



EMPLOYEE BENEFITS AND EXPENSES – EXEMPTION FOR PAID OR REIMBURSED EXPENSES

ICAEW welcomes the opportunity to comment on the consultation paper *Employee benefits and expenses – exemption for paid or reimbursed expenses* published by HM Revenue & Customs on 18 June 2014.

This response of 10 September 2014 has been prepared on behalf of ICAEW by the Tax Faculty.

Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

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MAJOR POINTS

Introduction

1. We welcome the opportunity to comment on the proposals in HMRC's consultation document of 18 June 2014.
2. We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. In 2013 we gave evidence in meetings to the Office of Tax Simplification to help them compile their [interim report on employee BiK and expenses](#) published on 8 August 2013 and their [second report \(formerly called final report\) on employee BiK and expenses](#) published on 14 January 2014. Since then, OTS published on 18 July a note on HMRC's condox on employee BiK published in June 2014 (including this one) and on 31 July another [final report](#).

Key point summary

4. We welcome the proposal to replace dispensations, and the need for deductible expenses not covered by dispensations to be entered on forms P11D by the employer and then subjected to a deductions claim by employees, with an exemption for deductible expenses. This will simplify compliance and administration for employers, employees and HMRC.
5. We recommend that:
 - Employers should be encouraged to claim expenses on the basis of benchmark scale rates set at reasonable amounts and not hedged around with conditions so onerous that simplification is not in practice achieved.
 - Expenses should be able to be paid free of tax and NIC up to the benchmark scale rates, and where employees comply with conditions laid down by employers, eg they are not at a permanent workplace, there should be no need to obtain and retain a receipt.
 - HMRC should publish benchmark scale rates, and keep them updated, perhaps linked to inflation.
 - We believe that custom scale rates will need to continue to be able to be negotiated because different industries have different circumstances, but having a wide range of appropriately set benchmark scale rates might help reduce the need for custom scale rates.
 - Micro businesses and one person companies should be included in the new regime.
 - Rules designed to discourage salary sacrifice expense arrangements should not inadvertently outlaw flex benefit arrangements, under which employers motivate employees by allowing them to swap cash salary for benefits-in-kind. More rigorous enforcement by HMRC of national minimum wage rules would help to identify instances where taxable and NIC-able salary is being unlawfully converted into tax and NIC-free expenses, and cases where employees' entitlement to state pension and other contributory state benefits is being jeopardised.
 - Existing dispensations and local agreements should continue until the underlying circumstances or law changes – this will help ease the transition, especially (we would have thought) for HMRC.
 - HMRC should publish very clear and comprehensive guidance and keep it updated.
 - We suggest that consideration be given to streamlining and aligning NIC and tax rules, as this would make it simpler for employers to comply and HMRC to draft guidance that is easy to follow.
 - The new regime should not start until the law is certain, and HMRC has amended and tested its new processes and drafted and consulted on guidance. This suggests that the change should not be before 6 April 2016, because many employers – and HMRC – are still trying to get to grips with PAYE real time information; the onshore and offshore intermediaries rules; split years under the statutory residence test; and auto-enrolment.

