ICAEW KNOW-HOW
TAX FACULTY

OFF-PAYROLL WORKING: CROSS-BORDER WORKING

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Off-payroll working/IR35: cross-border working: questions and answers guidance published in December 2021

This guidance note comprises the text of questions put to HMRC in December 2019, which with our suggested responses was originally published as TAXguide 07/20.

The answers in this guidance note issued on 1 December 2021 reflect the current position based on the latest legislation and HMRC guidance, mainly in ESM10000 (20 April 2021 version). It replaces TAXguides 17/21 and 07/20.

This guidance is based on our understanding of the measures. We asked HMRC to confirm that it is happy with our interpretation or to provide clarification if needed. This guidance contains HMRC's replies. The previous version of this TAXguide contained HMRC's comments on Sections A and B and this updated TAXguide completes the picture with HMRC's comments on Section C.

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Introduction

In all the following scenarios the end client is medium or large, i.e. subject to the off-payrolling rules, unless otherwise stated.

In the scenarios in Section A we have not discussed the interaction of tax treaties on the income tax position as this is considered in a separate question in Section C.

SECTION A – SIX SCENARIOS

Scenario 1

UK resident client engages contractor's PSC.

Contractor and the contractor's PSC are resident in Germany.

No duties are performed in the UK.

Q1: If these facts applied to a direct employment, no income tax is chargeable on any earnings and there is no need for the employer to operate PAYE. If the contractor is a deemed employee, will there be no UK tax liability and therefore no obligation on the client to operate PAYE? Are there any RTI reporting requirements?

Suggested response:

1. Provided the end client has taken reasonable care to confirm that the contractor is resident in Germany and that no duties are performed in the UK, there will be no UK tax liability on the payment for the duties performed.
2. There will be no requirement to pay UK NIC because the worker is not gainfully employed in the UK. As there is no UK social security due, there is also no requirement to pay the apprenticeship levy on any payments. There is no requirement to perform an employment status determination or to issue a status determination statement (SDS) or to put in place a disagreement process for such a contractor.
3. Payments to the contractor's PSC should not be reported via RTI and there is no need to apply for an NT code number for the contractor.

HMRC's guidance:

HMRC's guidance at ESM10025 confirms that no tax or NIC are due. It states that:

> ***"The worker must be a person who is within the UK charge to tax and/or liable for Class 1 NICs.***
>
> *"Where a worker should be subject to UK tax and NICs (based on existing domicile and residency rules), then UK domestic legislation applies to the engagement. This means the engagement could be subject to Chapter 10 (tax) / Part 2 (NICs) rules. A client does not need to consider whether Chapter 10 / Part 2 rules apply where there is no liability to tax and NICs in the UK.".*

HMRC's response:

Our view is that the suggested response is correct. If the worker is outside the charge of UK income tax and NICs, Chapter 10 cannot override residency rules to generate a liability. Chapter 10 would therefore not apply.

Scenario 2

UK resident client engages contractor's PSC.

Contractor and contractor's PSC are resident in Germany and not UK resident under the UK's domestic legislation. The contractor is expected to perform 25% of the work in the UK.

Q2: What are the client's off-payroll working obligations?

Suggested response:

4. The client will be obliged to undertake an employment status determination and issue it to the worker and account for PAYE if the contractor is a deemed employee. There will also need to be a dispute resolution process put in place.
5. The client will be classed as an employer under s690 ITEPA 2003 and can apply under s690(2) ITEPA 2003 (Employee non-resident etc.) to HMRC for a direction to operate PAYE on just the 25% UK-related income. Without such a direction the client should operate PAYE on 100% of the fee paid unless the end client can accurately measure the percentage of the work performed in the UK and operate PAYE on that percentage so that there is no underpayment of PAYE. If the client is liable to pay the apprenticeship levy the client will also be liable for the apprenticeship levy in respect of the fees paid to this contractor's PSC.
6. If the worker had an A1 certificate confirming that the worker was liable to German social security, no UK social security would be due. If no UK social security is due, then there would also be no requirement to pay apprenticeship levy.

