

# National Minimum Wage workers: Travel and subsistence expenses schemes

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# Contents

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		Page
Chapter 1	Introduction	3
Chapter 2	Travel and subsistence schemes	5
Chapter 3	NWM workers and travel and subsistence schemes	9
Chapter 4	The solution being proposed and its impact	17
Chapter 5	Summary of questions and the consultation process	19
Annex A	NICs and access to earning-related contributory benefits	23
Annex B	Impact Assessment	27



# 1

## Introduction

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**1.1** At 2009 Pre-Budget Report (PBR) the Government announced that it is committed to addressing the problem of the potentially exploitative arrangements which are implemented for some temporary workers paid at or near the National Minimum Wage (NMW). It also announced that HM Treasury, HM Revenue and Customs (HMRC) and the Department for Business, Innovation and Skills (BIS), would consult in the New Year, inviting views on proposed changes to the NMW Regulations and whether this is the best approach to tackling this problem.

**1.2** Many temporary workers, including those who are paid at or near the National Minimum Wage (NMW), participate in travel and subsistence schemes operated by some Employment Businesses<sup>1</sup> and umbrella companies. These schemes take advantage of the tax relief and the disregards that exist for the purposes of National Insurance Contributions (NICs) in relation to travel from home to a temporary workplace. By creating a single employment contract for each worker, these schemes convert what would otherwise be a series of permanent workplaces (for which there is no tax relief available on travel expenses) into temporary workplaces (for which tax relief on travel expenses is due). Workers agree that an amount of pay, which would otherwise be subject to tax and NICs, is replaced with expenses payments for travel to a temporary workplace. In this way, these schemes deliver tax and NICs savings for workers. Also, the Employment Businesses or umbrella companies save employer's NICs on the pay which has been replaced with tax and NICs free travel expenses. More detail on the background to these schemes and how they operate is set out in Chapter 2.

**1.3** Workers paid at or near the NMW are able to participate in these schemes as the expenses paid for travel to a temporary workplace can count towards NMW pay.

**1.4** This consultation only concerns the participation of NMW workers in these travel and subsistence schemes; it is not concerned with the participation of other workers in these schemes. A previous consultation was carried out by the Government in July 2008 which looked at the tax relief for travel expenses provided to workers as a result of these arrangements. This consultation does not reconsider the tax and NICs issues which were raised there.

**1.5** A number of problems arise as a result of NMW workers' participation in travel and subsistence schemes. Firstly, the reduction in their pay for tax and NICs purposes in return for the payment of tax and NICs free travel expenses can adversely impact on NMW workers' access to earnings-related contributory benefits. In addition, the cases that HMRC have seen suggest a worker participating in a travel and subsistence scheme is only very slightly better off in terms of take home pay. In some schemes, it is the Employment Business or umbrella company employing the worker who retains the largest part of any financial benefits, with only a small proportion of these being passed on to the worker.

**1.6** Some businesses do not wish to implement travel and subsistence schemes for NMW workers as they consider that they involve profiting from low paid workers. Also, some businesses, for a number of reasons, are not able to implement such schemes. Such businesses

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<sup>1</sup> As defined in the Employment Agencies Act 1973, as amended by the Employment Relations Act 1999.

suffer a competitive disadvantage compared to those businesses which do implement these schemes. Also, the participation of NMW workers in travel and subsistence schemes gives rise to an Exchequer risk, as not all NMW pay is subject to tax and NICs.

**1.7** The Government has identified a potential solution to this problem which involves amendment to the NMW Regulations. This solution targets the particular issue of NMW workers participating in these schemes and does not affect other workers. This solution does not impact on the tax and NICs treatment of travel expenses.

**1.8** The effect of this amendment to the NMW Regulations would be that where expenses are paid in respect of travel to a temporary workplace, which qualify for tax relief and which are disregarded for NICs, then these would not count as pay for NMW purposes. Employers would have to pay any travelling and subsistence expenses on top of NMW rates of pay.

**1.9** The objective of the consultation is to develop the best solution to this problem, and the Government welcomes feedback on the proposal outlined.

**1.10** Chapter 5 sets out the questions for consultation and gives details of the consultation process. Comments should be submitted by 6 May 2010.

# 2

## Travel and subsistence schemes

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**2.1** Where these travel and subsistence schemes are implemented, the use of overarching employment contracts changes what would otherwise be viewed as normal home to work travel into travel to temporary workplaces, for which tax relief is due. By way of background, this section explains in more detail how these schemes operate to deliver tax and NICs savings.

### Tax relief – permanent and temporary workplaces

**2.2** Most employees have a fixed workplace where they work for the majority of their time, but they may also be required to work in other locations from time to time. Temporary workers generally work in various locations for different engagers or end clients, often for short periods of time.

**2.3** As a general rule, tax relief is not given for the cost of travelling between home and an employee's permanent workplace, as this is regarded as a personal expense. Relief is given under S338 Income Tax (Earnings and Pensions) Act ("ITEPA") 2003 for journeys from home to a temporary workplace. A workplace is temporary if the employee's attendance is for a limited duration or for a temporary purpose. Examples of journeys to a temporary workplace, which would be eligible for relief, include where:

- a worker undertakes an engagement at a workplace other than their usual one. For example, a London-based employee attending a meeting in Norwich would be eligible for relief on travel expenses between his home and Norwich;
- a worker in continuing employment works at a succession of places for short periods of time; and
- a worker in a continuous employment is asked to undertake a secondment of, say, 18 months at a different workplace. The worker will be entitled to relief for travel expenses for the duration of the secondment.

This is providing that, in each of the cases, the journey does not constitute ordinary commuting or private travel.

**2.4** Where a worker's attendance at a workplace is for a limited duration or for some temporary purpose, the workplace will nevertheless be considered to be permanent if he:

- goes to the same workplace in the course of a period of continuous work which lasts, or is likely to last, for more than 24 months; or
- goes to the same workplace for all or almost all of the time for which the worker is likely to hold, or continues to hold, the same employment.

**2.5** For the purposes of the tax relief, travel expenses include the cost of travel, subsistence (food and drink) and accommodation (when the worker needs to stay overnight).

## Overarching employment contracts

**2.6** An overarching employment contract works by linking a series of separate assignments into a single, ongoing employment. This changes what would, for temporary workers, otherwise be a series of permanent workplaces (for which there is no tax relief available on travel expenses) into temporary workplaces (for which tax relief on travel expenses is due).

**2.7** Most temporary workers on short contracts are not entitled to tax relief for expenses for travelling between home and work, since they will usually only work at the one location during that employment. This would be considered as travel to a permanent workplace (not a temporary one) and it would therefore not be eligible for tax relief. The same applies for temporary workers contracted to work on different engagements through the same Employment Business. This means that temporary workers are usually treated the same as permanent employees. However, the use of overarching employment contracts to create a single employment allows temporary workers access to tax relief on travel expenses, which would not otherwise be available to them.

## Salary sacrifice

**2.8** In most travel and subsistence schemes, the expenses paid to the worker for travelling to a temporary workplace are not paid on top of the worker's salary. Instead, the worker enters into a salary sacrifice arrangement, where he "sacrifices" part of his salary, which reduces the amount of pay subject to tax and NICs. The travel expenses are then paid to the worker, in addition to this reduced pay, and are free of tax and NICs.

**2.9** The Employment Business and umbrella company also save employer's NICs on the amount of the pay which has been given up. In some cases, the amount that the employee agrees to sacrifice is greater than the amount paid to him in expenses, which may reflect, for example, contributions to holiday pay. An example of how this might operate is set out at the second part of Example D, which follows paragraph 3.32. In this example, the worker gives up pay of £95 per week and in return receives expenses of £72. This still gives rise to an increase of £6.45 per week in the worker's take home pay. The result of the worker giving up more pay than he receives in expenses may be that some of the tax and NICs savings that would otherwise be made by the worker are passed to the Employment Business or umbrella company.

