



HM Revenue  
& Customs

# Employment Intermediaries: Temporary workers – relief for travel and subsistence expenses

## **Discussion document**

Publication date: 16 December 2014

Closing date for comments: 10 February 2015

<b>Subject of this discussion:</b>	This paper seeks views on the use of overarching contracts of employment (OAC) by employment intermediaries in the temporary labour market.
<b>Scope of this discussion:</b>	To understand how OACs are currently used by employment intermediaries in the temporary labour market the scope, to inform potential future action
<b>Who should read this:</b>	Views on the issues and questions set out in this paper are invited from all interested parties from the temporary labour market, and any other interested parties.
<b>Duration:</b>	16 December 2014 until 10 February 2015.
<b>Lead official:</b>	All enquiries regarding the content or scope of the discussion or further information about the discussion should be addressed to:  <b>HM Revenue &amp; Customs  Employment Status Team  Room 1E/10, 100 Parliament Street  London  SW1A 2BQ</b>  <b>Email: <a href="mailto:oac.review@hmrc.gsi.gov.uk">oac.review@hmrc.gsi.gov.uk</a></b>
<b>How to respond or enquire about this discussion:</b>	Responses to this discussion paper are requested by 10 February 2015 and should be sent by email to the review team using the following address: <a href="mailto:oac.review@hmrc.gsi.gov.uk">oac.review@hmrc.gsi.gov.uk</a> .
<b>Additional ways to be involved:</b>	HM Treasury and HMRC will consider written submissions addressing the questions and issues raised in this discussion paper.
<b>After the discussion:</b>	Responses to this discussion paper will be considered by the government and used to inform potential future action.

**Getting to this stage:**

The government has already taken a number of steps to address unfair practices in the temporary labour market during the course of this parliament:

- In 2011 the National Minimum Wage rules were amended to prevent travel expenses paid under salary sacrifice schemes counting towards the National Minimum Wage
- At Budget 2013 the government announced new rules to tackle the use of offshore intermediaries to avoid employment taxes
- At Autumn Statement 2013 the government announced rules to deal with onshore intermediaries used to facilitate false self-employment
- In October, the Secretary of State for Business, Innovation and Skills announced an internal review of employment status.

**Previous engagement:**

In parallel to this review, following the Office of Tax Simplification (OTS) review of benefits and expenses, the government is also simplifying the rules for employers who wish to pay or reimburse qualifying expenses to their employees

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**On request this document can be produced in Welsh and alternate formats including large print, audio and Braille formats**

# 1. Foreword

Income tax and National Insurance Contributions (NICs) account for over 40% of total government receipts and are paid by around 30 million individuals. One of the government's important priorities has been to give more support to those on low and middle incomes through increases to the income tax personal allowance to £10,600 by 2015-16. This represents a rise in the personal allowance of more than 64% in just five years. As a result of this government's policies, a total of 3.4 million low paid individuals have been taken out of income tax altogether.

The government believes this is the most effective way to support those on low and middle incomes, because it enables people to keep more of the money they earn. Reducing the amount of income tax that people pay also rewards those who want to work hard and progress.

The government wants the tax system to be fair for everyone. It is committed to ensuring that the tax system is not exploited by businesses and individuals who seek to pay less tax than others in similar circumstances. Tackling tax avoidance, tax evasion and addressing unfair outcomes has been a priority for this government.

Temporary labour plays an important role in the UK's dynamic labour market, and helps provide flexibility to both employees and employers. At present, 1.7 million people are temporary employees, around 6.5 percent of all employees – the same as the 20 year average share of employment.

However, there is evidence that some businesses in this part of the labour market are seeking to avoid paying employment taxes, including National Insurance, for their workers. This is not fair and undermines businesses that don't participate in this behaviour.

The government has already taken a number of steps to address unfair practices in the temporary labour market during the course of this parliament:

- In 2011 the National Minimum Wage rules were amended to prevent travel expenses paid under salary sacrifice schemes counting towards the National Minimum Wage
- At Budget 2013 the government announced new rules to tackle the use of offshore intermediaries to avoid employment taxes
- At Autumn Statement 2013 the government announced rules to deal with onshore intermediaries used to facilitate false self-employment

Taken together, these measures will raise £600m this year, and around a further £1.5bn in the next three years.

However, the government cannot stand still on tax avoidance in this area. Despite this action, some businesses continue to seek to avoid tax and deprive people of basic employment rights like the minimum wage. Most recently, there has been an increase in the use of overarching contracts by umbrella companies and employment agencies who seek to use such contracts to exploit the tax rules for travel and subsistence for

temporary workers. This is estimated to be costing the exchequer at least £400m a year.

