# Tax Efficient Remuneration 2016

## 1. Introduction

### 1.1 Legislative background

As Sir David Tweedie CA observed when he was President of ICAS, the Lord's Prayer has only 56 words. The US Declaration of Independence has 300. And the European Commission Directive on the Importation of Caramel Products has 26,911.

The Taxes Act defies such a word count especially when Finance Bill 2015 introduced so many changes and the Autumn statement was followed by the publication of draft clauses which will be introduced as Finance Bill 2016. Last year's budget and Autumn Statement have made it clear that this government is committed to tackling tax avoidance and is considering challenges to salary sacrifice arrangements.

In addition to these changes, the tribunals and courts have been busy issuing decisions which can change the law. The Court of Session decision in Rangers Football club and also the decision of the Upper tribunal, delivered by Justice Warren in December 2015, illustrate that this is an area of the law which changes rapidly.

The webinar and this paper have been written using the law in force as at 31 January 2016. Where I consider it relevant, I have summarised some prospective changes which are expected in Finance Bill 2016.

### 1.2 Webinar's objective

My objective today is to extract some nuggets of information, suggesting ways to reward and retain good staff in a tax efficient way. Whilst every care has been taken to ensure the accuracy of the content of this work, no responsibility for loss occasioned to any person acting or refraining from action as a result of the material in this publication can be accepted by the author, editors, publishers or AAT

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Aggressive or egregious tax avoidance can now be challenged by the General anti abuse rules which were enacted in Finance Act 2013. In addition recent decisions have challenged aggressive arrangements which have attempted to convert earnings into dividends. Offshore arrangements also face challenge.

This webinar will examine the considerable opportunities which exist to reward staff in a tax efficient way. It relies on the Tax legislation which is in force as at 31 January 2016.

### 1.3 Importance of detail and planning

In taxation, there is a truism that "It ain't what you do but the way that you do it." Structured properly, it is possible to save substantial tax and NIC but it is an area which is potentially liable to challenge from HMRC.

Tax avoidance is perfectly legal. It is common sense to plan to pay tax ensuring that the cost of compliance is kept to a minimum and that the right tax is paid at the right time. This paper with its accompanying presentation are designed to provide you with some ideas for tax planning and some practical guidance on how to deal with some of the challenges facing tax practitioners and their clients in the coming 12 months. Tax planning must carry a health warning especially if the Government believes it is not within the spirit of the legislation.

The more aggressive the avoidance planned, the more aggressively HMRC can be expected to react. For example, using EBTs may be like a red flag to a bull and the risk assessment score will ratchet upwards considerably. The Court of Session decision delivered in Rangers Football club and summarised at the start of the webinar illustrates that the underlying principle is for tax to be charged on earnings derived from the employment. The interesting decision of the Upper Tribunal delivered in December 2015 on a golden handshake described as a capital receipt for customer relationships illustrates that the Courts are inclined to look through structures and contracts and expand the interpretation of earning from the employment. The decision of R&C v Smith and Williamson and a Mr. Smiley is summarised at Chapter 8.1 below (page 21)

The key is that if an employer plans to avoid tax and NIC legitimately and plan an efficient employee reward scheme, it needs to make sure that every I and t is dotted and crossed. Of course everyone should pay the right tax at the right time. The issue is that HMRC have different expectations of what is acceptable as reasonable care. Tax is complex and a mistake should not be penalised. But any taxpayer practising tax planning should be aware that more care is needed to ensure that the tax return is correct and complete.

HMRC now uses a risk assessment approach but it has also become more commercial. HMRC publish yield and cost ratios and these illustrate that checking employer compliance gives a good yield in return for the HMRC cost. The largest 'source' of revenue to the consolidated fund is the tax collected from employers and the second largest source is employers' collection of NIC.

From April 2009, an enforcement regime will apply penalties in circumstances when an enquiry discloses an error which HMRC contends arose from a failure to take reasonable care. That penalty regime, found in Schedule 24 FA 2007, means that a prompted error arising from a failure to take reasonable care faces a penalty of at least 15% of the tax and NIC omitted as a result of the mistake. In the author's view, there is considerable evidence that HMRC are abusing the penalty legislation and seeking penalties for mistakes which should not be penalised. The problem with such mission creep and maladministration on the part of HMRC is that our appeal system is becoming less accessible to ordinary taxpayers. Cases such as the Ward case and indeed the recent case decided at the FTT for Mr. Akhtur Ali illustrate that HMRC are abusing the penalty regime.

It is important therefore to plan remuneration efficiently ensuring that any risk areas are identified and corrected.

A less obvious but real commercial risk is the public and political attitude to tax avoidance. Watching the Panorama programme on 16 September 2013 which criticised avoidance and those that 'promote' legitimate schemes, it is clear that there is a political and media driven campaign against avoidance which is ill informed and emotive. A business accused of avoiding tax may find itself the target for protestors. The recent controversy over the Google settlement illustrates that the public emotional reaction, even though based on ignorance of UK tax law, can still be adverse.

Finance Bill 2016 will contain legislation to challenge tax avoidance and some of the things which have already been announced include:

- a new criminal offence for tax evasion which will remove the need to prove intent for the most serious cases of failing to declare offshore income and gains;
- new tax geared civil penalties for offshore tax evaders and those who help them. Naming and shaming evaders and their enablers is on the cards
- a new criminal offence for corporates failing to prevent tax evasion. or facilitating tax evasion;
- new measures for serial avoiders (i.e. those who persistently enter into tax avoidance schemes that are defeated by HMRC). Including restrictions on accessing certain tax reliefs.
- a new penalty (of 60%) for cases successfully tackled by the General Anti-Abuse Rule (GAAR) which will be amended so that it targets abusive avoidance better

Salary sacrifice arrangements are under scrutiny and I anticipate legislation coming soon to challenge this practice if tax avoidance is thought to be the motive.

The above list is not exhaustive but it illustrates that those who plan for tax will need to understand where the watershed lies between acceptable tax planning and egregious avoidance.

Draft legislation and an overview of the policy has been published and it provides a taster for Finance Bill 2016 but it is a long read. For example, there are 32 announcements relating just to income tax but for practitioners it should be required reading as we plan for 2016 and onwards.

https://www.gov.uk/government/publications/finance-bill-2016-draft-legislation-overview-documents/overview-of-legislation-in-draft

## 2. Tax Efficient Remuneration

As an employer (or adviser to employers) you need to make sure that the remuneration package offered, both helps to retain your best people and meets their needs in a tax efficient way. The following report seeks to describe some of the more common forms of tax efficient remuneration. The report has been written on the basis of the tax Law which was in force at 31 January 2016 but it has also tried to take into account anything drafted for inclusion in Finance Bill 2016 which might be relevant.

