Tax Law Rewrite

Eleventh Exposure Draft

Employment Income: Part 2

Comments are welcome on the clauses in this Exposure Draft. They will be made public on request, unless we are asked to treat them in confidence.

This document is available on the Internet at **www.inlandrevenue.gov.uk**
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Please send comments to reach us by **30 April 2001.**

Foreword by the Paymaster General

This is the second Exposure Draft in the series on employment income. It continues the process of rewriting and restructuring the legislation in an area of taxation that affects a great many ordinary taxpayers.

The consultation process is a vital part of the project's work, which is why Exposure Drafts, and the responses to them, are so important. They give anyone with an interest in tax the opportunity to comment on any aspect of the rewritten material at a relatively early stage in the rewrite process.

I am pleased to say that support for the project remains solid within the tax community and I am grateful for all the comments that the project has received in the past. I hope you will take this opportunity to comment on these draft clauses.

DAWN PRIMAROLO

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Key Points

This Exposure Draft

- Another batch of draft rewritten legislation from the Tax Law Rewrite project
- It deals with the tax rules for employment income, concentrating on deductions and exemptions
- It follows on from Exposure Draft No 6, which was published in May 1999
- In due course this legislation will be part of an Income Tax Act
- We aim to rewrite the existing legislation without changing its effect
- But we are proposing some minor changes in the rules to improve the legislation

A new approach to writing tax legislation

- A new, more logical structure for the rewritten legislation
- A new format and layout to make it easier to read
- Shorter sentences and better use of definitions
- Use of modern language – as long as we can do this without changing the law or making its effect less certain
- Better signposts and similar rules grouped together, to make the rules easier to find

How To Use This Document

This document is in six parts.

Part 1 gives some background information about the Tax Law Rewrite project.

Part 2 outlines some important aspects of our approach to the work.

Part 3 gives some background information about the employment income clauses included in this Exposure Draft. It explains the structure we have used for the employment income Part of the proposed Income Tax Act. It discusses and explains how we have rewritten the various employment income deductions and exemptions.

Part 4 summarises the proposed rewrite changes. These are minor changes which, if agreed, would improve the legislation. They fall into four main types:

- changes in approach but not in the underlying law;
- changes to the law and policy;
- changes to the law but not to policy (such as enacting extra-statutory concessions); and
- removal of unnecessary material.

Part 5 is a detailed commentary on the draft clauses.

Part 6 (in Volume 2) contains the draft clauses in the form of draft sections of Part 4 of the proposed Income Tax Act. It also contains a Table of Origins which shows the current provisions from which the clauses are derived.

Navigational aids to the reader

At the beginning of Volume 2 there is a table of all the chapters so far planned for Part 4. Those chapters marked with an asterisk (*) appeared in Exposure Draft No 6; those marked with a dagger symbol (†) will form part of the next Exposure Draft. This table is followed by a full table of arrangement for the clauses in the chapters included in this Exposure Draft. The items that are listed *in italics* do not form part of this Exposure Draft.

In this Exposure Draft there is some signposting incorporated within the clauses in Volume 2. These point to other provisions that might be relevant.

At the end of Volume 2 is a Table of Origins and which shows the current provisions from which the clauses in this Exposure Draft are derived.

Status of this document

This second Exposure Draft on the income tax treatment of employment income focuses on deductions and exemptions. We fully expect to make changes to the clauses in the light of this consultation and our further work in this area. Changes may also be needed

as a result of future work on other areas, or as a result of changes in the law before enactment of the relevant rewrite Bill. Our approach is to publish our work for comment at an early stage rather than to put forward what we might confidently expect to be the finished product.

We are rewriting the law as it currently stands. Changes to the law, other than minor ones in the interests of simplification, will continue to be dealt with through the Budget and Finance Bill process. The presence or absence of provisions in this rewritten legislation does not indicate any future change in tax policy.

Statutory references

References are to the Income and Corporation Taxes Act 1988 (ICTA) unless otherwise stated.

This Exposure Draft includes references to the Capital Allowances Bill. That Bill was introduced on 9 January 2001. It is currently being considered by the Joint Committee (see paragraph 2.10 below). The Bill, and the explanatory notes which accompany it, can be obtained from The Stationery Office. They are on the Internet at www.parliament.the-stationery-office.co.uk/pa/pabills.htm.

This Exposure Draft rewrites only legislation that is currently on the statute book. It does not take account of any changes announced by the Chancellor in his Pre-Budget Report published in November 2000.

Part 1: Introduction

Background

1.1 In December 1995 the Inland Revenue presented a report to Parliament on the scope for simplifying the United Kingdom tax system. The main recommendation was that United Kingdom direct tax legislation should be rewritten in clearer, simpler language.

1.2 This recommendation was warmly welcomed, both in Parliament and in the tax community. After further work on important practical issues and a period of preliminary consultation, the then Chancellor of the Exchequer announced in his November 1996 Budget speech that the Inland Revenue would propose detailed arrangements for a major project to rewrite direct tax legislation in plainer language. In *Tax Law Rewrite: Plans for 1997*, published in December 1996, we did this and set out our provisional programme for 1997.

1.3 In May 1998 we published a further report – *Plans for 1998/99*. This explained why progress in 1997 had been slower than we had originally hoped, outlined the steps taken to achieve better progress in future and set out a programme of work for 1998/99.

1.4 *Plans for 1999/2000*, published in March 1999, included a report sent to the Chancellor of the Exchequer in December 1998 taking stock of the project.

1.5 We published our latest annual report – *Plans for 2000/2001* – in April 2000. Once again, this reviews our progress in the past year and looks forward to the work planned for the year ahead.

Our purpose

1.6 Our overall aim is to rewrite all (or most) of the United Kingdom's existing primary direct tax legislation to make it clearer and easier to use, without changing or making less certain its general effect.

1.7 Underlying this overall aim are six critical success factors, all of which must be fully achieved if the project is to succeed.

- The rewritten legislation must be accepted by all the main users as clearer and easier to apply and as preserving the effect of the present legislation apart from minor agreed changes in policy.

- Parliament must be able to scrutinise and enact the rewritten legislation in accordance with clearly defined and appropriate Parliamentary procedures and an agreed timetable.

- The main users, both inside and outside the Inland Revenue, must be kept fully informed about progress throughout the life of the project and, when appropriate, properly consulted in good time for their views to influence the rewrite work.

- The operational implications of the rewrite work for the Inland Revenue must be identified and properly addressed.

- The lessons learned from the experience of successfully rewriting the legislation should be developed, in close consultation with the users, into new best practice for producing tax legislation in the future.

- The project – including all the people in the project team – must be managed effectively and efficiently and the project's objectives must be achieved within the agreed programme and budget.

1.8 We are not solely – or even mainly – responsible for ensuring that some of these critical success factors are met. But we will have a contribution to make to all of them as our work proceeds.

Part 2: Main features of the Tax Law Rewrite project

Structure

2.1 The Tax Law Rewrite is run on project lines. Our project team currently comprises almost 40 people, including five tax professionals recruited on fixed term contracts from the private sector. Four multi-disciplinary rewrite teams work on particular areas of tax legislation. There is also a drafting team headed by a senior Parliamentary Counsel on loan from the Office of Parliamentary Counsel, together with a small policy and project support team.

2.2 A Steering Committee chaired by the Rt Hon the Lord Howe of Aberavon CH, QC provides strategic guidance to the project. It ensures that the project is meeting its objectives of clarity and user friendliness, and is taking full account of private sector concerns.

2.3 This Committee brings together a wide range of talents and experience, with members drawn from both Houses of Parliament, the judiciary, the legal and accountancy professions, consumer interests and business. It meets regularly and its minutes are published on the Internet.