## Dispensations

**2.10** Where an employer, including an Employment Business or umbrella company, pays expenses to workers, details of the payments have to be reported annually to HMRC. However, the employer can obtain an HMRC dispensation for (amongst other things) the travel expenses that it pays. The employer can agree scale rate payments with HMRC that reflect their particular circumstances for inclusion in the dispensation or opt to use HMRC's advisory benchmark scale rates for periods commencing after 6 April 2009. This means that, where an Employment Business or umbrella company obtains a dispensation, it can pay the worker's travel and subsistence expenses without having to report them to HMRC.

**2.11** HMRC can withdraw a dispensation where they believe additional liability to tax exists (for example: workers claiming expenses that were not genuinely incurred).

## Employment Businesses

**2.12** Where the worker is paid through an Employment Business using a travel and subsistence scheme, he will have an overarching employment contract with that company. This differs from the usual agency-worker arrangements where the Employment Business does not employ the worker.

**2.13** The Employment Business sources the contract with the end client and then places the worker in the contract.

**2.14** The payment to the Employment Business by the end client is generally based on the worker's hourly rate of pay, the amount of employer's NICs payable (based on that rate of pay) and the commission/fee charged by the Employment Business for providing the worker. By implementing a travel and subsistence scheme for workers, the Employment Business makes savings of NICs as it does not have to pay employer's NICs on the amount of the salary sacrificed nor on the travel expenses paid to the worker. These amounts, once multiplied by the number of workers who are participating in travel and subsistence schemes, give rise to significant savings for the Employment Business. Also, as outlined at paragraph 2.9, it may be the case that the Employment Business retains more of the financial benefits of the arrangements than the employer's NICs savings on the salary given up.

## **Umbrella companies**

**2.15** Where an umbrella company pays the worker, this company operates between the worker and the Employment Businesses. The worker sources work through an Employment Business and payment is made to the umbrella company, rather than the worker. The umbrella company deducts employer's NICs and its fee from the payment made by the Employment Business for the worker's services. The umbrella company then pays the balance to the worker as salary subject to income tax and NICs and tax/NICs-free travelling and subsistence expenses. Generally, the worker and the umbrella company agree the rate of pay and level of travel and subsistence expenses for each assignment without the need for a formal salary sacrifice arrangement.

## **Compliance issues**

**2.16** There are many different variations of travel and subsistence schemes in operation. It is worth emphasising that the availability of tax relief for travel expenses (and for the expenses to be disregarded for NICs) depends very much on the way in which all these arrangements are implemented. For example, the overarching employment contract must be valid, creating a single employment and the employee must, on the basis of the facts and supporting evidence, be incurring expenses in travelling to a temporary workplace. If, for any reason, the arrangements as implemented are not effective in securing tax relief, then the expenses will be taxable and liable to NICs.

**2.17** HMRC polices these arrangements and takes action where appropriate to deal with non-compliance with the PAYE, NICs and NMW rules.

## **Previous consultation**

**2.18** A previous consultation was carried out by the Government in July 2008, entitled *Tax relief for travel expenses: temporary workers and overarching employment contracts*. This consultation also looked at structures using overarching employment contracts – Employment Businesses and umbrella companies – and the tax relief for travel expenses provided to their employees as a result of these arrangements.

**2.19** The outcome of this previous consultation was an announcement that no action would be taken to change the rules on tax relief for travel expenses, but that HMRC would refocus its efforts to address the poor levels of compliance in this area. Following this announcement HMRC commenced compliance activity to identify and take action against those Employment Businesses and umbrella companies which are operating in contravention of tax, NICs or NMW legislation.

**2.20** This current consultation does not revisit the tax and NICs issues arising as a result of the use of overarching employment contracts and it is not proposing to change the rules regarding tax relief for travel expenses.

**2.21** This consultation focuses only on the particular issues arising as a result of NMW workers participating in travel and subsistence schemes: the impact on their access to earnings-related social security benefits; the possible exploitation of workers; the effect on competition; and the impact on the Exchequer.

# 3

## NMW workers and travel and subsistence schemes

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### Background - National Minimum Wage

**3.1** The National Minimum Wage (NMW) was introduced in the UK in 1999 and sets minimum hourly rates that employers must pay their workers. It was introduced to protect the most vulnerable workers and ensure that they receive at least minimum rates of pay.

**3.2** Since its introduction, NMW has become an important part of the UK labour market, creating a level playing field amongst employers by standardising minimum levels of pay across many sectors.

**3.3** NMW covers almost all workers in the UK and is currently divided into three rates that apply to workers of different ages, which are usually updated in October each year. NMW was introduced by Government as part of a strategy to provide fair standards in the workplace and make work pay.

**3.4** The rates that apply from 1 October 2009 are as follows:

- workers aged 22 years or more: £5.80 per hour;
- workers aged 18 to 21 inclusive: £4.83 per hour; and
- workers aged under 18 (but above compulsory school age): £3.57 per hour.

**3.5** Almost all workers who work in the UK are entitled to the NMW. There are some exceptions, including self-employed people, apprentices under the age of 19, apprentices aged 19 or over (but only for the first year of their apprenticeship), and children who are still of compulsory school age. Full time and part time workers are entitled to the NMW, as are agency workers, temporary or casual workers, piece workers and home workers.

**3.6** NMW pay is calculated in accordance with Regulations 30 to 37 of the NMW Regulations.<sup>1</sup> The starting point for NMW is all payments to a worker - the pay received before income tax and NICs deductions have been made. Many of the payments that a worker receives will count towards NMW pay, but some will not. For example, a worker's basic pay (before deductions of tax and NICs) counts towards NMW pay, but some payments for expenses may not count. Where employers make deductions, or receive payments from workers they must still ensure that the worker is paid at least NMW rates. They cannot pay a worker below NMW, even if they have the worker's permission to do so.

### Participation in travel and subsistence schemes

**3.7** Workers who are paid at or around NMW rates are not able to participate in salary sacrifice arrangements if the amount sacrificed would reduce their pay below NMW rates. In all cases, whether or not the worker participates in a salary sacrifice, it is a matter of looking at all the payments made to and deductions made from the worker to consider whether, in accordance with the Regulations, the worker has been paid at least the NMW.

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<sup>1</sup> SI 1999/584

**3.8** This also holds true where low paid workers are employed by Employment Businesses or umbrella companies and participate in travel and subsistence schemes, i.e. all the payments to (and deductions made from) the worker must be considered in order to determine whether the employer has complied with his obligations under the NMW Regulations.

**3.9** The best way of illustrating how the Regulations operate in relation to travel expenses schemes is to consider an example:

**Box 3.A: Example A**

Gross pay – 40 hours @ £5.80	£232.00
Salary Sacrifice	£ 95.00
Taxable pay	£137.00
PAYE	- £ 2.40
NI	- £ 2.97
Travel Expenses	+ £ 95.00
Net Pay	£226.63

In this case, the worker’s pay for NMW purposes is £232 (i.e. pay of £232 plus £95 expenses less salary sacrifice of £95). This equates to £5.80 per hour (i.e. £232/40). For tax and NIC purposes, the worker’s gross pay is £137 which is equivalent to £3.42 per hour (i.e.£137/40).

**3.10** Whether the payment of the travel expenses is included for the purposes of determining NMW pay depends on if the expenses are “in connection” with the employment or not (Regulation 31(1)(f)) and this is discussed further in the next section.

**NMW pay: expenses “in connection” with the employment**

**3.11** NMW legislation does not distinguish travel expenses from any other expenses. When calculating the amount of NMW pay being paid to a worker, any expenses reimbursed by the employer to the worker which the worker has incurred in connection with his employment are deducted in the calculation of NMW pay (under Regulation 31(1)(f)).