The government is committed to tackling tax avoidance. This discussion paper sets out the issues the government is concerned about and proposes potential solutions. It will inform the government's decisions at Budget 15 on how to best address this avoidance whilst ensuring that arrangements that do not seek to exploit the tax rules are not affected.

A handwritten signature in black ink, appearing to read 'David Gauke'.

**David Gauke MP**

## 2. Introduction

1. Autumn Statement 2014 announced that the government would review the use of overarching contracts of employment (OAC) by employment intermediaries in the temporary labour market to take advantage of the rules for travel and subsistence expenses. These arrangements mean that some people are able to benefit from tax relief on home to work travel expenses that is not generally available to others. This can enable intermediaries to reduce the gross taxable pay of their workers at the expense of the general taxpayer. The cost to the Exchequer from these practices is substantial, amounting to around £400m a year from umbrella companies alone and we know that other employment intermediaries use similar OACs, although the extent to which they are used to confer employment rights as opposed to solely being a mechanism to avoid tax is unclear.
2. This discussion paper:
  - Sets out the background to the issue, explains how these contracts work in practice and the interaction with the tax rules for travel and subsistence (Section 3)
  - Sets out the case for change, including the impact of these arrangements on the Exchequer (Section 4)
  - Outlines proposals for tackling these issues (Section 5)
  - Summarises the key questions and issues we would like to test with external stakeholders and sets out next steps (Sections 6 and 7)
3. The response to this document will inform decisions for Budget 2015. However, any proposed measure to address this misuse will not come into effect until 2016 at the earliest. This will allow time for people working under an OAC to make informed decisions, and to remove themselves from an OAC if they wish without being disadvantaged.
4. Alongside this review, following the Office of Tax Simplification (OTS) review of benefits and expenses, the government is also simplifying the rules for employers who wish to pay or reimburse qualifying expenses to their employees<sup>1</sup>. As announced at Autumn Statement 2014, from 6 April 2016 employers will be able to pay or reimburse certain expenses without being required to report these payments to HMRC or apply for an agreement not to deduct tax from these payments in advance (known as a 'dispensation'). However, the exemption will not apply to expenses paid by the employer through a salary sacrifice scheme. This will prevent businesses engaging in these schemes to take advantage of the travel and subsistence rules to avoid paying the full amount of employer National Insurance on their workers' pay. This will, in part, address some of the concerns raised in this paper and is covered in more detail in paragraphs 57 to 59.

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<sup>1</sup> The exemption applies to certain business expenses that have to be paid in the course of the employee's work and where, if the employee had met the costs themselves, they would have been able to claim tax relief. For example the cost of maintaining tools needed for the employee's job.

5. The government is also undertaking a wider review of the tax rules for travel and subsistence expenses with a view to modernising these rules to reflect current practices. However, as any changes introduced as a result of the wider review will take a number of years to come into force, this discussion paper has been published now as the government cannot overlook the current avoidance.
6. In parallel to the work conducted by HMRC and HM Treasury, in October, the Secretary of State for Business, Innovation and Skills announced an internal review of employment status<sup>2</sup>. OACs may be the right option for many individuals and businesses regardless of whether changes are made to the tax rules, in part because of the employment rights that the individual can be entitled to as a result of being an employee. However, in deciding whether using an OAC is the right choice, individuals and employers need to understand what the status of 'employee' means for them.
7. Determining employment status and interpreting benefits can be complicated and for some, and the consequences of their working relationship are sometimes not fully understood. The government wants to address this which is why the Department for Business, Innovation and Skills is conducting the review of employment status. The review seeks to consider what the UK labour market looks like and how the government can deliver a framework that strikes the right balance between the rights of the individual and the needs of business, improving transparency for everyone. This review will report to Ministers next year. In addition the OTS is undertaking a review into employment status for tax purposes which will produce a report in time for Budget 2015.<sup>3</sup>
8. To ensure that the issues of the use of OACs to avoid tax are taken in the wider context, and noting the implications on employment status and rights, the government will continue to work closely with interested parties. It will consider any emerging themes from reviews by the Department for Business Innovation and Skills and OTS reviews, in addition to reflecting upon responses to this discussion document when coming to a decision at Budget 2015.

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<sup>2</sup> <https://www.gov.uk/government/news/employment-review-launched-to-improve-clarity-and-status-of-british-workforce>

<sup>3</sup> <https://www.gov.uk/government/publications/employment-status-review/key-questions>

### 3. Background

9. This section explains how overarching contracts of employment (OAC) work in practice and how they can be used by some to secure a tax advantage. It also sets out some of the other reasons employment intermediaries use overarching contracts.