2.4 There is also a standing Consultative Committee, whose role is to ensure continuous consultation on the rewritten law with all the main private sector interests. Chaired by the Project Director, it consists of:

- a core group of the main representative bodies in the tax professions, business and consumer interests;
- a group of specialist representative bodies who receive all the Committee's papers but attend meetings only when a subject relevant to their interests is being discussed; and
- project team members and, where appropriate, Inland Revenue officials dealing with the subject matter being discussed.

2.5 This Committee's minutes are also published on the Internet.

Consultation

2.6 We are committed to proceeding with our work on the basis of full consultation at every stage of the process.

- As we develop draft clauses, we involve specialists in Revenue Policy (and, where appropriate, interested parties outside the Department) and produce "work in progress" papers for consideration by our Committees.
- In the light of comments from both Committees and further work within the project, we refine the draft clauses (with further Revenue Policy involvement) and work up Exposure Drafts for public consultation. These contain a general

commentary and a more detailed clause-by-clause commentary. Near final drafts are considered by both Committees before publication.

- We publish these Exposure Drafts for written comments.
- Usually we publish a response document, summarising the comments received from formal consultation and our response to these points. This provides feedback to all those who have commented.
- Finally we will publish rewrite Bills – with a commentary – for a final round of formal consultation before introducing them in Parliament for enactment.

2.7 All this consultation places heavy demands on those whom we consult. We are very grateful to them for the time and resources they have been prepared to devote in order to give us their comments. Their input has been invaluable, and it will remain so as the project progresses.

Parliamentary procedures

2.8 The sheer volume of direct legislation makes it impractical for rewritten clauses to be included in a Finance Bill and, since we aim to reproduce the effect of the existing law, this should not be necessary. Rewrite Bills will not be consolidation Bills, although they share many of the same features, and it is clear that Parliament will not be able to deal with them under the ordinary procedure for Public Bills. Parliament has therefore adopted a new streamlined procedure which will allow it to scrutinise the rewritten legislation properly but without opening up debate on the full range of fiscal policy matters.

2.9 The House of Commons Procedure Committee published their report – *Legislative Procedure for Tax Simplification Bills* – on 30 January 1997. This recommended that rewrite Bills should be introduced in the House of Commons and then referred, on Second Reading, to a joint Committee of both Houses. The report also proposed that the joint Committee should have a Commons majority and be chaired by a member of that House.

2.10 These recommendations were accepted by the House of Commons and reflected in Standing Order No 60, passed on 20 March 1997. The House of Lords Procedure Committee has indicated that they are content with this approach. Parliament has now appointed a Joint Committee to consider Tax Simplification Bills. The Joint Committee has seven members from the House of Commons and six from the House of Lords. Their remit is "to consider Tax Simplification Bills, and in particular to consider whether each Bill committed to it preserves the effect of the existing law, subject to any minor changes which may be desirable."

Techniques

2.11 We use a number of techniques when rewriting legislation. These are all different ways of meeting our paramount objective of making the legislation easier for the reader to understand, while preserving its technical accuracy.

Structure

2.12 By far the most useful of these is to establish the correct structure for the present purpose of the legislation (as opposed to its original purpose). This process involves the detailed analysis of all the existing legislation on a particular topic, as well as any relevant extra-statutory concessions and other non-statutory material, followed by a reconstruction of the propositions in a more logical order. This initial analysis is usually much harder and more time consuming than first expected.

2.13 This reordering at a detailed level is complemented at a higher level by the reordering of material within the Acts and between Acts. We have been working on the assumption that the rewrite will produce the following main Acts:

- Capital Allowances
- Income Tax
- Corporation Tax
- Capital Gains
- Stamp Duties
- Inheritance Tax
- Management

2.14 We published, in Plans for 1997, a provisional framework to show broadly how a full Income Tax Act for individuals might look. It showed several blocks containing the computational rules for different types of income. One of these blocks related to "employment income". To provide a general guide, an updated version of this provisional framework is attached as Appendix 1.

2.15 As announced on 5 July 2000, we have modified our plans slightly and we are now working towards a first Income Tax Bill to be ready for introduction in Parliament in November 2002. This Bill will contain the provisions relating to employment income. It may also contain the provisions relating to pension income and social security income.

2.16 In conjunction with the work for this Bill, we will also rewrite the Pay As You Earn Regulations.

2.17 A second Income Tax Bill – probably covering trading income, property income and savings and investment income – should follow in November 2003.

Drafting style

2.18 We use colloquial English wherever we can, adopting shorter sentences in the active, rather than passive, voice. We replace archaic expressions with more modern ones, taking care not to change the law inadvertently by rewriting words or expressions that have a well understood meaning. We harmonise definitions across the Acts where possible, and then make it easier for the reader to find defined terms. We group similar rules together in one place, and make greater use of signposts to guide the reader to other relevant provisions. And we continue to explore other techniques for making

legislation more accessible – method statements, formulae and, where appropriate, tables.

Format and layout

2.19 We have always recognised that the way the text is presented on the page can make an important contribution to the overall clarity of the legislation. We have tried out a new format for the draft clauses in our Exposure Drafts. Features of this rewrite format have included a new, broader font; a larger typeface; more white space; and a new three part numbering system.

2.20 But we also acknowledge that any decision on the format of Bills remains a matter for Parliament. In February 1998, partly as a result of our work, a working group was set up under the chairmanship of the Clerk Assistant, House of Lords to review the format of the statute law. This working group recommended a new format for all public Bills, which drew heavily on our research. Their recommendations were considered by both Houses in 1999 and accepted.

2.21 The new statutory format will apply for all public Bills from the start of the 2000/2001 session. It incorporates many – although not all – of the new features developed by the project. We are pleased that our work has been influential in contributing to this significant improvement.

Numbering

2.22 Our previous Exposure Drafts have used a three part numbering system, in which each component corresponded to Part: Chapter: Section. The Steering Committee and many of those we consulted found this more informative than sequential numbering, while recognising that it also gave rise to some practical disadvantages. The relevant authorities in Parliament were concerned about these practical difficulties and decided, on balance, not to adopt three part numbering for rewrite Bills.

2.23 Exposure Draft No 6 (Employment Income: Part 1) was of course drafted using three part numbering. And the bulk of the material contained in this Exposure Draft was already drafted using three part numbering before this decision was made. So we have retained three part numbering for this Exposure Draft. We are still considering what numbering system we should use for future Exposure Drafts.

2.24 The three part numbers we have used start with "4" reflecting the original intention that employment income would form Part 4 of a single Income Tax Bill. We have kept to this numbering convention in this Exposure Draft for consistency with Exposure Draft No 6, Employment Income: Part 1. To avoid confusion, we have also continued to refer to "Part 4" instead of the proposed "Employment Income Bill".

Proposed rewrite changes

2.25 To achieve our overall aim our rewritten legislation has to be not only clear, but also technically accurate. It must reproduce the effect of the existing legislation, except where we can make minor changes to improve the legislation still further. The project

team is responsible for the overall accuracy of the rewritten legislation. Accuracy is assured largely by exposing the draft clauses to the close scrutiny of a series of internal and external experts through our extensive consultation processes.

2.26 Minor changes in law or in approach are called "proposed rewrite changes" in these Exposure Drafts. Typically they involve correcting small errors, legislating an extra-statutory concession or dropping material which is no longer necessary. We aim at every stage of the consultative process to identify clearly all such changes and to highlight any issues which may arise. When a Rewrite Bill is introduced in Parliament, minor changes in the law are written up in an annex to the Explanatory Notes accompanying the Bill. Some of the points flagged up in Exposure Drafts as proposed rewrite changes involve textual changes which we do not think change the legal effect of the provisions. These are written up in another annex.

