TAXREP 29/01

NIC: MILEAGE ALLOWANCES AND PASSENGER PAYMENTS

Memorandum submitted in November 2001 to the Revenue by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to an invitation to comment originally issued in August 2001

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NIC: MILEAGE ALLOWANCES AND PASSENGER PAYMENTS

INTRODUCTION

1. We welcome the opportunity to comment on draft regulations. We welcome also the adoption of the tax law rewrite style in the drafting.

EXECUTIVE SUMMARY

2. Any national insurance contributions ('NIC') charge on excess mileage allowance and passenger payments should be to Class 1A rather than Class 1.

3. The draft regulations fail to recognise the heavy additional compliance costs for employers. In particular:
   - charging the excess payments to Class 1 rather than Class 1A which will mean that the cost to business of complying will be out of proportion to the cash benefit to the Exchequer;
   - the mileage breakpoint which can necessitate significant additional record-keeping which will be a further heavy compliance burden; and
   - the absence of provisions to cater for instances where mileage payments are made in an earnings period other than the one in which the journey was made (especially as this will be the almost universal circumstance) particularly where there has been a change in the mileage rates in the meantime.

4. A Class 1A charge would significantly reduce these burdens.

5. In addition, the provision in the regulations for a NIC charge on excess payments with no compensating allowance for payments of less than the statutory limits does not achieve the symmetry that the notes to the regulations suggest is being aimed for.

CONSULTATION PROCEDURES

6. We are concerned that the text of the draft regulations as published on the Revenue's website was changed significantly during the consultation period without any mention of this fact and without highlighting the changes. Clearly consultation is unlikely to be very effective if some respondents are commenting on one document and others on another. Furthermore, some of our concerns on the draft do not arise on the original one. It may well be therefore that some people who have not raised points because they were happy with the original draft would have wanted to comment on the revised one.

7. Those interested in commenting on draft legislation cannot be expected continuously to revisit the Revenue's website to check if the draft has changed.

8. We accept that if a draft is thought to be defective after it has been published it would be wrong to allow consultation on that draft to continue. On the other hand we consider that the Revenue have a responsibility to try as much as possible to bring any changes to the attention of respondents. In particular, the Revenue are aware that professional bodies such as the Tax Faculty normally comment on virtually all consultation documents and we believe that it would have been sensible to alert them to the changes.

9. For the avoidance of doubt, we attach as an annex the version of the draft regulations that we are commenting on. It is disappointing that it is necessary to do this.

DETAILED COMMENTS

Class 1 NIC compliance problems

10. In the context of the expressed aim of the Government to achieve the same treatment for tax and NIC (as noted in the first paragraph of the introduction to the draft regulations), we are disappointed that the NIC is chargeable under Class 1. Whilst we accept that it is arguable that the excess payment constitutes pay for PAYE purposes, we believe that the better argument is that it does not do so. In practice mileage payments are invariably treated for income tax purposes as P11D items. Charging them to Class 1 NIC will be extremely burdensome to employers, not only because it creates a difference in treatment for tax and NIC but also because such payments are invariably included as part of an employee's expenses claim and thus are not readily available when preparing the payroll.

Earnings periods

11. The very practical issue about charging such payments to Class 1 NIC is that it means that employers have to contend with earnings periods. Collecting and processing the relevant mileage/passenger etc information in time for any given payroll run is likely to be wholly impractical. This will be even more so for employers who use payroll bureaux, where in most cases payroll information has to be committed before the end of the earnings period. Furthermore, a number of payroll software systems may need integration with expenses claims and may not cope with the excess amount.

'Losses'

12. A particular problem of imposing a Class 1 charge is that the mileage allowance has a two-tier structure, the rate for the first 4,000 miles being higher than for subsequent miles. Many employers find it impractical to operate two rates and pay a single rate for all business mileage. This works satisfactorily on an annual basis as any underpayment in respect of the early miles is recouped against the overpayment on subsequent ones. With a Class 1A NIC charge this automatic correction would apply also for NIC. Using a Class 1 NIC charge there needs to be a provision in the legislation to enable the 'loss' on the early miles to reduce the taxable amount on later ones. The draft does not contain such a provision and thus does not achieve either symmetry or fairness.

