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Expatriate taxation in the United Kingdom and Germany

The taxation of an expatriates' employment income in Europe varies significantly from one country to another. This article summarises the differences in the UK and German treatments of such income.

As a general rule an expatriate will become liable to tax on his employment income in the state in which he is sent to work. Social security contributions in Europe are now rarely an issue for expatriates as reciprocal agreements often offer protection for short term employment secondments.

In both the UK and Germany the taxation liability for an expatriate employee hinges on tax residence as well as the elements of a remuneration package.

It is fair to say that a Japanese expatriate who works in either the UK or Germany for a very short period (less than 6 months) will probably not become resident in either jurisdiction. Although in theory they are subject to tax where the duties are performed, in most cases they will be able to obtain relief through the Double Tax Treaty with Japan.

Once tax residence is established in either the UK or Germany the differences are more pronounced.



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The UK has different categories of residence and the way in which an individual is taxed depends on which category they fall into. These are considered more fully below. In Germany, on the other hand, you are either resident or not; once resident, an expatriate is taxable on their worldwide income.

The UK is unusual in that taxation of employment income not only depends on residence, but also on an individual's domicile. A non UK domicile status gives a significant potential tax advantage. An individual acquires a "domicile of origin" at birth which is retained unless he takes a domicile of choice or dependency. It is extremely difficult to displace one's domicile of origin. Domicile is not determined by physical presence but more closely tied to where an individual belongs and considers to be his natural home. It is often described as "where your heart belongs" thus most Japanese nationals on secondment retain a domicile of origin in Japan.

The UK has two classes of tax residence which are determined both by physical presence and by intentions on arrival in the UK. Although a highly complex area, an individual who comes to the UK with the intention of staying less than 3 years would normally be classified as resident but not ordinarily resident from the date of arrival, provided he spends at least 183 days per tax year in the UK. If he intends to stay for more than 3 years, he will be both resident and ordinarily resident from arrival. Once a non-ordinarily resident individual has been present in the UK for 3 years he will be treated as ordinarily resident from the beginning of the tax year following the third anniversary of his arrival. The taxation implications of each of the above residence categories for a non domiciled employee can be summarised in the following table.



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| | | Duties of employment performed wholly or partly in the UK | | Duties of employment performed wholly outside the UK |
|--------------------------|---|---|------------------------------|--|
| | | In the UK | Outside the UK | |
| Overseas employer | Employee resident and ordinarily resident in the UK | Liable | Liable | Liable if received in the UK |
| | Resident but not ordinarily resident | Liable | Liable if received in the UK | Liable if received in the UK |
| | Not resident | Liable | Not liable | Not liable |
| UK employer | Resident and ordinarily resident | Liable | Liable | Liable |
| | Resident but not ordinarily resident | Liable | Liable if received in the UK | Liable if received in the UK |
| | Not resident | Liable | Not liable | Not liable |

It should be noted that remuneration for duties performed outside the UK can be outside the scope of UK taxation in certain circumstances and therefore with appropriate structuring such individuals can mitigate their tax burden.

The above is only a summary and is not intended to be relied upon as constituting tax advice. No liability can be accepted by the author or Greenback Alan LLP for an act, or omission to act, based on this article.



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On the other hand Germany imposes tax on an expatriate's worldwide income once he becomes resident in Germany. Residence is defined as having a customary abode in Germany. Normally this requires the individual to have accommodation available for his use and to be physically present in Germany for at least 6 consecutive calendar months. Individuals who are not resident are subject to tax only in respect of German duties.

Both countries define taxable employment income to include not only cash but also benefits-in-kind e.g. overseas adjustments, cost of living allowances, education and home payments are all taxable. The measure of a benefit in kind is usually the cost to the employer or a cash equivalent. However in some cases certain benefits in kind are subject to tax under specific legislation. E.g. in both jurisdictions company cars provided by their employer are taxed by reference to a percentage of their market value. It should be noted that exceptionally, Germany exempts from tax the rental of a German apartment. In the UK, apart from short term secondments of less than 2 years, accommodation provided is a taxable benefit.

The effective rates of tax vary between 20% - 40% in the UK and 15% - 42% in Germany. In addition Germany levies Solidarity and Church Taxes which raise the effective highest rate to in excess of 50%. Each country has a system of allowances and exemptions which allow an element of pay to be received tax free and it should not be overlooked that often expatriates are tax protected so that the effective rates on a 'net to gross' calculation appear higher.



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In conclusion it is clear that the taxation regimes of both countries, although complex offers opportunity for tax savings and many pitfalls. No two situations are similar and we therefore recommend that professional advice is sought each time.