2.27 We included the Steering Committee's stocktake of the project in our annual report – *Plans for 1999/2000*. They recognised in paragraph 3.19 of Appendix 2 that substantial changes in the present law should be made in a Finance Bill. They went on to say that there might be other desirable changes which, while not minor, would not be controversial and so might be enacted by Parliament in a rewrite Bill.

2.11 Our consultation from time to time reveals suggestions for policy change that go beyond our remit. We aim to record these suggestions when responding to our consultation, and we pass all of them on to our Revenue Policy colleagues to consider further and, where appropriate, to inform Ministers. With them, we continue to look for opportunities to further improve and modernise our tax system.

Part 3: Introduction to the clauses

3.1 Although it seems familiar, employment income is not a term presently used in the legislation. It has been used by commentators and indeed by the Inland Revenue in some of its publications, but at present it has no precise meaning. The income that we see as falling within coincides largely, but not entirely, with income within the existing Schedule E.

3.2 The rewritten provisions will cover

- what is chargeable as employment income,
- how to compute earnings,
- what is exempt from tax,
- what may be deducted,
- certain other income chargeable under Part 4 as employment income, and
- when the charge on employment income arises.

3.3 We are covering this block in four stages. Exposure Draft No 6 covered Stages 1 and 2, concerning the main charging provisions together with associated material and the provisions that charge specific benefits. This Exposure Draft deals with Stage 3 - deductions and exemptions. We had hoped to cover both Stages 3 and 4 in this Exposure Draft. But we now intend to publish a further Exposure Draft for Stage 4, dealing with the remainder of the provisions, and particularly with share schemes and the provision of services through an intermediary.

3.4 The rules for what we define as employment income and what deductions and exemptions apply are not arranged logically at present. We are trying to bring them all together and arrange them in a more logical and helpful structure. And we are using new drafting techniques to make them clearer and easier to understand.

3.5 Obviously the existing statutory provisions can only be construed in the light of judicial interpretations which have, on occasion, shaped the understanding of the words. Beyond this, practice has developed from the common understanding of users as to how the law works. Sometimes this is embodied in a statement of practice. At other times, it is simply set out in less formal guidance. Sometimes there are published extra-statutory concessions. We have tried to reflect much of this material in the rewritten legislation where appropriate. Most case law has not been incorporated into the rewritten clauses, because it is often relevant only to a narrow point of law.

3.6 Some minor changes to the law are proposed. They are listed on pages 15 to 26. These changes are proposed in the interests of making the law clearer. There are other changes that might be proposed in the interests of simplifying the tax system but the Project's remit does not go that far.

3.7 We have sometimes found it difficult to express non-statutory practices in statutory language. Legislation requires greater precision than the language of concessions. Our general aim is to legislate practices and concessions so as to bring the text of the legislation into line with the tax system as it is administered in practice. But not all practices and concessions can, or should, be put into legislative form. There are some practices which we have not tried to legislate even though they are recognised in text books and in the Inland Revenue's published guidance. In these cases, we think that the flexibility which the practice provides is probably of greater value to both the Inland Revenue and the taxpayer than the certainty of statute.

3.8 From now on this commentary is devoted to the Stage 3 of our work on Part 4. To set the draft clauses in a wider context, as with previous Exposure Drafts, we have shown in Appendix 2 what we call "overview" provisions. These are simply an early sketch of how an Income Tax Act might start.

3.9 The commentary in this part of the Exposure Draft should be read in conjunction with the clauses in Volume 2. We fully expect to make changes to the clauses in the light of this consultation. It is also likely that amendments will be needed as a result of our further work on this and other parts of the Act. Throughout the Project we will publish our work for comments at a relatively early stage rather than put forward what we might confidently expect to be the finished product.

3.10 We have used the same format for the clauses as we used in Exposure Draft No 10. It is very similar to the format for rewrite Bills.

3.11 **Comments are welcome on the format and content of all or any of these rewritten clauses. But there are some questions on which we should be particularly glad to receive views and these are printed in bold in the commentary.**

Part 4: Proposed Rewrite Changes (PRCs)

4.1 In rewriting this legislation we have suggested a number of changes which would make it simpler and easier to use. Exposure Draft No 6 set out 48 PRCs.

4.2 A further 98 suggested changes are listed in this Exposure Draft, cross-referenced to the commentary on the clause where the change is discussed. In the commentary we have categorised each proposed rewrite change into one of the four groups used below and indicated how the change would affect income tax liabilities. **We welcome views on whether these changes should be made**.

1 Changes in approach but not in the underlying law

Changes with wide-ranging application

(1) Deductions allowed in charging earnings to tax. We propose to include a number of general rules relating to deductions and consequently to omit wording included in the separate deductions provisions which will be reflected in the general rules. See paragraphs 5.17 to 5.19 of the introductory commentary to the clauses on page 29.

(2) Deductions for expenses paid on behalf of the employee. We propose to state explicitly that a deduction may be allowed where expenses are incurred by the employee but the pecuniary liability for them is met by someone else and so constitutes earnings of the employment. See paragraphs 5.23 and 5.24 of the introductory commentary on the clauses on page 30.

(3) Deductions for expenses reimbursed. We propose to make explicit provision for cases where expenses incurred by an employee are reimbursed. See paragraphs 5.25 and 5.26 of the introductory commentary on the clauses at page 30.

(4) References to deductions. We propose not to rewrite the provisions at sections 193(7), 194(10) and 195(11). These require references to deductions under section 198 and other provisions to be read as including references to other deductions. Instead we will reflect these additions in rewriting the individual provisions where these references occur. See paragraphs 5.31 to 5.33 of the introductory commentary to the clauses on page 31.

(5) "Foreign emoluments". We propose to drop the label "foreign emoluments" and instead set out the relevant circumstances in each provision where the expression in used. See paragraphs 5.36 to 5.41 of the introductory commentary to the clauses on page 32.

(6) Exemptions. We propose to standardise the form of the words used to indicate that income is exempt from income tax. See paragraphs 5.42 and 5.43 of the introductory commentary to the clauses on page 33.

(7) Exemptions from tax charges on vouchers and credit-tokens. We propose to gather together into single clauses the exceptions from such charges in cases where the vouchers or tokens are used to obtain things which if provided as benefits would be exempt. See paragraph 5.44 of the introductory commentary to the clauses on page 33.

Changes arising in particular individual clauses

(8) Accommodation benefits of ministers of religion. We propose to reword the definitions of "statutory amount" and "statutory deduction" presently in section 332(4) to be more specific. See paragraph 5.608 of the commentary on clause 4.35.1 at page 114.

2 Changes to the law and policy

(9) Deductions for fees and subscriptions to professional bodies. We propose to introduce a registration system for bodies to which fees and subscriptions paid are allowed as a deduction. See paragraphs 5.181 to 5.187 of the introduction to clauses 4.17.10 to 4.17.12 at page 56 and paragraph 5.198 of the commentary on clause 4.17.12 at page 58.

(10) Deductions for expenses of ministers of religion. We propose that such deductions should be allowed only from earnings and not against any profits or fees chargeable under Schedule D. See paragraph 5.212 of the commentary on clause 4.17.17 at page 60.

(11) Deductions for expenses of ministers of religion. We propose to change the deduction rule in section 332(3)(b) so that the amount deductible is determined on the basis of a just and reasonable apportionment. See paragraph 5.214 of the commentary on clause 4.17.17 at page 60.