**3.12** Similarly, where a worker incurs costs in connection with his employment which are not reimbursed by the employer these are also reduced from the calculation of NMW pay (under Regulation 34(1)(b)).

**3.13** To reduce the calculation of NMW pay the expense has to be “in connection with the employment”. This phrase is not specifically defined in NMW legislation so a general interpretation is applied relating to a cost incurred in the performance of the worker’s duties.

**3.14** Such an application is consistent with the approach taken to identify the time which counts for NMW purposes, which distinguishes between the time workers spend travelling in the course of their work and the time they are not working but travelling between a home and a place of work (for example, under Regulation 15(2) for time work).

**3.15** Therefore, neither the time spent travelling between home and place of work, nor any costs associated with such travelling, are regarded as being in connection with the employment and so are not counted for NMW purposes.

**3.16** Where an employer provides payment to a worker for an expense which is not in connection with the employment, the payment will be counted for NMW purposes.

**3.17** In contrast to tax and NICs rules, set out in paragraphs 2.3 to 2.6 there are no special arrangements in NMW Regulations for workers engaged to work at a temporary workplace.

**3.18** In summary, expenses which are allowable for tax purposes, because they relate to travel from home to a temporary workplace, will usually count as pay for NMW purposes. Therefore, travel and subsistence schemes which are implemented for NMW workers are capable of complying with the rules for tax and NIC and those relating to NMW. Whether they do in fact comply will very much depend on how they have been implemented.

**Compliance with NMW legislation**

**3.19** Although, as noted above, travel and subsistence schemes may comply with NMW legislation, in some cases that HMRC have seen, the arrangements are not fully compliant. This may be due to additional deductions associated with the scheme, which are being made from the worker, such as an administration charge, or simply because the scheme does not pay enough to the worker. Again, this lack of compliance is best illustrated by the use of an example that HMRC has seen:

**Box 3.B: Example B**

Gross pay – 40 hours @ £5.80	£232.00
Salary Sacrifice	£ 95.00
Taxable pay	£137.00
PAYE	- £ 2.40
NI	- £ 2.97
Travel Expenses	+ £ 72.00
Net Pay	£203.63

In this example, the worker is sacrificing an amount of pay which is greater than the amount of travel expenses that he receives.

The worker’s pay for NMW purposes is £209 (i.e. pay of £232 plus £72 expenses less salary sacrifice of £95) which equates to £5.23 per hour, i.e. less than the NMW.

**3.20** Where HMRC identify any non-compliance with the Regulations, enforcement action is taken which will result in the employer having to pay the shortfall in NMW pay to the worker and a penalty for NMW non-compliance to HMRC, in addition to the PAYE and NICs payable on the shortfall.

**Problems arising as a result of the participation of NMW workers in travel and subsistence schemes**

**3.21** As set out in paragraphs 3.11 to 3.15, in general the NMW rules do not treat travel expenses between home and a temporary workplace paid in accordance with these schemes as being in connection with the employee’s employment. So, NMW workers are able to participate in travel and subsistence schemes but this has adverse consequences for the worker, other Employment Businesses and the Exchequer. The impacts are set out in more detail below.

**The Worker – access to earnings-related contributory benefits**

**3.22** In order to have access to certain earnings-related contributory benefits, such as the State Pension, a worker must achieve the qualifying earnings factor (equivalent to 52 times the Lower Earnings Limit (LEL) for NICs purposes, which for the 2009-10 tax year is £4,940).

**3.23** Where the worker participates in a travel and subsistence scheme, the salary sacrifice operates to reduce the worker’s gross pay for NICs purposes, which can impact on the worker’s ability to achieve the qualifying earnings factor. This has implications for the worker’s access to earnings-related contributory benefits.

**3.24** Example D, set out in Box 3.D after paragraph 3.32, compares the tax and NICs position of a worker earning £227.50 per week who does not participate in a travel and subsistence scheme, with the position of the same worker who does participate, giving up pay of £95 per week in return for the payment of travel and subsistence expenses. Using this example, the worker not in the travel and subsistence scheme would only need to work for 22 weeks in order to achieve the qualifying earnings factor. The worker participating in the travel and subsistence scheme, with gross pay for NICs purposes of £132.50 per week, would need to work for 38 weeks to achieve the qualifying earnings factor.

**3.25** For the worker who participates in the travel and subsistence scheme to have to work for a further 16 weeks to have access to earnings-related contributory benefits may not seem significant. However, the seasonal or temporary nature of the assignments means that supply of work may not always be assured.

**3.26** Furthermore, the Labour Force Survey for 2009 shows those temporary workers who are paid at or near the NMW are likely to work less than 30 hours per week; the average weekly hours across the population of temporary workers being 27<sup>2</sup>.

**3.27** If workers are working a reduced number of hours and sacrificing their pay, they put themselves at a high risk that they may not achieve a qualifying earnings factor over the year. Again, an example illustrates this point:

***Box 3.C: Example C- Miss A, part-time worker and “qualifying earnings factor”***

If, during 2009-10, Miss A has average weekly hours of 27 hours at NMW, her pay will be £156.60 per week (27 x £5.80) - this means she will have to work at this rate for 32 weeks of the year to achieve the qualifying earnings factor.

If Miss A participated in a travel and subsistence scheme and sacrificed her salary to reduce her gross pay to £95, she would have to work for 52 weeks of the year to achieve the qualifying earnings factor.

If Miss A participated in a travel and subsistence scheme and sacrificed her salary to reduce her gross pay below £95, even if she worked at this rate for 52 weeks, she would still not achieve a qualifying earnings factor and this would affect her entitlement to certain earnings-related contributory benefits.

**3.28** Annex A sets out in more detail how the earnings-related contributory benefits system operates and how the qualifying earnings factor and payment of NICs interacts with the UK benefits system. However, in general terms, if a worker does not achieve the qualifying earnings factor in a year, then this adversely impacts on his entitlements to both basic and additional State Pension and it can also impact on his ability to access working-age contributory benefits, such as Jobseeker’s Allowance (JSA) and Employment Support Allowance (ESA).

**3.29** In some cases, a UK NICs record will also be important if the worker has come from another EU Member State to work in the UK. Social Security in the EU is co-ordinated under European law. Workers are normally covered by the social security scheme in the state in which they are working and there are rules which specify how workers will be protected in making a claim for benefits if they have been insured in more than one Member State. Normally a person would claim unemployment benefit in the state they were working in. That state would use the

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<sup>2</sup> Based on the Labour Force Survey dataset covering the 2008-09 tax year.

NICs paid in other Member States if they needed it to meet entitlement conditions. There is a special provision for people who return to their state of residence after working somewhere else. For example, if someone has worked in the UK but returns to his home country following that employment, that Member State will use the worker's UK NICs record towards meeting their own conditions of entitlement for their equivalent of JSA.

**3.30** Often workers have little choice about participating in travel expenses schemes and, as low paid workers, they are attracted by the small uplift in take home pay being offered. They may have little appreciation of the implications that these arrangements have for their access to earnings-related contributory benefits.

### **The worker – savings retained by the Employment Business or umbrella company**

**3.31** In the case of workers being paid at NMW rates, the amount of the salary sacrifice represents a significant proportion of their total pay. Examples that HMRC have seen suggest that in some cases these expenses can be as much as 25 per cent to 40 per cent of gross pay.

**3.32** The worker will be better off in cash terms as a result of these arrangements, but, in many of the cases that HMRC has seen, not to any significant extent, with the Employment Business or umbrella company taking most of the financial benefits. The way in which the financial benefits are divided up is best illustrated using example D:

### Box 3.D: Example D

#### Worker engaged by an Employment Business and not in a travel and subsistence scheme

Gross pay – 35 hours @ £6.50	£227.50
Salary Sacrifice	£ 0.00
Taxable pay	£227.50
PAYE	- £ 20.40
NI	- £ 12.92
Travel Expenses	£ 0.00
Total payments	£194.18

Here the worker is paid above the NMW level of £5.80 per hour.

