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REPORT ON
TAX IMPLICATIONS OF APPOINTMENT OF NEW CEO

1. INTRODUCTION

This Report relates to the proposed appointment of Phoebe Sutherland as Chief Executive Officer of Skateways plc following a meeting held with Ethan Reece, Chairman of Skateways plc, on 1 May 2019.

For the remainder of this Report we will refer to Ms Sutherland as Phoebe.

This Report focuses on three main areas:

1) The draft offer letter to Phoebe

2) Additional tax matters to be considered by Skateways plc in relation to Phoebe's appointment

3) Additional tax matters to be considered by Phoebe in relation to her move to the UK.

Please note that this Report is prepared for Skateways plc and no other person or entity may rely on the contents.

Once you have had the opportunity to consider this Report, we would be pleased to discuss any questions you may have.

2. EXECUTIVE SUMMARY

- Phoebe is likely to be treated as UK tax resident throughout the three years she is working in the UK.

- UK NIC will be due on all employment income arising during her time in the UK. A portable document A1 needs to be obtained from HMRC to avoid potential NIC issues in Germany.

- The following amendments to the draft offer letter should be considered:

    - Phoebe can be reimbursed relocation costs of up to £8,000 tax and NIC free. The travel costs of coming to the UK to start work (and the costs of returning to Germany in three years) will be tax free if borne by Skateways plc. This could be incorporated into the offer, and the signing-on bonus (which attracts PAYE and NIC), reduced accordingly.
    - As employer pension contributions are tax free up to the level of the annual allowance, the level of pension contributions should be re-evaluated to ensure annual allowances are being fully used but not exceeded.
    - If Phoebe opts for the car and fuel, her total annual net cost is £22,441. Skateways plc will also be liable for Class 1A NIC. Alternative cars with lower CO_2 emissions should be considered to reduce costs. Phoebe should also pay for her own fuel and be reimbursed her business mileage to avoid punitive tax charges.
    - The cost of her mother's flights will be a taxable benefit. Consideration should be given to covering the costs of Phoebe returning home instead, as these are exempt.
    - It should be made clear that Phoebe is provided a laptop only for the duration of the appointment and for work purposes only
    - If Skateways plc is paying for her tax return preparation and associated advice, we would propose to invoice Skateways plc direct. This prevents the payment being treated as cash earnings and attracting PAYE and Class 1 NIC.

- Phoebe is non-UK domiciled and therefore can claim (annually through self-assessment) to be taxed on her overseas income and gains only when they are remitted to the UK

- If Phoebe does choose the remittance basis, Skateways plc can apply for a direction from HMRC that PAYE need not be operated on the income relating to her overseas workdays.

- A separate and new overseas bank account should be set up by Phoebe and her earnings paid into that to ensure she benefits from this.

- The tax liability in relation to any shares acquired by Phoebe under the group plan will be determined by reference to her overseas and UK workdays during the period from grant to vesting. Her decision as to when she exercises therefore has no bearing on this. Similarly, the date of exercise has no impact on UK NIC liability. Class 1 NIC will be due on any gains attributed to days between grant and vesting when she was within the UK NIC regime.

- Phoebe will have to pay SDLT on the purchase of a property. On a sale, she is responsible for Capital Gains Tax on any gain regardless of where she is tax resident. However, this gain may be reduced (potentially to nil) by principal private residence relief.

3. PROPOSED OFFER LETTER

General Liability to UK Tax and NIC

Before commenting on the tax efficacy of the proposed offer, it is necessary to determine whether Phoebe has any actual liability to UK tax and NICs.

Phoebe's Tax Residency and Domicile

Based on current expectations, Phoebe will be based in the UK from 1 June 2019 to 31 May 2022.

Even allowing for the time she is expected to spend overseas, she will have more than 183 days presence in the UK in the 2019/20, 2020/21 and 2021/22 tax years. As such, she is automatically UK tax resident for those years under the statutory residence test.

While she will not have 183 days of presence in the UK during 2022/23, the two months that she is in the UK to complete her assignment will fall at the end of a 365-day period during which she is expected to work for more than 75% of her time in the UK. This "full-time work" in the UK is a trigger for UK tax residence.