(12) Deductions for corresponding payments by non-domiciled employees with foreign employers. We propose that the relief offered by section 192(3) should be allowed as a deduction instead of (in effect) as an exemption. See paragraphs 5.242 to 5.244 of the commentary on clause 4.17.21 at page 64.

(13) Deductions from benefits code earnings. We propose under the rewritten sections 141(3), 142(2), 145(3) and 156(8), to limit the amount of deductions allowed rather than providing that the deduction is set only against the earnings chargeable in respect of the benefit provided. See paragraphs 5.252 to 5.255 of the commentary on Chapter 4.18 at page 66.

(14) Deductions for earnings representing benefits or reimbursed expenses. We propose to drop the requirement that the provision or payment should be "by or on behalf of the employer". See paragraphs 5.288 to 5.290 of the introductory commentary to Chapter 4.20 at page 71.

(15) Payments and benefits on termination of employment treated as employment income. We propose to apply the "for this purpose" condition

which relates to the charge for the year of receipt to the whole of Chapter 4.23. See paragraph 5.385 of the commentary on clause 4.23.1 at page 83.

(16) Payments and benefits on termination of employment: valuation of benefits. We propose to allow the valuation of the cash equivalent to be made by reference to the person chargeable or the recipient of the benefit. See paragraph 5.418 of the commentary on clause 4.23.12 at page 89.

(17) Exemption of payments connected with exempt heavy goods vehicles. We propose to extend this exemption to the lower-paid. See paragraph 5.437 of the commentary on clause 4.30.3 at page 91.

(18) Exemption of incidental overnight expenses. We do not propose to list all relevant deduction provisions currently mentioned in section 200A(1)(b) separately, but instead to refer to expenses that "would not be deductible under this Part". See paragraph 5.440 of the commentary on clause 4.30.4 at page 91.

(19) Exemption of removal benefits and expenses: travelling and subsistence. We propose to extend the exemption to cover a child's journeys to and from the employee's temporary accommodation. See paragraphs 5.576 to 5.578 of the commentary on clause 4.34.9 at page 109.

(20) Exemption of removal benefits and expenses: replacement of domestic goods. We propose to remove the current requirement in paragraph 14(2) Schedule 11A to deduct from the amount potentially within the exemption any sale proceeds of replaced domestic goods. See paragraph 5.593 of the commentary on clause 4.34.13 at page 111.

(21) Exemption of removal benefits and expenses: limit on exemption. We propose to include in the list of items counting towards the £8,000 limit any benefits that are funded by use of a non-cash voucher or credit-token. See paragraph 5.597 of the commentary on clause 4.34.15 at page 112.

(22) Exemption of removal benefits and expenses: limit on exemption. We have recast the provisions setting out the amounts that count towards the £8,000 limit in terms of the amounts that are treated as earnings (under whatever section that may be). See paragraph 5.598 of the commentary on clause 4.34.15 at page 112.

3 Changes to the law but not to policy

Changes with wide-ranging effect

(23) Deductions for employee's expenses. Where the Inland Revenue does not currently trace the source of funds used for an employee's expenditure in allowing deductions for expenses paid by him, we propose to omit the requirement for the employee to have paid the expenses from the emoluments of the employment. See paragraphs 5.20 and 5.21 of the introductory commentary to the clauses on page 29.

(24) Deductions for employee's expenses. The present rule limits the amount of deductions by requiring the employee to have paid the expenses from the emoluments of the employment. We propose instead to say that deductions from earnings are not to exceed earnings. See paragraph 5.22 of the introductory commentary to the clauses on page 29.

(25) Deductions operating through section 198(1). We propose to rewrite the deductions at section 193(2), (3), (5) and (6) and 198(1B) independently of section 198(1) and not to repeat requirements that have to be met for section 198(1) deductions or the deeming provisions which currently link these deductions with section 198(1). See paragraphs 5.27 to 5.30 of the introductory commentary to the clauses on page 30.

(26) Deductions for earnings representing benefits or reimbursed expenses. We propose to group together the provisions allowing a deduction of an amount equal to the amount included in the employee's earnings in respect of certain costs or expenses borne by others. We will express those deductions by reference to "the included amount". See paragraphs 5.34 and 5.35 of the introductory commentary to the clauses on page 32.

Changes arising in particular individual clauses

(27) Payments to non-approved personal pension arrangements. We propose to limit the application of the clause to contributions which are not otherwise "treated as earnings" (rather than "chargeable to income tax as income"). See paragraph 5.83 of the commentary on clause 4.14.4 at page 41.

(28) Earnings excepted from clause 4.50.2. We do not propose to list separately the deductions mentioned in section 192(5). We will include all the deductions which may be made from earnings under this Part. See paragraphs 5.94 and 5.95 of the commentary on clause 4.50.3 at page 43.

(29) Prevention of double deductions. We propose to allow an employee to choose whether to make a fixed sum deduction under Chapter 4.19 or a deduction for the expense actually incurred, regardless of which is greater. See paragraphs 5.123 to 5.126 of the commentary on clause 4.16.5 at page 48.

(30) Deductions for business entertainment and gifts. We propose to make it clear that the disallowance relates to the employer's trade, business, profession or vocation and not that of the employee. See paragraph 5.129 of the commentary on clause 4.16.6 at page 49.

(31) Deductions for business entertainment and gifts. We have not specified the provisions under which the employer's expenses must be disallowed for the employee's expenses to escape disallowance. See paragraph 5.132 of the commentary on clause 4.16.7 at page 49.

(32) Deductions for business entertainment and gifts. We propose to replace "donor" in the opening words of section 577(8) with "employer". See paragraph 5.138 of the commentary on clause 4.16.8 at page 50.

(33) Deductions for business entertainment and gifts. We propose to clarify the application of section 577(8) to employees. See paragraph 5.139 of the commentary on clause 4.16.8 at page 50.

(34) Deductions for car hire. We propose to exclude hire purchase agreements where there is no option to purchase from the restriction on deductions. See paragraph 5.145 of the commentary on clause 4.16.9 at page 51.

(35) Deductions for expenses: the basic rule. We have omitted the part of section 198(1)(b) which provides that this provision does not apply to qualifying travelling expenses. See paragraph 5.158 of the commentary on clause 4.17.3 at page 53.

(36) Deduction for professional membership fees. We propose to extend the deduction for "professional fees" by defining them by reference to enactments relevant to all professions, not just those mentioned in section 201(2). See paragraph 5.190 of the commentary on clause 4.17.10 at page 57.

(37) Deduction for professional membership fees. We propose to change the rule determining when a deduction may be allowed. We will include payments made at any time from the beginning of the tax year in which a body seeks approval to the date on which approval being granted. See paragraph 5.192 of the commentary on clause 4.17.10 at page 57.

(38) Deduction for professional membership fees. We propose to require the Board to notify a body in writing of their decision on an application for registration. See paragraph 5.194 of the commentary on clause 4.17.11 at page 58.

(39) Expenses of ministers of religion. We propose to import the definition of "charity" currently in section 506(1). See paragraph 5.218 of the commentary on clause 4.17.17 at page 61 and also paragraph 5.607 of the commentary on clause 4.35.1 on page 114.

(40) Agency fees paid by entertainers. We propose to change the earnings by reference to which the 17.5% limit on the amount deductible is calculated to refer to the earnings chargeable in the tax year. See paragraphs 5.225 to 5.227 of the commentary on clause 4.17.18 at page 62.

(41) Deductions from earnings charged on remittance. We propose make it clear that a deduction may be allowed where expenses are paid by another person on the employee's behalf and so constitute earnings of the employment. See paragraph 5.231 of the commentary on clause 4.17.20 at page 62.