HMRC's guidance:

HMRC's guidance at ESM10025 states:

> ***"Worker in the UK***
>
> *"A worker carrying on duties in the UK for an end client will normally fall within scope of the UK charge to tax and be within the off-payroll working rules. There are some exceptions for non-UK residents visiting the UK briefly:*
>
> *https://www.gov.uk/tax-come-to-uk* [Tax if you come to live in the UK]
>
> *https://www.gov.uk/tax-return-uk* [Tax if you return to the UK]
>
> *"Where a worker carries on duties in both the UK and abroad, the deemed employer may be able to apply to operate PAYE on the worker's earnings for work they do in the UK only. Further details can be found at:*
>
> *https://www.gov.uk/guidance/new-employee-coming-to-work-from-abroad* [New employee coming to work from abroad]
>
> *https://www.gov.uk/government/publications/rdr4-overseas-workday-relief-owr* [RDR4 overseas workday relief]
>
> *"Primary Class 1 NICs should be deducted and Secondary Class 1 NICs paid unless the worker coming to the UK can present a certificate of continuing liability, such as Form A1, confirming that they are liable to pay social security contributions in another country for which special rules apply. For example, a non-UK resident worker provides their services in the UK, but holds a certificate of continuing liability for another country. In this situation the worker would be liable for social security in their home country and so are exempt from NICs in the UK.*

"Alternatively, UK domestic legislation may deem NICs not to be due. For example, if an individual comes to the UK from a country without any form of agreement relating to social security, NICs may not be due for the first 52 weeks the individual is in the UK."

HMRC's response:

Our view is that the suggested response is correct, except for the second sentence in paragraph 5. If the client is resident in the UK and the worker is within the charge of UK income tax and NICs by virtue of carrying on duties in the UK, Chapter 10 would apply and the client would need to comply with its obligations under the legislation.

The client would be able to apply to HMRC under section 690 ITEPA 2003 for a direction to only operate PAYE on the percentage of the worker's total earnings that are for work in the UK. If no direction has been given, they must operate PAYE on all payments made to the worker for work done both in and outside the UK. UK social security contributions would not be due if the relevant evidence is provided showing contributions being paid elsewhere.

Scenario 3

UK resident client engages contractor's PSC.

Contractor is UK resident but non-UK domiciled and contractor's PSC is UK resident.

Contractor performs 75% of the work in the UK.

Q3: What are the client's off-payroll working obligations?

Suggested response

7. Where the contractor meets the conditions for the remittance basis and the conditions in s26A ITEPA 2003 are met so that s26 ITEPA 2003 is satisfied, the client can benefit from what is commonly referred to as Overseas Workday Relief (OWR) and apply for a s690 ITEPA 2003 determination to operate PAYE only on the 75% UK-related payments. This is subject to at least 25% of the payments being made into an offshore bank account and the payments not being remitted to the UK.
8. Many individuals who qualify for OWR are not liable to UK NIC. If the individual had an A1 or other certificate of coverage exempting the individual from UK national insurance, no national insurance contributions would be due. There would also not be any apprenticeship levy liability.
9. If an appropriate certificate is not held UK NIC and the apprenticeship levy would be due on 100% of the payments and not just 75% of the payments for UK duties.

HMRC's guidance:

HMRC's guidance at ESM10025 states:

"Worker in the UK

"Where a worker carries on duties in both the UK and abroad, the deemed employer may be able to apply to operate PAYE on the worker's earnings for work they do in the UK only. Further details can be found at:

https://www.gov.uk/guidance/new-employee-coming-to-work-from-abroad [New employee coming to work from abroad]

https://www.gov.uk/government/publications/rdr4-overseas-workday-relief-owr [RDR4 overseas workday relief]".

HMRC's response:

The response is correct assuming the individual meets the conditions of section 26A ITEPA 2003. The off-payroll working rules in Chapter 10 would apply to the engagement and the client would need to comply with its obligations under the legislation. A direction under section 690 ITEPA 2003 may apply to only operate PAYE on the UK-related income. Section 690 will not apply where the individual is chargeable on overseas income under section 22 ITEPA 2003.

UK social security contributions would not be due if the relevant evidence is provided showing contributions being paid elsewhere.

Scenario 4

German resident client engages contractor's PSC.

Contractor and PSC are resident in UK.

All duties are performed in UK.