13. By way of example, the statutory tax-free mileage rates will, from April 2002, be 40p a mile for the first 10,000 miles in the tax year and 25p a mile thereafter. Suppose that in 2002/03 an employee does 14,000 business miles, so the tax-free payments would total £(4,000 + 1,000) = £5,000. As the employer does not want to operate two rates, he estimates the business mileage in advance and sets a rate of 35p for all miles. The total payments to the employee are therefore £4,900.

14. £4,900 is less than £5,000 so there will be no income tax charge on the employee because the law provides that the year is considered as a whole (section 197AD(3), ICTA 1988).

15. However, the policy embodied in the draft regulations means that there would be NIC on the 10p excess over the statutory maximum paid for the 4,000 miles over the break point. The draft regulations prevent taking into account the 5p shortfall which arises on the first 10,000 miles. This is because the NIC regulations apply to each claim or each earnings period (week or month) separately, rather than to a year as a whole.

16. The decision to adopt a Class 1 rather than a Class 1A charge is particularly burdensome in such cases as it requires the employer to keep a running total of mileage payments for each employee so that he is aware in which pay period the 4,000-mile threshold is breached. It ironic that a Government that professes to be anxious to reduce burdens on business should require an employer to adopt a burdensome process that his own commercial procedures have been specifically designed to avoid. This problem would not arise under a Class 1A charge as all that would be then need to be identified is the total mileage.

Divergent business miles and miles for which mileage allowance paid

17. Some employers do not pay for all business mileage but offset the saving that an employee might incidentally achieve on his personal travel costs as a result of having to make the business journey. The income tax legislation recognises this by allowing the employee himself to claim tax relief for the extra mileage.

18. Whilst we recognise that it would be difficult to give such additional relief for NIC purposes under the Class 1 rules, this clearly ought to be done if symmetry is to be achieved. It would be relatively easy under a Class 1A charge as the employee need only notify the employer of the additional relief he intends to claim in his tax return to allow the employer to take this into account when ascertaining the NIC payment. As currently drafted the regulations do not address this problem at all.

19. Indeed, not only do the draft regulations provide that there is no relief for the 'loss' but they actually impose a charge. This arises because, in new regulation 7A, N is the number of business miles for which payment is made rather than the number of business miles driven. As an example, assume an employee makes a business journey of 200 miles in his own car but is allowed by his employer to claim only 170 miles to take account of normal home-to-work mileage and the per-mile rate paid by the employer is 50p per mile. The amount received by the employee from the employer will be 170 miles @ 50p = £85.00.

20. For tax purposes relief is due on 200 miles @ 40p = £80 so that he has made a 'loss' of £5 which can be set against his other income (assuming that his year-to-date mileage has not exceeded 10,000).

21. However for NIC, in new regulation 7A 'N' is 170 miles and 'R' is 40p and as under the formula the amount claimed of £85.00 exceeds the product of 170 x 40 = £68 by £17, NIC of £2.02 (secondary: employer at 11.9%) and a possible £1.70 (primary: employee at 10% if not contracted out) will be payable.

Change in allowable per-mile rates

22. Many payroll administration systems are not integrated as far as expenses and salaries are concerned and the costs for employers of re-writing computer programs to achieve integration, even if technically feasible, would be disproportionate.

23. There is also the question of what happens when payments to employees are made in a tax year different from that in which the journey was made. Logic would determine that whilst the rates of tax and NIC ruling at the time of payment should apply, the per-mile payment that the employee can claim is at the rate ruling at the time the journey was made.

24. There are many employers who currently pay 'own car' allowances greater than the 40p and 25p limits that will apply from 6 April 2002. The lowering for most types of car of the per-mile rate in 2002/03 will mean that employers will pay employees either at a lower per-mile rate than they were expecting when they did the travelling, which will at the very least have a detrimental effect on employer/ employee relationships, or at the rate ruling when the payment is made, which may result in an unintended tax and NIC liability.

25. In the light of this we would welcome confirmation that if employees are paid in a different tax year at the per-mile rate ruling when the journey was made, the Revenue will not seek to collect tax or NIC on the difference in mileage rates, particularly in the first year (2002/03). Not to do this will lead to additional burdens on business.