(42) Deductions: exclusion of accommodation expenses of MPs and other representatives. We propose to change "under this section" in section 198(4) to "under this Chapter". See paragraphs 5.246 to 5.249 of the commentary on clause 4.17.22 at page 65.

(43) Deductions from benefits code earnings. In rewriting sections 141(3), 142(2), 145(3) and 156(8), we propose to refer to deductions under the whole of Chapter 4.17, deductions for employee's expenses instead of the provisions currently referred to. See paragraphs 5.256 and 5.257 of the introductory commentary on Chapter 4.18 at page 66.

(44) Deductions where living accommodation provided. We propose to limit the deduction made under the rewritten section 145(3). It will be calculated on the basis that the amount paid by the employee for the accommodation is the cash equivalent. See paragraphs 5.264 to 5.266 of the commentary on clause 4.18.3 at page 67.

(45) Fixed sum deductions for repairing and maintaining work equipment. We propose to legislate Extra-Statutory Concession A1. This allows employees who bear the cost of maintaining tools and special clothing a deduction for a flat rate expense fixed after negotiation with the trade unions concerned. See paragraphs 5.272 to 5.274 of the commentary on clause 4.19.2 at page 69.

(46) Deductions for earnings representing benefits or reimbursed expenses: date of arrival condition. We propose to restate the five-year test in terms of the dates upon which the journeys are made. See paragraphs 5.313 to 5.315 of the commentary on clause 4.20.7 at page 74.

(47) Deductions from seafarers' earnings: taking account of other deductions. Within this provision, we propose to refer to deductions "under "Chapters 4.17 to 4.20", rather than listing the relevant deduction provisions as in paragraph 1A of Schedule 12. See paragraphs 5.335 to 5.341 of the commentary on clause 4.21.4 at page 79.

(48) Payments to non-approved pension schemes. Where payments are potentially within both section 595 and section 148, we propose to give priority to the charge under section 595. See paragraphs 5.352 to 5.361 of the introductory commentary to Chapter 4.22 at page 80.

(49) Payments to non-approved pension schemes: exception: seafarers with overseas earnings. We propose to except from the charge under clause 4.22.1 payments made in respect of seafarers who have no net chargeable earnings for the year as a result of the foreign earnings deduction. See paragraphs 5.371 and 5.372 of the commentary on clause 4.22.6 at page 82.

(50) Payments to non-approved pension schemes: relief where no benefits paid or payable. We propose to allow applications for relief to be made by a deceased employee's personal representatives. See paragraphs 5.373 to 5.375 of the commentary on clause 4.22.7 at page 82.

(51) Payments and benefits on termination of employment: reduction in certain cases of foreign service. We propose to restate the limit on reduction so that where tax is deducted from a payment enough tax remains in charge to satisfy the tax on that payment. See paragraph 5.413 of the commentary on clause 4.23.11 at page 88.

(52) Payments and benefits on termination of employment: valuation of benefits. We propose to rewrite the valuation of benefits in terms of the benefits code. See paragraphs 5.415 and 5.416 of the commentary on clause 4.23.12 at page 88.

(53) Exemption of travelling and subsistence during public transport strikes. We propose to legislate Extra-Statutory Concession A58. This exempts the provision of travelling and subsistence when there is a disruption in public transport. See paragraph 5.451 of the commentary on clause 4.30.9 at page 93.

(54) Exemption of transport to work for disabled employees. We propose to legislate Extra-Statutory Concession A59. This exempts the provision of home to work travel for disabled employees. See paragraphs 5.455 to 5.460 of the commentary on clause 4.30.10 at page 93.

(55) Exemption of transport home: late night working and failure of car-sharing arrangements. We propose to legislate Extra-Statutory Concession A66. This exempts the provision of transport home after late night working or if a car-sharing arrangement fails. See paragraphs 5.461 to 5.465 of the commentary on clause 4.30.11 at page 94.

(56) Exemptions of work-related training provision and for contributions to individual learning account training. We propose to make it clear that training funded by a third party is exempt to the same extent as if the employer had incurred the expenditure. See paragraphs 5.470 and 5.471 of the commentary on clause 4.31.1 at page 95 and paragraphs 5.484 and 5.485 of the commentary on clause 4.31.5 at page 97.

(57) Exemptions of work-related training provision and contributions to individual learning account training. We propose to relax the "wholly, exclusively and necessarily" condition on travelling and subsistence related to the undertaking of training. This will bring Chapter 4.31 into line with Chapter 4.41, in which sections 588 to 589B are rewritten. See paragraph 5.472 of the commentary on clause 4.31.1 at page 95 and paragraph 5.486 of the commentary on clause 4.31.5 at page 97.

(58) Exemptions of work-related training provision and contributions to individual learning account training. Within this exemption, we propose to refer to travel expenses being deductible "under this Part", rather than specifically under the clauses rewriting section 198. See paragraph 5.473 of the commentary on clause 4.31.1 at page 96 and paragraph 5.487 of the commentary on clause 4.31.5 at page 97.

(59) Exemptions of work-related training provision contributions to individual learning account training. We propose to make the definitions of "training materials" in sections 200C(7) and 200F(5) more flexible by referring to an illustrative list rather than an exhaustive definition. See paragraphs 5.481 and 5.482 of the commentary on clause 4.31.4 at page 97 and paragraphs 5.494 and 5.495 of the commentary on clause 4.31.8 at page 98.

(60) Exemption of contribution to individual learning account. The rewritten section 200G broadens the terms of the required arrangements (ensuring that contributions are available to employees generally) to cover third party contributions. See paragraph 5.497 of the commentary on clause 4.31.9 at page 98.

(61) Exemption of annual parties and functions. We propose to legislate Extra-Statutory Concession A70B. This provides a limited exemption for benefits otherwise chargeable in respect of annual staff parties. See paragraph 5.515 of the commentary on clause 4.32.4 at page 102.

(62) Exemption for small gifts from third parties. We propose to legislate Extra-Statutory Concession A70A which provides an exemption for small gifts from third parties. See paragraphs 5.547 to 5.550 of the commentary on clause 4.33.5 on page 106 and paragraphs 5.768 to 5.770 of the commentary on clause 4.42.11 on page 136.

(63) Exemption of removal benefits: disposal benefits and expenses. We propose to rephrase the test to determine whether a loan relates to a residence to enable a loan to meet the test where different parts of the loan each meet one of the stated conditions. See paragraph 5.570 and 5.571 of the commentary on clause 4.34.7 at page 109 and paragraph 5.587 of the commentary on clause 4.34.12 at page 110.

(64) Exemption of removal benefits: exclusion where car and van benefits otherwise taxable. We propose to rewrite this rule so that it can only apply if the vehicle is provided for private use (other than in connection with the move) in the same tax year that the employment change takes place. See paragraphs 5.583 and 5.584 of the commentary on clause 4.34.11 at page 110.

(65) Exemption of removal benefits: bridging loan expenses etc. We propose to explain how to allocate the total loan interest between what is, and is not, exempt. See paragraph 5.589 of the commentary on clause 4.34.12 at page 111.

(66) Exemption of removal benefits: limit on exemption. We propose a new rule to encompass all the ways of quantifying the benefit from the provision of living accommodation. This sweeps up the consequential effect of legislating Extra-Statutory Concession A91(b) (living accommodation provided by reason of employment). See paragraph 5.599 of the commentary on clause 4.34.15 at page 112.

(67) Exemption for visiting forces and staff of designated allied headquarters. We have amended the cross-references to the Visiting Forces Act 1952. See paragraphs 5.658 and 5.659 of the commentary on clause 4.35.14 at page 121.

