

Double checking

Employment Tax



01 September 2016

Jon Claypole and Michelle Perry ask whether the abolition of P11D dispensations will make life easier.

Key Points

What is the issue?

Will the abolition of the P11D reporting dispensation make year end reporting easier?

What does it mean for me?

All employers who pay expenses or benefits to employees need to consider whether they have a P11D reporting requirement. The recent changes to dispensations may mean that you need to make system changes.

What can I take away?

An overview of what the new legislation means and the changes you may need to make.

As part of the recommendations made by the Office of Tax Simplification, from April 2016, the P11D reporting dispensation will no longer be required. The change has also seen the introduction of a statutory exemption within legislation for business expenses which means in certain circumstances there will be no need to report business expenses to HMRC on forms P11D. This of course puts an employer and employee in the same position as when a P11D dispensation was available.

Notwithstanding this apparent status quo, the abolition of the dispensation regime from April 2016 does represent a significant change to employment tax compliance.

Following the recent P11D reporting deadline of 6 July, we have heard comments to suggest that the P11D reporting for 2016/17 will be much easier as a result of this change. Although that may be the case in some instances, employers do need to take care. If appropriate systems, procedures and processes are not in place from the start of 2016/17, there may be even more work to do when we reach the P11D reporting deadline next year and it is possible that there could have been an impact

on payroll obligations through the year which have not been considered.

Under the previous rules, providing a comprehensive application was made to HMRC for a dispensation, employers had a high degree of comfort that what they were paying or reimbursing to employees as expenses did not have to be reported on forms P11D and were not therefore subject to the deduction of tax and/or NIC through payroll. With dispensations generally being updated every five years, employers had an opportunity to review their systems, procedures and processes to ensure they were still adequate. Under the new regime employers will need to effectively 'self-certify' that the expenses in question fall within the exemption and therefore do not need to be reported. Employers will need to have systems in place to demonstrate that employees have actually incurred the expense and the expense is allowable, together with retaining appropriate evidence. With the risk of facing penalties for carelessness if they are unable to do so.

The HMRC Employment Income Manual states that almost all expenses or benefits that were covered by a dispensation should be covered within the new exemption at Section 289A ITEPA 2003. However, care needs to be taken by employers in respect of the definition of a business expense. For a deduction to be available an expense must be wholly, exclusively and necessarily incurred in the performance of employment duties. During our work with employers there is often a misunderstanding around what is an allowable expense. For example, the reimbursement of an employee's home broadband cost is often viewed as a business expense on the basis the employee is required to work from home in the evenings/weekends. Whilst this view is understandable, such a cost does not meet the wholly, exclusively and necessarily test because it is a reimbursement of a personal cost and should therefore be reported on form P11D and/or included in payroll.

Any expenses or benefits paid to employees which are not within the exemption will need to be subject to the deduction of tax and NIC or reported on forms P11D. It is for the employee to then make a claim direct to HMRC if appropriate.

Travel and subsistence

The new regime has placed an emphasis on payments made for travel and subsistence, in particular where employers utilise scale rates to reimburse employees.

It is important to remember that payments for travel and subsistence will not be exempt from tax and NIC if they are paid as part of a salary sacrifice arrangement or when salary levels are dependent upon the amount of the expenses paid.

The benchmark scale rates are now included within legislation at Section 289B ITEPA 2003. These are the maximum amounts that employers can pay their employees for qualifying subsistence costs when travelling for work, without having to agree a rate with HMRC. Bespoke rates can be agreed with HMRC and are effective for up to five years. To agree rates an employer will need to make an application to HMRC based on a sampling exercise. The sampling exercise will in our experience need to be based on a random 10% sample of mobile workers for a one month period.