Secondary legislation

26. The effect of the proposed regulations will be to extend the definition of earnings in section 4, Social Security Contributions and Benefits Act 1992. Whilst we accept that section 4(6) provides the vires, in cases like this, where NIC is being imposed where there is not necessarily a true commercial profit to the employee, we consider that secondary legislation should not be used to extend the charge to NIC to what are effectively fictional 'earnings', because regulations are not subject to any meaningful scrutiny by Parliament. Primary legislation ought to be used for such changes, although we recognise that in this instance the time-frame is not good to amend the primary legislation as it will need a Social Security Bill, and Royal Assent to that would fall after 6 April 2002.

Impact on other payments

27. The proposed amendment in draft regulation 5(5) to Part 8 of Schedule 3, Social Security (Contributions) Regulations 2001 (SI 2001/1004) is indiscriminate as it could be used to affect other payments.

28. We consider that it should state: '(2) – Sub-paragraph (1) does not authorise the disregard of an amount specified in paragraphs (5) or (6) of regulation 22.'.

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PCB
2.11.01

ANNEX

CONSULTATION MATERIAL ON WHICH WE ARE COMMENTING [downloaded 15 October 2001]

Draft regulations for comment: national insurance contributions (NICs) on mileage allowance and passenger payments

Introduction

During debate in Finance Bill Standing Committee the then Financial Secretary Stephen Timms explained that the Government aims, as far as possible, to achieve the same treatment for NICs as for tax on payments that employees receive for using their own cars for business journeys.

The draft regulations, which amend the Social Security (Contribution) Regulations 2001, provide alignment for NICs with the new statutory tax free approved mileage rates and the 10,000 miles breakpoint introduced in the 2001 Finance Act. They also include alignment with the new 5p per mile passenger rate.

A technical amendment is also included to regularise the liability for NICs on fuel provided for use in a company car.

Approved mileage allowance payments

The draft regulations provide that mileage allowance payments which an employer pays to employees who use their own cars for business travel, are disregarded from earnings on which Class 1 NICs are due so long as they do not exceed the approved rates set out for income tax purposes in Schedule 12AA to the Income and Corporation Taxes Acts 1988 (ICTA 1988). These regulations place on a statutory basis the previous administrative arrangements applied to NICs of using the Inland Revenue's authorised mileage rates as a means of identifying whether a NICs liability arises on mileage allowances.

They also introduce for NICs the 10,000 business miles breakpoint. This means that employers will need to keep sufficient records of the mileage payments made to their employees to enable them to identify when the lower mileage rate needs to be applied to the NICs calculation.

Passenger payments

The regulations allow an employer to pay up to 5p per mile to an employee for carrying a passenger without incurring a NICs liability. The passenger must be an employee for whom the travel is business travel.

The regulations also disregard from earnings for Class 1 NICs purposes payments in respect of car fuel which are provided for use in a company car and on which a charge to income tax under section 158 of ICTA 1988 arises. The amendment confirms the current Class 1A NICs liability on these payments.

The regulations will come into force from 6 April 2002.

Consultation

Comments would be welcomed on these regulations. They should be sent to: mellanie.merrifield@ir.gsi.gov.uk by 31 October 2001

STA TU TORY I NSTRUMENT

2001 No.

SOCIAL SECURITY

The Social Security (Contributions) (Amendment No. 6) Regulations 2001

Made - - - - 2001
Laid before Parliament 2001
Coming into force - - 2001

The Treasury, with the concurrence of the Secretary of State in so far as required, in exercise of the powers conferred upon them by sections 3(2) and (3) and 4(6) and (7) of the Social Security Contributions and Benefits Act 1992(1) and, with the concurrence of the Department for Social Development in so far as required, in exercise of the powers conferred on them by sections 3(2) and (3) and 4(6) and (7) of the Social Security Contributions and Benefits (Northern Ireland) Act 1992(2) and of all other powers enabling them in that behalf, hereby make the following Regulations:

Citation, commencement and interpretation
1.—(1) These Regulations may be cited as the Social Security (Contributions) Amendment No.6) Regulations 2001 and shall come into force on .
(2) In these Regulations—
"the principal Regulations" means the Social Security (Contributions) Regulations 2001(3);
"regulation", without more, means a regulation of the principal Regulations; and
"Schedule", without more, means a Schedule to the principal Regulations.