(68) Exemption for experts seconded to European Commission. We propose to legislate Extra-Statutory Concession A84. This exempts daily subsistence allowances paid by the European Commission to "Detached National Experts". See paragraphs 5.661 to 5.664 of the commentary on clause 4.35.15 at page 121.

(69) Exemption for offshore oil and gas workers: mainland transfers. We propose to legislate Extra-Statutory Concession A65. This exempts the provision of transport for that part of the journey between home and work which is from the mainland departure point to the offshore installation. See paragraphs 5.665 to 5.669 of the commentary on clause 4.35.16 at page 122.

(70) Exemption for miners etc: coal and allowances in lieu of coal. We propose to legislate Extra-Statutory Concession A6. This exempts the provision of coal and allowances in lieu of coal to miners etc. See paragraphs 5.670 to 5.675 of the commentary on clause 4.35.17 at page 122.

(71) Exemption: priority share allocations: offer to employees separate from public offer. We propose to drop any reference to companies whose shares are only subject to public offer. See paragraph 5.694 of the commentary on clause 4.39.3 at page 126.

(72) Exemption: priority share allocations: application to directors and other office-holders. We propose to include the definition of "director" from section 136(5)(b) which applies in relation the grant of share options. See paragraph 5.702 of the commentary on clause 4.39.7 on page 127.

(73) Exemption: priority share allocations: minor definitions. We propose to include the definition of "shares" from section 288 Taxation of Chargeable Gains Act 1992. See paragraph 5.705 of the commentary on clause 4.39.8 on page 127.

(74) Exemption of death or retirement benefit provision. We propose to legislate Extra-Statutory Concession A72. This widens the scope of section 155(4), which only applies to death etc benefits payable to an employee's spouse, children or dependants, to cover such benefits payable to other members of the family or household. See paragraphs 5.707 to 5.709 of the commentary on clause 4.40.1 at page 128.

(75) Exemption of counselling and other outplacement services. We propose to make the two-year requirement relate to the employment that is ceasing, not to employment by the particular employer. See paragraph 5.717 of the commentary on clause 4.41.2 at page 129.

(76) Exemptions of counselling and other outplacement services and retraining courses. The rewritten sections 589B and 589(6) include an assumption that the expenses are incurred and paid by the employee. See paragraphs 5.718 and 5.719 of the commentary on clause 4.41.2 at page 129 and paragraph 5.724 of the commentary on clause 4.41.3 at page 130.

(77) Exemptions of counselling and other outplacement services and retraining courses. Within these exemptions, we propose to refer to travel expenses deductible under this Part, rather than specifically under the clauses rewriting section 198. See paragraph 5.720 of the commentary on clause 4.41.2 at page 130 and paragraph 5.725 of the commentary on clause 4.41.3 at page 130.

(78) Exemption of retraining courses. We propose to drop the condition in section 589B(1) for the course to be undertaken with a view to retraining. See paragraph 5.723 of the commentary on clause 4.41.3 at page 130.

(79) Exemption of subsidised meals. We propose to legislate Extra-Statutory Concession A74. This provides an exemption for the provision of free or subsidised meals on the employer's premises. See paragraphs 5.731 to 5.732 of the commentary on clause 4.42.2 at page 132.

(80) Exemption of suggestion awards. We propose to legislate Extra-Statutory Concession A57. This provides a limited exemption for awards paid to employees under suggestion schemes. See paragraphs 5.748 to 5.749 of the commentary on clause 4.42.8 at page 134.

(81) Exemption of long service awards. We propose to legislate Extra-Statutory Concession A22. This exempts from tax the provision of long-service awards. See paragraphs 5.761 to 5.767 of the commentary on clause 4.42.10 on page 135.

(82) Interpretation of this Part: "personal representatives". We propose to use the same definition of "personal representatives" as first appeared in clause 6.4.28 in Exposure Draft No 2. See paragraph 5.793 of the commentary on clause 4.48.2 at page 140.

(83) Interpretation of this Part: "workplace". We propose to adopt the term "workplace" and apply it throughout Part 4, using the definition that applies for travel expenses. See paragraph 5.794 of the commentary on clause 4.48.2 at page 140.

4 Removal of unnecessary material

(84) Deductions for business entertainment and gifts. We propose to omit the reference in section 577(3)(b) to "in whole or in part" in relation to a sum being disallowed. See paragraph 5.135 of the commentary on clause 4.16.7 at page 50.

(85) Agency fees paid by entertainers. We propose not to reproduce section 201A(6), on the basis that it is spent. See paragraph 5.223 of the commentary on clause 4.17.18 on page 62.

(86) Deductions for travel costs and expenses of non-domiciled employees where duties performed in UK. We do not propose to rewrite section 195(13). See paragraph 5.307 of the introductory commentary to clauses 4.20.5 to 4.20.7 at page 74.

(87) Deductions for costs and expenses in respect of personal security assets and services. We do not propose to reproduce the reference in section 52(3)(b) Finance Act 1989 to "living accommodation". See paragraph 5.323 of the commentary on clause 4.20.9 at page 76.

(88) Deductions for earnings representing benefits or reimbursed expenses: personal security assets and services. We propose to rewrite section 52(2) Finance Act 1989 so that it refers only to the provision of security services. See paragraphs 5.324 to 5.326 of the commentary on clause 4.20.9 at page 76.

(89) Deduction from seafarers earnings: limit where UK duties etc make amount unreasonable. We propose to omit the words "but paragraph (b) above shall not be construed as requiring an individual to be treated in any circumstances as under the control of another person" in paragraph 2(3) Schedule 12. See paragraph 5.334 of the commentary on clause 4.21.3 at page 77.

(90) Payments and benefits on termination of employment. We do not propose to rewrite section 148(5). See paragraph 5.379 of the introductory commentary on Chapter 4.23 at page 83.

(91) Exemption of parking expenses. We propose to omit the definitions of "motor cycle" and "cycle" in section 49(2) Finance Act 1999. See paragraph 5.430 of the commentary on clause 4.30.1 at page 90.

(92) Exemptions of work-related training provision and contributions to individual learning account training. We propose to omit sections 200C(4) and 200H which indicate that the exemption does not apply to expenditure that is exempt under section 588. See paragraphs 5.476 to 5.479 of the commentary on clause 4.31.3 at page 96 and paragraph 5.492 of the commentary on clause 4.31.7 at page 98.

(93) Exemption of work-related training provision. We propose to omit any reference to expenditure eligible for relief under section 32 Finance Act 1991 (vocational training) as that relief has been repealed. See paragraph 5.478 on page 96.

(94) Exemption for removal benefits and expenses: conditions applicable to change of residence. We do not propose to reproduce the words in brackets in

paragraph 5(1)(b) and (c) Schedule 11A. See paragraph 5.563 of the commentary on clause 4.34.3 at page 108.

(95) Exemption of termination payments to MPs and others ceasing to hold office. We propose to omit the reference to the Parliamentary Pensions Act 1984. See paragraph 5.612 of the commentary on clause 4.35.2 at page 115.

(96) Exemption of armed forces' allowances. We propose to leave out section 316(1), (2) and (5). See paragraph 5.634 of the commentary on clause 4.35.8 at page 118.

(97) Exemption: priority share allocations. We do not propose to rewrite section 68(6) Finance Act 1988. See paragraph 5.685 of the introductory commentary to Chapter 4.39 at page 125.

(98) Exemption of mobile telephones. We do not propose to rewrite section 155AA(3). See paragraph 5.733 of the commentary on clause 4.42.3 at page 132.

Part 5: Commentary

What does this Exposure Draft include?