#### What is an overarching contract of employment?

10. OACs are a legitimate form of employment contract used by some employment businesses<sup>4</sup> and umbrella companies to place temporary workers on multiple separate work placements, but on terms and conditions of a single permanent employment. The employment business or umbrella company becomes the employer of the temporary worker. However, their premises are not the employees' normal place of work, and they are not the organisation which directs the employee in their day to day tasks. This contractual arrangement enables individuals to access tax relief on travel costs and daily subsistence costs.
11. This is contrasted with the position under direct contracts of employment – temporary or permanent – where the employer provides the temporary employee's normal place of work, and the employer directs the employee in their day to day tasks.
12. Direct contracts only represent a small proportion of the total temporary labour market. Temporary agency workers placed under assignment-based contracts make up most of the market. Under these more common contracts, the individual contracts with a third party, typically an employment business, to undertake work for a client of the employment business. For tax purposes, each separate work placement is treated as a permanent employment contract in its own right, and each work location is treated as permanent. As there is no contract between the end client and the individual, they cannot be an employee of the client. However, key aspects of the individual's terms and conditions are directly linked to the client: the client's premises become the designated workplace of the individual, and after twelve weeks in the same work placement, the individual becomes entitled to equal basic employment and working conditions as comparable workers or employees directly hired by the client.
13. For both direct contracts of employment and assignment based temporary worker contracts, tax relief isn't generally available for travel between home and work. The terms and conditions of an OAC generate the difference in treatment with individuals on more common employment business contracts. OACs can provide for ongoing mutual obligations between the individual and the employment business or umbrella company between work placements. They must also relate to payment for work personally performed by the individual. On the strength of these obligations being included in the OAC, the individual is treated as having an

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<sup>4</sup> Throughout this document the term 'employment business' is used in relation to the employment intermediaries colloquially referred to as 'temporary employment agencies', or 'temping agencies'.

ongoing employment with the employment intermediary rather than a series of separate engagements.

14. As such, where an individual is engaged on an OAC, they are treated as having a permanent base location (usually at the address of the umbrella company or employment business engaging them). Each separate work placement they undertake is then treated as part of their permanent employment but taking place at a temporary location.
15. OACs generate differences in access to travel and subsistence reliefs, confer additional employment rights on an individual and change the incidence of administrative obligations particularly with respect to operating PAYE compared to an agency worker. Taken together, these can provide a rationale for why OACs are put in place by umbrella companies and some employment businesses.

## **Why are Overarching Contracts of Employment (OACs) used?**

### ***Travel & subsistence expenses***

16. Generally tax and NICs relief is not available for the travel and subsistence expenses incurred by employees on travel between their home and their normal place of work as noted above. However an employee can get tax and NICs relief if the place they are travelling to is a “temporary workplace”.
17. Broadly speaking, a temporary workplace is somewhere that the employee must go to in order to perform a task of limited duration, provided that they do not expect to be at the workplace for more than 24 months. If an employee is expecting to be at a workplace for the whole of their employment (even if that is less than 24 months) then it is not classed as a temporary workplace and so no tax or NICs relief is available for travel between the employee’s home and that workplace. This would normally include employment business workers who have a separate contract for each distinct engagement.
18. By creating a single employment relationship spanning all of the engagements, OACs stop these rules applying, meaning that each workplace is treated as a temporary workplace provided that the individual expects to be there for less than 24 months.
19. Therefore, under certain OACs the individual is entitled to claim tax relief on their travel and subsistence expenses from their home to each temporary place of work. This tax relief is not available to a temporary agency worker engaged directly by an employment business, or to those who are directly employed by businesses using their labour. It is an established principle in the tax system that people should not be able to claim travel and subsistence expenses with respect to their regular travel from their home to work; in line with this, ordinary commuting costs incurred by the vast majority of workers are not tax deductible.

**Example:**

Sarah finds work in a call centre on a 6 month contract through an employment business. Sarah spends £35 a week on travelling from home to work and £25 a week on lunch. If Sarah was engaged by an employment intermediary under an OAC, she would likely be entitled to tax relief on her home to work travel costs and lunch costs of up to £5 a day (assuming she works more than 5 hours each day). However, if Sarah was engaged on a common employment business contract or was recruited directly, then no tax relief would be due for these costs.