### 2.1. Remuneration Packages

Nowadays most benefits provided to employees attract a tax charge equal to the cost of providing the benefit. Given that cash is the simplest way to remunerate an individual, why therefore are benefits provided? Probably the most common reason for providing benefits is that such provision is widespread in the UK and if other employees are provided with benefits it may be necessary to follow suit to attract the right calibre of staff. Furthermore, an employee may perceive the benefit to be worth more than an equivalent sum in cash even though he will suffer tax on it.

If an employer does decided to provide benefits it will therefore be important to ensure that staff are given the right benefits – those that will attract them to the employer or will motivate them in their work. Unfortunately it is often difficult to decide which benefits to provide. It is also difficult to know whether the cost of the benefit is justifiable in terms of the incentive effect that it will have on staff.

These problems can be minimised by the use of remuneration packages. A remuneration package can be fixed or flexible.

## 2.2 Fixed Packages

A fixed package generally comprises a standard package, the components of which the employer is normally prepared to convert into cash if the employee so desires.

## 2.3 Flexible Packages

With a flexible remuneration package the employer fixes the amount he is prepared to spend to obtain or keep the employee and leaves the employee to decide how much of that he would like as salary and how much as benefits and what benefits he would like provided.

This has a number of advantages e.g. it ensures that the employee realises what it costs to provide the benefit. It may also give the employer a competitive advantage, as some of the benefit he may be prepared to provide, if he is willing to respond positively to the employee's wishes, may not be available to the employee from other prospective employers.

From the employers' perspective there is a balance to be struck between offering a fixed suite of benefits which are easier to administer and the greater complexity and inevitable extra cost of administering a flexible benefits package.

## 2.4 Salary Sacrifice

In essence a salary sacrifice arrangement is a simple arrangement where an employee gives up an amount of his salary in exchange for a benefit, usually one which is tax free. Thus, it is fair to say that the main aim of a sacrifice scheme is to enable the employer and employee to benefit from savings in tax and national insurance. HMRC may take a suspicious view of such schemes, though they state in their guidance:

"*Salary sacrifice is commonly used by employers or employees to take advantage of the exemption of certain benefits from tax or NIC or both. It is important to recognise that employers and employees have* *the right to arrange the terms and conditions of their employment and to enjoy the statutory tax and NIC exemptions on qualifying benefits.*

*Arrangements which are designed to make use of these exemptions should not be regarded as avoidance.*"

It is important to ensure that such a scheme is set up properly to benefit from such a legitimate way of minimising tax and national insurance. This is achieved through varying the employee's terms and conditions of employment relating to pay or entering into a new contract of employment. Care should be taken when structuring salary sacrifice agreements and legal advice should be sought, ensuring that the contractual right to future cash remuneration is given up.

The need for careful structuring was highlighted in the case of *Heaton v Bell*, a case heard at the time when the tax payable on a company car was very low. A reduction in salary was agreed by the employee in exchange for the ability to borrow a car from his employer. As part of the contract the employee had the option available to give up the use of the car in return for the restoration of his salary to its previous level. It was held in the House of Lords that the employee should be taxed on the gross amount of his salary irrespective of whether the option of the car or the full amount of the salary was taken up. Their interpretation of the arrangement was that the benefit of the car was capable of being turned into cash because of the existence of the option of surrendering the benefit. [***Heaton v Bell [1969] 46 TC 211***] Hence the employer needs to ensure that the employee has contractually given up his right to part of their gross pay. PAYE need only be applied to the reduced salary figure in a successfully constructed salary sacrifice scheme.

It should also be borne in mind that, if on a true construction of the varied contractual terms, it can be shown that the employer is merely applying part of their remuneration towards the cost of providing a benefit in kind, such a scheme will fail.

Once an entitlement to income has arisen i.e. the work has been done to earn the salary, it is probably not possible to sacrifice part of the salary. Only future salary can be sacrificed.

HMRC have issued guidance regarding salary sacrifice arrangements and this can be found at: http://www.hmrc.gov.uk/specialist/salary_sacrifice.pdf.

From July 2011, HMRC announced that it would be seeking VAT in respect of the consideration foregone when a salary sacrifice arrangement was started. From January 1 2012, companies will have to pay VAT on non-cash goods and services provided to employees in exchange for some of their salary. In the AstraZeneca decision the ECJ agreed with HMRC, ruling that the salary sacrificed was a supply of services in return for a payment and was therefore subject to VAT. Before the court ruling it was generally assumed that salary sacrifice schemes would not be subject to VAT.

Full details of the implications were announced in briefing 28/11 which can be read at: http://www.hmrc.gov.uk/briefs/vat/brief2811.htm It gives detail if cycle to work, vouchers, childcare vouchers and canteens are provided linked to a salary sacrifice..

The main employee benefits which can be provided using a salary sacrifice arrangement are employee pension, company cars and additional holidays. These are likely to remain available as it is government policy to promote pensions and low emission cars. However, the taxation of company cars has been subject to change and uncertainty as well as political whim. In 2013 it was announced that the 3% diesel surcharge would be abolished from April 2016 but the Autumn statement in 2015 announced that it would continue.

In taxation the law can be changed by decisions of precedent in the Court of Appeal, Court of Session, House of Lords or the Supreme Court. Consequently, it is important to realise that this paper has been written reflecting the legislation in force as at 31 January 2016. The author and AAT cannot be held responsible for persons acting or failing to act as a consequence of information contained within this paper.

## 3. Company Cars

### 3.1 Benefit in Kind

Where a car is made available for an employee's use a taxable benefit arises under ss114 and 120 of ITEPA 2003. The cash equivalent of the benefit of a company car is calculated by applying a percentage to the list price of the car. This percentage is related to the $CO_2$ emissions level of the car and ranges from 5% to 37% in 1% increments for a petrol car. In addition, most diesel cars attract a 3% supplement on petrol percentages. This had been due to be withdrawn from 2016 but the Autumn statement in 2015 confirmed the change in policy and that the diesel supplement would continue until 2021.

You can calculate the benefit in kind on a company car using the table with the link http://www.contracthireandleasing.com/guides/company-car-tax-ratesbenefit-in-kind-bik/

### 3.2 Low Emissions Cars

For 2016/17, the lower threshold (the CO2 emissions figure which sets the 5 per cent rate) will be reduced from 75g/km to 50g/km. Jogging your memories, the lower emission threshold in 2011/12 was dropped from 125g/km to 120g/km. This is of historical relevance as practitioners and taxpayers are expected to be completing tax returns for 2015/16 in the run up to the electronic filing deadline of 31 January 2017. My point is that in tax what was a sensible decision to buy a low emission car can change and the tax bill increase because of political whim. We saw this in the Autumn statement when it was decided to continue the 3% diesel surcharge when it had been announced in 2013 that this surcharge would be withdrawn from 2016/17 onwards.

The lowest appropriate percentages are now for 2016/17 the BIK rate of 7 per cent but assuming there is no change then by 2019/20 the lowest benefit in kind per cent will be 16%.