5.1 The bulk of this Exposure Draft contains clauses on deductions and exemptions. However, we have also included a few provisions that were first published in Exposure Draft No 6. These have subsequently been amended either to take account of comments received or to achieve a better fit with the deduction and exemption clauses.

5.2 We have also included chapters dealing with two of the free-standing tax charges within Schedule E. They cover payments to non-approved pension schemes (Chapter 4.22) and payments and benefits on termination of employment (Chapter 4.23).

5.3 This Exposure Draft also includes a plan of Part 4 setting out the arrangement of the chapters as currently envisaged. We have made several changes to the arrangement published in Exposure Draft No 6. It is still provisional and may be revised in the course of rewriting the remaining Part 4 provisions or as a result of comments received in response to this Exposure Draft.

5.4 What was previously Chapter 4.3, earnings, payments treated as earnings, is now Chapter 4.14. We have moved it here to become the last chapter dealing with what counts as earnings, immediately before the chapters on deductions from earnings. This is because it is less important than the benefits code.

5.5 In Exposure Draft No 6 we showed the deductions chapters as immediately preceding the exemptions chapters. However, some exemptions apply not just to income which would otherwise count as earnings but also to other types of employment income. We have therefore moved the exemption chapters further down so that they come after both the earnings chapters and the chapters under which other employment income is taxed. As all the exemption chapters are gathered together in one block they should still be easy to find.

5.6 Any arrangement involves some degree of compromise. What works well in one respect might not do so in another. Our reordering does have the side effect that the clauses do not necessarily appear in the order in which they would actually have to be considered for particular kinds of income. For example, in many cases, an employee would look first at the main charging provisions to see if there is a potential charge to tax as earnings, then move on to see if that charge is removed by an exemption before considering the deductions provisions.

5.7 **We welcome any views on the current proposed order of the clauses.**

5.8 In addition, we have moved Chapter 4.50, chargeability and year of charge: earnings, so that it follows the chapters which determine what income counts as earnings and precedes the deduction chapters. This is because the amounts to be charged to tax as earnings and the year in which they are to be charged have to be

determined **before** any deductions are allowed. Also, the precise charging provision is relevant for some of the deduction provisions in Chapter 4.17, deductions for employee's expenses, Chapter 4.20, deductions for earnings representing benefits or reimbursed expenses, and Chapter 4.21, deductions from seafarers' earnings.

5.9 Continuing in the same pattern as set out in Exposure Draft No 6 the provisions on deductions and exemptions are arranged in short chapters, each dealing with a separate topic.

5.10 This Exposure Draft also includes a summary of a new arrangement of clauses within the chapters. We comment on the detailed effects of the arrangement of material in the context of the individual clauses.

5.11 **We welcome comments on the way we are arranging the material in this Exposure Draft.**

Overall changes in approach

5.12 In rewriting the material included in this Exposure Draft, we have tried to provide a cohesive structure and a common approach wherever possible.

5.13 In the current legislation, many of the provisions offering exemptions or deductions from earnings include the same repetitive material. Where this occurs we have tried to reduce the degree of repetition by stating a proposition only once at the beginning of the relevant group of rewritten provisions.

5.14 We have also tried to standardise and simplify the wording used for deductions and exemptions, so far as possible. For example, one phrase that crops up throughout the legislation on benefits, as well as elsewhere in the Tax Acts, is "a benefit consisting in". In the legislation regarding employment income it generally means either "a benefit consisting in the provision of" or "the benefit consists in providing".

5.15 We have looked into the history and case law surrounding the use of these words and have come to the conclusion that the words are intended to identify the benefit itself. We also think that the use of "consists in" and "consisting in" does not convey anything in the current legislation on benefits that "is" or "which is" would not. We have therefore dropped the references to "consists in" or "consisting in" in rewriting most the existing provisions.

Proposed rewrite changes with wide-ranging effect

5.16 Our various strands of work have led to a number of proposed rewrite changes affecting a wide range of clauses, rather than just one particular rewritten provision. We have identified these wide-ranging changes under the separate sub-headings in the list of proposed rewrite changes above. We invite comment on these proposed changes in this part of the Exposure Draft, rather than asking readers to comment on the change in respect of each clause that they affect.

5.17 We propose to set out some general rules about deductions. Under the current legislation many deduction provisions make use of section 198. We have set

out the deduction provisions in a new way, grouping them according to the type of deduction and the type of expense involved. But we do not want to repeat the main propositions of section 198(1) (and similar provisions) several times over. Instead we have brought these common rules together in Chapter 4.16 where we have set out some propositions of general application to the deductions provisions. For example, we have set out in clause 4.16.2 the general proposition that deductions are only allowed from the earnings of the employment in question.

5.18 Setting out general propositions has also allowed us to make clear some points that are not easy to discern in the current legislation. For example, we have set out in clause 4.16.5 that a deduction for a particular expense is not allowed more than once.

5.19 This approach has helped us to simplify some of the individual deduction provisions. And it has saved a certain amount of repetition. This change is relevant to all of the clauses in Chapters 4.17 and 4.18. It is a change in approach but not in the underlying law. It will not in itself affect anyone's liability to tax. **We welcome comments on this proposed rewrite change**.

5.20 Under section 198(1), and other deduction provisions, a deduction is only allowed where an expense has been incurred and defrayed out of the emoluments of the employment. Inland Revenue guidance (see SE31655) makes it clear that the employee does not have to demonstrate that an expense has literally been paid out of the emoluments rather than out of some other source of money. It is sufficient that the emoluments charged to tax in a particular tax year are greater than the deductions to be made from those emoluments. Where the Inland Revenue does not currently trace the source of funds used by the employee to pay expenses we propose to omit from the rewritten provisions the requirement that the employee must pay expenses from the emoluments of the employment.

5.21 This change is relevant to many of the clauses in Chapters 4.17 to 4.21. It is a change to the law but not to policy. In theory it is in favour of the taxpayer, but in practice it is unlikely to affect anyone's liability to income tax, and has the advantage of providing greater certainty. **We welcome comments on this proposed rewrite change**.

5.22 The current legislation also provides that no single deduction, or the total of such deductions, can exceed the emoluments of the employment. We have translated this into the general proposition, set out in clause 4.16.3, that deductions from earnings are not to exceed earnings. This change is relevant to all of the clauses in Chapters 4.17 to 4.21. It is a change to the law but not to policy. As this simply follows existing practice, it will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change**.

5.23 There is a further consequence of the present rule in section 198(1) and elsewhere. A deduction may be allowed where the employee has incurred the expense but the actual liability is met by someone else, usually the employer. Where the employee's pecuniary liability is met in this way it is an emolument and it is taxed

under section 19(1) paragraph 1. As the expense is met in a way that constitutes emoluments, it is accepted that it has been defrayed out of those emoluments. So the employee is allowed a deduction if the liability met comes within the wording of section 198(1) or some other such provision. This is also the approach taken in practice. (See, for example, SE32940. This indicates that, where the employee's telephone bill is paid by the employer, the employee is allowed a deduction in respect of any business use of the telephone.)

5.24 The current legislation does not state explicitly that a deduction may be allowed where the employee incurs the expense but the liability is met by someone else. We propose to make the position clearer by stating in clause 4.17.1(2) the employee is treated as paying the expense where the actual liability is met by someone else and constitutes earnings of the employee. This is a change in approach but not in the underlying law. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.25 A further issue that may arise in connection with deductions from employments concerns the position where the employee is reimbursed for an amount that has been paid. At present, a reimbursed amount may be dealt with for income tax purposes in either of two possible ways:

- First, the reimbursed amount may constitute part of the earnings from the employment, and then the deduction may be allowed in full.
- Second, the reimbursed amount does not constitute part of the earnings from the employment, and then the deduction of the expense is not allowed to the extent that reimbursement has been made. The speeches of Lord Guest and Lord Pearce in Pook (HM Inspector of Taxes) v Owen (1969) 45 TC 571[1] envisage that a reimbursed amount may be dealt with in this way.

