships: beware the complex rules

How to report mixed membership partnership taxable profit/(loss) calculations

In a mixed membership partnership, two computations of taxable profits must be carried out. One under the IT rules relating to individuals, and the second under CT rules relating to the corporate partner. This means there will also be two reportings of the partnership results, calculated using both IT and CT rules. The individual member taxable income is calculated under IT rules, and the corporate member's income under CT rules.

What next for partnerships?

Mixed membership partnership tax reporting is not an easy area of law and has become a key focus for HMRC. HMRC has been sending more communications to partnerships regarding their compliance with the Mixed Members rules in recent years. The objective of the rules may well be to tackle tax avoidance, but even commercially minded taxpayers now bear the brunt of the rules' complexity.

It's increasingly important for taxpayers involved in mixed membership partnerships to invest more time in identifying and documenting the evidence to demonstrate their calculations and profit share entitlements from the partnership. Above all, care should be taken to ensure that profits allocated to the corporate partner are commercially justifiable.

The information in this article is intended for general guidance only. It should not be regarded as comprehensive for decision-making purpose. If you would like advice or further information on any of the above, please contact Tilak Lamsal or Stephen Kenny.

Stephen Kenny
Partner

+44 (0)20 7516 2200
skenny@pkf-l.com

Tilak Lamsal
Assistant Manager

+44 (0)20 7516 2364
tlamsal@pkf-l.com

Company cars: back with a difference

Electric company cars can save employees and employers tax and NICs, but how does a salary sacrifice arrangement work?

Company cars are here again. The once favourite benefit for employees, typically middle managers and above, had slowly been declining in popularity since 2017. Why was this? Most likely because of the introduction of optional remuneration legislation, increasing scale rates, and changes to the way a car's CO2 emissions are measured.

But now that electric cars are becoming more viable for day-to-day use and there are favourable tax rules for pure electric and some hybrid cars, the company car is back in fashion. Many companies are introducing them as an optional employee benefit.

The cost to the employer of providing this benefit is low, as leasing costs are often funded entirely by employees through a salary sacrifice arrangement.

Company car tax

Unlike most employee benefits the value of this benefit (for Income Tax purposes), in providing a company car to an employee, is not the cost to the employer. Instead, the annual benefit is calculated based on the list price of the car (plus any extras) and the 'scale rate' %, based on the CO2 emissions of the vehicle.

The scale rates applicable to company cars have been steadily increasing for almost a decade. A car that in 2016/17 had a scale rate of 15%, would today have a rate of 37% applied to its list price. Although other factors have also contributed to the downfall of the company car, the rise in scale rates is by far the main cause. Petrol and diesel company cars simply stopped being a worthwhile benefit for employees. They would have to pay more in tax over the three-year life of the car than they would if they took a cash alternative.

Let's look at a simple example for the 2022/23 tax year of a company car provided to an employee. It uses petrol and has a CO2 emissions of 144g/km.

List price of car	£35,000
Scale rate per HMRC guidance	33%
Annual benefit value	£11,550

If the employee is a 40% taxpayer, Income Tax of £4,620 is payable and the company will incur £1,593 in Class 1A NICs (this ignores the one-off rate of Class 1A NICs applicable for 22/23).

Company cars: back with a difference

The impact of the electric car

If we go back just five years, most electric cars had a very limited range and were not seen as a viable option for everyday use.

The public's perception of electric cars is changing fast. There have been rapid advances in electric car technology, specifically the ability of the battery to provide enough charge to travel more realistic distances. What's more, the Government's well publicised intention to ban the production of all new petrol and diesel cars by 2030 has influenced people's thinking. Many people would now consider the option of an electric car when they come to change their current vehicle.

The problem, however, is that a petrol or diesel car can be much less expensive than the equivalent electric model to buy outright through the retail market. So huge is the difference in price, in fact, that it is rare for someone to buy an electric car retail. Why spend an extra £20,000 on a car that will do 400 miles less on a single charge than its petrol equivalent and has the added challenge of finding or purchasing a charging point?

So if people aren't purchasing electric cars, why are we seeing so many on the roads?

The number of electric cars on the roads has been steadily increasing in recent years. But almost all electric cars are provided, in one form or another, as a company car.