20. Some employment intermediaries using OACs (as well as some other employers whose employees incur relievable expenses) take these arrangements one step further and reimburse travel and subsistence expenses in return for a deduction in salary rather than reimbursing the expenses on top of the individual's salary. This effectively swaps pay that would have been subject to tax and employee NICs for reimbursed expenses which are not. This also reduces the employment intermediary's employer NICs liability at no additional cost since the employee's wages have been reduced accordingly. Some arrangements go further, and involve the employment intermediary keeping some of the tax and NICs relief in the name of the employee for themselves. The reductions in salary which are a feature of all these arrangements can potentially impact peoples' statutory payment and contributory benefit entitlements.
21. One common way expenses are paid instead of, rather than on top of salary is through salary sacrifice. However the government has announced at Autumn Statement 2014 that, as part of the proposals to simplify the way that expenses are administered, from April 2016 tax and NICs relief will no longer be available on expenses which are given under a salary sacrifice arrangement. This raises £360m over the next five years.
22. Whilst individuals engaged under an OAC by an umbrella company may be in a position to pay less tax than an identical worker engaged under traditional employment business arrangements, any financial benefit to the individual can often be offset by the administrative fees charged to them by their umbrella company. This can mean there is only marginal, or even negative financial benefit to the individual to being engaged under an OAC instead of under a traditional employment business arrangement. For some, the fee due to the umbrella company is greater than the value of the travel and subsistence tax relief they are able to claim.

### **Umbrella companies**

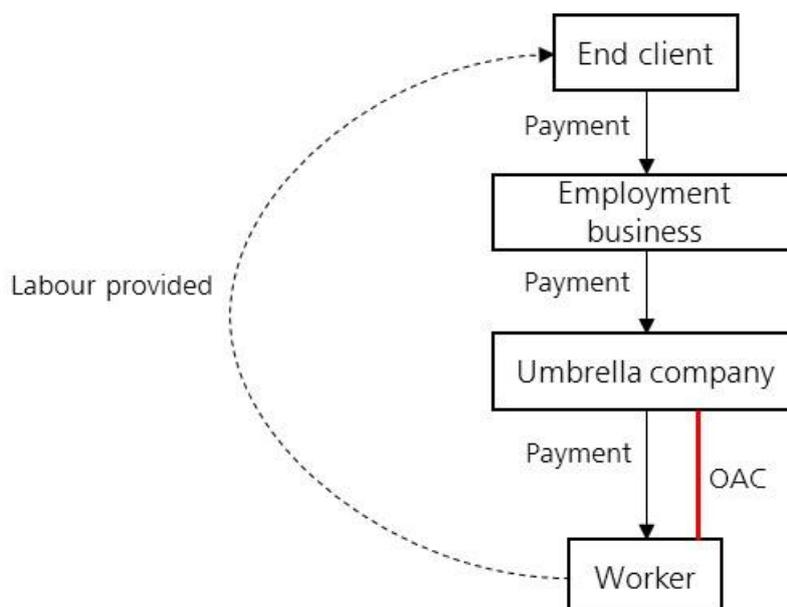
23. Umbrella companies have been around for some time. They employ temporary workers on OACs; these workers are engaged, or directed on a day to day basis by other businesses.
24. Umbrella companies differ from employment businesses that directly employ people using OACs in that:

- The umbrella company does not source the work from end clients for its employees;
- The umbrella company levies a direct fee on its employees for its services.

25. Initially, umbrella companies were largely used by specialist contractors and similar skilled individuals. These individuals may personally source work from many different end clients over the course of a year. One of the key advantages these individuals obtained from using an umbrella company was the single conduit through which payments, including tax, are made. However, in recent years, the market has expanded and those employed through an umbrella company now may have their work sourced through an employment business and be less skilled in nature.

26. Usually the umbrella company will deduct its fee, (depending on the pay period, typically around £15-30 a week or £70-120 a month), employer NICs and put aside a sum to be paid to the individual later as holiday pay. The umbrella will then pay the individual as a mixture of tax-free reimbursed expenses, to the extent that the individual has incurred any, and salary subject to PAYE. The umbrella company usually has no other source of income aside from the amounts it invoices.

**Typical set-up for an individual employed by an umbrella company:**



27. While umbrella companies can offer a useful service to temporary agency workers, the government is aware that some companies market themselves, at least in part, on the basis that they allow individuals to legitimately maximise their income through the tax-free reimbursement of home to work travel expenses, unavailable to temporary workers not employed under an OAC.

28. The government is aware that some umbrella companies operate models, commonly referred to as “pay day by pay day” that are designed to provide relief to individuals on unreimbursed home to work travel expenses each pay day. HMRC is of the view that these arrangements are not compliant with tax and Social Security legislation and have published statements to that effect. The government is also aware that some umbrella companies operate models that are intended to

exploit confusion over employment status, these are discussed in more detail below.