#### Worker employed by an Employment Business within a travel and subsistence scheme

Gross pay – 35 hours @ £6.50	£227.50
Salary Sacrifice	£ 95.00
Taxable pay	£132.50
PAYE	- £ 1.40
NI	- £ 2.47
Travel Expenses	+ £ 72.00
Total payments	£200.63

Here the worker is paid £5.84 per hour i.e. above the level of NMW pay (assuming the travel is classed as 'not in connection with the employment'). By participating in the travel and subsistence scheme the worker is better off in cash terms by £6.45 per week, i.e. by just over three per cent. In this example, which is typical of some of the cases seen by HMRC, the Employment Business benefits by £35.16. This is made up of the amount of employer's NICs saved on the salary sacrificed, i.e. £12.16, and the £23 of the salary sacrificed which is kept by the Employment Business. (Although the employee sacrifices £95, the Employment Business only pays £72 as expenses.)

So, although the worker is better off by £6.45, the Employment Business has benefited significantly more – by more than five times as much.

**3.33** The arrangements are marketed to workers on the basis of this small uplift in their take home pay and, as low paid workers, they are attracted by this. They will usually be unaware of the financial benefits accruing to the Employment Business or umbrella company. In practice, workers may have little choice about participating in travel and subsistence schemes and they may not appreciate that they are able to opt out of these arrangements.

**3.34** The significant savings to be made by the Employment Business or umbrella company are also made clear in promotional material put forward by providers of travel and subsistence schemes:

#### **Box 3.E: Quote from provider's marketing material which has been provided to HMRC**

"If a temp worker works around 25 hours a week or more, even on minimum wage, they will definitely take home more money each week.

You will improve your bottom line profit by a minimum of 30% when you work in partnership with us."

## Employment Businesses and umbrella companies

**3.35** Some Employment Businesses and umbrella companies are unwilling to offer travel and subsistence schemes to workers paid at or near the NMW as they believe them to involve profiting from low paid workers. Also, some businesses, for a number of reasons, are not able to implement these schemes.

**3.36** By not doing so, these businesses are at a competitive disadvantage, since they are not able to offer their workers an increase in their net take home pay. Those Employment Businesses operating these schemes for NMW workers may also be able to undercut their competitors by virtue of the significant savings that they themselves are making from these arrangements.

### Risk to the Exchequer

**3.37** Where a worker participates in a travel and subsistence scheme, the amount paid to the worker for expenses related to travel to his temporary workplace is not subject to PAYE and NICs. We estimate that the risk to the Exchequer in relation to those travel and subsistence schemes, which involve workers paid at or near the NMW, is £85million per year.

**3.38** As set out above, from the cases that HMRC has seen, the benefit of the reduction in tax and NICs payable as a result of these schemes is not being passed on in full to the worker. For NMW workers, it seems that the Employment Businesses and umbrella companies are retaining the majority of the financial benefits, potentially representing a significant proportion of the risk to the Exchequer.

### Tax Credits

**3.39** The participation in travel and subsistence schemes also impacts on the worker's eligibility for working tax credits and again this is best illustrated by the use of example E – using the same details as Example D above (i.e. pay of £227.50, salary sacrifice of £95 and expenses paid of £72):

### Box 3.F: Example E – tax credits

Worker B, not participating in a travel and subsistence scheme, with gross pay for tax purposes of £227.50 per week or £11,862.50 per annum:

- If the worker is single, then he is eligible to receive working tax credit of £545 per annum or just over £10 per week; or
- If the worker is married and his spouse is not working then he is eligible to receive working tax credit of £2,407 per annum or just over £46 per week.

Worker C, participating in a travel and subsistence scheme, with gross pay for tax purposes of £132.50 per week or £6,908.92 per annum, i.e. after a reduction for travel expenses paid:

- If the worker is single, then he is eligible to receive working tax credit of £2,477 per annum or just over £47 per week; or
- If the worker is married and his spouse is not working, then he is eligible to receive working tax credit of £4,338 per annum or just over £83 per week.

In both cases, if the workers have children, then they will be eligible to receive child tax credit. However, working tax credit and child tax credit is paid as a total award and working tax credit is tapered away first as income rises. Therefore, at these relatively low levels of income, participation in the travel and subsistence scheme has no impact on the level of child tax credit payable.

**3.40** These examples show that workers paid at or near the NMW who participate in travel and subsistence schemes are eligible to receive significantly greater levels of working tax credit than those NMW workers who do not participate in these schemes.

# 4

## The solution being proposed and its impact

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**4.1** As announced at 2009 Pre-Budget Report (PBR), the Government is committed to addressing the problem of National Minimum Wage (NMW) workers being able to participate in travel and subsistence schemes. This is because these schemes are potentially exploitative – by participating in a salary sacrifice arrangement, the worker’s access to earnings-related contributory benefits may be adversely affected. The worker benefits little, but in the examples seen by HMRC, the Employment Business or umbrella company benefits significantly, enabling them to obtain a competitive advantage against those business who do not operate such schemes. In addition, there is a risk to the Exchequer in relation to these schemes.

**4.2** The solution being proposed to deal with this problem is to amend the NMW Regulations. These would be amended so that expenses, which qualify for tax relief under the temporary workplace rules, would no longer count as pay for NMW purposes. This would be the case whether or not the expenses are paid in accordance with a travel and subsistence scheme. One approach could be to amend Regulation 34 of the NMW Regulations<sup>1</sup> so that references to “the worker’s expenditure in connection with his employment” include expenses related to the worker’s attendance at a temporary workplace. “Temporary workplace” could then be defined in accordance with the definition contained in S339 ITEPA 2003.

**4.3** This approach has no effect on the tax and NIC rules. Tax relief continues to be available for these workers for travel to a temporary workplace, for example, where workers are paid these expenses in addition to NMW pay.

**4.4** This solution targets the particular problem for NMW workers that the Government wishes to address. Workers, other than those paid at or near the NMW, who also participate in travel and subsistence schemes would be unaffected by this proposed change.

**4.5** The change, if introduced, would take effect from 1 October 2010.

### Questions for consultation

**4.6 Question 1:** The Government believes that amending the NMW Regulations to exclude expenses which relate to travel to a temporary workplace from counting towards NMW pay is the best approach in dealing with this problem. Are there alternative approaches which would achieve the same outcome and which you believe that the Government should consider? If so, then please give details of these.

**4.7 Question 2:** Will amending the NMW Regulations in this way adversely impact on NMW workers in a way that we have not anticipated? If so, please provide details.

**4.8 Question 3:** What are your views on the potential implementation date of 1 October 2010, if the proposed changes to the Regulations are adopted?

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<sup>1</sup> SI 1999/584.

## Impact of the proposed solution

**4.9** Those Employment Businesses and umbrella companies currently using travel and subsistence schemes for NMW are likely to find that their competitiveness against Employment Businesses not making use of these schemes is reduced. Depending on the proportion of their profit margin that is made up of the tax relief they were accessing through these arrangements for NMW workers, some may find that their business model is no longer viable. (Assuming the end clients will not pay more per worker, this will result in a lower profit margin.) Some of those Employment Businesses and umbrella companies specialising in the provision of low paid workers to end clients may cease trading. This may then reduce the number of Employment Businesses providing lower paid temporary workers.

**4.10** However, as outlined above, the proposed solution only affects those workers paid at or near the NMW. So, business models which are based on the operation of travel and subsistence schemes for other, higher paid workers, will continue to be viable.

