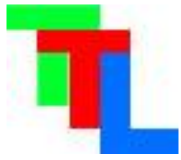

Disguised remuneration

Produced by Tax Training Ltd. www.taxtrainingltd.co 020 8224 5695. March 2018

Introduction

Disguised remuneration is when payment is made to an employee in such a way as to bypass the payroll and so bypass the payment of PAYE and national insurance.

The good news is that most payrolls will be totally unaffected by disguised remuneration. The new provisions generally only apply when you try to do something clever. These new provisions are anti-avoidance measures. However, there has been great difficulty in drafting them so as not to catch non-avoidance transactions.

It should be noted that an arrangement can come within the scope of disguised remuneration even when there is a sound commercial reason for it. In other words, these provisions do not only catch tax avoidance schemes.

Overview

Using the abbreviations of the Act, disguised remuneration involves three parties:

- A is an employee
- B is his or her employer
- P is a third party working with A and B.

There are three broad types of disguised remuneration:

- P earmarks money or assets for A
- P pays money or transfers assets to A
- P makes an asset available to A.

It can be seen that a whole range of normal payroll activities from luncheon vouchers to pension schemes come within this definition. So the provisions are full of exceptions for non-avoidance arrangements.

When not excepted, each of the three cases above triggers a PAYE liability payable by B. It will also trigger a national insurance liability.

Where an employer is a company in a group, the group is generally regarded as the employer. This means that a benefit will not come within the scope just because it is provided by another group company.

It should also be noted that an employer can be the third party when acting in a different role. For example, an employer setting aside a sum to buy a pension for an employee (such as an employer-financed retirement benefit scheme or EFRBS), comes within the scheme as the employer is acting as a trustee.

Date

Payments of PAYE for disguised remuneration must be made on the first PAYE payment after 18 August 2011 (30 days after Royal Assent to Finance Act 2011) but be backdated to apply to all such disguised remuneration from 6 April 2011.

There is a further backdating for disguised remuneration provided between 9 September 2010 and 5 April 2011. Unless such arrangements are unwound, they are regarded as having been provided on 6 April 2011 and so come within the scope.

The legislation

The first thing to note is the sheer quantity of impenetrable prose that these changes have made.

The law is contained in Finance Act 2011 Sch 2. This creates 47 new sections of Income Tax (Earnings and Pensions) Act 2003 numbered s554A to 553Z21 — incidentally a new system of numbering added sections to an Act.

This primary legislation alone adds 68 pages to British tax law which the Chancellor of the Exchequer has already said is too long. (During the course of considering the Finance Bill this section has doubled in length. Most of the additional material is to include more exceptions for non-avoidance arrangements.)

We have yet to see the supporting legislation, the guidance, and the new material for the Inspector’s Manual. The mirror national insurance legislation has now been published.

Despite this huge volume of comprehensive legislation, gaps are still being found in legislation. Finance Act 2016 tightened up the rules to disallow an exception when it is used for tax avoidance. Finance Act 2017, deals with loan transfer exclusion, rules on loan releases and clauses in trust deeds. Finance Act 2018 further deals with close companies.

One of the problems is that the clauses on disguised remuneration have themselves been used to create new forms of disguised remuneration.

Transferring assets

This is a very wide-ranging provision in the new s554C. It includes every conceivable method by which money or an asset may be transferred for the benefit of an employee.

This includes lending money, as there has been avoidance when "loans" are made on the quiet understanding that they need not be repaid, at least not for a long time.

Earmarking

This provision is triggered when an asset is "earmarked" for an employee however informally this is done. This is contained in the new s554B.

A decision does not have to be made as to *which* employee will receive the asset; it is sufficient that the asset is earmarked.

This provision covers most forms of deferred remuneration, including schemes that come within the Financial Services Authority's Remuneration Code. However it does not cover any arrangement that is subject to conditions. So a bonus if sales exceed a certain figure is not disguised remuneration; it is simply taxed as gross income when earned.

A scheme must identify a date to be disguised remuneration. This must be within five years.

Making an asset available

This is when an asset is provided to an employee on terms which are the equivalent to owning it, such as permanent loan. This is contained in the new s554D.

This involves more than simply having access to the asset or possession of it. A company car is not within this scheme. Usually the employee would need to have a right to determine how it is disposed of and to benefit from the proceeds of disposal.

An exception is made for transactions under an employee benefits package, but this is now subject to the condition that it must available to at least half the employees or a substantial number. This is designed to prevent relief for directors and senior managers.

Payment of tax

The employer is liable to pay the PAYE. The first such payment was due with the other PAYE on 19 September 2011.

If a disguised remuneration is unwound, the PAYE cannot be claimed back with the exception of a charge that arose from earmarking.

If PAYE has already been paid on a step that is now regarded as disguised remuneration, that PAYE may be offset against the disguised remuneration tax. This means that, for example, no tax is repayable if an asset value falls.

The employer must pay this PAYE even if the employer cannot recover it from the employee.

If the employer does not recover the tax within 90 days, the tax is itself regarded as a taxable benefit in kind. This means that tax must be paid on the grossed up amount. This mirrors the provision for payment of wages in readily convertible assets.

Exclusions

These arrangements are specifically excluded from the scope of disguised remuneration:

- holiday pay schemes
- dividends on shares acquired by employees
- company car provided on a lease
- most salary sacrifice schemes
- assets made available to an employee before 6 April 2011
- a loan to an employee before 6 April 2011.

Some traps

The following could be caught by the new provisions:

- employee benefit trusts (EBTs)
- employer-financed retirement benefit schemes
- loans of more than four years for an employee to buy a car
- exercise of an option where the sum is not paid by the employee within 40 days
- loan arrangements that involve a third party
- non-approved share plans
- arrangements in which any pay and benefits are outsourced
- use of a hospitality suite under an arrangement made by the employer

Despite all the guidance produced, it is clear that these are shark-infested waters where even innocent transactions risk being caught.

In addition to having to pay unexpected tax, the employer could be liable for the inevitable penalty notice. In the Construction Industry Scheme, it could also count as a black mark towards losing your gross payment certificate. Be careful.

© 2018. Robert Leach. Licensed to Tax Training Ltd. This article may be freely downloaded, printed and copied, provided this notice appears. It may also be quoted, provided the source is acknowledged. For other use, please see our Fair Dealing policy or contact the company. It must be appreciated that this is a summary of detailed provisions. No responsibility can be accepted for any error or omission in this article.