

**HM Revenue & Customs (HMRC) discussion document
Employment Intermediaries: Temporary workers – relief for travel and subsistence
expenses**

Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

- 1.1 We are disappointed at the very short period allocated to this discussion document and hope that it will not result in hasty decisions. As change is not planned until 6 April 2016 at the earliest, we recommend that there is further consultation and plenty of time allocated to consider draft legislation.
- 1.2 Our recent report ‘Travel expenses for the low-paid – a time for a rethink?’¹ took a very close look at umbrella arrangements – and in particular the use of ‘Pay Day by Pay Day’ (PDPD) schemes by low-paid agency workers. Our extensive research around the subject throughout 2014 resulted in a much better understanding of the matter and we refer to that report throughout this response.
- 1.3 We are particularly concerned about the situation of low-income workers, for whom the existing scheme arrangements may be difficult to understand and present various ‘hazards’ such as the possibility of HMRC pursuing them rather than their employer for a tax underpayment. In turn, this could lead to contention that they have over-claimed tax credits. We therefore recommend that if change is implemented from 6 April 2016, that HMRC do

¹ See

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

not pursue workers for liabilities for years up to then caused by having unwittingly been caught up in a non-compliant scheme.

- 1.4 We believe that great care should be taken such that there are no unintended consequences of a change in the legislation, be it under either option 1 or 2. In particular, we would wish to ensure that there are no adverse effects on mobile workers, such as those in the care industry.
- 1.5 Further, HMRC and other arms of Government such as the Department for Business, Innovation and Skills (BIS) will need to be watchful that anti-avoidance measures in this area do not simply give rise to other schemes (with potentially worse consequences for low-paid workers). The Government must be prepared to react quickly at the first signs of any such developments to safeguard workers' rights.
- 1.6 We recommend that HMRC work with the Department for Work and Pensions (DWP), such that those who decline to work under PDPD or similar arrangements do not receive benefits sanctions.
- 1.7 We believe that thought should be given to the considerable disincentive to work of travel costs, particularly for temporary workers who may not be able to minimise these by adjusting their housing situation, and how this might be ameliorated by means other than giving tax relief – for example, via the Universal Credit system.

2 About Us

- 2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 Our approach to this discussion document

- 3.1 We are disappointed in the short time frame given to respond to what is a very important area of discussion, particularly as the eight weeks allocated to it span Christmas and New Year.
- 3.2 Respondents and potential respondents are unlikely to have had sufficient time to digest the document, to establish whether they have an interest, what that interest might be and to respond to it in any meaningful way.
- 3.3 Furthermore, a deadline of 10 February 2015 with ‘results to be announced in the 2015 Budget’¹ raises concerns as to whether there will be sufficient time to digest the responses and duly consider all of the issues before announcing an outcome. We are also surprised that the outcome will be announced so soon, given that this is called a ‘discussion document’ rather than a ‘consultation’, thus suggesting it has been published to develop early thoughts and capture initial views rather than as an immediate precursor to decisions being taken.
- 3.4 Nevertheless, we see that any proposed change is not intended to come into effect until 6 April 2016. We would therefore recommend this intervening time is used for further consultation and early publication of draft legislation so that any wider or unintended impacts can be fully assessed.

4 Introductory comments

- 4.1 One of the ways that LITRG try to make a difference for those on low incomes is by researching particular tax and related areas that may be giving cause for concern and writing reports recommending change.
- 4.2 Our recent report ‘Travel expenses for the low-paid – a time for a rethink?’² shone a light on the use of a particular umbrella arrangement by low-paid agency workers to obtain relief for their travel costs (the so-called Pay Day by Pay Day model – ‘PDPD’). This had been declared ‘non-compliant’ by HMRC, but was still, evidently, widely in operation. Our extensive research around this subject in 2014 gives us good grounding for responding to this current HMRC discussion document.
- 4.3 We do not reiterate the detail of that report here, but we do refer the reader to parts of it where appropriate.

¹ Due on 18 March 2015.