Q4: What are the client's off-payrolling obligations?

Suggested response:

10. Following FA20 deleting s61R(7) ITEPA03 and inserting s60I we consider that in this scenario the obligation to determine whether the engagement is within IR35 falls on the PSC in the same way as if the client were small (ie Chapter 8 ITEPA03 applies).
11. It will be necessary to ensure that the duties of the contractor do not give rise to the creation in the UK of a permanent establishment of the client.

HMRC's guidance:

HMRC's guidance confirms the above answer. ESM10025 and ESM10026 both state:

> *"**Section 61R Chapter 10, Part 2 ITEPA 2003***
>
> ***"Client wholly overseas***
>
> *"Where a medium or large-sized non-public sector client is based wholly overseas, so there is no UK connection immediately before the beginning of the tax year because it is not UK resident and does not have a UK permanent establishment, then the rules at Chapter 10, Part 2, ITEPA 2003 do not apply (see ESM10006). The worker's intermediary should consider whether Chapter 8, Part 2, ITEPA 2003 applies for these engagements.".*

HMRC's response:

Clarification is required on whether the German resident client is wholly overseas or if it operates through a permanent establishment in the UK. In the former situation, the client is outside of the scope of Chapter 10 by virtue of having no UK connection. The client does not have to determine the status of the contractor, nor operate PAYE. Instead, Chapter 8 will continue to apply to the engagement, with the PSC determining if the rules apply.

In the latter situation, the client will be within scope of the rules by virtue of its UK permanent establishment. As such, the client will be responsible for determining the status of the contractor and complying with its obligations under Chapter 10.

Scenario 5

As for Scenario 4 (German resident client engages contractor's PSC, and contractor and PSC are resident in UK) save that 75% of the duties are performed in the UK.

Q5: What are the client's off-payrolling obligations?

Suggested response

12. Following FA20 deleting s61R(7) ITEPA03 and inserting s60I we consider that in this scenario the obligation to determine whether the engagement is within IR35 falls on the PSC in the same way as if the client were small (ie Chapter 8 ITEPA03 applies).
13. It will be necessary to ensure that the duties of the contractor do not give rise to the creation in the UK of a permanent establishment of the client.
14. If the contractor works 25% abroad and meets the conditions in s26A and s690 ITEPA03 (for example, the contractor is non-UK domiciled and it is their first, second or third consecutive year of UK residence having immediately previously been non-UK resident for three consecutive years), the PSC would be able to apply to HMRC under s690 for a determination to be able to operate PAYE on only the UK proportion of the earnings paid by the PSC to the contractor if at least 25% of the earnings were paid into a non-UK bank account.
15. Many individuals who qualify for OWR are not liable to UK NIC. If the contractor had an A1 or other certificate of coverage exempting the individual from UK NIC, no NIC would be due. There would also not be any apprenticeship levy liability.
16. If an appropriate certificate is not held then UK NIC and (if applicable) apprenticeship levy would be due on 100% of the payments and not just the 75% of the payments for UK duties.

HMRC's guidance:

HMRC's guidance doesn't fully cover this scenario.

HMRC's guidance in ESM10025 says:

> ***"Section 61R Chapter 10, Part 2 ITEPA 2003***
>
> ***"Client wholly overseas***
>
> *"Where a medium or large-sized non-public sector client is based wholly overseas, so there is no UK connection immediately before the beginning of the tax year because it is not UK resident and does not have a UK permanent establishment then the rules at Chapter 10, Part 2, ITEPA 2003 do not apply (see ESM10006). The worker's intermediary should consider whether Chapter 8, Part 2, ITEPA 2003 applies for these engagements.*
>
> *"For more information on whether a company is UK resident see INTM120000*
>
> *"Chapter 10, Part 2 ITEPA 2003 uses the definition of permanent establishment at section 1141 Corporation Tax Act 2010. For the purposes of Chapter 10, the reference to company in the Corporation Tax Act should also be read as a reference to persons that are not companies. A permanent establishment includes a fixed place of business which includes, amongst others, a branch, an office or a factory. A permanent establishment can also be any agent who has, and habitually exercises, authority to do business on behalf of the client. INTM153060 gives some further detail. If a worker provides services to an offshore client through a UK resident intermediary, that UK intermediary is not a permanent establishment of the offshore client for the purposes of Chapter 10, Part 2 ITEPA 2003.*
>
> *"If the client is based overseas but has a UK connection through a permanent establishment such as a branch, it is the overseas client who is responsible for discharging its responsibilities (such as issuing an SDS). If the overseas client does not meet its*

responsibilities it will, as a consequence, be liable for tax and NICs where the rules apply, and HMRC will pursue this debt through the UK permanent establishment.".