The fuel benefit multiplier is £22,100 for 2015/16 (SI2014/2896)and historically it has consistently increased. For example, it was £21,700 in 2014/15 when fuel prices were considerably higher than they are currently. At the time of writing in January 2016 fuel prices are as low as £1.009 per litre for both Diesel and Petrol. If, for example, the BIK was 20% , an employee using private fuel would be taxed on £4,402. That buys a great deal of fuel. It is unlikely that company fuel is an efficient benefit in kind. If the average motorist does 8000 miles each year, the average motorist would be better advised to buy the fuel himself (and seek additional salary from the employer).

Electric cars had an incentive of a scale benefit charge for the five years from April 2010 of 0%. For these five years the employee and employer can benefit from a nil scale benefit charge and no Class1A NIC but from April 2015 the scale charge rose to 5%. And as mentioned above it increases each year by 2% until by 2019/2020 it is 16%

### 3.3 Capital Allowances

The 100% first year allowance (FYA) for expenditure on cars with $CO_2$ emissions not exceeding 120 g/km was due to end on 31 March 2008.. Cars with $CO_2$ emissions not exceeding 95g/km will be eligible for a 100%FYA until 31 March 2015 after which the threshold drops to not exceeding 75g/km up to 31 March 2018

Therefore if a company car with a $CO_2$ emissions level of 70 g/km was provided to an employee in 2015/16, not only would the reduced 9% (12% if diesel) level apply in calculating their benefit in kind but the employer could claim a 100% FYA on the price of the car. Currently, and looking forward, a car with an emission level of less than 75g/km will benefit from the FYA and if say 74g/km and a petrol engine will get a 9% car benefit charge. But for 2016/17 this same car will increase to 11% scale benefit charge.

The improvements in low emission levels which have been achieved in recent years are remarkable and demonstrate that tax policy can influence behaviour and manufacturers will adapt to meet customer needs.

Hybrid cars can provide a vehicle with low emissions but as a general rule they are more expensive to buy. The base model for the Toyota Prius has a list price of £21,995 and the tax charge for 2015/16 would be £2859 but that increases for 2016/17 to £3299. As an illustration, if free company fuel were provided, the tax charge would be £1332 for a 40% taxpayer and the break-even point before the free fuel became attractive would require the car to do over 25,500 private miles each year.

## 4. Exceptions to the Benefit-in-kind regime

### 4.1 Childcare Benefits

An employer can provide childcare vouchers of up to £55 per week (£243 per month) to employees free of tax. In order to qualify for tax exemption, the conditions to be satisfied are:

- Vouchers are offered in a scheme that is generally available to all employees or all those at a particular location.
- The recipient employee must have been in receipt of the childcare voucher scheme before the change of law in 2011(see EIM16553 and s35 FA 2011)

- The childcare is carried out by someone who is registered or approved for that purpose.
- The employee has parental responsibility for the child and a person is only a child until the last day of the week which falls 1 September following the child's $15^{th}$ birthday.
- The exemption limit applies to each employee and not to each child and to the tax week or month that childcare vouchers are provided to the employee.

There is no requirement to use the voucher in the week or month that it is provided. As a result, accumulated vouchers may be used to cover periods, for example school holidays, when higher childcare costs arise.

If an employer provides childcare in a nursery or play scheme on their premises or on premises provided jointly with others, no tax liability is due on the benefit to the employees. The employer must be wholly or partly responsible for financing and managing the arrangements and this is a risk that many employers are unwilling to assume. The care must be provided on premises which are not wholly or mainly used as a private house and the facilities must meet all local authority registration requirements.

Depending on the partial exemption position, management expenses fees which bear VAT may have the input tax denied because the supply deemed to occur is exempt.

In August 2013, the Government published a consultation document with proposals to provide tax free child care capped at an annual top up of £1.200 with the government contributing 20p for every 80p of parental contribution.  The proposals are to be phased in from Autumn 2015 and the current employer supported child care incentives are to be phased out.

### 4.2 Training

There is no liability to income tax by virtue of:

- the provision for an employee of work-related training (or any benefit incidental to such training); or
- the payment or reimbursement to or in respect of an employee of:

a) the cost of work-related training or of any benefit incidental to such training; or
b) any costs of a kind specified in ITEPA 2003, s250(2), provided certain conditions are met (s250 (1) ITEPA 2003)

Section 250 (2) specifies the following types of exempt costs:

- costs which are incidental to the employee undertaking the training;
- expenses incurred in connection with an examination or other assessment of what the employee has gained from the training; and
- the cost of obtaining any qualification, registration or award to which the employee becomes or may become entitled to as a result of the training or such an examination or other assessment.

Section 250 (2) would cover expenses such as travelling and subsistence, which itself includes food, drink and temporary living accommodation, only to the extent that such expenditure would either have qualified for relief under sections 336 or 337 ITEPA 2003 or attracted mileage allowance relief if the employee had undertaken the training as one of the duties of his employment and the employee had incurred and paid the expense.

*Perrin v HMRC 2008 SpC 671*

**Point at Issue:**

Whether a trainee accountant training towards his ACCA qualification was entitled to deduct the expense of the courses from his emoluments.

**Facts:**

The good news is that Mr Perrin was successful in his examination but the bad news is that he failed to get a tax deduction.

He was employed by a firm of chartered accountants and his contract of employment with the firm obliged him to incur payments in respect of course fees and reference materials designed to enable him to qualify for ACCA. Mr Perrin made the payments and claimed a tax deduction arguing that they were incurred wholly, exclusively and necessarily in the performance of the duties of his employment and according to the contract of employment. In 2004/2005 he claimed a deduction of £2,492 and in 2005/2006 £2,591.

He was not paid for work at the weekend and some of the courses attended were held on Saturdays. Attendance at other days' courses was at the partners' discretion although once authorised it was mandatory.

**Statutory Background:**

The Tax (Earnings and Pensions) Act 2003 (ITEPA) at Section 336 provides:

(1) The general rule is that a deduction from earnings is allowed for an amount if:

(a) the employee is obliged to incur and pay it as the holder of the employment, and
(b) the amount is incurred wholly, exclusively and necessarily in the performance of the duties of the employment

**Argument:**

In Snowdon v Charnock (2001) STC 152, the point at issue arose over a specialist registrar's trainee costs of psychotherapy sessions to obtain an additional qualification were held by the courts not to be deductible. Distinguishing this, Mr Perrin had to do the training course as an absolute condition of his employment. He was not taking the training course to do them better.

**Decision:**

Based on past decisions, one might have anticipated that this was a clear cut result. However the analysis of the decision makes it clear that it was very close to the watershed and some of the factors which pointed away from the nature of the job requiring the attendance at courses was the fact that some of the courses took place on Saturdays and his contract of employment made it explicit that he was not paid for attendance on Saturdays. In addition, study leave was granted at the discretion of the firm and paid leave to attend courses was discretionary. This led to the conclusion that the nature of Mr Perrin's job did not require the expenditure on the course even though it enabled him to do the job better with consequent benefit to himself and the firm. Even though attendance was required by his contract, the cost of attendance was not incurred in the performance of the duties of his employment. Mr Perrin lost but it would appear he came surprisingly close to success and perhaps being paid for Saturday attendance as well as being obliged to attend courses rather than given discretionary leave would have made the difference.