29. The government is also aware of the wider issue around whether individuals employed by umbrella companies understand how or what exactly they are paid. This is due to the complexity of the payslips they are given and the number of employment intermediaries involved as well as the wider complexity surrounding employment status. This complexity, and the issues of employment rights are being considered as part of the employment status review undertaken by the Department for Business, Innovation and Skills.

## Other features of OACs

### ***Employment status***

30. Individuals employed under an OAC benefit from the employment status of 'employee'. This entitles the individual to an enhanced set of rights in comparison to working under a more common employment business contract. In many cases, these differences will benefit individuals engaged under an OAC and could be the main driver behind the decision to engage on this basis. For example, temporary agency workers are not automatically entitled to rights such as redundancy pay or to claim unfair dismissal. These rights are only available to employees and can provide greater security for the individual.
31. However, it is important that an individual's decision of whether or not to enter into a contract with an employment intermediary is made on complete information. The Conduct of Employment Agencies and Employment Businesses Regulations 2003 (the Conduct Regulations) already outline some of the key information that must be made available to the individual at the point at which they sign their contract with an employment business. However, more can be done and in October, the Secretary of State for Business Innovation and Skills announced a review of employment status, focused on enhancing transparency and clarity around some of the issues raised here.
32. The reliance on a definitive understanding of employment status to determine rights and protections can create unnecessary confusion for both individuals and employers. The issue centres on the fact that an individual's employment status is ultimately for an employment tribunal to establish. This is because the current legal framework is complicated and open to interpretation. By the time an individual reaches an employment tribunal to seek a final answer, the relationship with their employer is normally broken and the situation irreversible.
33. This is far from ideal and so the Department for Business, Innovation and Skills review of employment status will consider what the UK labour market looks like now and how government can deliver a framework that strikes the right balance between the rights of the individual and the needs of business, supporting growth and prosperity in the 21st century.
34. This Department for Business, Innovation and Skills led review of the complexity surrounding employment status and the options for simplification aims to give business and individuals more certainty. The review will present a range of options

for Ministers next year that address the concerns of individuals and employers, ensure the right balance of transparency and fairness, and ensure that future policy decisions are based on more robust data, and avoid unintended consequences. This will result in an employment status framework in the UK that is fair and flexible meets the needs of everyone involved.

### ***Schemes put in place to avoid National Minimum Wage (NMW)***

35. The government is aware of some schemes, used by a minority of umbrella companies that rely on this confusion over employment status to succeed. For example, the government is aware of some arrangements which seek to reduce individuals pay below the NMW, which in turn affects pension contributions and holiday pay. Paying a worker less than the NMW is illegal.
36. One such model involves engaging the individual under a contract which purports to be an OAC for the purposes of income tax and NICs, but not an employment contract for employment rights purposes including the NMW. The promoters and users of this model incorrectly believe that this entitles the individual to tax and NICs relief on travel and subsistence expenses which they aim to exploit without granting the individual any employment rights or entitlement to the NMW. However, a worker's entitlement to NMW is based on the reality of the working relationship and not what has been drafted in the contract.
37. A second, similar model involves setting up the individual as a director of an incorporated entity – or in more colloquial terms a personal service company, which is then essentially managed by the umbrella company. This again aims to maintain the individual's entitlement to tax and NICs relief for expenses while appearing to prevent them from being a 'worker' for the purposes of NMW regulations. Again, an employment tribunal will look at the reality of the working relationship and it is possible that NMW is payable.
38. The government takes the enforcement of employment rights including the NMW seriously and HM Revenue and Customs will take action against businesses seeking to exploit workers by not giving them their full NMW entitlement. Employers who fail to pay their workers the minimum wage they are legally entitled to will face a financial penalty, be publicly named and shamed and may even be prosecuted.

### ***Payments and process simplification***

39. For individuals who source their own work, working through an umbrella under an OAC will result in a reduction in their personal administrative burden. The umbrella company will take on the administrative burdens that they would otherwise have had as a self-employed individual including the administration of tax and NICs liabilities. This frees the individual to concentrate on delivering their labour to the end client. The employment of such people by the umbrella companies also lowers the regulatory burden on both the end client and the individual of ensuring compliance with employment status regulation.
40. However, aside from this group it seems reasonable to conclude that when solely considering payments and process simplification, the use of OACs may merely

result in a shuffling of payments and process obligations. Employment businesses employing people using OACs take on the payroll obligations with respect to those employees, removing a burden from the end client relative to directly employing the individual.