In 2019/20, Phoebe is starting full-time work in the UK and is starting to have a UK home. These are both conditions for the split year rules to apply. Consequently, she will be treated as non-UK resident for the first part of the tax year and UK resident for the second part. The exact date she will become UK resident will be the earlier of the day she buys her UK home and her first UK workday.

In 2022/23 she is also likely to be able to split the tax year on the basis of either starting full-time work abroad or ceasing to have a home in the UK. (Note that 'home is given its' everyday meaning. Therefore, even if she doesn't sell the UK property straightaway, it will not amount to a "home" unless she actually uses it as such.) She will therefore be UK resident for the first part of the tax year and non-UK resident for the second part. We will need to revisit the position in 2022/23 to determine the exact date she will become non-UK resident as it will depend on her working pattern at the time.

Phoebe has a domicile based on her father's German domicile, unless displaced by a clear intention to be permanently domiciled elsewhere. Given Phoebe's connections to Germany and her desire to return there, it is reasonable to assume that she remains domiciled outside the UK.

Impact of Residence on Employment Income

Ordinarily a UK tax resident is subject to UK tax on worldwide income and gains. However, as Phoebe is non-UK domiciled, there is an opportunity to be taxed on overseas income and gains on a remittance basis (i.e. only subject to UK tax to the extent income or gains are brought to or enjoyed in the UK).

It will be up to Phoebe as to whether she decides to claim the remittance basis or not. More details on the impact of this for Skateways plc are contained in Section 4.

Liability to UK National Insurance Contributions (NICs)

Liability to NICs is independent from liability to UK Income Tax and is determined by different rules.

Because Phoebe is moving between EU countries, the NIC position is governed by EU regulations. Given she works in more than one EU country for the same employer, she is subject to the social security legislation of the country in which she is habitually resident if she carries out at least 25% of her work there. Although, it is not clear where Phoebe's place of habitual residence is given she is only in the UK for three years, she does in any event works for less than 25% of her time there. Accordingly, the applicable social security system is the one where her employer's registered office is situated; the UK.

A portable Document A1 needs to be obtained from HMRC and we can assist with this. UK NIC should be accounted for by Skateways plc on all relevant employment income.

Signing-On Bonus

Although the bonus is merely intended to encourage Phoebe to accept the new role, it will be regarded as employment-related and taxable as earnings.

However, an employer can pay up to £8,000 in relocation costs free of tax and NIC.

The definition of relocation costs is quite wide and covers removal costs, costs associated with acquiring a new property, travel costs incurred whilst seeking a new residence and the costs of replacement domestic goods. The expenses must actually be incurred and therefore, you should ask Phoebe for appropriate receipts.

In addition, because Phoebe is non-UK domiciled and has not been in the UK or resident in the UK in the two tax years preceding the year she comes to the UK, the costs of paying for her flights, transfers and subsistence when she first comes to the UK to start work (and to return at the end of the assignment) are also free of tax and NIC. This would be in addition to the £8,000.

It is therefore recommended that you adjust your offer to reflect the £8,000 reimbursement of relocation costs and the payment of her travel expenses to the UK and reduce the signing-on bonus accordingly.

Bonus Scheme

Although any liability to tax will arise on the date of payment (1 April), you will need to consider where Phoebe is tax resident during the period for which the bonus is earned, i.e. the preceding year ending 31 December. If she is UK resident during the earnings period, she will be subject to UK PAYE even if at the time of payment, she is non-UK resident. This is only likely to be relevant in respect of the year ended 31 December 2022 which will be paid after Phoebe has returned to Germany.

Class 1 NIC will only be due if Phoebe is within the UK NIC regime at the payment date.

Pension Contributions

Provided certain conditions are satisfied in relation to Phoebe's personal pension scheme, contributions by Skateways plc will be deductible for corporation tax purposes and will also be a tax-free benefit for Phoebe.

However, it is important to note that Phoebe's tax position is affected by the annual allowance. Because of the level of Phoebe's salary, she will have a maximum allowance of £10,000 a year. Any excess will be subject to an annual allowance charge (based on her top rate of income tax). Subject to certain conditions, she may be able to bring forward unused allowances from the preceding three tax years to reduce the excess. It is recommended that we consider this further. If Phoebe has unused allowances, it may be worth increasing the pension contribution whilst she is in the UK to utilise these (and reduce an otherwise taxable part of the package accordingly). Equally if no unused prior year allowances are available, we recommend exploring whether the annual contributions should be reduced to £10,000 to avoid unexpected charges.