Amendment of the principal Regulations
2. Amend the principal Regulations as follows.

3.—(1) Amend regulation 22 (payments to be treated as earnings) as follows.

(2) For the heading substitute—
"Amounts to be treated as earnings"

(3) In paragraph (1) for "paragraphs (2) to (4)" substitute "paragraphs (2) to (6)".

(4) At the end of the regulation add—
"(5) The amounts specified in this paragraph are—

(1) 1992 c.4. Section 3(2) was amended by paragraph 3 of Schedule 3 to the Social Security Contributions (Transfer of Functions, etc.) Act 1999 (c. 2)("the Transfer Act"), section 4(6) was substituted by section 74(3) of the Child Support, Pensions and Social Security Act 2000 (c.19) and subsection (7) was inserted by paragraph 1(3) of Schedule 3 to the Social Security Contributions (Transfer of Functions, etc.) Act 1999 (c. 47).

(2) 1992 c.7. Section 3(2) was amended by paragraph 4 of Schedule 3 to the Social Security Contributions (Transfer of Functions, etc.) (Northern Ireland) Order 1999 (S.I. 1999/ 671), section 4(6) was substituted by section 78(3) of the Child Support, Pensions and Social Security Act 2000, and section 4(7) was inserted by paragraph 2 of Schedule 3 to the Social Security Contributions (Transfer of Functions, etc.) (Northern Ireland) Order 1999 (S.I. 1999/ 671). The functions of the Department of Health and Social Services for Northern Ireland under the Social Security Contributions and Benefits (Northern Ireland) Act 1992 were transferred to the Department for Social Development by Article 8(b) of, and Part II of Schedule 6 to, the Departments (Transfer and Assignment of Functions) Order (Northern Ireland) 1999 (S.R. 1999 No. 481).

(3) S.I. 2001/1004.

(a) the amount of any mileage allowance payment; and
(b) the amount of any passenger payment,
to the extent that apart from this regulation those payments would not be earnings for the purposes of the Act.

In this paragraph—
"mileage allowance payment" has the meaning assigned by section 197AD(2) of the Taxes Act(4); and
"passenger payment" has the meaning given by section 197AE(2) of the Taxes Act(5).

(6) The amount specified in this paragraph is the amount equal to the cash equivalent, in respect of car fuel, which is chargeable to tax under Schedule E by virtue of section 158 of the Taxes Act.".

4. In Part V of Schedule 3 (non-cash vouchers to be disregarded as payments in kind) for paragraph 1(2) substitute—
"(2) A non-cash voucher may also be disregarded—
(a) by virtue of paragraph 7C of Part VIII (car fuel); or
(b) in the circumstances specified in paragraph 4 of Part X (payments by way of incidental expenses).".

5.—(1) Amend Part VIII of Schedule 3 (payments to be disregarded in the calculation of earnings for the purposes of earnings-related contributions: travelling, relocation and other expenses and allowances of the employment) as follows.

(2) After paragraph 7 insert—
"Mileage allowance payments
7A.—(1) So much of a mileage allowance payment as does not exceed—
N x **R**
Here—
N is the number of miles of business travel in respect of which the payment is made; and
R is the rate applicable for the time being in respect of the business travel and the qualifying vehicle in question in accordance with paragraph 4(2) of Schedule 12AA to the Taxes Act.
(2) In this paragraph—
"business travel" has the meaning given by paragraph 2 of Schedule 12AA to the Taxes Act(6)
"mileage allowance payment" has the meaning given by section 197AD(2) of the Taxes Act; and
"qualifying vehicle" has the meaning given by paragraph 3 of Schedule 12AA to the Taxes Act.
Passenger payments
7B.—(1) So much of a passenger payment as does not exceed—
N x A
Here—

(4) Section 197AD was inserted by section 57(1) of the Finance Act 2001 (c. 9).

(5) Section 197AE was inserted by section 57(1) of the Finance Act 2001.

(6) Schedule 12AA was inserted by section 57(2) of the Finance Act 2001.