We would find it helpful to get stakeholder views on the following questions:

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

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

***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?***

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

***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?***

## 4. The case for action

41. The government is concerned about the use of OACs by some employment businesses and umbrella companies. As discussed above they can allow temporary workers employed under them to benefit from tax and NICs relief on home to work travel expenses which others cannot. This is unfair and is believed to cost the Exchequer at least £400m a year.
42. In addition to the cost to the Exchequer, potential improvements could be made in levelling the playing field between businesses that misuse the tax rules and those that don't. Improvements could also be made in enabling individuals to make a more informed choice when entering into arrangements that may not in fact benefit them. The Department for Business, Skills and Innovations' review of employment status aims to address this.

### Cost to the general taxpayer

43. The use of OACs is perceived to be increasing. Evidence available to HMRC supports this perception, with the number of individuals engaged by over fifty of the larger umbrella companies increasing by 50% between 2011/12 and 2013/14. By 2013/14 these companies alone employed 150,000 different individuals on OACs in the course of the year.
44. Based on an analysis of these umbrella companies, combined with average travel expenses incurred by people in travelling to their place of work, and subsistence expenses, the income tax and NICs avoided through the use of OACs operated by umbrella companies is estimated to amount to be around £400m per annum. As this figure relates solely to umbrella companies, and employment businesses also use OACs, the overall tax avoided each year will be more.

### Impact of these arrangements on the low paid

45. Although working for an umbrella company under an OAC will typically enable people to claim travel and subsistence relief that other individuals cannot, it also requires the payment of a fixed or sliding scale weekly or monthly fee to the umbrella company. For people who do not have any travel and/or subsistence costs (for example because they walk or obtain a free lift to work, or take a packed lunch), this can mean they find themselves in a worse financial position than if they had been hired on a more common employment business contract.
46. This holds true for people who incur little travel and subsistence costs, and those on low incomes. For the latter group, this is because a potential income tax or NICs liability is necessary to obtain relief. Hence people with income that is too low to be subject to income tax or NICs cannot obtain travel and subsistence relief, whilst people with a relatively low income and therefore a small potential income tax and NICs liability, can only claim commensurately small travel and subsistence reliefs. The governments' increases to the personal allowance mean such people make up an increasingly large portion of the workforce.

47. Based on analysis of a group of over fifty of the larger umbrella companies, for around a quarter of umbrella employees, the fee due to the umbrella company is greater than the travel and subsistence relief in relation to their employment. More than a tenth of umbrella company employees – the lowest paid – have annual income and expenses of below the annualised NICs Primary Threshold, and are unlikely to be able to claim significant, or possibly any travel and subsistence relief at all. However, there are some individuals who get a net benefit from working through an OAC and claiming travel and subsistence relief. If the ability to claim this relief was removed these people could see a reduction in their take home pay if they are already paid above the NMW.
48. As described above, some umbrella companies are also involved in various schemes which purport to remove employee status from individuals, and/or reduce their pay to below the NMW. These schemes involve dubious interpretations of government regulations, which expose the businesses using them to significant adverse tax and regulatory risks, but which in the interim potentially allow the businesses to secure some reduction in employer costs, through lower worker pay.
49. Dubious practices by organisations using OACs can also create a risk to their workers that travel and subsistence relief granted to them is not compliant with tax rules, exposing the individual to potentially large claims for the payment of tax.
50. As a result of the issues listed in this section, there are potential pitfalls for individuals using OACs.

### Levelling the playing field

51. The misuse of travel and subsistence rules to obtain relief for home to workplace travel enables firms using OACs to pay employees at a similar net pay rate as their competitors who do not, at a lower overall cost to the employer. As a result, competition is tilted between employment businesses and umbrella companies not misusing travel and subsistence rules, and employment businesses and umbrella companies who put OACs in place and misuse travel and subsistence reliefs. The businesses that do obtain a financial benefit from this misuse.
52. As set out previously, the misuse of travel and subsistence rules and schemes to pay individuals below the NMW can result in adverse outcomes to the individuals directly involved. The misuse of the rules has a potential impact on gross pay rates in the temporary labour market so may disadvantage those individuals not directly involved.