The primary reason for this is because the tax on the provision of an electric company car (in stark contrast to petrol and diesel cars) has been exceptionally low since 2021/22. So low (1- 5%) that there is a significant tax saving for employees where they contribute towards the cost of leasing the car.

Let's look at a similar car model to the one used in the example above but assume its list price is £10,000 more. As a fully electric car, it has CO2 emissions of 0g/km (scale rates still apply) and we are calculating the benefit for the 2022/23 tax year.

List price of car	£45,000
Scale rate per HMRC guidance	2%
Annual benefit value	£900

A 40% taxpayer would incur just £360 tax on this benefit, and the employer would pay only £124 in Class 1A NICs.

In a like-for-like comparison, there is a combined saving of £5,729 for the employee and the company in having an electric car versus a petrol one.

Company cars usually come with all services included: servicing, insurance, road tax, breakdown cover, even new tyres are all standard provisions for company car schemes. This low hassle factor of driving a brand new car every three years is what made the company car the favourite benefit it used to be.

With the possibility of actually saving tax, as well as removing the hidden expense of driving a car you own, it's no wonder employees are beating down boardroom doors all over the country demanding their employer introduces a car scheme as soon as possible.

When it comes to the costs of an employee car scheme many companies have adopted the mantra: 'If it is employees who want this benefit, then it is employees who can pay for it'.

Company cars: back with a difference

Salary sacrifice and tax complications

Salary sacrifice is the general term given to arrangements where an employee has the option of being paid an amount in cash, or 'sacrificing' their entitlement to that cash and instead receiving a company provided benefit.

Using a salary sacrifice arrangement, the costs of leasing a vehicle through the Electric Car Scheme are met entirely by the employee and this is key to unlocking the tax saving. Often employers are bearing only minimal costs (for administration) in providing a new car scheme for their employees. Salary sacrifice is not a new concept and most people associate it with generating immediate tax relief and Class 1 NICs savings on employee pension contributions.

It's quite straightforward, right? Just a matter of deducting an amount from an employee's taxable pay and calling it salary sacrifice on the payslip? The short answer is no.

Be warned. Familiarity with salary sacrifice for pension contributions is misleading many companies into thinking that setting up an equivalent arrangement for cars is simple and that they can 'DIY a scheme' without help from tax and legal professionals.

A contractual matter

The key element for a salary sacrifice arrangement to work for tax and NIC purposes is the 'giving up the right to receive cash and, instead, being provided with a benefit'. The rights of an employee (what they will be paid, when they will be paid, what benefits they are entitled to, and so on) are generally a contractual matter.

Any change to what the employee will be paid (especially if it will be less) must effect a change on a contractual level. Simply instructing payroll to process an amount as a deduction from taxable pay does not make the sacrifice valid for tax purposes.

The contractual change is needed because employees are subject to tax on employment income received. Section 18 ITEPA 2003 states that a payment is treated as received at the earlier of: the date the money is paid to the employee or the date on which the employee is entitled to receive it.

Employees can be subject to Income Tax on money they do not receive if they legally had a right to receive the money but it was just agreed (between employee and employer) that they would not be paid.

It is this key point regarding salary sacrifice arrangements that many companies miss, as they assume that simply stating something will be a salary sacrifice is sufficient for tax purposes.

The effect on tax and NICs

There's no doubt the return to popularity of electric company cars will increase the use of salary sacrifice arrangements to generate the very appealing tax savings on offer to employees. For example, an employee can choose either to receive £5,000 in salary as a car allowance or to give up that right in exchange for a zero emissions company car.

Taking the car option means Income Tax (as well as employer Class 1A NICs) is payable on the benefit value of the car.

Taking the cash allowance means Income Tax and NICs are payable on the total allowance at their marginal rate of tax and NI. Using the previous example for a 40% taxpayer the difference is clear to see:

Opting for a zero emissions company car:	
Tax	£360
Class 1A NI	£124
Total	£484

Opting for a £5,000 car allowance:	
Tax	£2,000
Class 1 NICs employee	£100
Class 1 NICs employer	£690
Total	£2,790

Organisations should take advice when introducing a salary sacrifice arrangement to ensure that they implement it correctly and make the necessary contractual change to benefit from tax and NIC savings.