## Administrative burdens

**4.11** On the available evidence it does not seem that amending the NMW Regulations in this way would result in any impact to ongoing administrative burdens or other compliance costs to businesses. Any related costs depend on how Employment Businesses and umbrella companies respond to the new amended Regulations:

- for those businesses which continue to operate a travel and subsistence scheme via salary sacrifice but change the parameters in their current payroll system to adhere to the new NMW regulations, this will result in a negligible one-off cost to the business; or
- for those businesses which stop operating travel and subsistence schemes via salary sacrifice for NMW workers and process all payments through the payroll, again this will result in a negligible one-off cost to the business.

## Questions for consultation

**4.12 Question 4:** What would be the impact of changes to Regulations on administrative processes and costs to business?

**4.13 Question 5:** Do you have any comments on the accompanying Impact Assessment?

## Labour Market

**4.14** In some cases the financial benefits of travel and subsistence schemes are used by the Employment Business or umbrella company to reduce the amounts they charge to the end client. This may take the form, for example, of a reduction in the fee charged by an Employment Business for providing the worker's services. In other cases, the full amount of the financial benefit is retained by the Employment Business and is not passed on to the end client. Where the financial benefits of these arrangements have been used to reduce the costs charged to end clients, the proposed amendments to the Regulations will have the effect of increasing the costs to the end client.

# 5

## Summary of questions and the consultation process

### 5.1 Questions for the Consultation

#### Box 5.A: Questions for the consultation

We welcome comments on this document and the impact assessment set out at Annex B and in particular in response to the following questions:

**5.2 Question 1:** The Government believes that amending the NMW Regulations to exclude expenses which relate to travel to a temporary workplace from counting towards NMW pay is the best approach in dealing with this problem. Are there alternative approaches which would achieve the same outcome and which you believe that the Government should consider? If so, then please give details of these.

**Question 2:** Will amending the Regulations in this way adversely impact on NMW workers in a way that we have not anticipated? If so, please provide details.

**Question 3:** What are your views on the potential implementation date of 1 October 2010, if the proposed changes to the Regulations are adopted?

**Question 4:** What would be the impact of changes to Regulations on administrative processes and costs to business?

**Question 5:** Do you have any comments on the accompanying Impact Assessment?

### Process and Timeline for Consultation

**5.3** Comments on this consultation should be sent by 6 May 2010 to:

Rebecca Nunn

National Minimum Wage workers: Travel and subsistence expenses schemes Consultation

Personal Tax Team

HM Treasury, 2/SE

1 Horse Guards Road

London

SW1A 2HQ

Or email: [NMWconsultation@hmtreasury.gsi.gov.uk](mailto:NMWconsultation@hmtreasury.gsi.gov.uk)

Telephone queries: 020 7270 4307

## About the Consultation Process

**5.4** This Consultation has been conducted in accordance with the criteria in the Government's Code of Practice on Consultation. If you wish to have access to the full version of the Code, you can obtain it at:

<http://www.berr.gov.uk/whatwedo/bre/consultation-guidance/page44420.html>

### **Box 5.B: The Consultation Criteria**

1. When to consult - Formal consultation should take place at a stage when there is scope to influence the policy outcome.
2. Duration of consultation exercises - Consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
3. Clarity of scope and impact - Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
4. Accessibility of consultation exercise - Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
5. The burden of consultation - Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
6. Responsiveness of consultation exercises - Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
7. Capacity to consult - Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

If you feel that this consultation does not satisfy these criteria, or if you have any complaints or comments about the process, please contact:

Richard Bowyer  
Better Regulation Unit  
100 Parliament St  
London  
SW1A 2BQ  
020 7147 0062 or [richard.bowyer@hmrc.gsi.gov.uk](mailto:richard.bowyer@hmrc.gsi.gov.uk)

## Confidentiality Disclosure

**5.5** Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes (these are

primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004).

**5.6** If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals, amongst other things, with obligations of confidence. In view of this it would be helpful if you could explain to us why you view the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Department.

**5.7** The Department will process your personal data in accordance with the DPA and in the majority of circumstances, this will mean that your personal data will not be disclosed to third parties.



# A NICs and access to earning-related contributory benefits

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**A.1** National Insurance Contributions (NICs) are paid to build up entitlement to certain earnings-related contributory benefits, including the State Pension. The type and level of NICs paid depends on how much is earned and whether the worker is employed or self-employed.

**A.2** Entitlement to earnings-related contributory benefits, such as State Pension and the contributory element of Jobseeker's Allowance (JSA) is determined by the amount of NICs paid.

## Lower Earnings Limit

**A.3** The Lower Earnings Limit (LEL) is the minimum level of weekly earnings that an employee needs in order to achieve a qualifying earnings factor in a tax year. The 2009/10 LEL is £95 per week (£97 for 2010/11); this is the amount that someone would need to earn each week to achieve a qualifying earnings factor over 52 weeks. If an employee's earnings reach or exceed this level, but do not exceed the Earnings Threshold,<sup>1</sup> they will not pay NICs but will be treated as having paid them for the purpose of benefit entitlement.

**A.4** For example, in 2009/10 Mr B earns £95 per week, he will have to work 52 weeks of the year at this amount ( $£95 \times 52 = £4,940$ ) to achieve the qualifying earnings factor of £4,940.

**A.5** If Mr B earns £130 per week, he will have to work 38 weeks of the year at this amount ( $£130 \times 38 = £4,940$ ) to achieve the qualifying earnings factor.

## Basic State Pension

**A.6** Basic State Pension is NICs based. A person's NICs record is used to calculate the qualifying years needed for a State Pension. Up to and including 5 April 2010, a man with a State Pension age of 65 would normally need 44 qualifying years for a full basic State Pension; a woman with a State Pension age of 60, would normally need 39 qualifying years for a full basic State Pension. (A qualifying year is one where the person achieves the qualifying earnings factor.) A minimum basic State Pension would be paid on 25 per cent of these qualifying years and a person would need to have at least one year of paid NICs; a NICs record of credits only would not give any entitlement.

**A.7** From 6 April 2010, for both men and women, entitlement to a full basic State Pension will be from 30 qualifying years. A minimum basic State Pension will be paid from just one qualifying year based on paid or credited NICs. So, achieving the qualifying earnings factor is key to determining entitlement to state pension; each year that the worker has qualifying earnings of at least 52 x the LEL (or has NICs credits) gives an additional qualifying year of entitlement to basic state pension up to a maximum of 30. In a year where the worker does not achieve the qualifying earnings factor, that year will not count for the purposes of calculating entitlement to basic State Pension.

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<sup>1</sup> The Earnings Threshold is the level at which NICs become payable by the employee and employer, set at £110 per week or £5,715 per annum for 2009-10.

## Additional pension

**A.8** The additional pension is earnings-related; therefore, any reduction in the level of earnings may result in a corresponding reduction in a person's additional pension entitlement. Low earners are eligible for the low earners boost. This is targeted at people with annual earnings between the qualifying earnings factor and the low earnings threshold (£14,100 in 2010-11). People falling into this category are treated, for the purposes of the additional pension, as if they had earned £14,100. Workers paid at or near the NMW fall into the target group for the low earners boost – a worker being paid £5.80 per hour for 35 hours per week for 48 weeks would earn £9,744. This is of significant benefit to them.

**A.9** But, worker will qualify for this additional pension and therefore low earnings boost only if they achieve the qualifying earnings factor. Salary sacrifice arrangements, which impact on workers' ability to achieve the qualifying earnings factor, can affect their entitlement to additional pension.

## Jobseeker's Allowance

**A.10** This is the benefit for those who are unemployed. Up until October 2010, the main contribution conditions for Jobseeker's Allowance (JSA) are that the earner must have:

- actually paid Class 1 (employee) NICs producing an earnings factor of at least 25 times that year's LEL in respect of one of the last two complete years before the beginning of the relevant benefit year; and
- have paid Class 1 NICs or been credited with earnings of at least 50 times the LEL in each of the last two complete tax years before the beginning of the relevant benefit year.