General comments

6. We welcome the proposal to introduce an exemption for allowable expenses that are paid or reimbursed by employers. We also welcome that that exemption will apply to all qualifying expenses paid or reimbursed by an employer and that it will cover all employers rather than be opt in or out. We believe that the spirit of the proposals aligns with what happens in practice by and large, which is that employers do monitor expenses to ensure that only business expenses incurred by employees are reimbursed.
7. This will replace the current dispensation regime and, for those employers without dispensations, will save them from having to enter expenses on form P11D and employees from having to make deduction claims under section 336 Income Tax (Earnings and Pensions) Act (ITEPA) 2003. It will also avoid HMRC having to include in code numbers expenses which although on P11D are in fact deductible: we therefore trust that this will lead to many more accurate code numbers. The amount of time that is currently spent having tax codes corrected is disproportionate, so the proposed exemption will save considerable amounts of time and therefore costs for employees, employers and HMRC.
8. As employers will have to decide, in effect in real time, whether expenses are exempt, it will be imperative for HMRC to provide clear guidance, suitable for the layman, on what expenses are and are not allowable and the tax and NIC treatment in such cases. HMRC will need to keep this guidance up to date to reflect change.
9. One point not raised in the condoc is that the tax and NIC rules for expenses are different. It is even more difficult to get it right first time when contracts, for example for telephone lines and calls, mobiles and broadband, are in the employee's own name. It would obviously help employers to apply the law correctly if tax and NIC rules were aligned, and it would also make it easier for HMRC to write guidance that can be understood by the typical employer.
10. We agree with the recommendation made by OTS at para 6.68 of its [second report](#) that many expenses for subsistence should be able to be claimed on the basis of benchmark scale rates with no need to obtain or retain a receipt when necessary conditions are met, for example the employee is at a temporary workplace. For many taxpayers, the benefit of certainty arising from being able to use scale rates will outweigh the fact that the scale rates may be less than what they might otherwise spend. Also many meals, especially lunches, are taken 'on the run', for example from burger vans, where receipts are unlikely to be available.
11. However, we believe that to get buy-in by employers into using scale rates, the UK benchmark scale rates need to be better aligned with prices in the real world and the conditions of use need to be more user-friendly.
12. In particular, we suggest that UK benchmark scale rates should include a rate for staying with family and friends. The reintroduction of such a rate would be welcomed by many employers as it will cost them less than hotel bills, and the exchequer would benefit as there will be a commensurate reduction in the cost of tax relief.
13. We recommend that to obviate the need to reinvent benchmark scale rates, civil service scale rates be published and be available for use by all employers.
14. Whilst HMRC should publish scale rates, this should not preclude claims for actual amounts spent if higher.
15. Current dispensations and local and collective agreements should continue until superseded by circumstances and changes in the law.

RESPONSES TO CONSULTATION QUESTIONS

Chapter 4: Assurance

Record keeping

Q1: If the Government were to provide ‘models’ of acceptable record keeping and checking processes would this be helpful for employers? Where the models are not appropriate for employers, would those employers feel disadvantaged, even if it is made clear that they are not exhaustive?

16. We think that it would be helpful for HMRC to provide guidance on what records it considers acceptable, provided that
- there is consultation on the models,
 - HMRC’s models are not prescriptive or rigid but are guiding principles,
 - the existence of HMRC models does not preclude employers from adopting other procedures more appropriate to their business (otherwise we foresee endless arguments), and
 - the models address the problems over getting receipts by allowing employers to pay up to amounts in benchmark scale rates when certain conditions are met, for example being away from the permanent workplace for a set number of hours, including reintroducing a benchmark scale rate for staying with family and friends.

Protection against abuse

Q2: Are you aware of any types of arrangement that seek to replace taxable pay with payments of non-taxable expenses which the Government should focus on in particular when tackling this issue? Are you aware of any types of these arrangements where tackling them might disturb business practices that are not tax or NICs motivated?

17. Our meetings with HMRC on false self employment and onshore and offshore employment intermediaries and evidence provided recently by HMRC to Parliamentary Committees suggest that HMRC is already aware of non-taxable expenses arrangements, for example, amongst umbrella companies.
18. We note that the government is concerned about expenses awarded in exchange for salary sacrifice and para 4.18 proposes a targeted anti abuse rule which would prevent salary sacrifice arrangements being used to pay expenses.
19. We suggest that more rigorous enforcement of the minimum wage (NMW) rules by HMRC would have multiple benefits, as this would help to ensure not only that low paid workers receive NMW but also are not being paid less than the national insurance lower earnings limit and thereby foregoing rights to contributory state benefits, including the NI retirement pension, as well as identifying cases of sacrificing salary for expenses contrary to government policy.
20. As to arrangements where tackling them might disturb business practices which are not tax or NIC motivated, we suggest, first, that specific local agreements between employers and HMRC should continue to be honoured and renegotiated as circumstances change.
21. Secondly we would mention here that many employers offer remuneration packages under which salary can be sacrificed in exchange for benefits so that the value of their employees’ remuneration is unaffected by whether they choose to take cash or one or more BiK from a list; these are sometimes referred to as flex benefits packages. The objective of these is to attract new staff and encourage existing staff. We would not like to see this motivational baby thrown out with the bathwater.