HMRC's response:

See response to Scenario 4. In either case, where the conditions at section 26A ITEPA 2003 are met, section 690 may apply.

Scenario 6

German resident client engages contractor's PSC via an agency.

Agency, contractor and contractor's PSC are resident in UK.

All duties are performed in UK.

Q6: What are the client's off-payrolling obligations?

Suggested response

17. Following FA20 deleting s61R(7) ITEPA03 and inserting s60I we consider that in this scenario the obligation to determine whether the engagement is within IR35 falls on the PSC in the same way as if the client were small (ie Chapter 8 ITEPA03 applies).
18. It will be necessary to ensure that the duties of the contractor do not give rise to the creation in the UK of a permanent establishment of the client.

HMRC's guidance:

ESM10025 states:

"Client wholly overseas

"Where a medium or large-sized non-public sector client is based wholly overseas, so there is no UK connection in the form of being UK resident or having a permanent establishment then the rules at Chapter 10, Part 2, ITEPA 2003 do not apply (see ESM10006). The worker's intermediary should consider whether Chapter 8, Part 2, ITEPA 2003 applies for these engagements."

HMRC's response:

See response to Scenario 4.

SECTION B: OFF-PAYROLL RULES AND INTERACTION WITH S689 ITEPA 2003

How do the off-payroll rules interact with the "Host employer rules" in S689 ITEPA 2003?

Consider the scenario where the contractor and the contractor's PSC are both non resident but the client is UK resident and contracts directly with the PSC. The contractor does carry out the engagement in the UK.

If the client correctly issues a determination that the engagement is outside the off-payroll rules, can there be a charge under the "Host employer" rules in S689 ITEPA 2003?

Under this scenario there can be a charge under S689 ITEPA 2003 if the PSC pays employment income to the contractor in respect of the services performed under the engagement because the conditions of S689 ITEPA 2003 would be met.

There would not be a charge under S689 ITEPA 2003 in respect of the payments made by the end client because the end client cannot be regarded as an employer if the SDS stating that the engagement is outside the off-payrolling rules is correctly issued. The SDS is issued based on looking at a hypothetical contract between the contractor and the end client. If that is not regarded as a deemed employment any payments made under that engagement cannot be regarded as employment income and consequently the host employer rules cannot bite because the condition in S689 (1) (b) ITEPA 2003 that

> *"any payment of, or on account of, PAYE income of the employee….."*
> is not met.

Now consider the situation where the end client, contractor, and the contractor's PSC are all non resident. The client although non resident has a UK branch and contracts directly with the PSC. The contractor does carry out the engagement in the UK.

The payments by the end client to the contractor's PSC would potentially appear to be within S689 ITEPA 2003. If the end client has issued a SDS to say that the contractor should be subject to withholding we could have withholding due to the Off-payroll rules and S689 ITEPA 2003.

If the end client has determined that the contract for services is not within the off-payrolling rules could withholding be due to S689 ITEPA 2003?

S689 (1) uses the phrase "works for". Works for is broader than working as an employee but there has to be a payment of PAYE income and if the end client has correctly determined that the contract is outside the PAYE rules the payment from the end client to the PSC cannot be considered PAYE income. This is not however the end of the analysis. If the PSC pays the contactor any "PAYE income" "in respect of the period that the contractor works for the end client, a withholding obligation can arise under S689 ITEPA 2003 on the contractor's PSC.

HMRC's response:

Section 689 ITEPA 2003 concerns the PAYE treatment of payments received by an employee of a non-UK resident employer who provides services to a person in the UK, and applies when the non-UK resident employer pays the employee employment income that is in respect of the services performed.

