Global Tax Update

GERMANY

New administrative opinion disrupts practice for temporary employees

Contained within Germany's Income Tax Regulations 2023, is a change in the administrative opinion regarding the calculation of the income tax deduction for employees who are not working continuously in Germany. Specifically, this concerns the question of which income tax table should be used to calculate the tax due in the case of temporary employment in Germany.

If an employment relationship does not exist throughout a full month, the income received during this period is to be converted to individual calendar days. The income tax due results from the amount of the income tax day table multiplied by the number of calendar days worked. For tax purposes, these cases are referred to as a partial income payment period. The application of the daily income tax table results in a higher tax burden than the application of the monthly income tax table.

If the employee was at work in Germany only temporarily during a calendar month, working days falling within the income payment period for which the employee did not receive taxable wages were previously also to be counted if the employment relationship continued. According to the previous administrative interpretation, no partial income payment period resulted for income tax purposes if an employee either starts or stops doing work abroad (work that is tax-exempt under a double taxation agreement or under the Foreign Employment Decree (Auslandstätigkeitserlass) for the employer in the course of the month, or if the employer works part of the time in Germany and part of the time abroad during the income payment period.

Effective 2023 - despite the unchanged legislative situation - working days on which the employee received wages, not subject to domestic income tax deduction, should no longer be counted when calculating the income payment period (e.g., receipt of tax-exempt income under a double taxation agreement or employment in Germany on a daily basis only). This results in a considerably higher income tax burden for the persons affected, for which no legal basis is apparent in view of the (in our opinion) unambiguous wording of the law.

As an example, a pro rata taxable salary in Germany of EUR 1,000 based on five working days per month, will result in a tax burden of approx. EUR 225 as of 2023. Under the previous regulation applicable until 2022, the income tax based on the monthly table would have amounted to EUR 0.

For individuals with limited tax liability, given the basic settlement effect of the withholding, this higher tax burden will also be – in many cases - permanent. For EU/EEA nationals who are resident or ordinarily resident in one of these states, an application assessment can be carried out, but this again involves greater time and effort. Moreover, an application assessment would also lead to the tax-exempt foreign income having to be taken into account within the framework of the so-called progression proviso (a determination of the applicable tax rate).

The regulations also apply to taxpayers with unlimited tax liability. However, those taxpayers are likely to have already made an assessment in the past, into which the higher income tax deduction will then flow in the future and be offset accordingly.

> The regulations also apply to taxpayers with unlimited tax liability

Since the new regulation cannot be derived from the relevant legislation in this context, it may well be possible to continue to calculate the income tax on the basis of the monthly table, as has been done to date, if the amounts involved are large enough. However, the tax office would have to be informed of this deviation. Since the tax office is unlikely to follow this due to the self-imposed obligation of the tax authorities under the regulations, an appeal would have to be lodged against a corresponding decision by the tax authorities, and legal action would also have to be considered.

If the income tax is to be determined on the basis of the daily table, as now advocated by the tax authorities, a decision would have to be made as to whether the employee is to bear the income tax incurred or whether the employer is to assume the consequences of the net income agreement for German working days, and thus take on a corresponding additional burden. In this respect, whether and how the employment contracts would have to be amended would have to be examined.

BDO Comment

Given Germany's shortage of skilled workers, the higher tax burden does not contribute to making the country more appealing as a favourable location on the labour market. The possibility of disputes between employers and employees cannot be ruled out.

Inflation Compensation Premium Free Tax And Social Security Contributions

Germany's upper house of Parliament recently approved a measure that would give all employers the opportunity to provide their employees a special payment of up to EUR 3,000 as an inflation compensation premium, free of tax and social security contributions.

The inflation compensation premium is part of the "Act on the Temporary Reduction of the Value Added Tax Rate on Gas Deliveries via the Natural Gas Grid" and the so-called "Third Relief Package" from the federal government.

The law has been forwarded to the federal president for signature and will then be promulgated in the Federal Law Gazette. It will enter into force retroactively as of 1 January 2022.

Tax Exemption

According to the legal wording of the German Income Tax Act, "Tax-free are [...] benefits granted by the employer in the period from 26 October 2022 to 31 December 2024, in the form of subsidies and benefits in kind in addition to the remuneration owed in any case to mitigate increased consumer prices up to an amount of EUR 3,000."

The basic prerequisite for tax and contribution exemption is that the benefit is provided in addition to an employee's regular salary. Benefits paid by the employer for employment are only paid "in addition to the wages owed in any case" within the meaning of the German Income Tax Act if:

- The benefit is not offset against the entitlement to wages
- The entitlement to wages is not reduced in favour of the benefit
- The benefit for a specific purpose or use is not granted in lieu of a future increase in wages already agreed upon; and
- If the benefit is discontinued, the salary is not increased.