**A.11** The current maximum weekly JSA rates are:

- Age 16 - 25: £50.95;
- Age 25 or over: £64.30.

**A.12** From October 2010, the contribution conditions will be as follows:

- the earner must have paid, or been treated as having paid, Class 1 NICs on earnings at or above the LEL for at least 26 weeks in respect of one of the last two complete years before the beginning of the relevant benefit year; and
- have paid Class 1 NICs or been credited with earnings of at least 50 times the LEL within the last two complete tax years before the beginning of the relevant benefit year.

**A.13** Currently, a worker's participation in a travel and subsistence scheme may prejudice his ability to satisfy both of the contribution conditions for JSA, as the reduction in the worker's gross pay increases the number of weeks of earnings that the worker needs in order to secure access to JSA. As a result of the changes being brought in October this year, such schemes will no longer significantly affect a worker's ability to meet the first contribution condition, but could still have an adverse impact on the worker being able to satisfy the second condition.

## Employment and Support Allowance

**A.14** Employment Support Allowance (ESA) was introduced on 27 October 2008, replacing Incapacity Benefit, for employees not qualifying for Statutory Sick Pay (SSP) and persons that fall sick whilst they are unemployed. ESA consists of 2 time periods – the assessment phase rate (paid for the first 13 weeks of a claim) and the main phase (starting from 14 weeks of a claim). The weekly ESA rate for 2009-2010 is £64.30 for the assessment phase and £89.90 for the main phase.

**A.15** The qualifying conditions for ESA are being broadly aligned with JSA with effect from October 2010 (one of the major differences that will remain for ESA is that Class 2 contributions are counted towards meeting the qualifying criteria).

**A.16** So, from October 2010, the contribution conditions will be as follows:

- must have paid or been treated as having paid Class 1 or Class 2 NICs on earnings at or above the LEL for at least 26 weeks in respect to one of the last two complete years before the beginning of the relevant benefit year; and
- having paid Class 1 or Class 2 NICs or been credited with earnings of at least 50 times the LEL within the last two tax years before the beginning of the relevant benefit year.

## How travel and subsistence schemes can affect benefit entitlement

**A.17** As set out at paragraphs 3.25 to 3.32, by participating in travel and subsistence schemes, NMW workers reduce their pay on which NICs is paid. This, depending on how many weeks they are able to work for, puts at risk their ability to achieve the qualifying earnings factor and may affect entitlement to certain earnings-related contributory benefits, in particular basic and additional State Pension and to some extent working-age contributory benefits, such as ESA and JSA.



# B

## Impact Assessment

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Impact Assessment follows overleaf.

## Summary: Intervention & Options

<b>Department /Agency:</b> <b>HM Revenue and Customs</b>	<b>Title:</b> <b>Impact Assessment of Travel &amp; Subsistence Schemes for NMW Workers.</b>	
<b>Stage:</b> Consultation	<b>Version:</b> 1	<b>Date:</b> 4 February 2010
<b>Related Publications:</b> Schemes	National Minimum Wage workers: Travel and Subsistence Expense	

### Available to view or download at:

[http://www.hm-treasury.gov.uk/consult\\_fullindex.htm](http://www.hm-treasury.gov.uk/consult_fullindex.htm)

**Contact for enquiries:** Rebecca Nunn

**Telephone:**

**020 7270 4307**

### What is the problem under consideration? Why is government intervention necessary?

Temporary workers paid at or near the National Minimum Wage (NMW) can participate in travel and subsistence schemes, operated by some Employment Businesses and umbrella companies. These are designed to provide tax and NICs savings and to comply with NMW rules. Participation may adversely affect workers' access to social security benefits and the Government believes this introduces unfairness. Many Employment Businesses etc retain most of the financial benefits from the schemes - the impact on pay and benefits is often not fully explained to workers. Those businesses not wishing to operate these schemes for NMW workers suffer a competitive disadvantage, leading to market distortion.

### What are the policy objectives and the intended effects?

The Government's objective is to address this problem by allowing full access to earnings related social security benefits, creating a level playing field for businesses engaging temporary NMW workers and protecting the Exchequer. The proposed amendment to the NMW Regulations would protect the contributory benefit position of low paid workers currently participating in these schemes and stop others being potentially prejudiced. It would also result in a fairer market as there would be competition on more equal terms. Expenses for travel to a temporary workplace would no longer count as NMW pay, so more NMW pay would be subject to tax and NICs, increasing the amount paid to the Exchequer.

### What policy options have been considered? Please justify any preferred option.

The options that have been considered are:

- no change - continue with the status quo; or
- amend the NMW Regulations so that expenses paid to a worker for travel to a temporary workplace, as defined for tax and NICs purposes, will not count towards their NMW pay.

Amending the Regulations is the preferred option. This deals with the potential adverse impact of these schemes on workers' access to social security benefits and creates a level playing field for Employment Businesses providing temporary workers paid at or near the NMW.

### When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

A final impact assessment taking into account stakeholders' responses to the consultation will be produced prior to implementation.

### **Ministerial Sign-off** For consultation stage Impact Assessments:

*I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.*

Signed by the responsible Minister



.....Date: 4 February 2010

## Summary: Analysis & Evidence

**Policy Option: 1**

**Description: No change**

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' Employment Businesses and Umbrella Companies will continue their current payroll system.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£ 0		
	<b>Average Annual Cost</b> (excluding one-off)		
	£ 0		<b>Total Cost (PV)</b> £ 0
Other <b>key non-monetised costs</b> by 'main affected groups' NONE			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' NONE
	<b>One-off</b>	<b>Yrs</b>	
	£ 0		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 0		<b>Total Benefit (PV)</b> £ 0
Other <b>key non-monetised benefits</b> by 'main affected groups' NONE			

**Key Assumptions/Sensitivities/Risks** The expected growth in travel and subsistence schemes available to temporary workers will lead to a reduction in the amount of tax and NICs payable to HMRC.

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £ 0	<b>NET BENEFIT (NPV Best estimate)</b> £ 0
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	N/A			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	£ Not Quantifiable			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	N/A			
What is the value of the proposed offsetting measure per year?	£ 0			
What is the value of changes in greenhouse gas emissions?	£ 0			
Will the proposal have a significant impact on competition?	Yes			
Annual cost (£-£) per organisation (excluding one-off)	Micro £0	Small £0	Medium £0	Large £0
Are any of these organisations exempt?	No	No	No	No

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)
Increase of £ 0	Decrease of £ 0	<b>Net Impact</b> £ 0

Key: Annual costs and benefits: (Net) Present

## Summary: Analysis & Evidence

**Policy Option: 2**

**Description: Amend the National Minimum Wage Regulations.**

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' Employment Businesses and umbrella companies may have to change the control parameters in their current payroll system or revert to the standard payroll system to secure the NMW of some workers. This is estimated to be negligible.	
	<b>One-off</b> (Transition)	<b>Yrs</b>		
	<b>£ NEG</b>			
	<b>Average Annual Cost</b> (excluding one-off)			
	<b>£ 0</b>		<b>Total Cost (PV)</b>	<b>£ NEG</b>
Other <b>key non-monetised costs</b> by 'main affected groups' NONE				

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' NONE	
	<b>One-off</b>	<b>Yrs</b>		
	<b>£ 0</b>			
	<b>Average Annual Benefit</b> (excluding one-off)			
	<b>£ 0</b>		<b>Total Benefit (PV)</b>	<b>£ 0</b>
Other <b>key non-monetised benefits</b> by 'main affected groups' Amending the Regulations removes a tax distortion in the labour market and increases the availability of earnings-related contributory benefits to workers receiving at or around National Minimum Wage.				