HMRC is first asked to consider the scenario where the worker and their PSC are both non-UK resident, but the client is UK resident and directly engages the PSC to carry out services wholly in the UK.

Where the worker is an employee of their non-UK resident PSC and works for a UK resident client in the UK, and the PSC pays the worker a salary in respect of that work, the UK resident client will be regarded as the 'host employer' and be required to operate PAYE on the amount of that salary

under section 689. However, if the PSC pays the worker via dividends, section 689 will not apply. This is regardless of whether the client has determined that the worker falls outside the off-payroll working rules.

If the engagement is determined to be inside the off-payroll working rules, PAYE will already be operated by the UK resident client on the deemed direct payment under Chapter 10 of Part 2 ITEPA 2003. Section 61W provides that the payment shall not be subject to income tax again when paid by the PSC to the worker. Therefore, section 689 would not apply in relation to such a payment.

HMRC is then asked to consider the scenario above if the client is instead non-UK resident, but with a permanent establishment in the UK.

The position would be the same as in the scenario above, as the client would have a tax presence in the UK. It would be necessary to consider whether the relevant conditions for section s689 to apply are met, as well as whether the engagement is within the off-payroll working rules.

It is worth noting that section 689 will not apply at the time the client pays the PSC, but at the time the PSC pays the salary to the worker.

SECTION C: OFF-PAYROLL RULES AND THE INTERACTION WITH TREATIES

HMRC guidance at ESM10025 is clear that:

> "*Where a medium or large-sized non-public sector client is based wholly overseas, so there is no UK connection immediately before the beginning of the tax year because it is not UK resident and does not have a UK permanent establishment, then the rules at chapter 10, part 2 ITEPA 2003 do not apply".*

It is then the responsibility of the PSC to determine whether the IR 35 rules apply.

HMRC guidance on the meaning of a permanent establishment at ESM10025 explains that:

> *"Chapter 10, Part 2 ITEPA 2003 uses the definition of permanent establishment at section 1141 Corporation Tax Act 2010. For the purposes of Chapter 10, the reference to company in the Corporation Tax Act should also be read as a reference to persons that are not companies. A permanent establishment includes a fixed place of business which includes, amongst others, a branch, an office or a factory. A permanent establishment can also be any agent who has, and habitually exercises, authority to do business on behalf of the client. INTM153060 gives some further detail.".*

Helpfully the guidance continues to explain that:

> *If a worker provides services to an offshore client through a UK resident intermediary, that UK intermediary is not a permanent establishment of the offshore client for the purposes of Chapter 10, Part 2 ITEPA 2003.".*

What is the position, however, if we have a UK resident individual with a UK resident PSC which contracts directly with an overseas client who has a UK branch? Again, HMRC guidance is clear that the end client is within the off-payrolling rules. HMRC guidance at ESM10025 explains that:

> *"If the client is based overseas but has a UK connection through a permanent establishment such as a branch, it is the overseas client who is responsible for discharging its responsibilities (such as issuing a SDS). If the overseas client does not meet its responsibilities it will, as a consequence, be liable for tax and NICs where the rules apply,* ***and HMRC will pursue this debt through the UK permanent establishment."***
> [Emphasis added]

In the above scenario with an offshore end client with a UK branch it is clear that the rules governing the withholding operate as if the offshore client was in the UK. If HMRC pursues the branch for the income tax and NIC debt through the branch, would HMRC allow a deduction in the branch accounts for the debt if the engagement had been with the overseas headquarters?

Now consider the same situation but that the individual contractor and the PSC is a Dual Resident of the UK and France whilst the end client is a German entity. The contractor is treaty resident in France.

Let us also assume that none of the services/duties are carried out in the UK. If an SDS is issued that says the individual is within the off-payroll regime and a deemed employee, how does the contractor report his income? Is the employer for the purposes of article 15 of the UK/French treaty the German entity? In other words, can the individual exempt from UK taxation the income received because the employer is viewed for treaty purposes as the German entity?