**Commentary:**

If the firm had paid the costs, it would have been deductible from the firms' profits and it would have qualified under s250 ITEPA 2003 so that there would not have been a tax charge on the employee. Doing it right saves tax and NIC.

*SpC 557 Consultant Psychiatrist v Revenue and Customs Commissioners – [2006] STC (SCD) 653*

**Point at Issue:**

Whether professional training expenses incurred wholly exclusively and necessarily in the performance of the duties of employment and therefore entitled to tax relief as a deduction against employment income.

**Facts:**

The consultant psychiatrist appealed against a closure to an enquiry into her tax return for 2003/04 denying tax relief on professional training costs of £9,118. Throughout 2003/04 the appellant was employed by the NHS Trust as a consultant psychiatrist in psychotherapy under a pre-2003 national consultant contract, part-time. Her job description set out the duties of the post and listed the following:

Essential qualifications – registered medical practitioner with membership or fellowship of the Royal College of Psychiatrists. This was held by the appellant.

Essential training – high training equivalent to CCST in psychodynamic and systematic psychotherapy. This was also held by the appellant.

Desirable training – experience of specialist higher training in psychodynamic or systematic psychotherapy or group psychotherapy.

The deduction was claimed in respect of training in psychodynamic psychotherapy, included under the heading of desirable training in the job description. The NHS Trust was extremely short of funds; as such the appellant incurred the training costs.

In addition to the requirements of the post, as a member of The Royal College of Psychiatrists, the appellant was required to carry out continuing professional development. Their policy for CPD stated that 20 hours of external and 30 hours of internal CPD continued to be the minimum annual requirement for its members. This was in addition to an expected 100 hours of reading or other self directed learning.

In a letter written by the appellant's head of department, it was stated that she was expected to engage in CPD. However, it was also stated that it was normal practice for the holder of this post to undertake the training, as apposed to it being a contractual requirement.

**Decision:**

The Commissioner concluded that the professional training expenses incurred by the employee were not wholly, exclusively and necessarily incurred in the performance of the duties of the employment. As such, tax relief was denied and the appeal dismissed.

The test for deduction of expenses by an employee is narrowly defined and has been interpreted strictly in the past. First the employee must be obliged to incur and pay the expense as a holder of the post, and secondly, it must be incurred "*wholly, exclusively and necessarily in the performance of the duties of the employment*".

Firstly it was held that there was no contractual obligation to incur the expenditure, even though the Commissioner accepted that the appellant may not have been recruited, had she informed her employer that she had no intention of undertaking the training in question. It was also held that she was obliged to pay some part of the expenses as part of her CPD requirements.

Secondly, the Commissioner analysed whether the expenditure was incurred "*in the performance of the duties of the employment*". It was found that the appellant was undertaking further qualification in order to continue to hold the employment, similar to the doctor in Simpson v Tate. In addition, like the psychiatrist in Snowdon, the training, including personal psychotherapy sessions, did not in any way constitute the performance of duties under her contract of employment.

If it was found that the expenditure was incurred 'in the performance of the duties of the employment', it would have been necessary for the Commissioner to consider the wholly, exclusively and necessarily test.

**Commentary:**

With the growing emphasis on meeting CPD requirements, cases such as this are extremely topical. It is of course important to undertake ongoing training to ensure your knowledge is kept up to date, thereby maintaining your professional qualification. However, this case serves to highlight that the narrow conditions of s336 ITEPA 2003 must be met where the employee pays for training.

In the case where work related training is provided by an employer, s250 applies. Here, there is no liability to income tax. Work related training covers training courses designed to improve or reinforce the knowledge and skills of the employee, where this is likely to prove useful in the performance of their duties and training that will serve to better qualify the employee. Had the Trust paid for the training, this would have been exempt from income tax.

**The wider application in tax efficient remuneration.**

"Work-related training" is defined as any training course or other activity which is designed to impart, instil, improve or reinforce any knowledge, skills, or personal qualities which:

- are, or are likely to prove, useful to the employee when performing his/her duties; or
- will qualify or better qualify the employee to undertake the employment, or to participate in charitable or voluntary activities arising through the employment.

The training must relate to the employee's current employment or to a "related employment".

There is no restriction on the way the training can be delivered. Self-tuition packages, computer based training, distance learning, work experience or work placement and informal teach-ins are all acceptable as are more formal classroom based methods. It does not matter whether training is delivered internally or externally, or on a part-time or full-time basis.

All elements of genuine schemes will qualify. There is no need for the Training scheme to be arduous or unpleasant. So work related training schemes could include many things that the individual employee would really appreciate. Some ideas of training which benefit the employer and employee include:

- Where leadership and team skills are appropriate to the employee, participation in activities such as Outward Bound, Raleigh International, or Prince's Trust;
- Work related first aid and health and safety courses;
- Language training in preparation for overseas communication
- Driving lessons if the employee might need to drive on business
- Safe-driver training, taken up by those with a company car or an advanced motorist course including the examination to get the qualification
- Martial arts course leading to qualifications

It is almost inevitable that there is a boundary and that some courses may cross that boundary in part although be within the exemption for work related training in part also. For example, a genuine residential work-related training course is held in a hotel and the attendees remain at the hotel for a golfing weekend paid for by their employer. The costs of travel to and from the hotel and the costs incurred during the course are not taxable but the cost of the golfing weekend is clearly taxable as it is a reward. The costs would be apportioned. If the employer bore the cost of the golfing weekend, that would be reported on the P11D.

In May 2013 it was reported that Iceland had been challenged by HMRC for failing to report a benefit in kind when it sent 800 managers on a course on Customer Service which is provided by Disney Florida. The report suggests that HMRC are seeking a settlement of 2.5 million and HMRC contends that the trip was an assessable benefit in kind. I suspect that this case will come before the tribunal. It is a warning that HMRC believe that there is a watershed and will challenge when HMRC believes that a tax exemption is being abused.

http://www.telegraph.co.uk/finance/newsbysector/retailandconsumer/10090633/Iceland-boss-baulks-at-2.5m-Disney-tax-bill.html

### 4.3 Environmentally friendly transport

The following items are not taxable:

1. Pool cars (s167)
2. Work buses with a seating capacity of nine or more which are used to carry all employees to and from work (s242)
3. General subsidies to public bus services used by employees to travel to work provided the employees pay the same fare as other members of the public (s243)
4. Bicycles and cycling safety equipment made available for employees to get between home and work (s244)

4.3.1 Cycles and cyclists safety equipment

Since 1999/00 no benefit has arisen from the provision of a cycle or cyclists safety equipment, in accordance with the following conditions:

- that the facility is available generally to all employees; and
- the employee uses the cycle or equipment mainly for ‘qualifying journeys’.