**Key Assumptions/Sensitivities/Risks**

This option is expected to increase the amount of tax and NICs collected by £35m in 2010-11 and £85m for 2011 onwards due to the reduction of workers using travel and subsistence schemes. This additional revenue will be collected from Employment Businesses and workers using such schemes.

Price Base Year 2010	Time Period Years 5	<b>Net Benefit Range (NPV)</b> <b>£ NEG</b>	<b>NET BENEFIT (NPV Best estimate)</b> <b>£ NEG</b>	
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	October 2010			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	<b>£ NEG</b>			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	N/A			
What is the value of the proposed offsetting measure per year?	<b>£ 0</b>			
What is the value of changes in greenhouse gas emissions?	<b>£ 0</b>			
Will the proposal have a significant impact on competition?	Yes			
Annual cost (£-£) per organisation (excluding one-off)	Micro £0	Small £0	Medium £0	Large £0
Are any of these organisations exempt?	No	No	No	No

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)	
Increase of	£ 0	Decrease of	£ 0
		<b>Net Impact</b>	<b>£ 0</b>

Key: Annual costs and benefits: (Net) Present

## Evidence Base (for summary sheets)

### 1. Background

Traditionally, temporary workers placed with end clients by Employment Businesses have been engaged under “agency contracts”. This means that each placement is considered to be a permanent place of employment for tax and National Insurance Contributions (NICs) purposes. As a consequence the cost of the worker’s travel to the end client and any associated subsistence costs are not eligible for tax relief as this is home to work travel.

In recent years there has been a growth in travel and subsistence schemes operated by some Employment Businesses and umbrella companies. These schemes involve the engagement of workers under an overarching employment contract. This changes what would otherwise be home to work travel into travel to a temporary workplace. The cost of travel to a temporary workplace and associated subsistence costs are eligible for tax relief and are disregarded for NICs purposes.

Many travel and subsistence schemes use salary sacrifice arrangements. This means the worker sacrifices from his gross pay for tax purposes, a sum equivalent to, or in some cases greater than, the travel and subsistence payments which are paid by the Employment Business or umbrella company. Providing the arrangements are implemented correctly, no PAYE and NICs are payable on the salary sacrificed, nor on the travel and subsistence expenses paid.

Workers who are paid at or around the National Minimum Wage (NMW) rates are not able to participate in salary sacrifice arrangements if the amount sacrificed would reduce their pay below NMW rates. Where a salary sacrifice arrangement is entered into, it is a matter of looking at all the payments made to, and deductions made from, the worker to consider whether the worker has been paid at least the NMW. The NMW legislation and the expenses rules for income tax and NICs treat expenses paid by the employer for travel to a temporary workplace in different ways. For NMW purposes, these expenses are treated as not being “in connection” with the worker’s employment and so are classed as pay for NMW purposes. This is in contrast to the tax and NIC position, where these travel and subsistence expenses do not count as pay for tax and NIC purposes, as they are eligible for tax relief and are disregarded for NICs.

The availability of tax relief for travel expenses (and for the expenses to be disregarded for NICs) and whether there is compliance with the NMW Regulations depends on the way that these travel and subsistence scheme arrangements are implemented. In some cases that HMRC have seen the arrangements are not fully compliant. Where non-compliance is identified, HMRC will take enforcement action.

In many cases, travel and subsistence schemes result in the NMW worker taking home only slightly more each week in his pay packet than a worker not in a scheme. This small uplift in pay, which is still important to a low paid worker, is emphasised strongly to the worker by the Employment Business or umbrella company. However, it is usually the Employment Business or umbrella company which benefits the most from the scheme, retaining most of the financial benefits – a fact the worker may be unaware of.

The worker is not usually advised of the longer term, potentially adverse, consequences for his entitlement to earnings-related social security benefits that can result from participation in these schemes. In cases that HMRC has seen, workers paid at the NMW, currently £5.80 per hour for those aged 22 or more (equivalent to £232 for a 40 hour week) and using travel and subsistence schemes can be sacrificing as much as 40% of their wages in return for the payment of travel and subsistence expenses. Entitlement to earnings-related contributory benefits is based on a worker attaining the “qualifying earnings factor”. This means a worker needs earnings on which NICs are due equivalent to 52 x the Lower Earnings Limit, (which for 2009/10 is £4,940) to accrue entitlement to certain benefits, in particular basic State Pension and additional State Pension. These travel and subsistence schemes, which reduce workers’ earnings subject to NICs, particularly for temporary workers who frequently work less than 40

hours per week, potentially prejudice a worker's ability to attain a qualifying earnings factor. This results in adverse consequences for entitlement to earnings-related social security benefits.

It is also important to note that where a worker participates in a travel and subsistence scheme, the reduction in his gross pay for tax purposes may mean that the amount of Working Tax Credits which he is entitled to claim may increase, compared to a NMW worker who does not participate in such a scheme.

The Government has received a number of complaints from businesses in connection with these schemes.

## **2. Policy Objectives**

The Government is committed to tackling the problem of NMW workers being able to participate in travel and subsistence schemes, which potentially exploit low paid workers. The Government's objective is threefold:

- 1) To ensure that the contributory benefit position of temporary workers paid at or near the NMW is not prejudiced by the reduction of earnings liable to Class 1 NICs;
- 2) To ensure that Employment Businesses and umbrella companies do not gain an unfair competitive advantage through the use of travel and subsistence schemes for these temporary workers: and
- 3) To protect the Exchequer.

## **3. The Options**

Option 1: Do nothing.

Leave the existing NMW Regulations unchanged allowing temporary workers to continue to use travel and subsistence schemes not counting this expense when calculating their pay for NMW purposes.

Option 2: Amend the National Minimum Wage Regulations.

In this option the NMW Regulations would be amended so that expenses paid to an employee for the cost of travel from home to a temporary workplace along with associated subsistence costs will not count as pay for NMW purposes.

## **4. Consultation**

The Government already liaises extensively with stakeholders in the temporary labour market. As a result of that liaison and HMRC's operational compliance activity it believes that, in general terms, it has an understanding of the costs, benefits and risks of the options outlined. However, given the nature of the low-paid temporary labour market, with changing and evolving labour providers and business models, the precise behavioural effects would be better informed by a consultation process which enables stakeholders to comment in detail on a specific proposal.

## **5. The Risks and Expected Impacts**

*Option 1: Do nothing.*

If the existing Regulations are left unchanged then temporary workers will continue to be paid through travel and subsistence schemes, reducing their pay for tax and NICs purposes with consequential potential prejudice to their contributory benefit entitlement.

HMRC compliance staff have been asked by Employment Businesses how they can set up their own travel and subsistence schemes and others have complained that they are being undercut

by users of such schemes. Scheme promoters emphasise the financial benefits of such schemes to prospective clients and scheme users emphasise the financial benefits to prospective workers (although not the disadvantages). Additionally, there appears a general upward trend in the number of businesses placing low paid workers (certainly the Gangmasters Licensing Authority projects an increase in licence applications in 2010-11 in the GLA-licensed sector). There is a risk that these schemes will become more widely used by Employment Businesses or umbrella companies to secure an unfair competitive advantage over those not using such schemes. This is achieved both by being able to entice workers away from competitors with the promise of greater take home pay and by using some of the financial savings to undercut competitors. The use of such schemes will continue to distort the temporary labour market. Already the reality is that workers have limited choices in terms of working through such schemes and a further risk is that more workers will have little option but to be paid through such schemes with the potential prejudice to their contributory benefit position.