Our analysis:

Deeming provisions and the interaction with a treaty were discussed in the Supreme Court decision *Fowler v Commissioners for Her Majesty's Revenue and Customs* [2020] UKSC 22 (20 May 2020). That case ignored the deeming provision when interpreting the treaty but they did so because:

> *"section 15 creates this fiction not for the purpose of deciding whether qualifying employed divers are to be taxed in the UK upon their employment income, but for the purpose of adjusting how that income is to be taxed, specifically by allowing a more generous regime for the deduction of expenses."*

and

> "*Section 15, understood in the light of section 6(5) of ITEPA, charges income tax on the employment income of an employed diver, but in a particular manner which includes the fiction that the diver is carrying on a trade".*

Consequently, we do not think that that decision necessarily means you always ignore deeming provisions particularly as the judgement summarised the approach to deeming provisions as follows:

> *"(1) The extent of the fiction created by a deeming provision is primarily a matter of construction of the statute in which it appears.*
>
> *(2) For that purpose the court should ascertain, if it can, the purposes for which and the persons between whom the statutory fiction is to be resorted to, and then apply the deeming provision that far, but not where it would produce effects clearly outside those purposes.*
>
> *(3) But those purposes may be difficult to ascertain, and Parliament may not find it easy to prescribe with precision the intended limits of the artificial assumption which the deeming provision requires to be made.*
>
> *(4) A deeming provision should not be applied so far as to produce unjust, absurd or anomalous results, unless the court is compelled to do so by clear language.*
>
> *(5) But the court should not shrink from applying the fiction created by the deeming provision to the consequences which would inevitably flow from the fiction being real. As Lord Asquith memorably put it in East End Dwellings Co Ltd v Finsbury Borough Council [1952] AC 109, at 133:*
>
> > *"The statute says that you must imagine a certain state of affairs; it does not say that having done so, you must cause or permit your imagination to boggle when it comes to the inevitable corollaries of that state of affairs."*

The discussion of the treaty in the case explained that:

> *"Article 3(2) is all-important: "As regards the application of the provisions of this Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which this Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State."*

and

> *"The OECD Commentaries are updated from time to time, so that they may (and do in the present case) post-date a particular double taxation treaty. Nonetheless they are to be given such persuasive force as aids to interpretation as the cogency of their reasoning deserves: see Revenue and Customs Comrs v Smallwood (2010) 80 TC 536, para 26(5) per Patten LJ. Existing UK authority gives some relevant general guidance on the interpretation of double taxation treaties. In Comrs for Her Majesty's Revenue and Customs v Anson [2015] STC 1777 this court was considering the UK / USA Treaty. It was common*

ground that article 31 of the Vienna Convention applied. At paras 110-111, giving the leading judgment, Lord Reed said:

> *"Article 31(1) of the Vienna Convention requires a treaty to be interpreted 'in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose'. It is accordingly the ordinary (contextual) meaning which is relevant. As Robert Walker J observed at first instance in Memec [1996] STC 1336 at 1349, 71 TC 77 at 93, a treaty should be construed in a manner which is 'international, not exclusively English'.*
>
> *[111] That approach reflects the fact that a treaty is a text agreed upon by negotiation between the contracting governments. The terms of the 1975 Convention reflect the intentions of the US as much as those of the UK. They are intended to impose reciprocal obligations, as the background to the UK/US agreements from 1945 onwards makes clear.".*

If we look at the OECD commentary on article 15 it explains that:

"8.1 It may be difficult, in certain cases, to determine whether the services rendered in a State by an individual resident of another State, and provided to an enterprise of the first State (or that has a permanent establishment in that State), constitute employment services, to which Article 15 applies, or services rendered by a separate enterprise, to which Article 7 applies or, more generally, whether the exception applies. While the Commentary previously dealt with cases where arrangements were structured for the main purpose of obtaining the benefits of the exception of paragraph 2 of Article 15, it was found that similar issues could arise in many other cases that did not involve tax- motivated transactions and the Commentary was amended to provide a more comprehensive discussion of these questions.

8.2 In some States, a formal contractual relationship would not be questioned for tax purposes unless there were some evidence of manipulation and these States, as a matter of domestic law, would consider that employment services are only rendered where there is a formal employment relationship.