All the above conditions must be met.

The preferential treatment therefore does not apply if:

- A bonus is paid and in return the monthly wage or other bonuses or special payments are reduced
- Bonuses, special payments or other salary components already owed are to be fulfilled "as a substitute" by the bonus; or
- The wage is temporarily reduced and is increased again after the inflation compensation premium has ceased to exist.

The inflation compensation premium is an allowance that benefits employees even if an amount higher than EUR 3,000 is paid. However, the portion in excess of EUR 3,000 is fully taxable and subject to social security contributions.

The bonus can also be granted in the form of a benefit in kind (for example, a voucher, a bicycle, a smartphone or a tablet).

Payment of the inflation compensation premium is voluntary for employers. Employees have no claim to the bonus; it is merely a favour under tax law in the event the bonus is paid. In order to be tax-exempt, the bonus must have actually accrued to the employee; that is, it must have been paid out by 31 December 2024 at the latest.

BDO Comment

The benefit is valid from 26 October 2022 to 31 December 2024. The long period is intended to give businesses a high degree of flexibility. However, employers who would like to pay all or part of the inflation compensation premium to their employees this year need to act, as payment would have to be arranged for the December wage payment period at the latest.

SPAIN

Amendments to special tax regime for inbound expatriates

Effective 1 January 2023, Spain's special tax regime for inbound expatriates has been amended to improve Spain's tax competitiveness and attract talent from abroad.

The requirements for applying to benefit from the special tax regime have been relaxed, and now highly qualified entrepreneurs and self-employed workers who provide services to emerging companies (startups) may apply. In addition, spouses and children under 25 may also apply for the special regime.

Individuals who move to Spain and acquire tax residence in Spain may opt to be taxed under the Non-Resident Income Tax (NRIT) rules instead of being taxed under the Spanish Personal Income Tax (PIT) rules. This would imply being taxed at a flat rates of 24% on Spanish-source employment income up to EUR 600,000.

The special tax regime will apply during the tax period in which tax residence in Spain is acquired (once the individual has moved to Spain) and during the five following tax periods, without prejudice to cases of renunciation or exclusion.

The requirements for applying the special regime include the following:

- The individual must not have been tax resident in Spain during the five tax years before moving to Spain
- The move to Spanish territory must have one of the following purposes:
  - A work contract (this requirement is met when the individual signs an employment contract with a Spanish employer or when he is relocated to Spain by the foreign employer pursuant to an assignment letter to a Spanish entity)
  - Appointment as administrator of a Spanish entity, if the individual does not acquire an ownership interest in that entity, or if he/she does, the ownership interest does not render them related parties under Spain's transfer pricing rules
  - To work remotely from Spain through the exclusive use of computer and telecommunication means and systems. In this case, a relocation order from an employer is not necessary, as long as the individual has an international telework visa
  - To carry out economic activity in Spain that qualifies as entrepreneurial activity
  - Highly qualified professional providing services in Spain to start-up companies or carrying out training, research, development and innovation activities, for which the individual will receive remuneration that represents more than 40% of the total income from business, professional and personal work
- The individual may not obtain income that would be classified as obtained through a permanent establishment situated in Spanish territory, unless the purpose of the move to Spain is described in the last two points above.

Individuals taxed under the special tax regime will be subject to personal income only on income obtained in Spanish territory, except for employment income. All employment income obtained by the individual (in Spain and abroad) during the application of the special regime will be considered obtained in Spanish territory. If the work performed abroad is also taxable in the other country, the individual could apply for an international double taxation deduction. Spain, as state of residence, would apply a tax credit to avoid double taxation.

BDO Comment

There is a strict six-month deadline to apply for the special tax regime. The Spanish tax authorities deem this period to begin from the date of commencement of the employment activity in the Spanish Social Security or the documentation that allows the maintenance of home legislation of Social Security.

UK

Employment intermediaries – Have you done your due diligence?

The use of employment intermediaries has never been more prevalent than today, as the modern-day workforce becomes more flexible and transient.

Intermediaries are increasingly an attractive means of engaging workers for several reasons, notably the flexibility they offer in onboarding workers quickly, often for short engagements. Intermediaries also reduce internal administrative duties, particularly when it comes to operating payroll and the statutory payments associated with employment.

Despite the benefits employment intermediaries offer, recent court decisions highlight the risks they may give rise to. The following cases demonstrate the complexities involved, from both an employment tax and a legal perspective.

Employment Contracts

The rulings in Mainpay Ltd v HMRC and Exchequer Solutions Ltd v HMRC provide two examples in the last 12 months where agencies have come under scrutiny. In both cases, HMRC were successful in recovering income tax and National Insurance Contributions (NIC).

