

Tax-free Christmas parties

Although the tax legislation contains an exemption to prevent employees from suffering a benefit-in-kind tax charge on the staff Christmas party, the exemption is limited in scope and application. It is unwise to assume that there will be no tax to pay – without proper planning, an unwanted tax charge may accompany the post-party hangover.

Nature of the exemption

The exemption applies to an annual party or similar function which is provided to the employer's employees generally, or to those at a particular location. Where only one annual party or similar function is provided in the tax year, no income tax liability arises as long as the cost per head figure does not exceed £150. Where more than one such function is provided in the tax year, the exemption applies if the cost per head of the exempt party or parties does not exceed £150 in aggregate.

Trap 1 – annual functions only

The first trap is that the exemption applies only to annual functions – i.e. functions that are held each year. Thus, the staff Christmas party or annual summer barbecue may qualify, but a one-off event, such as party to celebrate the company's 10-year anniversary, will not.

Where the function is not an annual function, a benefit in kind charge may arise. However, if the cost is less than £50 per employee, it may fall within the trivial benefits exemption.

Trap 2 – all employee condition

The exemption only applies if the party is open to all employees, or to those at a particular location. So, for example, if the company has sites in Birmingham and Manchester, an annual Christmas party for the Manchester-based employees would be permitted under the terms of the exemption, a party to which only directors and senior managers were invited would not.

Trap 3 – exemption capped at £150 per head

The exemption is limited to £150 per head. There are several points to note as regards to this condition.

The first is that the cap is applied per head, not per employee. The cost per head figure is found by dividing the total cost of providing the function by the number of people attending the function – employees and guests. The total cost of the function includes not only the expenses of providing the function itself, but also the cost of any transport and accommodation which may also be provided. The cost is inclusive of VAT – even if this is subsequently reclaimed.

Thus if the total cost of a function is £5,440 and it is attended by 38 employees and 30 guests at a total of 68 people - the cost per head figure is £80 per head ($£5,440 \div 68$).

The second point to note is that the exemption is not a tax-free allowance – if the cost per head figure is more than £150, the whole amount is taxed, not just the excess over £150. Where, say, the cost per head is £175 and an employee brings a guest, the amount of the benefit on which the employee is taxed is £350 (employee plus their guest).

Where there is more than one qualifying function, the exemption can be used to best effect. So, if an employee attends three functions with cost per head figures of £80, £60 and £65, best use may be to

use the exemption for the functions costing £80 and £65 per head. The remaining £5 is lost as it cannot be set against the cost of the £60 per head function.

Tip

Remember to consider the impact of guests – in the above example, if the £65 function was for employees only but the £60 function was for employees and guests, it would be better to use the exemption for the £80 and £60 functions, leaving the £65 function in charge. If the £60 function was left in charge, the cash equivalent of the benefit would be £120 for the employee and guest – which is more than £65.

Any tax liability could potentially be met by the employer via inclusion in a PAYE Settlement Agreement.