Deloitte Tax LLP
Global Employer Services

GES NewsFlash

United Kingdom – Regular Expatriate Assignments could be Hit by the Draft Legislation on "Disguised Remuneration"

In this issue:

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Summary

On 9 December 2010 the UK Government released draft legislation which it intends to apply to what is referred to as "disguised remuneration". It would be easy for professionals involved in the planning and management of regular expatriate assignments to assume that the draft legislation will not apply to such arrangements. Unfortunately this is not the case.

Where the rules apply, tax will need to be withheld (by the employer or host employer) under the UK's Pay As You Earn (PAYE) system and National Insurance contributions (NICs) accounted for where applicable. The effect can be to accelerate the tax point, increase the total amount of tax due and in some instances create a double charge to tax.

This GES Newsflash highlights some of the ways that the draft legislation could apply to internationally mobile employees even though there is no intention on behalf of the employer or the employee to avoid or artificially defer UK tax or NICs. We are engaging with HMRC to try and ensure such innocent arrangements are carved out.

Overview of the draft legislation

In summary, the draft legislation is targeted at third party arrangements (typically arrangements involving the employer, the employee and a third party such as a trust or pension provider) which the Government believes:

- Avoid, reduce or defer a liability to UK tax or National Insurance contributions, or
- Avoid the restriction in pensions tax relief as a result of the reduction in the annual and/or lifetime allowance.

In order to be caught the arrangement must in some way be concerned with the provision of:

- Reward or recognition in connection with the employee's employment, or
- A loan.

In essence, the draft legislation operates by assuming that anything that meets the criteria outlined above is caught unless it can be excluded under one of a limited number of exclusions. This legislation is intended to take precedence over the benefit in kind tax charges, and unless the legislation is amended some common exemptions may be lost.

The legislation applies with effect from 9 December 2010 to payments, including loans, made by a third party (including a group company other than the employer). Any such payments made before 6 April 2011 will attract PAYE/NIC on 6 April 2012, unless repaid before that date. The employer is liable to account for PAYE/NIC on payments and benefits from third parties.

The draft legislation is very widely drawn and unless substantive amendments are made it will catch a number of innocent arrangements including some that commonly occur when employees are seconded to work abroad or simply work partly in the UK and partly overseas. HMRC is currently consulting on the final scope of the rules and, subject to ministerial approval, commercial arrangements and ones that cause employers significant difficulties may be excluded as long as that does not create avoidance possibilities. There is, though, no assurance that the changes we seek will be made.

The draft legislation provides that a tax charge arises when:

- A sum of money is paid to the employee or an asset is transferred to the employee,
- A sum of money or asset is provided to secure a loan,
- A sum of money or an asset is "earmarked" for the employee,
- An asset is made available for the employee to benefit from as if transferred to him, or
- A loan is advanced.

Do secondment arrangements give rise to third party arrangements?

Because the legislation operates on payments or benefits provided by a "third party" it is vital to know who is the employer where staff are seconded or assigned to another group company. HMRC advise that there is no special meaning of "employer" in this context. Consequently, it appears that a third party arrangement exists where an employee is legally employed by one company but seconded to another company under a typical international secondment arrangement. This means that all employees who are seconded to work for a company in the UK by their non-UK resident employer and all employees who are seconded by their UK employer to work for a company outside of the UK are, in the first instance at least, caught by the disguised remuneration rules in respect of payments or benefits from the host entity.

Loans

In cases where a third party is involved in the provision of a loan, there will be a tax charge on the amount of the loan at the time it is advanced. The loan itself can then be caught under the normal beneficial loan rules such that a deemed interest benefit in kind charge arises. The rules allow no repayment of the tax paid when the loan was advanced, even where it is fully repaid later, a clear case of double taxation.

Host employers or other group companies may make loans to an internationally mobile employee for any number of perfectly legitimate reasons including:

- Tax loans in cases where an employee is liable to tax in both the country where they are working and the country in which they are resident. The loan, made so that the employee can pay the tax due in the host location, will normally be repaid in whole or part after the home country tax return is filed, a credit claimed for the host country taxes paid and repayment of the relevant amount of home country taxes received. Tax loans made since 9 December and not fully repaid by 5 April 2012 are caught.
- To purchase shares under an employee share scheme. Often the loan is repaid when the shares acquired under the share plan are sold.

Issues related to an employee's relocation to or from the UK

There could be a number of issues related to the relocation of employees including where:

- A loan is made to ease cash flow problems on relocation for example in the case of a bridging loan when there is a delay in the sale of property.
- The employer uses a relocation company or some other third party to assist with the relocation of an employee seconded to work abroad. As currently drafted, the £8,000 exemption available under existing rules will be lost unless the draft legislation is amended to include such an exemption.

Deferred compensation plans

HMRC has confirmed that deferred compensation arrangements are within the scope of the new rules. Nevertheless an exclusion is being considered for mandatory deferred compensation arrangements, particularly those where the deferral is required under the UK's FSA Code and possibly extending to those expected to adopt the Code as best practice, albeit there may be no obligation to do so. Mandatory deferrals under similar foreign Codes may also be excluded from the new disguised remuneration rules. However, HMRC has been unable to give clear assurances that non-mandatory deferrals will be excluded. The position for voluntary deferrals or foreign equivalent remains uncertain. These may not be excluded under any exclusion carved out for mandatory deferrals, despite the fact that the deferral may be fully taxable under normal UK tax rules if and when the deferred remuneration is received eventually.

Non-UK pension arrangements

Broadly speaking, non-UK pension arrangements fall into one of two categories:

- Overseas pension schemes that fall within the scope of the recovery charges (the annual allowance charge, the lifetime allowance charge and the unauthorised member payment charges), and
- Non-UK pension schemes that fall outside of the recovery charges.

We expect that all non-UK pension arrangements that are not within the scope of the special pensions tax charges that apply to excessive contributions or distributions will fall within the scope of the disguised remuneration rules. It had been thought that some such schemes would be excluded under the exclusion for "all-employee schemes" but it appears that this will not be the case. It is important for employers to understand the status of any non-UK pension scheme of which employees working in the UK are members.

Deloitte's View

The draft legislation catches more than is necessary to meet the Government's aim of ensuring that certain tax avoidance arrangements are no longer effective. Deloitte is actively working to try and ensure that the final legislation will be more targeted and fairer in its application. However, employers should not assume that any or all of the problems outlined above – and there are plenty of other examples – will be resolved. Employers need to understand the extent of their potential exposure – and that could be on third party payments being made currently - and work with their advisers to determine what, if anything, they can do to minimise the impact of these rules.

People to Contact

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