Car

Phoebe may choose to give up her right to £15,000 of salary in return for the use of a car and the provision of private fuel.

These benefits are covered by the optional remuneration legislation and therefore we will need to compare the usual cash equivalent with the amount foregone (in this case £15,000). If the £15,000 is greater, this will be the taxable amount.

The calculation of the tax position is set out in the Appendix. If Phoebe opts for the car and fuel, not only will her salary be reduced by £15,000 but she will have a taxable benefit of £31,536. Assuming she is an additional rate taxpayer, her total net cost (ignoring any German liability) is £22,441 per annum. There will also be Class 1A NIC payable by Skateways plc at the rate of 13.8%

This contrasts with additional net salary of £8,085 if she decides to keep the higher salary. She would, however, have to fund her own transport out of her net earnings.

Consideration should be given to amending the car/fuel offer as follows:

1. Ensuring Phoebe pays for her own fuel reduces the annual taxable benefit by £8,136. Furthermore, the company can reimburse her for any business mileage she does (other than commuting from home to office and vice versa) up to 22p per mile without any tax liability arising.
2. Selecting a lower emissions car. Non-diesels and hybrids attract a much lower charge. For example, if emissions are less than 50g/km, the taxable benefit will be 9% of list price instead of 36% of list price for the Porsche Cayenne.

Please note that if Phoebe does opt for some form of salary sacrifice as part of her package, it is important she does so before she becomes entitled to the salary. Furthermore, the agreement period needs to be at least 12 months with changes only allowed if there is a lifestyle event such as marriage or becoming a parent.

Visits by Phoebe's Mother

Although no taxable benefit arises in connection with the payment of the costs of travel for up to two visits a year by Phoebe's spouse or minor children, this exemption does not extend to Phoebe's parents. As such, any travel costs met by Skateways plc for visits by Phoebe's mother will form part of Phoebe's earnings.

Consideration should be given to paying Phoebe's travel costs when she visits her parents instead. On the basis that Phoebe is non-domiciled and ordinarily lives in Germany, these journeys should be tax exempt if reimbursed.

Fees

The payment of our fees for advice given to Phoebe will be a taxable benefit. However, the exact treatment depends on how this is structured.

If Skateways plc discharges an invoice raised to Phoebe, the amount paid will be subject to both PAYE and Class 1 NIC. However, if Skateways plc procure and pay directly for the advice given to Phoebe, there is only employer's Class 1A NIC. The value of the benefit will be dealt with through self-assessment or a PAYE code adjustment (unless Skateways plc decide to voluntarily payroll the benefit).

Mobile Phone and Laptop

The provision of a mobile phone is a tax-free benefit where the contract is between the provider and Skateways plc. The laptop will also be exempt provided it can only be used for work purposes. If there is an element of personal use, an appropriate proportion of the cost of the laptop will be taxable. The exact amount will depend on whether Phoebe is given the laptop or simply loaned it. It is recommended therefore that the offer letter is amended to reflect that a laptop will be provided for the duration of her appointment and specifically exclude any private use.

4. ADDITIONAL MATTERS FOR SKATEWAYS PLC

Impact of Being Non-UK Domiciled

As a non-UK domicile, Phoebe is entitled to claim the remittance basis.

If she does so, she will be eligible for Overseas Workday Relief (OWR) on her employment income in any tax year where, over the preceding five tax years, there is a period of three consecutive tax years where she is not UK tax resident.

On the facts given, Phoebe will be entitled to OWR up to and including the 2021/22 tax year. During this time, the proportion of her general earnings relating to her overseas work will only be subject to UK tax if and to the extent it is brought into the UK.

The amount of OWR will depend on the number of non-UK workdays during the tax year and whether Phoebe brings any of the funds delivered overseas into the UK.

It would therefore be advisable to pay all of Phoebe's pay into a German bank account. She can then withdraw the amount which relates to the UK element (which is subject to tax in any event) and leave the rest overseas (assuming she does not need it). If she sets up an overseas bank account especially for the purpose and keeps nothing in it but her employment income and any interest arising on the account, she can reduce administration by taking advantage of the "special mixed fund rules". These allow remittances to be examined at the end of the year to identify the nature of the income brought into the UK, rather than on a transaction by transaction basis.