The issue before the courts was whether the intermediary companies employed the individuals under an overarching or umbrella contract of employment, which would cover all of an employee's assignments and any gaps between those assignments, or whether instead there was a series of separate contracts of employment covering each individual assignment.

If there is an overarching contract of employment in place, each place of work is classified as being a temporary workplace and expenses can be reimbursed on a tax-free basis. However, if each assignment is covered by an individual contract, each place of work is considered to be a "permanent workplace" and any expenses that are reimbursed must be subject to tax.

The intermediaries in these two cases - Mainpay Ltd. and Exchequer Solutions Ltd - operated on the basis that the contracts held with workers represented overarching contacts of employment. In the Mainpay Ltd, case, the intermediary had obtained specific legal advice on the subject years before. As a result, both intermediaries allowed for income tax deductions in respect of expenses incurred by workers travelling to and from home and their workplace, on the understanding that travel linked to the end-user's workplace qualified under the "temporary workplace relief" legislation.

In fact, the contracts between the intermediaries and the workers were merely framework agreements. A subsequent

contract would be entered into for the worker to provide their services to an end-user, making that the permanent contract for their services.

HMRC argued that income tax relief was unavailable because, whilst each engagement with an end-user was temporary, it represented the entire period during which the worker held the employment. Consequently, income tax relief under the "temporary workplace relief" legislation would be unavailable in respect of any commuting costs.

The courts sided with HMRC in both cases, leaving the intermediaries with significant liabilities to settle dating back multiple tax years.

Holiday Pay Entitlement

In the recent case Harpur Trust v Brazel, the claimant was engaged on a part-year contract at a school. In calculating the claimant's holiday entitlement, the school utilised the 12.07% formula, as was common practice for employees who work irregular hours.

In adopting this approach, the calculation seeks to arrive at a proportionate amount of pay for irregular hour workers compared to their full-time counterparts. The claimant insisted this was unfair, resulting in a claim being made and the ensuing court case.

The court found the employer's method of calculating entitlement incorrect, and concluded that the holiday entitlement should instead be calculated in line with the method used for full-time workers. In reaching this conclusion, the court recognised that this approach could result in a part-time employee's entitlement being proportionally greater than that of a full-time employee. However, it concluded that this was not a reason to deviate from the method of calculating entitlement as outlined in the legislation.

Given that intermediaries typically engage workers on irregular/zero-hour contracts, it's imperative that they take note of this court ruling and update policies and processes accordingly.

BDO Comment

In light of the examples noted above, stakeholders should consider their supply chains now more than ever, particularly end users and agencies.

Organisations looking to engage workers via intermediaries should conduct the relevant due diligence before recommending "preferred" intermediaries. Due diligence should seek to clarify the policies and processes intermediaries have in place and should be conducted jointly by employment tax and legal professionals.

Typically, any marketing material that promises overly generous deductions or savings is at risk of not being compliant with relevant legislation.

Intermediaries, on the other hand, need to ensure that they are up to date with all relevant legislation and that any historic advice has been checked to ensure it remains relevant.

The agency business model is well known for operating on tight margins, increasing pressure to find new and creative ways to attract workers to grow profits. At the same time, the legislation relating to intermediaries has tightened over recent years, with the goal of achieving parity with the traditional employer/employee model and ensuring HMRC receive the tax revenue due. Consequently, ongoing monitoring of existing policy/process is vital to avoid unintended consequences down the line.

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USA

SECURE 2.0 Act of 2022 introduces key changes for workplace retirement plans

The Consolidated Appropriations Act, 2023, signed into law in December 2022 by President Joe Biden, includes the SECURE 2.0 Act of 2022, which introduces over 90 changes to the federal rules governing workplace retirement plans.

This landmark legislation builds on the original SECURE Act that was enacted in December 2019, and aims to expand coverage and increase retirement savings while simplifying and clarifying retirement plan rules.

Every employer, whether for-profit or tax-exempt, that currently maintains a qualified retirement plan or is evaluating a future plan, should consider implementing these new rules, since the changes are generally beneficial for employees.

Unless the Internal Revenue Service announces otherwise, employers that operate in accordance with the mandatory or optional changes in the law as of the provisions' applicable effective date, have until the end of the plan year beginning in 2025 to adopt the written amendment. Government employers have until the end of their 2027 plan year to amend the plan document.

BDO Comment

While many of the retirement plan provisions in SECURE 2.0 are not effective until later years (including some, like the new federal "Saver's Match" and mandatory paper benefit statements, that will not take effect until 2026), a number of important provisions require immediate attention. Some of the changes are especially helpful to small employers.

Almost all workplace retirement plans will need to be reviewed for possible amendments and operational changes to reflect SECURE 2.0.

While further guidance on many of the new provisions is needed, employers should review their plan document and operations in the meantime to determine what, if any, amendments will be needed, what operations need to be changed and what systems or processes should be updated.

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