² <http://www.litrg.org.uk/reports/2014/141117-LITRG-PAYE-report>

5 General comments

- 5.1 We note that the vast majority of the discussion document provides an explanation of the current situation. Within it, there is some reference to HMRC's existing activities to counter perceived avoidance of tax and National Insurance contributions (NIC) through umbrella schemes.
- 5.2 We welcome such activity from HMRC, as we have seen¹ a number of low-income workers caught up in these schemes – perhaps unwittingly – and receiving little or no tax or NIC advantage themselves from the arrangements, particularly when one takes into account the fees levied by the scheme provider. Yet we have also seen such low-income workers themselves being pursued for under-deducted tax (by way of P800 tax calculations and follow-up collection activities), rather than HMRC pursuing the employers (by way of a Regulation 80² determination). We therefore question the level of HMRC activity in pursuing the employers/scheme providers, as there has been little apparent evidence of this from the outside perspective.
- 5.3 For instance, our report (chapter 6) highlights that there are still plenty of umbrella companies operating in the low-income market, apparently undeterred by HMRC's past statements of their non-compliance. We have also seen no great evidence of scheme providers being shut down by National Minimum Wage or Pay As You Earn (PAYE) compliance enforcement activities – indeed, the discussion document acknowledges that this is a *growing* rather than shrinking area of concern.
- 5.4 Had HMRC been more robust in taking scheme providers to task, including taking a case to Tribunal to establish formal tax precedent, might we not have seen others removing themselves from the marketplace?

It is from this viewpoint that we aim to answer the specific discussion document questions below, and make recommendations that seek to safeguard low-income workers.

6 Question 1: Do you agree with our description of an OAC?

- 6.1 The description seems fair. Appendix 2 of our report³ discussed what is meant by continuous or overarching contracts of employment, including consideration of some relevant case law.

¹ Through direct contact to our website, www.litrg.org.uk and by means of our work with other voluntary sector organisations – in particular Tax Aid, the tax charity which supplied case studies for our report on this subject.

² PAYE Regulations, SI 2003/2682.

³ See page 54ff:

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

7 Question 2: Do you agree with our description of how OACs are used, are there variations which we haven't covered here?

7.1 Again, this description seems fair, in line with our report as referred to immediately above.

8 Question 3: Do you agree with our description of why OACs are used? What is the main motivation for using an OAC? Are there any other reasons not described here?

8.1 Broadly, yes we agree. There could however have been further mention in the discussion document of the role of NIC in terms of 'selling' the benefits of umbrella PDPD schemes to low-income workers. The document talks about the recent above-inflationary increases in the personal income tax allowance, but in fact class 1 primary NIC may be an arguably more important factor for those workers on the lowest incomes. This is particularly because such workers might have ad hoc working hours (and thus the non-cumulative nature of class 1 NIC calculation hits them harder than income tax if, for example, they work long hours one week, but none the next)¹ and because the primary threshold has not kept pace with the increased income tax allowance.²

8.2 It is very likely then, that workers in the bracket between the NIC primary threshold and the personal allowance are driven to use umbrella companies in the hope of a much appreciated 12% NIC saving – not a tax saving.

9 Question 4: On which of these reasons would you place most weight in explaining the recent increase in the use of OACs?

9.1 Our perception from researching our report is that PDPD schemes using overarching contracts have flourished in the absence of any concrete means of disproving their legality, such as a decided case in the tax tribunal. Although the Gangmasters Licencing Authority (GLA) won an appeal in their own tribunal system against a company operating a PDPD scheme, and the tax and NIC issues were considered and declared non-compliant by the Judge in that case, this did not set a precedent in pure tax terms, so was no deterrent to those operating outside the GLA's area of enforcement.³

¹ The non-cumulative nature of NIC may also mean that workers are missing out on making up 'contribution years' for other state benefit purposes.

² The income tax allowance for 2014/15 being £10,000, but class 1 primary NIC being due once a person earns over £153 a week (£7,956 a year).

³ See our report, page 35ff discussing the case of *FS Commercial v Gangmasters Licensing Authority* [2012].

10 Question 5: Do you have any other comments? For example, do stakeholders agree that it is unfair that workers engaged through OACs with employment intermediaries get access to travel and subsistence relief whilst others in similar circumstances don't?