4.3.1.1 Free meals and refreshments provided to cyclists on ‘cycle to work’ days

In order to encourage employees to participate in ‘cycle to work’ days, an employer may provide a free meal or refreshments. Under general principles these would be taxable as a benefit in kind. However, regulations exist which exempt them from tax, as long as they are provided on designated "cycle to work" days.

### 4.4 Events

Where a Christmas party or similar annual function takes place, no benefit will arise on expenditure of up to £150 per head per annum. If a number of events are held in a tax year, only those which exceed the annual limit will be liable to tax and Class 1A NIC. Here, strict chronological order does not require to be followed – an employer is able to mix and match to get the best result. If two or more functions are provided in a tax year and the total exceeds £150 but the aggregate of the two or more does not, the cost of those functions is not taxed but that of other functions is.

It is worth mentioning that the full cost per head must be covered by the £150 limit. Where expenditure exceeds this amount the full amount will be taxable.

In determining the cost per head, all costs have to be included such as room hire, entertainers, hire of mini buses etc. The total cost is then divided by the total number of attendees to determine whether the limit is exceeded. Non-attendees may become a problem where the cost of an event is close to the limit, as this could take the average over £150 per attendee rendering the full amount taxable and NIC-able.

### 4.5 Subscriptions

Professional subscriptions with a qualifying professional body are allowable for tax purposes and where these are reimbursed by the employer a dispensation (see Section 6.0 for further details) can be obtained so that it need not be reported on form P11D and the employee does not need to mention it on their tax return. A qualifying professional body is one which has been approved by HMRC or is listed in subsection 2 of s343 ITEPA 2003.

Fees which have been approved will be to a body or society which has one of the following aims:

a) the advancement or spreading of knowledge;
b) the maintenance of standards among the members of a profession;
c) the indemnification or protection of members of a profession.

In addition, the following require to be satisfied:

a) the fee must be payable for registration on a roll which is a condition of the performance of the duties of the office; or
b) the subscription is to a body whose activities are directly relevant to the performance of the duties of the office.

## 4.6 Financial Advice

With the arrival of pensions tax simplification on A-day (1 April 2006), many employees have been concerned at their pension provision. Specialist pension information and advice provided to an employee where this is generally available to all employees and the cost to the employer does not exceed £150 per employee in the relevant tax year is exempt from taxation.

## 4.7 Eye tests and corrective glasses

From 2006/07 onwards, the provision of eye tests and any necessary corrective glasses is exempt. This applies where health and safety legislation requires an employer to provide the above, particularly in relation to an employees' use of Visual Display Use (VDUs). Similarly, the provision of a voucher or credit-token to obtain such tests or glasses is exempt. The condition is that the benefit should be made available to all employees for whom it is meant to be provided.

## 4.8 Relocation Costs

Certain payments made in connection with job-related relocation are exempt. This enables qualifying relocation expenditure up to the limit of £8,000 to be exempted from charge as taxable earnings.

## 4.9 Canteen

The provision of free or subsidised meals in a canteen or on the employer's business premises which are provided to staff generally are exempt from taxation. (s317 ITEPA 2003)

## 4.10 Free Parking

The provision of workplace parking for an employee does not attract a liability to charge under the benefits code, nor does any liability to income tax arise. Workplace parking is defined as a parking space for a car, cycle or motor cycle at or near the employee's workplace.

There is no definition within the legislation of 'at or near', however HMRC do not tend to adopt a rigid approach in this area. The exemption will apply in any case where parking facilities can be said to be within a reasonable distance from the place of work, having regard to the nature of the locality. It will therefore not be denied simply because there is a car park nearer to the place of work.

## 4.11 Beneficial Loans

An employee may be offered a loan from his employer. Such an arrangement is commonly used in the provision of season tickets, though may be made available for any reason. These loans can be made interest free or at a reduced rate of interest and if the total balance outstanding on all loans does not exceed £5,000 up to 2014 and is now £10,000 then no taxable benefit will arise. It should be borne in mind that accrued interest is taken into account, though it is not added to the balance of a loan outstanding until the interest falls due for payment.

The official rate of interest is currently 3.25%

## 4.12 Mobile Phones

From 6 April 2006, the provision of one mobile phone to an employee is exempt. The exemption now specifically covers line rental and calls. In addition, the provision of a voucher or credit-token to obtain the use of a phone is exempt if the direct provision of a phone would have been exempt.

Prior to this there was no limit on the number of phones allowed and the provision of a mobile was to an employee or to his family or household. If a second phone is in existence and this was provided prior to 6 April 2006, the pre-2006/07 exemption continues to have effect.

In 2012 HMRC confirmed that smart phones were accepted to be phones and within the exemption.

## 4.13 Computer Equipment

Up to 2006/07 there was a limited exemption where the benefit consisted of the provision of computer equipment which was made available (without any transfer of property in it) to a higher paid employee or member of his family or household. This includes equipment such as printers, scanners, modems, discs and other peripheral devices.

The exemption applied only to the first £500 of the cash equivalent of the benefit made available in aggregate to an employee and members of his family or household. (s 320 (5) ITEPA 2003)

There was no requirement that the computer had to be used even partly for business purposes. The idea was to encourage computer literacy generally. However, where computer equipment or software was used solely for business it could be excluded in calculating the £500 figure.

The exemption was repealed by FA 2006 s61 except in relation to computer equipment which was first made available to the individual concerned before 6 April 2006. The Minister has given assurance that the repeal does not change the position where an employer provides the use of computer equipment solely for work purposes and private use by the employee is not significant.

## 4.14 Long service awards

For 2003/04 onwards, extra statutory concession (A22) has been replaced by a statutory exemption in Section 323 ITEPA 2003. The conditions for exemption are as follows:

- the award must be made to mark a period of not less than 20 years service with the same employer; and
- it must be in a form that satisfies the condition in Section 323(3) (broadly, it must be something other than money); and
- the taxable value of the award (before applying the exemption) must not be more than £50 for each year of service.

However, this gives flexibility to ensure that the employee is awarded with an asset which they will appreciate in a tax efficient manner.

Purchasing a flat screen TV worth £999 out of after tax income would cost a higher rate taxpayer £1,693. However, if your employer were willing to offer a long service award and you had worked over 20 years with that same employer then the TV could be given to you free of tax and NIC under s323.

## 5.0 Company Vans

The scale charge for unrestricted private use of a van is £3,150, excluding any private fuel element. If the employer provides free fuel for unrestricted private use there will be an additional charge to tax of £550 in 2012/13 and £564 in 2013/14, £581 in 2014/15 and £594 in 2015/16.. This can still represent a form of tax efficient remuneration especially given the tendency to drive luxury four wheel drive vehicles. There are a number of luxury versions of double cab pick up trucks which would qualify as a company van.