Chapter 5: Scale rates

Current scale rate process

Q3: In what circumstances would an employer currently apply for a custom scale rate? Other than the expenses covered by the benchmark scale rates, which expenses do employers commonly request a scale rate for?

22. An employer might apply for a scale rate to save costs, so that only amounts up to the scale rate are paid. Employers with large numbers of people working in central London temporary workplaces are likely to request custom scale rates because hotel rooms and subsistence cost more there than in the provinces.
23. An advantage of a scale rate is the certainty of treatment and the comfort employers get from having an agreed position with HMRC.
24. However, if simplification is to be achieved across the board then we believe that employers need to be encouraged to use the benchmark scale rates. To get buy-in by employers into using benchmark scale rates will necessitate UK benchmark scale rates to be better aligned with actual prices and the conditions of use to less restrictive. In addition, in contrast to the UK scale rates, there are scale rates for overseas accommodation, which includes a friend and family rate and a 'serviced flat' rate which it would be helpful to include in UK scale rates.
25. The benchmark scale rates conditions include:
 - The breakfast rate only applies if the employee has, exceptionally, left home before 6am;
 - a 'meal' includes food – it cannot just be drink, so you cannot just have, say, just a coffee or a milk shake; and
 - the employer has either written to HMRC and requested that these rates be used, or he has ticked the relevant box on the annual P11DX form – so what will be the new procedure?
26. In comparison with the rates for overseas, the UK ones are ridiculously low. For instance, for Australia the rates are \$44.95 for breakfast, with no requirement that you leave before 6am; and dinner in Austria is 45.5€, in Ottawa \$71.50, but in the UK only £15.
27. So if it really is the intention to simplify and stop every single meal having to be accounted for individually, then the scale rates and their conditions of use need to be reasonable.
28. We assume that expenses for which employers commonly request scale rates include subsistence and overnight accommodation, but we would have thought that HMRC would be best placed to answer this question.

Using custom scale rates under the exemption

Q4: Are there any examples of particular industries or types of employer who would be affected if custom scale rates could not be used with the proposed exemption? What would the impact be on those employers?

29. Industries that would be affected include local authorities and the construction industry, and any employer incurring expenses in London where costs are higher.
30. The impact on employers for whom custom scale rates are not available would presumably be the cost of more burdensome administration of expenses, potentially the additional cost of reimbursing employees, and if they are using a benchmarked scale rate, additional tax and NIC if they pay out amounts greater than the scale rate.

31. We consider that a scale rate should be effectively a limit below which expenses can be paid to an employee without supporting receipts, provided the employee satisfies the employer that he has complied with certain conditions, eg is away from a permanent workplace. If HMRC could publish scale rates, employers could then pay a scale rate to their employees of anything up to and including this amount without any reporting obligations. If they wanted to pay more than the HMRC published scale rate, they so could do, but any excess amount over and above the scale rate would have to be declared using a PAYE settlement agreement (PSA) type declaration. In other words, the excess amount paid over the scale rate would be subject to tax and NIC on the employer by way of the PSA, but there would be no other reporting requirement or taxable/NICable benefit.

Q5: Would employers be disadvantaged if a process to apply for custom scale rates were not retained? If such a process were retained, would it be seen as additional complexity by those employers who do not need it?

32. We believe that employers would be disadvantaged if a process to apply for custom scale rates was not retained, unless the benchmark scale rates reflect real costs, for example, distinguishing between London and the provinces, and are updated regularly. Being able to reference claims to publicly available scale rates makes it easier for employers to control employees' expenditure.
33. We suggest that a combination of the second and third approaches noted in para 5.11 (a specific mechanism for agreeing scale rates, and a self-certification process) be adopted.
34. We do not think that employers who do not use it would see it as additional complexity – it would just be a part of the system that they do not use.

Q6: Would employers welcome the ability to self-certify the sampling exercise undertaken to support a custom scale rate? If so, would a sampling process set out in guidance or regulations provide sufficient certainty for employers that wish to use a custom scale rate?