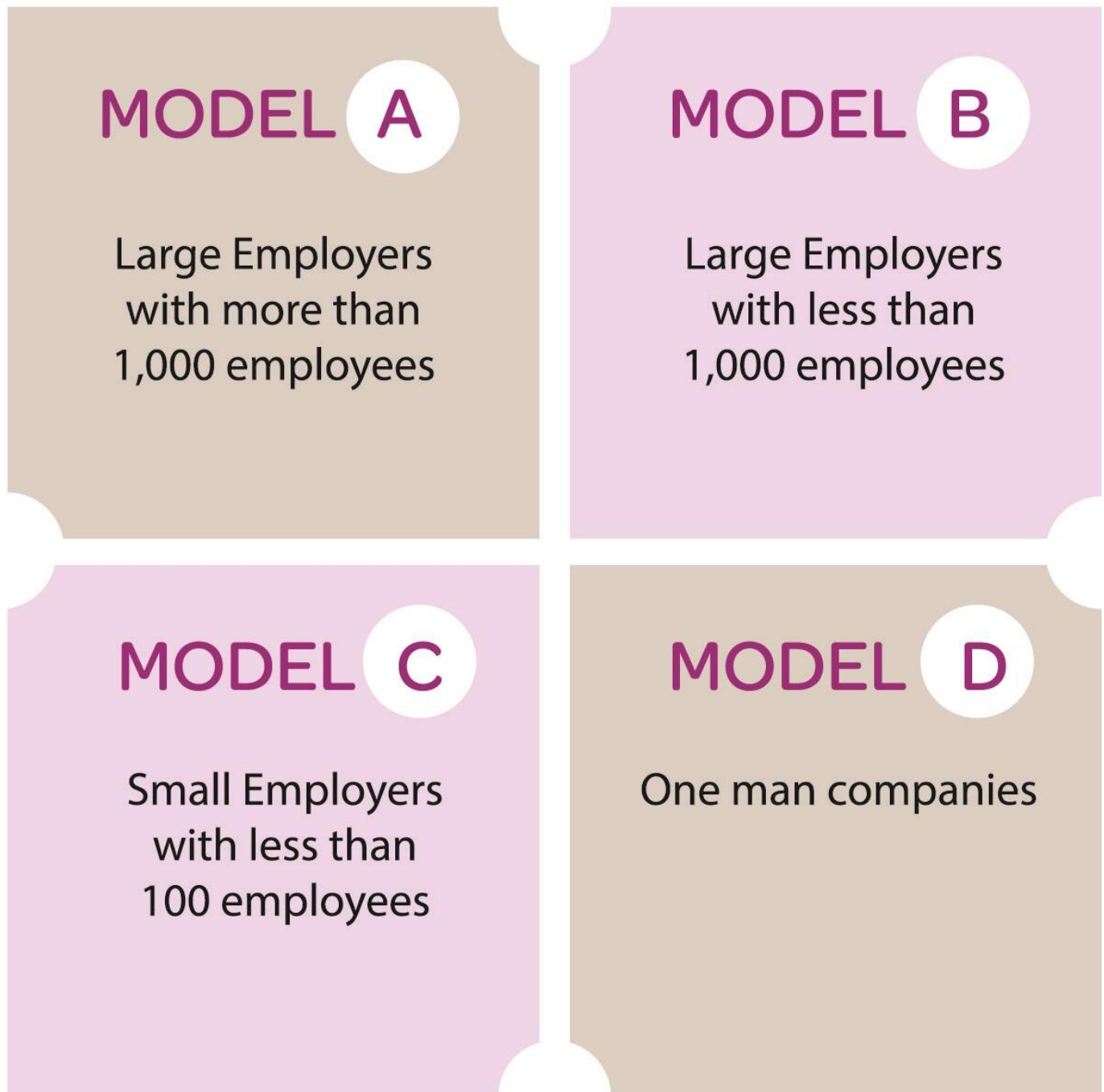
Transitional arrangements are in place for those employers who already have bespoke rates agreed with HMRC. Any rates agreed since April 2011 can continue to be used until the 5th anniversary of that agreement without the need to carry out a further sampling exercise. Employers will however need to submit an application to HMRC to get agreement to continue using them. It should also be noted that employers who utilise industry scale rates will also need to make an application to use the agreed rates. In our experience the fact that approval needs to be obtained for industry scale rates is something many employers are unaware of. Scale rates, whether approved rates, bespoke rates or industry agreed rates, can only be paid if there is an appropriate checking system in place under section 289A(3). The checking system must demonstrate that:

- Employees are in fact incurring and paying expenses of the kind reimbursed and
- That a deduction would (ignoring the exemption) be allowed under Chapter 2 or 5 of Part 5 ITEPA 2003 in respect of those amounts

HMRC has provided detailed guidance at Employment Income Manual 30270 on the form and regularity of the checks required but essentially the requirements will depend on the size and complexity of the workforce. HMRC expect the checking system to be able to demonstrate that someone other than the employee incurring the expense is responsible for ensuring the payment relates to qualifying travel, does not include disallowable items and is not excessive.

Employment Income Manual 30275 sets out four models that employers may wish to use as set out in **Box 1**. Whilst there is no requirement to use one of the models, HMRC will accept that the requirements of the exemption are met when Employers correctly utilise one of the models.

Image



Models A and B require a random 10% check of all expenses claims for a one month period every six months. The check should ensure:

- Claims are authorised and vouched by reference to employee diaries, work schedules and time sheets to demonstrate that employee were travelling in the performance of their duties
- Review of receipts to ensure costs are incurred

Model C requires a random 10% check of all expense claims and the checks should ensure the same points noted for models A and B.

Model D requires the employee to maintain diary and time sheet information together with the retention of receipts. A sample of these records should then be checked by an independent third party on a monthly basis to confirm that the relevant conditions for the exemption were met.

What systems should an employer have?

An Employer needs to be able to demonstrate that the employee has incurred an expense and it is allowable. This will mean that receipts should be provided wherever possible and sufficient detail should be retained. For example, claims for business entertaining should state the attendees and claims for subsistence should be able to show that there was related business travel.

All employers should ensure they have the following:

- A written expenses procedure that is understood by all employees
- A written expenses policy
- A standard expenses claim form
- A clear authorisation of expenses policy.

We recommend that anyone responsible or involved in the expense claims procedure should have full training in respect of what is an allowable expense and what is required when authorising claims. This is crucial where non-finance people are responsible for completing and/or signing off claims. For example, in the past we have provided training to personal assistants of executives who complete the expenses claims. Typically line managers are responsible for signing off expense claims and they may have limited knowledge of the requirements. Employers should

ensure full training and guidance is provided in these circumstances. Consideration should also be given to undertaking regular audits of expense claims to identify errors.

There should be systems in place to capture expenses which require inclusion in the payroll on a real time basis and to capture expenses which will need to be reported on forms P11D.

Conclusion

Employers of all sizes need to ensure they have suitable and robust systems in place to achieve compliance with the new regime. This is the first time we have seen requirements on systems included within legislation for employment tax. Although it is early days, it is clear that thought needs to be given to the implications of the new regime now rather than at the end of the tax year.