We would find it helpful to get stakeholder views on the following questions:

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

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

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

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

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

***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?***

## 5. Potential ways forward

53. The government cannot condone the use of arrangements in the temporary labour market that are designed to secure a tax advantage that would not otherwise be available to the individual or business concerned. However, the government also wants to ensure that any action it takes does not undermine genuine arrangements. It is therefore exploring possible changes to the tax rules in this area. In weighing up the merits of any proposal, the government wants to ensure that:

- The long established principle that the costs of ordinary commuting are not subject to tax relief is maintained
- The change does not undermine the effective operation of the temporary labour market or of intermediaries that do not misuse travel and subsistence relief
- That any changes will not result in intermediaries shifting into new contrived structures to achieve a tax and NICs saving.

### Current action

54. HMRC are already addressing some of the issues raised by the models referred to in section 2 and their effectiveness.

### Tax

55. As part of its risk based compliance activity HMRC is undertaking enquiries into umbrella companies and employment businesses using OACs. For example, HMRC recently won a significant case in the Upper Tribunal on a variety of issues surrounding temporary workers and temporary workplaces.

56. In July 2011 HMRC published a statement on the effectiveness of the “pay day by pay day” model and followed this in August 2012 with a further statement confirming that existing dispensations did not apply to payments under this model and that they could be revoked if use of the model was discovered. To ensure greater control over the granting of dispensations and monitoring those already in place, HMRC centralised this work in one team. Enquiries have been opened into companies who appear to be using this model.

57. As announced at Autumn Statement 2014, from 2016-17 the government is introducing a new tax exemption for certain expenses incurred by an employee and reimbursed by an employer. This was recommended by the Office for Tax Simplification in their review of expenses and benefits. As a result, employers will no longer have to complete P11Ds or apply to HMRC for the use of a dispensation.

58. However, as discussed in section 2, this new tax exemption will not apply if the payments are made through salary sacrifice schemes. This will stop umbrella companies and employment businesses who currently use OACs (as well as other employers) reimbursing travel and subsistence expenses through salary sacrifice

schemes. Employers use these arrangements to artificially reduce both their own and their employees' NICs liabilities.

59. This will not stop individuals engaged under an OAC from being able to benefit from relief on home to work travel expenses in the first place. Employees will still be able to claim income tax relief from HMRC if expenses are paid through salary sacrifice. However, as has always been the case, they will not be able to claim relief from NICs on expenses that they have met the cost of themselves.

### ***National minimum wage enforcement***

60. HMRC enforces compliance with NMW legislation on agencies or intermediary businesses in accordance with NMW legislation.
61. When considering entitlement to the national minimum wage, NMW officers consider the relationship between the parties. NMW wage entitlement arises if the person is a worker or deemed to be a worker under the special rules for agency workers.
62. NMW reviews of umbrella companies have revealed instances of workers' pay including elements of reimbursed expenses, which should not be taken into account in calculating pay for NMW purposes. Additionally, deductions from the workers' pay for an employer's own use and benefit, cannot bring a worker's pay below the NMW. The deductions identified include (but are not limited to) administration charges or fees for handling specific transactions on entry to a travel scheme, payment of transport costs, a charge for a uniform or the provision of third party insurance. These items will not count in calculating pay for NMW if they are for the employer's own use and benefit or considered to be an expense in connection with the worker's employment.

### ***Employment status***

63. In addition to this, the review of employment status being undertaken by the Department for Business, Innovation and Skills will look at how greater clarity can be delivered to both employers and individuals, ensuring that both parties can, and do, understand the implications of the contractual arrangement they enter into. For employers, this will ensure they are aware of their responsibilities in terms of NMW, holiday pay entitlement and other basic rights. For individuals, they will be better placed to know their rights and have the confidence to be able to sound the alarm where things go wrong.
64. A contract of employment through an intermediary, such as an umbrella company, will be right for some, but not others. The decision to enter into a contract of employment, overarching or otherwise, can bring with it significant benefits. However, in order to make this decision, the individual requires information from the umbrella company, but this does not appear to be happening in all cases. Where information is not provided, the employment business may be in breach of the Conduct Regulations, which can be investigated by the Employment Agency Standards Inspectorate, part of the Department for Business, Innovation and Skills.
65. The Department for Business, Innovation and Skills is commissioning research looking at the information made available to individuals employed through

employment businesses and umbrella companies. Specifically, it will look at what information is given to workers regarding the type of contract they are being offered and whether this is sufficient or, indeed, compliant. This research will complete next year and the Department for Business, Innovation and Skills will act if necessary.

66. However, the government believes there is a strong case for going further to address some of the underlying tax rules that are being exploited.

## Possible options for addressing this avoidance

### *Tax relief for travel expenses*

67. As recommended by the OTS, the government initiated a wide review of the tax rules for travel and subsistence expenses this summer. The aim of this review is to modernise these rules to reflect contemporary practices in the labour market. This is a long running review that will consider the rules in the round and any changes introduced as a result will take a number of years to come into force. However, as set out in this paper, the government is concerned at the growing use of OACs to enable some individuals to claim relief on home to work travel and subsistence expenses while others in similar situations cannot.