10.1 There is a *prima facie* unfairness in comparing the reliefs available in these two situations. If the playing field is to be 'levelled down' such as proposed in this discussion document – that is, that neither the overarching contract worker, nor the standard agency worker may in future obtain relief on travel and subsistence expenses to a temporary workplace – then we do feel there is some basis for considering alternative means of assisting low-income workers with travel costs. This might be via the benefits system, as we note below in answer to question 18.

10.2 Equally, there are other unfair situations which will hopefully be considered in the general travel and subsistence expenses review – for example the inability of workers to claim relief from primary NIC where their employer has not reimbursed legitimate expenses of employment; yet the reimbursed worker suffers neither income tax nor primary class 1 NIC on the amount reimbursed.

11 Question 6: Do you have any evidence on the extent of the usage of OACs by employment businesses?

11.1 Yes, we are aware from our research that a significant number of operators in the PDPD scheme market were – as at summer 2014 – still prepared to operate in the low-income worker sector, ie those earning at or near the National Minimum Wage. See our report¹ for more information of our mystery shopping exercise.

12 Question 7: Do you have any further evidence of the recent trends in the use of OACs?

12.1 No.

13 Question 8: Do these differ between umbrella companies and employment businesses?

13.1 Not applicable.

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

¹ See Chapter 6:

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

14 Question 9: Do you expect the prevalence of OACs to increase in the near future?

14.1 The general theme from our report¹ was that use of PDPD schemes was certainly not perceived to be in decline and, quite the reverse, that this was a thriving industry.

15 Question 10: Which income groups do you expect will be the greatest users of OACs in the future?

15.1 No comment.

16 Question 11: Do you have any evidence on the extent of any competitive distortions created by misuse of the tax rules through OACs and other schemes noted in this document?

16.1 No comment.

17 Question 12: Do stakeholders agree there is a strong case for the government legislating to restrict tax relief for travel and subsistence in these circumstances?

17.1 We find this a difficult question to answer. Our research has shown that there is a case for action to be taken; though whether an immediate change to restrict tax relief for travel and subsistence to holders of overarching contracts of employment is the right course of action is a matter for careful consideration. What *is* clear is that there is a case for simplicity in the temporary labour market so that workers – particularly those who might work in low-paid positions – understand their tax situation. The existence of the umbrella and the complexities of overarching arrangements, together with the confusing pay statements and contracts that workers are given, can hardly therefore be said to be a good thing from the viewpoint of ease of understanding.

17.2 Furthermore, the possibility that workers can find themselves the recipient of a tax underpayment calculation with consequent enforcement action by HMRC, is undesirable. This is particularly so when they have profited little, if at all, from the umbrella arrangement in the first place when one takes into account fees levied under the scheme.

17.3 If a change of the kind envisaged in either option 1 or option 2 to prevent future claims to tax relief were made with effect from 6 April 2016, there remains still the possibility that workers could be pursued for tax underpayments for years up to 5 April 2016. We therefore

¹ See

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

recommend (and indeed suggest it is essential) that HMRC and the Government should commit **not to pursue** individual workers for underpayments arising where a PDPD or similar complex scheme is in place; and that any compliance activity in respect of such scheme is confined to the employers and scheme operators.

17.4 We also believe that the Government should consider that there might be undesirable short term impacts, such as those outlined below.

17.5 ***Destabilisation of the temporary worker industry***

17.5.1 Temporary workers, assuming they understand the overarching contract arrangements they have entered into, may value tax relief on travel expenses. This presumably influences the short term assignments they undertake. A change in the rules could mean they may be less inclined to travel long distances, or will want higher pay rates to compensate.

17.5.2 The business model of those providing overarching contracts is dependent upon supplying the labour of their employees at a very small mark-up. They may not be able to absorb any cost increases, and so any changes will therefore have knock-on effects. It may not be financially viable for the vast majority of umbrella companies (as well as some agencies) to continue if relief was removed. They could cease to trade and make staff redundant. In turn, this would lead to an Exchequer cost of potentially having to support those workers through the welfare benefits system.