N is the number of miles of business travel by the earner, by car or van, for which the earner carries a qualifying passenger in respect of which the payment is made; and
A is the rate applicable for the time being in respect of the carriage of a qualifying passenger under paragraph 5 of Schedule 12AA to the Taxes Act.
(2) In this paragraph—
"passenger payment" has the meaning given in section 197AE(2) of the Taxes Act;
"qualifying passenger" means the same as in paragraph 5 of Schedule 12AA to the Taxes Act;
Car fuel
7C.—(1) A payment by way of the provision of car fuel in circumstances where an amount is chargeable to income tax under Schedule E, in respect of its provision, under section 158 of the Taxes Act(7).
(2) Subsection (3) of section 158 of the Taxes Act applies for the construction of the reference to car fuel in sub-paragraph (1) as it applies for the construction of that section.".
(3) Renumber the existing paragraph 9 (specific and distinct expenses) as sub-paragraph (1) of that paragraph, and amend the paragraph in accordance with the following provisions of this regulation.
(4) At the end of sub-paragraph (1) (as renumbered in accordance with paragraph (3)) add—
"This is subject to the following qualification.".
(5) After sub-paragraph (1) (as renumbered in accordance with paragraph (3) and amended in accordance with paragraph (4)) add—
"(2) Sub-paragraph (1) does not authorise the disregard of a payment of a mileage allowance payment (within the meaning of section 197AD(2) of the Taxes Act) in an amount greater than that determined in accordance with paragraph 7A of Part VIII.".

Name

Name

Date Two of the Lords Commissioners of Her Majesty's Treasury
The Secretary of State hereby concurs.
Signed by authority of the Secretary of State
Name
Parliamentary Under-Secretary of State,
Department for Work and Pensions
The Department for Social Development hereby concurs.
Sealed with the Official Seal of the Department for Social Development on 2001.
(L.S.)

(7) Section 158 was amended by section 53(2)(b) of the Finance Act 1989 (c. 26), section 53 of the Finance (No.2) Act 1992 (c. 48), paragraphs 1, 6(2) and 7 of Schedule 3 to the Finance Act 1993 (c. 34), paragraph 22 of Schedule 3 to the Vehicle Excise and Registration Act 1994 (c. 22), section 43(2) and (4) of the Finance Act 1995 (c. 4) and S.I. 2001/635

Senior Officer of the Department for Social Development

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Social Security (Contributions) Regulations 2001 (S.I. 2001/1004)("the principal Regulations") .

Regulation 1 provides for the citation and commencement of these Regulations and provides definitions for certain terms used in them.

Regulation 2 introduces the amendments made by these Regulations to the principal Regulations.

Regulation 3 amends regulation 22 of the principal Regulations (payments to be treated as earnings) by adding a new paragraph which treats mileage allowance payments (as defined in section 197AD(2) of the Income and Corporation Taxes Act 1988 (c.1) ("the Taxes Act") and passenger payments (as defined in section 197AE(2) of the Taxes Act) as earnings, to the extent that they would not otherwise be so treated. It inserts a new paragraph which brings into charge to Class 1A contributions the amount equal to the cash equivalent for car fuel provided for use by an employee which is charged to tax under section 158 of the Taxes Act. It also makes a consequential amendment.

Regulation 4 amends paragraph 1(2) of Part V of Schedule 3 to the principal Regulations to make it clear that a payment by way of the provision a non-cash voucher for car fuel is disregarded for the purposes of computing liability for Class I contributions where the car fuel attracts a charge under section 158 of the Taxes Act.

Regulation 5 amends paragraph Part VIII of Schedule 3 to the principal Regulations. It inserts three new paragraph 7A to 7C. The new paragraphs 7A and 7B provide for the disregard of approved mileage allowance payments (within the meaning of section 197AD of the Taxes Act), qualifying passenger payments (within the meaning of section 197AE of that Act). Paragraph 7C disregards a payment by way of provision of car fuel for the purposes of liability for Class 1 contributions where income tax is chargeable under section 158 of the Taxes Act in respect of its provision.

Regulation 5 also amends paragraph 9 of that Part (specific and distinct payments of expenses to be disregarded in the calculation of earnings for the purposes of earnings-related contributions). This amendment makes it clear that the disregard contained in that paragraph does not authorise the disregard of a mileage allowance payment in an amount greater than that permitted under paragraph 7A.