The phrase 'unrestricted private use' is important, as there is no tax charge where an employer makes a van available and this is used by employees mainly for business travel and any private use is insignificant. Home to work travel is disregarded in this context and has been since April 2005. There is no definition of the term insignificant, though HMRC guidance provides the following examples:

- Taking a mattress to the tip
- A slight detour to buy a newspaper
- Calling at a dentist on the way home

To avoid such a benefit it is necessary to take action to restrict private use of the van by, for example sending a memorandum to affected employees, though this in itself may not be enough. It may be necessary to demonstrate how, on an ongoing basis, this restriction is being monitored. Modern technology means that some employers now use vehicle tracking systems and maintain a complete record of all the vehicles' movements. HMRC are known to insist in some cases that a log book is kept so the employer and employee can demonstrate that the vehicle is actually used wholly and/or mainly for business purpose and any private use is negligible.

Guidance is available on the HMRC website at [http://www.hmrc.gov.uk/vans/vans-info.pdf](http://www.hmrc.gov.uk/vans/vans-info.pdf)

## 6.0 Dispensations

Section 65 ITEPA 2003 provides that where HMRC is satisfied that no tax will be payable on particular expense payments or benefits of a director or employee within the benefits code, it can give notice to the person paying or providing them that this is the case. This notice is called a dispensation.

When a dispensation is given all the legislation relating to the particular expenses payments and benefits of the director or employee no longer applies.

In practice HMRC should issue a dispensation where all of the following conditions are satisfied:

- Employees are reimbursed expenses that are deductible within Part 5 ITEPA 2003;
- Claims to expenses are independently checked and authorised;
- Where possible claims are vouched; and
- Where advances of expenses are made, the employer has procedures to ensure they are fully accounted for, and any excess is repaid by the employee.

Employment income manual (EIM) 30057 states that 'payments that are calculated in accordance with a scale intended to do no more than reimburse the expenses incurred by employees can be regarded as equivalent to reimbursement.'

From 2016-17 onwards dispensations have been replaced by an exemption for amounts which would otherwise be deductible. See **EIM30200** onwards. Employers who pay any non-allowable expenses or provide non-exempt benefits will still need to put those through the payroll and deduct tax and NICs, or put them on form P11D as they would now.

Benefits that are only partially exempted will need to be put through the payroll in full and employees will need to claim a deduction on the exempt part.

### 6.1 Scale rate expenses payments

A scale rate payment which is calculated to do no more than reimburse the expenditure incurred by employees on allowable expenses will not be regarded as a round sum allowance. The employer can be authorised to make such payments without deduction of tax under PAYE.

In general, scale rate payments are only appropriate for expenses which are widely incurred, in broadly similar amounts, but for which it is often difficult to get receipts e.g. subsistence, or the expenses of cleaning uniforms or protective clothing.

Subsistence expenses are a commonly reimbursed by means of a scale rate payment. A dispensation can be sought under s65 ITEPA 2003 for the payments you intend to make. In considering such an application HMRC needs to be satisfied that the proposed scale rate payments are set at a level which broadly represents the amount that your employees are actually spending on allowable subsistence expenses. You should therefore be prepared to provide HMRC with evidence of the amount that your employees are spending. Such expenses should ideally be in the form of receipts but other evidence, such as a contemporaneous record of expenses incurred, should also be considered.

For employees travelling outside the United Kingdom, HMRC have produced tables of benchmark rates. These can be found at EIM05290. Accommodation and subsistence payments at or below the published rates will not be liable for income tax or National Insurance Contributions for employees who travel abroad, and employers do not need to include these amounts on P11D forms.

Rates are quoted in the relevant foreign currency and the tables provide:

- A "room rate" per night
- A "subsistence only rate". This figure is intended to cover the total cost of meals in a period of 24 hours, plus the cost of daily travel between the employees hotel and office
- A "24 hour rate". This is the sum of the "room rate" and the "subsistence only rate"
- An "over 10 hour rate", which is intended to cover subsistence expenses for any period of more than 10 hours but less than 24 hours
- An "over 5 hour rate", which is intended to cover subsistence expenses for a period of more than 5 hours but less than 10 hours

The appropriate hour rate is measured by reference to times of arrival at and departure from the foreign country in question.

### 6.2 Revocation

A dispensation continues in force until it is revoked unless a term is placed upon it when it is first given. All dispensations will cease to have effect on 5 April 2016.

Where a dispensation has been revoked and HMRC believes that the employer (or the person making expenses payments or providing benefits) has been negligent in operating a dispensation, or has misrepresented the facts, when applying for a dispensation, HMRC may make the revocation retrospectively to the date the dispensation was granted or wrongly applied.

Furthermore, where the basis on which the expenses payments and benefits were provided has subsequently changed the dispensation can be revoked retrospectively.

## 7.0 Shares and Share Options

### 7.1 Shares

Offering an employee shares as an incentive can be done in a number of ways. However, the tax treatment will depend on how such a transaction takes place. As always 'it's not what you do, it's the way that you do it' that counts.

An employer may simply chose to provide the employee with free shares. In this situation, the employee will pay tax on the shares based on their value at the date of transfer. Where the employee makes a contribution which falls below full market value this will give rise to a benefit on the shortfall.

Alternatively the provision of share options provides a more tax efficient form of remuneration for the employee provided an approved scheme is in place. There are a number of H M Revenue & Customs schemes in existence which provide for preferential tax treatment in return for the imposition of more restrictive conditions. There are currently four HMRC 'tax-advantaged' schemes that provide employees and employers with income tax and National Insurance advantages. These are: -

Schedule 2 Share Incentive Plan (SIP) (ETASSUM20000),

Schedule 3 Save As You Earn (SAYE or Sharesave) (ETASSUM30000),

Schedule 4 Company Share Option Plan (CSOP) (ETASSUM40000), and

Enterprise Management Incentives (EMI) (ETASSUM50000)

Shares acquired under these schemes are generally free from income tax and National Insurance contributions.

The acquisition of shares and securities in connection with an employment other than through one of the above schemes are commonly referred to as 'non tax advantaged' or 'taxed' schemes'. What this means is that neither the employee nor the employer benefit from any income tax or National Insurance advantages.

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### 7.2 Enterprise Management Incentive Scheme (EMI)

EMIs are designed to help small, higher risk companies recruit and retain employees who have the skills to help them grow and succeed. They may also act as a way to reward employees for taking a risk by investing their time and skills to help small companies achieve their potential.

There are limits on shares that an individual may hold under option at any time, including the maximum limit on (unexercised) options which currently stands at £250,000 (increased from £120,000 for option grants on or after 16 June 2012, and previously from £100,000 for option grants on or after 6 April 2008) of a qualifying company, subject to a total share value of £3 million under EMI options to all employees. Budget 2012 announced that, subject to State aid approval, the Government will reform the EMI scheme in Finance Bill 2013 to allow gains made on shares acquired through exercising EMI options on or after 6 April 2012 to be eligible for capital gains tax entrepreneurs' relief.