#### *Option 2: Amend the National Minimum Wage Regulations.*

The proposed change to the NMW legislation means that those NMW workers currently participating in travel and subsistence schemes would see an increase in their gross pay and a small reduction in their weekly take home pay. This will increase the PAYE and NICs payable to the Exchequer. It will, however, ensure that temporary workers' pay on which NICs is payable and which is used for contributory benefit purposes, cannot be reduced below the NMW rate in return for the payment of travel expenses. Those workers currently in travel and subsistence schemes would be engaged on the same basis as those placed by Employment Businesses not using such schemes. Not only does the Government believe that this is equitable, but equal treatment of workers will restore the level playing field in the market place ensuring Employment Businesses tendering for work are doing so broadly on the same terms. Where workers are incurring travel and subsistence costs in attending work, it will be for individual Employment Businesses to determine how such costs are addressed when agreeing terms with workers.

Employment Businesses currently paying workers through travel and subsistence schemes may behave in a number of different ways as a result of changes to NMW Regulations. The Government believes the following scenarios are the two most likely:

- Some may revert to engaging workers through agency contracts meaning that any travelling costs to the client's premises and associated subsistence costs would not be eligible for tax relief;
- Some may continue to engage workers through overarching employment contracts and pay tax free expenses in addition to NMW pay.

It should be emphasised that that the proposed change is unlikely to result in a uniform reaction across all scheme users because of the nature of temporary labour provision. Different supply and demand issues in different sectors will influence responses, as will the size and underlying business plans of scheme users.

## **6. Costs and Benefits**

### *Option 1: Do nothing.*

#### Costs & Administrative Burdens

None for businesses directly. It is possible that cognisant of reputational damage, end clients will not wish to be associated with Employment Businesses using travel and subsistence schemes which appear to profit from low paid workers. HMRC may need to deploy more compliance resources to address the growth in the schemes.

## Benefits

None

## Revenue Effects

The expected growth in travel and subsistence schemes available to temporary workers will lead to a reduction in the amount of tax and NICs payable to HMRC. The Government estimate that this will result in an erosion of Exchequer receipts.

### *Option 2: Amend the National Minimum Wage Regulations.*

## Costs & Administrative Burdens

Employment Businesses and umbrella companies involved directly or indirectly in placing low-paid temporary workers across all sectors will be affected by this option. HMRC has received complaints from a number of Employment Businesses not using travel and subsistence schemes that they are being undercut by competitors which are using such schemes.

As a result, it is possible that in some instances this option will increase costs to end clients. However, since many Employment Businesses and temporary workers are currently operating without the financial advantages of such schemes, it is unlikely to have a profound effect on the average cost of labour to end users.

Where Employment Businesses and umbrella companies specialise in the low paid labour market, it may not be viable to continue with their current business model due to a reduction in their profit margin, resulting in either a change of business model or in a few cases to cease trading. Despite this, the Government does not believe that this option will affect labour supply.

On the available evidence, HMRC does not expect there to be any significant impacts, either in terms of one-off transitional costs, administrative burdens or other compliance costs to businesses. The related costs depend on precisely how Employment Businesses and umbrella companies respond to the new Regulations. Current travel and subsistence schemes are administered through the scheme user's payroll - the salary sacrifice which the worker enters into to reduce his gross pay and the expenses that are paid in addition to net pay for travel to a temporary workplace are processed as payroll adjustments. The change in Regulations would mean that these adjustments would no longer be required. The full amount of NMW pay would simply be processed as gross pay for tax and NICs, as would be the case if the worker did not participate in a travel and subsistence scheme.

## Benefits

The Labour Force Survey (LFS) estimates 1.3million temporary workers during 2009 and the Government estimates that this will rise to 1.4million in October 2010, the proposed implementation date of this option. Further analysis of the LFS data indicates that about 350,000 (25%) of temporary workers are paid at or near the National Minimum Wage. The Government then estimates that of this number, 90,000 will be paid using a travel and subsistence scheme.

Amending the NMW Regulations substantially helps to protect the contributory benefit position of those 90,000 workers and stops others being potentially prejudiced.

This option creates a level playing field, and results in a fairer marketplace where Employment Businesses are subject to the same levels of taxation. This is because a well functioning market, free from the distortionary impact of these schemes, underpins greater and fairer competition between firms which promotes better resource allocation. However, it is difficult to quantify the value of these benefits.

This option potentially reduces the risk of reputational damage to end user clients, as there will be less scope for Employment Businesses to prejudice workers' contributory benefits, and artificially distort the labour market.

## Revenue Effects

This option also increases the amount of income subject to tax and NICs. In practical terms this would mean that a worker working 40 hours per week at the NMW rate would need to be paid any travel and subsistence expenses *in addition* to the £232 NMW pay.

The Government estimates that on average, a temporary worker earning the National Minimum Wage works 27 hours per week. It is assumed that approximately 33% of their pay is sacrificed to the travel and subsistence scheme. This results in an expected Exchequer yield of £35m in 2010-11 and £85m for 2011 onwards. This is based on a proposed implementation date of October 2010 and that all businesses will comply with the change of Regulations.

It is standard practice for all tax measures that revenue effects or changes in tax yield are not incorporated into the main cost/benefit analysis. This is primarily due to the fact that they are pure transfers and, as they are generally much larger than the other costs and benefits, tend to distort the cost/benefit ratio. This could give a misleading picture of the balance between the costs and benefits of the measure. As a consequence, any quantified revenue effects are shown on the summary sheet within the 'Key Assumptions/Sensitivities/Risks' box, which is outside the main appraisal of the costs and benefits.

## **7. Impact Tests**

### Competition Assessment

Employment Businesses and umbrella companies using travel and subsistence schemes for NMW workers are likely to find their competitiveness against Employment Businesses using other business models is reduced. Depending on the proportion of their profit margin that is made up of the tax relief they were accessing through these arrangements, some may find that their business model is no longer viable. This may reduce the number of businesses providing lower income temporary workers.

The Government does not consider this to be an anti-competitive effect of this proposal. Employment Businesses and umbrella companies that are using salary sacrifice to reduce their costs and potentially reduce pay below the minimum wage are taking advantage of their business structure to obtain an unfair advantage over Employment Businesses and umbrella companies who are unwilling to do the same.

The proposed solution that travel and subsistence expenses would not count as pay for NMW purposes ensures that all Employment Businesses providing temporary workers are competing equally, regardless of the pay level of the workers.

### Small firms

In general, Employment Businesses and umbrella companies paying low-paid workers through travel and subsistence schemes place large numbers of temporary workers with end clients. Particularly for an Employment Business, engaging low-paid workers under an overarching employment contract is not financially viable where only small numbers of workers are concerned. Accordingly the Government does not believe that the proposed option will impact on small firms.

### Equality Assessment

In line with better regulation best practice and the Equalities Duties we have considered the impact of changing the law by gender. The Labour Force Survey indicates that around 45 percent of the temporary workforce are men and around 55 percent are women. We believe that there will be similar proportions of men and women who are directly affected by policy changes.

The Government estimate 90,000 temporary workers paid at or near the National Minimum Wage will be paid through some form of travel and subsistence scheme. This represents a weighted figure and it would not be sensible to attempt to disaggregate this figure further by ethnicity or disability as the results may not be reliable. The proposed changes reflect a broad policy and are designed to have a positive impact on all workers regardless of their gender, race or disability. Therefore the proposed changes are unlikely to create any barriers to equality in terms of gender, race and disability.

#### Rural proofing

Although some low-paid temporary workers work in rural areas (primarily in the agricultural sector), Government does not believe that the preferred option will have any significant impact on rural communities.

#### Other Specific Impact Tests

The Government has considered the remaining impact tests and does not think that the options will impact on small firms, legal aid, sustainable development, carbon assessment, other environment, health or human rights.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No





## HM Treasury contacts

This document can be found in full on our website at:

[hm-treasury.gov.uk](http://hm-treasury.gov.uk)

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