35. We believe that employers would welcome the ability to self sample.
36. It would be helpful for HMRC to provide guidance on the self sampling processes that it considers acceptable, provided that
- there is consultation on the guidance and proposed self sampling processes,
 - HMRC's guidance is not prescriptive or rigid but is more in the way of guiding principles, and
 - the existence of HMRC preferred self sampling processes does not preclude employers from adopting other processes more appropriate to their business (otherwise we foresee endless arguments).

Micro companies and directors of close companies

Q7: What are the reasons for one person companies and very small, close companies paying scale rates to directors in respect of expenses? Would such employers be disadvantaged if they were not permitted to pay scale rates to their directors under the proposed exemption? If so in what way?

37. We see no reason why one person companies should not be able to pay scale rates in respect of expenses. We do not believe that independent one person companies are any more likely to abuse scale rates than anyone else, and the current scale rates are not over-generous. There is considerable administrative convenience in being able to use scale rates and they should be available to all employees and officers including one person company directors. The apparent absence of on-going independent checks ought not to be an issue. Directors of one person

companies have to self assess their own income tax, so why can they not do so for PAYE? In addition, many one person companies engage external accountants to run the payroll and draw up the financial statements and complete forms P11D and in the course of these activities expenses paid to or on behalf of directors are subject to external review.

Chapter 6: Implementation and transitional arrangements

Existing dispensations

Q8: Would employers welcome being able to continue to rely on their existing dispensation for a transitional period, or would this be a source of unnecessary complexity? Is so, how long would the transitional period need to be to be useful?

38. We consider that existing dispensations and industry agreements should continue as long as they remain valid, ie until any changes to the underlying laws on expenses invalidate the agreements. We would note that it will ease the transition for HMRC if replacement processes and agreements do not have to be renegotiated all at the same time.

Q9: Independently of whether existing dispensations may continue to be used, would employers welcome being able to continue to use any custom scale rates they had agreed as part of their dispensation for a transitional period? Is so, how long would the transitional period need to be to be useful?

39. We consider that existing custom scale rates should continue until they expire, subject to any changes to the underlying laws on expenses. Presumably such custom scale rates would have been negotiated on the basis of the facts and circumstances of the employer or the industry, so it would seem appropriate to continue them until circumstances change. It will also ease the transition for HMRC if the department does not have to renegotiate every custom scale rate at one time.

Guidance

Q10: Are there any specific situations or circumstances in which employers would not feel confident paying expenses because of a lack of clarity in HMRC's guidance? Which changes could HMRC make to its guidance that would have the biggest impact on employers' confidence in paying these expenses?

40. The guidance is difficult to understand mainly because frequently the underlying law is difficult to understand. We recommend rectifying anomalies in the law first and then simpler guidance should naturally follow. The table on pages 60 to 65 of booklet CWG2 contains a long list describing how to treat expenses for tax and NIC; there are 19 instances where the tax and NIC treatments are different.

Implementation

Q11: Would employers and other affected parties welcome the exemption not coming into force for a period of time after the legislation is in place? If so, how long would employers and other affected groups need to prepare for the new exemption coming into force?

41. Whilst we welcome the proposed change because it will be a simplification, the implementation of PAYE real time information (RTI), which is still causing problems for many employers and payroll agents (and HMRC) (hence the setting up in November 2013 of the Joint Task Force by representatives of employers/payroll agents/bureaux and software houses to help HMRC with RTI) and the introduction of the onshore and offshore intermediaries legislation, where the guidance is still incomplete, split years and the statutory residence test, and auto-enrolment suggest to us that the new regime should not start until the law is known, employer obligations

have been clarified, and HMRC has established and tested new IT and other processes and consulted on and published comprehensive guidance, ie not until 6 April 2016 at the earliest.

Q12: How should dispensation applications that are made in the intervening period be handled?

- 42.** We recommend that as such dispensation applications will be made under the current rules, they be handled the same as currently. It would be helpful if HMRC warn employers that new legislation is on the horizon, and we suggest that dispensations granted in the intervening period have an end date, but not a date earlier than when the new regime comes into force.

PCB

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/-/media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)