To research the detail:

http://www.hmrc.gov.uk/shareschemes/emi-new-guidance.htm

This sets out the conditions for Qualifying employees, companies

Tax Advantages of EMI

The grant of the option is tax-free and there will normally be no tax or National Insurance contributions (NICs) for the employee to pay when the option is exercised. There will normally be no NICs charge for the employer.

If the shares are sold at a gain, any capital gains tax (CGT) charge may be reduced by entrepreneur relief

The employer must notify HMRC of an award of EMI options within 92 days of the grant of the option.

### Income Tax and NIC

There is no income tax or National Insurance contributions charged on the grant of a qualifying EMI option.

If an EMI option is exercised within ten years and there has been no disqualifying event, there will be no income tax or National Insurance contributions due, provided that the employee buys the shares at a price at least equal to the market value they had on the day the option was granted. If the option is a replacement option, it must be exercised within ten years of grant of the original option. (S530 Income Tax Earnings and Pensions Act (ITEPA) 2003)

### Where exercise price is less than full market value

If the option enables an employee to buy the shares at less than their market value at the date the option was granted, there will be an income tax charge when he exercises the option. There will also be National Insurance contributions where the shares are readily convertible assets.

The taxable amount is the lower of:

- the amount of the discount, or
- the difference between the market value of the shares at the date of exercise and the amount paid for them.

### Where exercise price is nil

Income tax is charged if the employee does not pay anything for the shares when he exercises the option. The charge is on the market value of the shares at the time the option was granted, or if lower, the market value of the shares at the time the option is exercised.

If the option is exercised after ten years have elapsed then there will be no tax relief when the option is exercised. (s529 ITEPA 2003)

### PAYE and National Insurance Contributions

Where an income tax charge arises upon the exercise of the option and the shares are readily convertible assets, the employer is required to operate PAYE and account for national insurance. (s700 ITEPA 2003)

Broadly speaking, readily convertible assets are shares that can be sold on a recognised stock exchange or for which trading arrangements are in place, or are likely to be put in place, at the time when the shares are acquired. (s702 ITEPA 2003)

### Disqualifying events

A number of changes or developments can disqualify an option from EMI relief. These are called disqualifying events. A disqualifying event restricts tax relief.

The following are disqualifying events:

- loss of independence
- the company no longer meets the trading activities requirement
- the employee is no longer eligible
- changes to the terms of the option
- alteration to the share capital of the company
- a conversion of shares or
- grant of a CSOP option that takes the option holder over the £100,000 limit.

**Other share incentives which can be offered to employees include:**
**Sharesave or Save As You Earn (SAYE)**
**Share Incentive Plan (SIP)**
**Discretionary Schemes**

## 8.0 Golden Hellos – s62 ITEPA 2003

A payment to induce an individual to take up an office or employment is taxable as earnings within s62 ITEPA 2003 if it is a payment from the employment. This payment is usually made by the new employer. However, payments made by third parties will be taxable as earnings if they are paid to induce an individual to become an employee.

In the case of Glantre Engineering Ltd. v Goodhand a lump sum was paid to an accountant, employed by a firm of accountants at the time, to induce him to become one of their directors. The payment was held to be taxable as earnings within s62 because it was an inducement for him to change his job and was referable to the services that he would give in his new post. [***Glantre Engineering Ltd v Goodhand (Inspector of Taxes) [1983] STC 1***]

On the other hand the case of Silva v Charnock it was held that a payment of £18,000 made to a taxpayer was exempt within s250 ITEPA 2003. The money represented a reimbursement of the taxpayer's tuition fees for an MBA and not an inducement to commence employment with the employer in question. [***Silva v Charnock (Insp of Taxes) [2002] STC (SCD) 426***]

This illustrates very clearly that in taxation it is not what you do but the way that you do it which can produce dramatically different results. This is an area where the law continues to evolve.

### 8.1 Payment to new employee for client relationships was earnings

Inland Revenue and Customs v Smith & Williamson Corporate Services Ltd [2015] UKUT 666, the issue was whether a payment received by a Mr. Smiley for his client relationships was a disposal of an asset liable to CGT or earnings from his new employment.

Mr Smiley had a contract of employment with Smith and Williamson Corporate Services (SWGS) and was the team leader, bringing with him his team and clients from his previous employment. In addition to his earning under the contract of employment, he received a payment of £957,296 from a different member of the group and the payment being made under a separate contract which described the payment as being for the team's client relationships and the successful transfer of those relationships to SWGS. Mr Smiley had declared the payment as a capital gain in his 2005/06 return.

Ten years later, he finds himself before the Upper Tribunal having succeeded at the First Tier tribunal. He and his employers must have thought that what they arranged was a tax efficient way to make a golden hello and they had good reasons for so doing.

Tax Planning can be risky and the risk is not merely that you have to pay the tax. In the future, tax planning that goes wrong may carry a penalty if the draft legislation announced for Finance Bill 2016 is enacted (see page 2, ch1.3 above)

The other group company capitalised the Payment in its accounts as expenditure on goodwill.

Crucial to understanding the Judge's reasoning, he observed that Mr Smiley and his team did not have an asset over which they had any right to sell and he also took the view that the separate contracts were an artificial arrangement that failed in its purpose to separate the payment for the client relationship from being a reward from the employment. At paragraph 142 (page58) the judge states:

"The reality is that both contracts reflect the single overarching agreement (whether or not contractually binding in all respects) found in the Covering Letter; there was a single "package" with the details to be determined later, and in fact determined through a process of separate negotiation of the 2006 Contract."

At Paragraph 164 he goes on to conclude: "In my judgment, the evidence establishes that the Payment was a reward to the Team for introducing the Butterfield clients to SWIM and procuring, or assisting in procuring, the transfer of those clients to SWIM. In other words, as Ms Wilson puts it, the Team provided a service. I do not consider that it is right to describe what the Team did as "the transfer of rights to exploit client connections"."

It is SWCS that faces the tax charge under a reg 80 assessment. Beware any employer thinking of making a tax free payment to an employee because the law can change with a decision of precedent. Judge Warren has decided that the payment came from the employment for providing the service of bringing the team client relationships to the new employer and so additional tax and NIC is due. Just as an observation, the difference in tax will not be much but who pays that tax is significant and the NIC difference to the employer's secondary contribution will be substantial.

http://www.bailii.org/uk/cases/UKUT/TCC/2015/666.html

**8.2 Recent developments that expands "from" the employment**

In Manduca v Revenue And Customs [2015] UKUT 262, an investment bonus of £310,000 paid to an investment fund manager was held to be taxable as earning confirming the decision of the First Tier tribunal.

