

## **EMPLOYMENT INCOME**

### **Employment or Self-Employment?**

There is a fundamental difference between income received as an employee and as a self employed person/independent contractor. Where income is paid as employment income, the employer must deduct income tax and National Insurance contributions under the PAYE system and remit it to HMRC. There are quite different rules in terms of allowable expenditure and deduction between the employment income and the trading income of a self employed person who provides his services as an independent contractor.

Difficult questions can arise as to whether an arrangement is really an employment or an independent contract. Generally an employee is somebody under the direction and control of the employer. This was a more traditional test. Because of how employment has changed, this has been refined to a test as to whether the person concerned is in business in his own account.

### **Basis of Tax Charge**

All employees and directors are assessed on earnings received in the tax year. Earnings include cash salary but also bonus, commissions and other benefits provided by the employer.

As in Ireland, there are very limited deductions allowable against an employee's income for the purpose of calculating tax. Expenditure must be wholly exclusively and necessarily incurred in the performance of the employment duties. This is much narrower than the test in respect of business expenses.

Certain expenses are allowed as deductions against employment income. These include contributions to pension scheme subject to certain limits, certain expenditures on travel subject to stringent rules and certain expenses incurred for equipment and machinery necessarily provided by the employee. Travel expenses may only be incurred where they are necessary incurred in the performance of the duties. Therefore the cost of commuting to and from work is not allowed. Necessary commuting within the working day is allowable if visiting a client. No relief is given for travelling between two separate employments.

As in Ireland, there are approved mileage allowances for employees who use motor cars for business purposes. The allowances are equivalent to the civil service rate allowed. They specify the maximum rates which can be claimed.

In addition to salary earnings, benefits in kind received by employees e.g. a company car are subject to income tax. There are certain exemptions for employees earning less than a certain amount.

### **Benefits in Kind**

There are certain exempt benefits such as certain subsidies, pension contributions, canteens, certain meals, right to certain car park spaces, provision of mobile phone, benefit aimed at encouraging employees to travel to work by public transport, Christmas parties and work place nurseries for childcare. Payments of up to £55.00 per week to approved childcare is allowed.

Where employers reimburse expenses, the employer must report these on form P11D (as in Ireland). A claim for deduction must be made against employment income. Approval can be obtained in advance from HMRC to dispense with the requirement to omit particular types of pre-approved expenses from the form P11D which would otherwise need to be reported.

Employees earning £8,500.00 per annum or more and directors are subject to the "PD 11 schemes". They are taxed on the basis of the cost of the benefits. A benefit provided

to a member of the family is also taxable in the same way. The benefit must be reported to HMRC on form PD11D.

Where a company car is available for private use, the benefit is subject to income tax. The benefit is calculated on the list price of car. The charge benefit is a percentage of the price of the car. This is 15% per annum but is increased in case of cars with certain emissions. The maximum amount is 35% per annum.

No individual use of pool car is assessed to tax. There are strict conditions on pool cars. It must be used by more than one employee and must normally be kept overnight at the residence of employee. Any private use must be merely incidental. There is separate benefit in kind rules in respect of fuel.

The benefit in kind rules are different for vans. No benefit arises when the private use of van is insignificant. The benefit of private use of a van depends on its age.

Benefit in kind is charged in respect of loans to employees below a stipulated interest rate. Benefit is charged on the difference between the official rate and the rate actually paid.

Where assets are provided for the use of the employee 20% of the assets market value is assessed at tax.

Where living accommodation is provided and expenses paid are generally taxable on the employee where the cost is met by the employer. There are certain limitations and special rules applicable.

### **Special Tax Rules**

Directors of limited companies are classed as office holders. The earnings from an office are automatically chargeable to tax as employment income and there is also liability for Class National Insurance contributions. Executive directors will nearly always be employees. Non-executive directors may be employees of the company or self-

employed under a contract for service, depending on the circumstances, terms and conditions.

In certain sectors, there is an obligation to deduct tax on payments to sub-contractors even if they are not employees. There is a special tax scheme for self-employed contractors and sub-contractors in the construction industry. This is equivalent to "relevant contracts tax" in Ireland.

There are special rules in relation to managed service companies, which have no counterpart in Ireland. A managed service company is a form of personal services company. Payments received by individuals who provide a service to an MSC are subject to PAYE and NIC. Special legislation ensures that individuals operating a managed service company, pay tax and NIC at the same rate as employees. PAYE and NIC contributions are recoverable from the MSCs. They can be assessed on certain third parties and recovered from certain third parties e.g. directors of the MSC and certain associates.

### **Tax Deduction for Contractors**

In certain sectors, there is an obligation to deduct tax on payments to sub-contractors even if they are not employees. There is a special tax scheme for self-employed contractors and sub-contractors in the construction industry. This is equivalent to relevant to contracts tax in Ireland.

### **Managed Service Companies**

There are special rules in relation to managed service companies which have no counterpart in Ireland. A managed service company is a company through which individual services are provided to clients. Payments received by individuals who provide a service to an MSC are subject to PAYE and NIC. Legislation ensures all workers operating a managed service company pay tax and NIC at the same rate as employees. PAYE and NIC contributions are recoverable from the MSCs.

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This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.

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