17.6 ***Scheme ‘phoenixism’***

17.6.1 A major concern is that companies using umbrella companies to recruit and pay low-income staff will, following the changes, have to put the staff through their own payrolls, or else devise some novel way of engaging them without actually employing them. If they choose to do the latter (as the savings from a new scheme may well outweigh costs of devising and implementing it), the workers’ status will be even less secure than they are under the current umbrella arrangements. Thus an anti-avoidance measure by HMRC could result in one abuse being struck down and an even worse one taking its place. HMRC and other interested arms of Government such as BIS will need to be watchful of this and prepared to react quickly at the first signs of any such developments.

18 Question 13: Do you have any evidence on the likely impact of option 1? Do you think any particular sectors will be affected more than others?

18.1 Without seeing proposed draft legislation, we find it difficult to comment on the two options presented and to understand fully the potential ramifications of each. We are particularly concerned that there should be no adverse impacts on other types of mobile worker – for instance, paragraph 72 of the discussion document suggests that there might be an impact on “... permanent employees who do not have a permanent workplace; for instance consultants who are placed consistently at the different premises of their employers or groups such as mobile meter readers”.

18.2 One group of workers potentially impacted could be those in the care industry, who travel from place to place visiting those they care for (usually in the person's own home). They may have no fixed workplace and spend a lot of time travelling, and many may not be reimbursed for the travel cost. We would not wish to see them further disadvantaged by removing their existing ability to claim tax relief on unreimbursed expenses (and indeed it is a pity that such relief does not currently extend to class 1 primary NIC where the expense is not reimbursed, as there is no facility to claim a refund of NIC).

18.3 We therefore recommend that draft legislation is published for early consultation so that stakeholders can consider the implications fully.

19 Question 14: Do you have any evidence on the likely impact of option 2? Do you think any particular sectors will be affected more than others?

19.1 The key difference between option 1 and option 2 is that the latter restricts impact to those engaged under overarching employment contracts, whereas the former may extend to other types of structure such as so-called 'personal service companies' (PSC). As noted above, it is difficult for us to gauge the wider impacts of option 1 without seeing draft legislation; but equally we would be concerned that option 2 alone could cause a migration of workers to other structures which could lead to further loss to the Exchequer.

19.2 For example, if overarching contract workers were excluded from tax relief on travel and subsistence costs, it may be that other structures evolve which may instead see people working through their own PSC. From enquiries to our website and other contacts within the voluntary sector, we believe that some low-income workers have already been caught up in such structures – having been pressured into setting up their own PSC and being paid through that rather than being engaged as an employee. This leaves the worker with an incredibly complicated tax situation, including Corporation Tax compliance considerations, and having to extract the money from the company but without being able to afford professional advice and assistance. It also means they are being deprived of employment rights by their 'client' who would otherwise be their employer.

19.3 We would not wish to see existing PDPD providers seeking alternatives such as the above, and workers therefore being drawn into further complexity. This does therefore suggest that option 1 may be preferable to option 2, but again is very much subject to seeing the detail of the proposals.

20 Question 15: Are there particular groups of people who will be significantly worse off if tax relief was restricted?**20.1 Tax credits claimants**

20.1.1 We are surprised that the discussion document makes no reference to low-income workers who might also be claimants of tax credits. Our report notes¹ (and indeed as Government itself has commented in previous consultations on this subject in the past), it may be that being able to claim tax relief on travel expenses in turn reduces a worker's income for tax credits purposes – thus resulting in a higher award.

20.1.2 This may initially appear to increase further the overarching contract worker's 'advantage' from participating in an umbrella scheme as against a worker engaged under standard agency terms. *Prima facie*, this might be true, but it also doubles their compliance problems if HMRC seek to argue that the expenses are not in fact relievable – that is, that the worker may face recovery of a tax credits overpayment as well as being pursued for underpaid tax.

20.1.3 Many will not have understood the precarious nature of their situation in signing up to the scheme. As pointed out in our report², those marketing the umbrella arrangements use slick materials which do not point out the risk of HMRC challenge – they are presented as compliant, tax-saving arrangements.

20.1.4 Furthermore, even if a worker is unsure of signing up to the scheme's terms, they may feel they have little or no choice in the matter; particularly if they are desperate for work to earn a living and perhaps even facing Jobseeker's Allowance sanctions if they fail to take up work offered.