The issue was the tax treatment of a payment of £310,000 received by Mr P. Manduca from Dexia Banque Internationale a Luxembourg ('Dexia') under the terms of an out of court settlement of High Court litigation brought against Dexia by Mr. Manduca who had returned this payment in his self-assessment as subject to capital gains tax. HMRC's decision was that the settlement sum was assessable to income tax under Schedule D Case VI (pursuant to section 18 of the Income and Corporation Taxes Act 1988).

Mr Manduca and Mr de Jerez started working for Dexia on 30 April 2001. Unfortunately, their relationship with Dexia deteriorated for various reasons. There was a delay in the payment of the Bonus. It was not paid until 2 August 2001 with the result that the payment to the two men was delayed. However, on 5 November 2001 (before the payment out to them of the Bonus) Mr Manduca and Mr de Jerez were told that they were going to be made redundant. The One Europe Fund was liquidated on 13 November 2001 and the amount which Dexia had paid in as the Bonus was withdrawn.

Mr. Manduca began legal proceedings but settled with Dexia out of Court. At this point it looks like a strong case for treating the payment as capital but the FTT found as fact that the subsequent documents indicate that the Bonus was intended to be payment for their role in facilitating the transfer of Tilney's fund management business to Dexia and they quoted passages from relevant documents. The Tribunal concluded:

"63. The Tribunal finds on its consideration of the evidence as a whole that the First Investment Bonus was a reward for the part played by the Appellant in enabling Dexia to acquire the OEF business from Tilney. It was not a capital sum. The conclusion of HMRC in this respect was correct. It follows that the "capital v revenue argument" fails."

In other words, the payment was a reward for services and fell to be treated as income. It was not however a reward from the employment so it was assessed under Schedule D case VI.

http://www.bailii.org/uk/cases/UKUT/TCC/2015/262.html

**8.3 Legal background to the tax plan**

In Hochstrasser v Mayes [1960] AC 376, a company scheme for the benefit of certain grades of employee provided for an interest-free loan to the employee for the purchase of a new home on his transfer from one location to another. The scheme also provided compensation for any capital loss suffered as a result of the move. The taxpayer was transferred to another location and in accordance with the scheme received £350 compensation for a loss suffered on the sale of his house. It was held that, although the employment was a causa sine qua non it was not the causa causans of the payment and that the payment did not, therefore, arise from the employment.

At first glance Hose v Warwick 27TC 459 favours SWCS' argument that the payment was capital. Mr Hose was an insurance broker. Up to the end of 1919, he was with a City firm (it is not clear whether he was employed or not). He had worked up a considerable personal connection. Mr Hose was,…. , head-hunted and went to work for a company called Lambert Brothers (Insurance) Ltd ("Lambert"). He entered into Lambert's service in November 1919 bringing with him what the directors described as his business connection, that is to say, as the Judge put it, bringing his personal connection with him.

He was to receive (under oral agreements with no fixed duration) a fixed salary of £750 pa and a half share of the commissions earned by the connections which he brought with him. He was also a director of the company but devoted all his time to his connections. The connection remained personal to him and he could have taken it with him if he had left the company's service. It seems that he was entitled to receive the same commission in respect of any new business which he generated since the Judge describes him as having done very well and that his connection grew, resulting in his share of commission amounting, by 1937, to about £10,000.

His clients were, and remained, his personal clients. As the Judge observed, "It is quite clear that if he left the company his connection would go with him". Mr Hose took two of the staff at the City firm with him to Lambert, Mr Pratt and Mr Hose's brother.

In 1939, following prolonged negotiations, Mr Hose took over the post of managing director. This change was significant. As the Judge noted:
"It meant giving up his post as what I have called departmental manager. It meant giving up everything that he had got out of that role. It meant that he would not retain his connection, as he would have to manage the whole concern. Of this connection, the Commissioners say, "he was possessed of his business connection which had a sale value, and which he could have taken away" if he had left the service of the company. Gradually but surely his personal clients would become clients of the company. The change meant that the goodwill of his personal connection, worth in 1937 £20,000 a year in commission…..went to the company…….

When the terms were arrived at the company sent a circular to its shareholders stating that the company had acquired the business of Mr S.J. Hose, and that he was acting as sole managing director of the company as from 1st April 1939."

Mr. Hose gave up a clear intangible asset being his right to share in the commission derived from his clients and so the £30,000 he received was a capital receipt which at that time was tax free. In Jarrould v Bowstead [1964] 3 All ER 76, where a signing-on fee paid to a professional rugby player was held to be consideration for relinquishing his amateur status for life and was for that reason held to be a capital payment and again tax free.

In SWCS and Smiley, summarised at 8.1 above, there was no asset and there was no right to dispose of anything. The UT therefore found that the source must be from the employment and the payment for facilitating the transfer of the clients from the old to the new employer. As such it was a reward for services and taxable as earnings.

## 9.0 Golden Handshake

If a payment is provided by an employer in the context of:

- A compensation for loss of office; or

- A payment to an employee which is not compensatory,

Then this payment will be treated as earnings for the purposes of NICs.

When dealing with 'golden handshakes' it is important to consider what the payment is, why it has been paid and how the amount paid is made up. It may be the case that this amount could include such contractual items as accumulated overtime, backdated pay, fees, bonuses or holiday pay. Such items are payments in compensation for the loss of office in question and as such will attract a liability to NICs.

## 10.0 Termination Payments

On termination of an employment, up to £30,000 can be paid tax free per s403 ITEPA 2003. However, this is not automatic and the first £30,000 is not always exempt from tax. There are a wide variety of issues to consider. Broadly speaking, if the payment in question is in any way a contractual entitlement or is a reward for services rendered the full amount will be taxable. A truly compensatory payment will fall within the provisions and become exempt from tax. Furthermore, regardless of the amount the payment will not be liable to NIC.

## 10.1 PILONS (Payments in Lieu of Notice)

Where an employee receives a contractual PILON, it is chargeable under s62 ITEPA 2003 as earnings from the employment. A contractual payment exists where a contractual arrangement between employer and employee is laid down in any of the following:

- The main contract document;
- A side letter to the main contract document;
- Staff handbook;
- Letter of appointment;
- The redundancy agreement; or
- An employer-union agreement.

It is therefore important to consider all possible contractual sources in determining whether the payment is taxable under s62.

A payment made without legal obligation may also be chargeable under s62 if it is customary to make it. Where an employer always makes a payment for any notice period that is not worked he inadvertently creates an expectation in the other employees. Thus the concept of an 'Autopilon' was born. HMRC's view is that where a PILON is paid as an automatic response to the termination of an employment then it is taxable and liable to Class 1 NIC in full. This need not be the case as it should not be possible to argue that a custom exists where a genuine review and assessment is performed prior to the making of a payment.

## 10.2 Damages

Where:

- there is no entitlement to or custom of making a PILON; and

- the employer unilaterally dismisses the employee with less notice than the employee is entitled to then

the employer has breached the contract.

A PILON in such circumstances represents damages for breach of contract and is taxable under Section 401 ITEPA 2003.

Derek Allen
31 January 2016