For more information on issues raised in this article, please contact Daniel Kelly.

Daniel Kelly
Senior Manager

+44 (0)20 7516 2461
dkelly@pkf-l.com

About PKF
Simplifying complexity for our clients

PKF is one of the UK's largest and most successful accountancy brands.

We provide a full range of audit, accountancy, tax and advisory services, and are experts at simplifying complexity – we're particularly well-known for working with large, high-profile businesses with challenging issues in fast-moving and highly technical areas.

We are also an active member of PKF Global, an international network of legally independent accounting firms that gives us an on the ground presence in 150 countries around the world.

PKF in the UK

10th largest Tax practice in the UK

£143 million annual fee income

2,035+ UK partners and staff

6th ranked auditor of listed companies in the UK

Our tax services At a glance

"By bringing together the extensive expertise and experience of our tax specialists we can provide a fully rounded service that offers excellent value for money."

We offer comprehensive tax compliance and advisory services to a range of clients, both in the UK and globally, helping them find their way in the increasingly complex world of tax.

We find practical solutions that we use to our clients' advantage. Our team of experts supports individuals, and businesses ranging from start-ups and SMEs to large international groups, both listed and privately owned.

Where understanding of our clients' sector makes the difference, our experts invest their in-depth industry expertise to provide invaluable support and insights.

We offer the following specialist tax services:

Corporate and business taxes

Our Business Tax team will ensure that you are both tax compliant and efficient.

We provide specialist corporate and business tax advice on both a local and international level, which includes senior accounting officer and large business compliance, transaction services, due diligence, R&D tax relief, employer solutions and global mobility. We also support both the personal and business affairs of partnerships and LLPs.

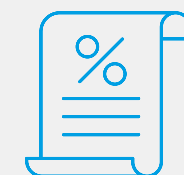
Read more

Personal tax and wealth management

Our team will guide you through the complex world of taxes, helping you meet all filing requirements and identifying risks and opportunities to help mitigate tax liabilities.

We advise individuals, the self-employed, partners, trustees and executors with their UK and international tax affairs. Our services include all aspects of tax, including Self Assessment, Capital Gains Tax, Inheritance Tax, property (both residential and commercial), trusts, family wealth and estate planning, residence and domicile issues.

Read more



VAT and Indirect taxes

Our indirect tax team will support you in meeting your VAT compliance objectives and advise you on any VAT issues that your business faces.

We can ensure that your VAT risk is assessed and managed, and that your VAT recovery is optimised. We can also provide advice and compliance services on other indirect taxes, such as Insurance Premium Tax, Customs duty, and Air Passenger Duty.

Read more

Tax disputes

HMRC is increasing the number and scope of tax investigations into both individuals and businesses, covering all aspects of potential underpayments of tax, including offshore investments, personal and corporate Self Assessment Tax Returns, PAYE and NIC compliance and VAT.

If an issue arises, our trusted advisors will match the right specialists with your needs to provide you the necessary support – whether for a routine HMRC enquiry or a more complex investigation.

Read more

w

This document is prepared as a general guide. No responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication can be accepted by the author or publisher.

PKF Littlejohn LLP, Chartered Accountants. A list of members' names is available at the above address. PKF Littlejohn LLP is a limited liability partnership registered in England and Wales No. 0C342572.

Registered office as above.

PKF Littlejohn LLP is a member firm of the PKF International Limited family of legally independent firms and does not accept any responsibility or liability for the actions or inactions of any individual member or correspondent firm or firms.

PKF International Limited administers a network of legally independent firms which carry on separate business under the PKF Name.

PKF International Limited is not responsible for the acts or omissions of individual member firms of the network.

PKF Littlejohn LLP

www.pkf-l.com

London

15 Westferry Circus,
Canary Wharf,
London E14 4HD

+44 (0)20 7516 2200

Leeds

3rd Floor, One Park Row,
Leeds, Yorkshire,
LS1 5HN

+44 (0)113 244 5141

Manchester

11 York Street,
Manchester,
M2 2AW

+44 (0)161 552 4220