If, as expected, Phoebe does prove to be UK tax resident for part of 2022/23, she will no longer qualify for OWR. As such, all her earnings, including any attributable to overseas workdays, will be taxable in the UK. Skateways plc may want to consider adjusting her work pattern so that more overseas days fall into the end of 2021/22 (when she benefits from OWR), rather the short period of her assignment which falls into 2022/23.

Payroll and reporting matters.

Technically, Skateways plc should deduct PAYE from all of Phoebe's remuneration in the usual way. However, it is possible to apply to HMRC for a "S690" direction. PAYE is then operated on a reduced amount to reflect the overseas proportion of Phoebe's duties. (This is assuming Skateways plc adopts the approach of paying all her salary into an overseas bank account as referred to above.) The direction can cover all three tax years that OWR is available for. We can assist with the application if required.

Trailing Liabilities

We recommend Skateways plc consult with its German tax advisers to ensure there are no trailing liabilities in Germany. If, however, there are any liabilities, credit would be given for this against the UK tax payable.

5. ADDITIONAL MATTERS FOR PHOEBE.

In addition to advising Phoebe on whether she claims remittance basis or not, we would like to draw her attention to two particular matters:

Participation in the Group Share Plan

Liability to UK tax depends on the number of UK and overseas workdays between the date of grant and the date of vesting (not exercise). The timing of the exercise is therefore irrelevant.

It is important to note that if there are any overseas workdays where Phoebe's earnings are taxed on a remittance basis, the option gain relating to those days will be deemed to have been remitted automatically to the UK. This is because the underlying shares are registered in the UK.

From a NIC perspective, liability totally depends on the extent to which she is liable to UK NIC over the period from the date of grant until the date of vesting.

Purchase of a UK Property

At the meeting, it was mentioned that Phoebe is buying a house near Leicester. She should be aware of the following:

1. On Acquisition

On completion of the purchase, Stamp Duty Land Tax (SDLT) will arise. The amount depends on the acquisition price of the property, ranging from 0% for properties costing less than £125,000 to 12% where the cost exceeds £1.2 million.

2. On Sale

Ordinarily, non-UK tax resident individuals are exempt from UK capital gains tax (CGT). However, there is an exception for residential property. In these circumstances, they will be subject to CGT at their marginal CGT rate on any gain made on sale.

Assuming Phoebe lives in the property, she will be eligible to claim principal private residence (PPR) relief. This effectively exempts any gain attributable to periods of occupation where the property is an individual's "only or main home".

If she also owns a home in Germany, she can nominate the UK property as her main residence to ensure she benefits from the relief. The election should be made in writing to HMRC within 2 years of obtaining a second property that could be considered as a private residence.

It is assumed that Phoebe will sell the UK property on her return to Germany. If she does not, this may affect the advice, although it is important to note that the last 18 months of ownership will be exempt even if not occupied, provided the property has been occupied as a main residence at some point.

Once she sells the property, she should file a return notifying HMRC of the disposal within 30 days. Ordinarily, any CGT due would be paid at the same time. However, if the sale is in 2022/23, Phoebe is likely to be submitting a UK tax return for that year and she can choose to defer the payment of the CGT until the usual self-assessment payment date, i.e. 31 January 2024.

APPENDIX
CAR AND FUEL v SALARY SACRIFICE

Annual taxable benefit	greater of amount foregone and cash equivalent
Amount foregone	$\boxed{\text{£15,000}}$
Cash equivalent of car	= (list price) x relevant percentage + (diesel supplement)
	= £65,000 x [(173 – 95) /5 + 18%] + 3%
	= £65,000 x 36%
	= £23,400
Cash equivalent of fuel	= £22,600 x 36%
	= £8,136
Total	£23,400 + £8,136
	= $\boxed{\text{£31,536}}$

As cash equivalent > the amount foregone, annual taxable benefit is £31,536.

Tax at 45% (additional rate) is £14,191.

Comparison

(i) Take car and fuel

	£
Loss of net salary £15,000 x 55%	8,250
UK tax payable	14,191
	£(22,441)

(ii) Take salary

	£
Additional net salary	8,250
Less Class 1 Employees' NIC @2%	(165)
	£8,085