8.3 If States where this is the case are concerned that such approach could result in granting the benefits of the exception provided for in paragraph 2 in unintended situations (e.g. in so-called "hiring-out of labour" cases), they are free to adopt bilaterally a provision drafted along the following lines:

> *Paragraph 2 of this Article shall not apply to remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State and paid by, or on behalf of, an employer who is not a resident of that other State if:*
>
> *a) the recipient renders services in the course of that employment to a person other than the employer and that person, directly or indirectly, supervises, directs or controls the manner in which those services are performed; and*
>
> *b) those services constitute an integral part of the business activities carried on by that person.*

8.4 In many States, however, various legislative or jurisprudential rules and criteria (e.g. substance over form rules) have been developed for the purpose of distinguishing cases where services rendered by an individual to an enterprise should be considered to be rendered in an employment relationship (contract of service) from cases where such services should be considered to be rendered under a contract for the provision of services between two separate enterprises (contract for services). That distinction keeps its importance when applying the provisions of Article 15, in particular those of subparagraphs 2 b) and c). Subject to the limit

described in paragraph 8.11 and unless the context of a particular convention requires otherwise, ***it is a matter of domestic law of the State of source to determine whether services rendered by an individual in that State are provided in an employment relationship*** *and that determination will govern how that State applies the Convention.* [Emphasis added]

8.5 In some cases, services rendered by an individual to an enterprise may be considered to be employment services for purposes of domestic tax law even though these services are provided under a formal contract for services between, on the one hand, the enterprise that acquires the services, and, on the other hand, either the individual himself or another enterprise by which the individual is formally employed or with which the individual has concluded another formal contract for services.

8.6 In such cases, the relevant domestic law may ignore the way in which the services are characterised in the formal contracts. It may prefer to focus primarily on the nature of the services rendered by the individual and their integration into the business carried on by the enterprise that acquires the services to conclude that there is an employment relationship between the individual and that enterprise.

8.7 ***Since the concept of employment to which Article 15 refers is to be determined according to the domestic law of the State that applies the Convention*** *(subject to the limit described in paragraph 8.11 and unless the context of a particular convention requires otherwise), it follows that a State which considers such services to be employment services will apply Article 15 accordingly. It will, therefore, logically conclude that the enterprise to which the services are rendered is in an employment relationship with the individual so as to constitute his employer for purposes of subparagraphs 2 b) and c). That conclusion is consistent with the object and purpose of paragraph 2 of Article 15 since, in that case, the employment services may be said to be rendered to a resident of the State where the services are performed.* [Emphasis added]

8.8 As mentioned in paragraph 8.2, even where the domestic law of the State that applies the Convention does not offer the possibility of questioning a formal contractual relationship and therefore does not allow the State to consider that services rendered to a local enterprise by an individual who is formally employed by a non-resident are rendered in an employment relationship (contract of service) with that local enterprise, it is possible for that State to deny the application of the exception of paragraph 2 in abusive cases."

Based on the above we have concluded that because:

- the off-payrolling rules are viewing the relationship as one of employment with the end client,
- the deeming is determining the reality of the position, and
- the UK is making that determination,

the UK should allow treaty relief.

If the individual was treaty resident in the UK, then the UK would allow a credit for any French and or Germen taxes paid. This would be if the income was taxed in those countries as employment Income or profits of a business.

HMRC's response:

The scenario underlying the ICAEW's questions is one where the individual contractor is dual resident in the UK and France, is engaged with a client in Germany who has a UK branch, and carries out no duties in the UK. You ask whether, in this situation, the individual could claim relief under the UK-France Double Taxation Agreement (DTA) for the UK tax charged on the deemed direct payment under the off-payroll working rules.

HMRC’s view is that, although the OECD Commentary is written from the perspective of the source state, the deeming provision should not be ignored when considering the application of the treaty. So, as the UK treats the relationship as one of employment under the off-payroll working rules, we consider that the employment income article (article 15) in the treaty would apply in these circumstances. This article would not give the UK a taxing right over the income. This outcome would be consistent with the treatment where an individual who is treaty resident in France is employed directly by a German client and exercising the employment there.

Where the individual is instead treaty resident in the UK, whether a foreign tax credit would be allowed would depend on what the specific treatment of the income is in France and Germany in respect of the engagement.

This view is based on the specific scenario outlined. However, the application and interpretation of any Double Taxation Agreement will be determined by the facts of each individual case.

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