20.1.5 All of these considerations must therefore be joined up before action is taken here. That is:

- HMRC must agree that workers caught in schemes up to the date of proposed change (6 April 2016) will not be pursued for overpaid tax credits if compliance activity proves that the schemes have been operating outside of the law; and
- HMRC and DWP must work together such that JobCentre Plus staff understand that workers must not be sanctioned for failure to accept terms which include an umbrella scheme or similar arrangement, and that people will not be precluded from

¹ For example, see page 40ff:

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

² See Chapter 7:

<http://www.litrg.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

claiming Jobseekers' Allowance or Universal Credit if they voluntarily give up work they are already doing under such contracts.

21 Question 16: Are there examples of where this may affect cases where it is fair that tax relief should apply?

21.1 As noted above, we believe that great care should be taken such that there are no unintended consequences of a change in the legislation, be it under either option 1 or 2. We noted concerns above as regards mobile workers such as those in the care industry and reiterate those here.

22 Question 17: Do you think the removal of relief for travel expenses under option 1 should be extended to PSCs?

22.1 As noted above, we have some concerns that if the proposed action is too narrow, it may mean that schemes evolve to take advantage of the rules in other ways.

23 Question 18: Do you have any other suggestions, including broad based T&S reform as part of the T&S review announced at Budget 2014, for how the identified unfairness could be removed?

23.1 We would have liked to have seen some more information in the discussion document about the nature and characteristics of temporary work. We would suggest that a minority of them are sophisticated, high earning, skilled IT specialists and engineers (the type of workers that one might call to mind when thinking of 'freelancers/contractors'). Indeed, from investigating the background to our report¹, we would suggest that the majority are exactly the opposite – young, with lower levels of education or poor English perhaps, low skilled and forced to turn to temporary work sourced through employment agencies as they have not been successful in finding a permanent job.

23.2 Life for these agency workers can be precarious and uncertain. In addition, the work they do is poorly paid – a 2013 Labour Force Survey² found that 47.9% of agency workers in London and 39.5% outside London were earning below the hourly living wage (£8.55 in London and £7.45 in the rest of the UK at the time of the survey). Shorter working hours also need to be factored in to their pay calculations, as does the fact that the workers often have to accept

¹ See chapter 3:

<http://www.litr.org.uk/Resources/LITRG/Documents/2014/11/LITRG%20PAYE%20report%20FINAL.pdf>

² Analysis of Quarterly Labour Force Survey, April-June 2013.

assignments very far away from wherever it is they call home. For instance, we have seen an example in an agency contract which included expected travel time of up to an hour and a half each way.

- 23.3 The unavoidable costs of low-paid temporary workers getting to their assignment locations to perform their duties can therefore take up a disproportionate amount of their weekly take home wages. Temporary workers do not have the luxury of being able to plan around the fixed costs of ordinary commuting. For example, an agency worker living on the outskirts of London and offered a day's work in an office in central London might have to buy an adult zone 1-6 day travel card which is currently £17.00. The equivalent daily cost if they were able to buy an annual travel card would be £10.06 (assuming 233 workdays in a year).¹
- 23.4 For the low-paid agency worker, who has to go to a variety of premises (often at short notice) and who cannot adjust home to achieve a reasonable commute, their income (and in turn their standard of living and inclination to work) is correspondingly and disproportionately depleted by these travel costs.
- 23.5 Therefore, whilst we note and in many ways understand the Government's stance outlined in paragraph 76 of the consultation document that they do not wish to level the playing field in the opposite direction – that is, to extend tax relief to other temporary workers, overarching contract or not – we feel that the above points need to be taken into account. This might be elsewhere than the tax system (indeed providing tax relief on travel expenses does not help those whose income is below the personal allowance in any case); for example, it could be taken into account if developing the Universal Credit system further in future.
- 23.6 This may, of course, present difficulties in itself, with travel expenses being variable from week to week for many temporary workers; but may be possible if Universal Credit does in fact prove to be responsive to changes in circumstances as ought to be achievable in the context of it being a monthly benefit. We would be happy to participate in a further discussion of this with relevant parts of government, and we are keen to contribute to the ongoing travel and subsistence review as it develops.

LITRG
10 February 2015

¹ <https://www.tfl.gov.uk/fares-and-payments/fares>