68. The interaction of OACs and the travel and subsistence rules applying to temporary workplaces distorts the application of these rules in relation to different groups of temporary workers as discussed above.

#### Potential option 1

69. One option to address this unfairness, and to reduce the cost of these arrangements to the general taxpayer, would be to introduce legislation to amend the tax rules on travel and subsistence expenses. This legislation would mean that individuals engaged under an OAC by an employment intermediary to work for a third party, cannot claim tax relief for travel, and associated subsistence, from their home to the workplace of the end client.

70. One way to achieve this would be to determine that where the individual is supplied through a third party the workplace of the end client would in all cases be a "permanent workplace". In this case no relief for travel from home to workplace, and associated subsistence, would be available. This would apply whatever the form of the third party. This would not change the position of individuals who are directly employed by employers for short periods as they are currently treated as working at a "permanent workplace".

71. The aim of this change would be to remove an unfair tax outcome, and level the playing field by putting all temporary workers on an equal footing in tax terms regardless of how they are engaged. It is consistent with the rules currently in place for more common agency contracts and would stop employment businesses from being unfairly undercut by those that use OACs to reduce their employer NICs liability.

72. Any change would seek to maintain the travel and subsistence expenses which can be claimed by individuals genuinely seconded to work temporarily away from their regular workplace by their permanent employer. This is consistent with the principle that the costs of ordinary commuting are not subject to tax relief. Consideration would also need to be given to the current position of “mobile permanent workers”. These are permanent employees who do not have a permanent workplace; for instance consultants who are placed consistently at the different premises of clients of their employers or groups such as mobile meter readers.
73. The government is particularly interested in the potential impacts on Personal Service Companies (PSCs) of any changes to the rules on relief for travel and subsistence expenses available to people working through an employment intermediary. Those who provide their services through PSCs will (usually) have a single employment covering all of their different assignments (much like employees who have an OAC). This means that they will also often be eligible for travel and subsistence relief for home to work travel. However, the government will want to consider the impacts very carefully before taking final decisions on the overall approach and how it is applied in these circumstances.
74. If PSCs were excluded from any changes, there is a risk that employment agencies may be incentivised to encourage individuals to work through their own limited company in order to continue to get tax relief on their home to work travel.

#### Potential option 2

75. An alternative option would be to restrict the availability of tax relief for travel from home to workplace, and associated subsistence costs, where the individual was employed by an intermediary specifically under an OAC. This could be accomplished by stopping OACs being treated for tax purposes as giving rise to a series of temporary “employments” under a permanent contract. This option would restrict access to existing rules for travel and subsistence to people employed under an OAC, rather than actually changing travel and subsistence rules, with the practical impact that the access of people employed under OACs to travel and subsistence is consistent with principle that the costs of ordinary commuting are not subject to tax relief. As this option would specifically or solely affect people employed under OACs, it would not have any impact on PSCs (unless they use an OAC).
76. The government is aware that some bodies have called for the government to address unfair practices by levelling the playing field by extending the availability of tax relief for home to work travel to agency workers who are not engaged under an OAC. Extending this tax relief to traditional agency workers would likely result in a large cost to the Exchequer and would not be well targeted and would go against the long established principle that the costs of ordinary commuting are not subject to tax relief. The government continue to believe that reducing taxes through increases in the personal allowance is a fairer way of supporting those on low and middle incomes. We would find it helpful to get stakeholder views on the following questions:

***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?***

***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?***

***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?***

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

***Question 16: Are there examples of where Option 1 or 2 may affect cases where it is fair that tax relief should apply?***

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

***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?***

## 6. How to respond and next steps

77. Views on the issues and questions set out in this paper are invited from all stakeholders from the temporary labour market, their agents and their representatives and any other interested parties.
78. HM Treasury and HMRC will consider written submissions addressing the questions and issues raised in this discussion paper.
79. Responses to this discussion paper are requested by 10 February 2015 and should be sent by email to the review team using the following address: [oac.review@hmrc.gsi.gov.uk](mailto:oac.review@hmrc.gsi.gov.uk).
80. Responses to this discussion paper will be considered by the government and used to inform firm action at Budget 2015.

## 7. Summary of discussion questions

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

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

**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?**

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

**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?**

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

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

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

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

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

**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?**

**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?**

**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?**

**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?**

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

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

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

***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?***