5.26 Against this background, this Exposure Draft contains a clause (clause 4.17.2) that has been drafted with the object of making explicit provision for cases where an amount is reimbursed. The clause is not derived directly from the current legislation, but it reflects current practice in cases where amounts deductible for income tax purposes are reimbursed. It is a change in approach but not in the underlying law. It will not in itself affect anyone's liability to tax. **We welcome comments on this proposed rewrite change.**

5.27 A number of deduction provisions (in sections 193(3) and (6), and 198(1B)) work by deeming certain travel expenses to have been necessarily incurred or expended in the performance of employment duties. This effectively makes them qualifying travel expenses within section 198(1A) which can qualify for deduction under section 198(1). But the way that the current provisions work means it is unclear to what extent the conditions in section 198(1) apply in these cases. Sections 193(3) and (6) and 198(1B) do not disapply any of the section 198(1) conditions, but in practice deductions are allowed in cases where those conditions are not all met. This

[1] (HL) [1970] A.C. 244

makes it difficult to see from the statute what requirements have to be met for each of those deduction provisions.

5.28 We propose to rewrite the provisions to operate independently, as we believe this makes it easier to work out whether a deduction is allowable for a particular expense. We propose to state for each rewritten provision exactly what conditions, in addition to those set out in the general rules for deductions in clauses 4.17.1 and 4.17.2, need to be fulfilled. We propose to follow current Inland Revenue practice in setting out those conditions.

5.29 We think that once these provisions have been decoupled from section 198(1) and (1A), there will be no reason to continue to deem the expenses to have been necessarily incurred performing employment duties, except in one case (see clause 4.17.7(2)). We propose to omit these deeming provisions except for that case. **We welcome comments on whether they may be needed for anything else**.

5.30 This change is relevant to clauses 4.17.7 to 4.17.9. It is a change to the law but not to policy. It will not affect anyone's liability to tax. **We welcome comments on this proposed rewrite change.**

5.31 We propose not to rewrite the provisions in sections 194(10) and 195(11). They require references to section 198 to be read as including references to sections 194(1) and 195(7) respectively. And they require references to deductions under sections 198, 199, 201 or 332 to be read as including references to deductions under sections 194(1) and 195(7) respectively. Similarly, we do not propose to rewrite the provision in section 193(7) that requires those references to be read as including references to section 193(4) and to deductions under section 193(4). (The references to section 193(3) are mistakes.)

5.32 Again, the approach adopted in these provisions is not very helpful. Obviously it makes the provisions containing references to section 198, or to deductions under the various provisions, difficult to construe. More importantly, perhaps, it is quite likely that the need to include those references will be overlooked in the first place. And it is probably significant that certain provisions (for example, section 192(5), relief from tax for foreign emoluments) actually include references to sections 193(4), 194(1) and 195(7) when they refer to section 198.

5.33 We believe it is much more helpful to include the appropriate references where they are required. This change is relevant to many of the clauses in Chapters 4.17 to 4.20. It is a change in approach but not in the underlying law. It will not affect anyone’s liability to income tax. **We welcome comments on this proposed rewrite change**.

5.34 We propose to operate the provisions that allow a deduction of an amount equal to an amount included in the employee’s earnings (in respect of costs or expenses borne by others) by reference to “the included amount”. Under sections 193 to 195, and section 50 Finance Act 1989, deductions are allowed for certain expenses which are included in the employee’s emoluments. These are expenses met by the employer,

or a third party, either by providing travel facilities or by reimbursing the employee's expenditure. The amount of such a deduction is "equal to so much of that cost or, as the case may be, those expenses as falls to be included in those emoluments". That rather long-winded formulation is included in all four sections. We have found it easier to group all these provisions together in a single chapter. This enables us to define such an amount under the label "the included amount" and then say simply "the deduction is equal to the included amount".

5.35 This change is relevant to the clauses in Chapter 4.20. It is a change to the law but not to policy. **We welcome comments on this proposed rewrite change**.

5.36 We propose to abandon the label "foreign emoluments". Section 192(1) defines these as the emoluments of an individual who is resident in the United Kingdom but not domiciled here from an employment with an employer who is resident outside the United Kingdom. In Exposure Draft No 6 we rewrote this for the rewrite of section 192(2), which identifies the amounts to be excluded from the Case I charge where the duties are performed wholly abroad. We gave those emoluments the label "foreign earnings" in clause 4.50.3.

5.37 The definition in section 192(1) includes earnings from employments where the duties of the employment are

- performed wholly in the United Kingdom,
- partly in the United Kingdom and partly abroad, or
- wholly abroad.

5.38 We think it is unlikely that an employee who is resident and ordinarily resident in the United Kingdom (but not domiciled here) would naturally regard the emoluments from an employment performed wholly or partly in the United Kingdom as being "foreign". We therefore propose to drop the label of "foreign emoluments" altogether. Instead, we have listed the circumstances relevant in each context. This makes each deduction provision more self-contained and easier to understand.

5.39 In particular, we have dealt with the "foreign emoluments" exclusions for certain deductions by requiring that, where the earnings are from an employment with a "foreign employer" (as defined in section 192(1)), the employee must be domiciled in the United Kingdom in order for a deduction to be allowable.

5.40 We have also followed this line of thinking in revisiting clause 4.50.3, first published in Exposure Draft 6. Then, we used the label of "foreign earnings" to describe those foreign emoluments excluded from the Case I charge by section 192(2). We have now decided to drop that label and simply list the circumstances relevant to that clause.

5.41 This proposed rewrite change affects clauses 4.50.3, 4.17.8, 4.17.9, 4.17.21 and 4.20.8. It is a change in approach but not in the underlying law. It will not affect anyone's liability to tax. **We welcome views on this proposed rewrite change.**

5.42 We propose to standardise the form of words used to indicate that income is exempt from income tax. The current legislation expresses exemptions in a number of different ways. Consequently, some exemptions remove all potential charges to tax, some remove any charge to tax under Schedule E and some remove only a particular charge to tax (for example, the charge to tax as emoluments).

5.43 This lack of consistency is not restricted to the exemptions affecting employment income. It is also a feature of exemptions affecting savings and investment income. As explained in previous Exposure Drafts, we have tried to introduce some much-needed consistency by using only the clearest and most straightforward form of expression – "is exempt from income tax". For employment income we have in some cases also added the words "as earnings" or "as a benefit within Chapter 4.12" to reflect the limited scope of particular exemptions. This change is relevant to many of the clauses in Chapters 4.30 to 4.43. It is a change in approach but not in the underlying law. It will not in itself affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change**.

5.44 We propose to gather together into two single clauses the exceptions from the charges relating to non-cash vouchers and credit-tokens. These apply in cases where the vouchers or tokens are used for benefits that are themselves exempt. This change is relevant to clauses 4.33.1 and 4.33.2. This is a change in approach, but not in the underlying law. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change**.

Changes we have not included

5.45 As noted above, we have incorporated a number of extra-statutory concessions in the draft clauses. However, many concessions are made to deal with minor or transitory anomalies under the legislation. Others meet cases of hardship at the margins of the tax code for which a legislative remedy would be difficult to devise or would run to a length out of proportion to the intrinsic importance of the matter. We have therefore left out concessions which are obsolete or have very limited application. We have also left out concessions which are too complicated to legislate, either because of complexity within the concession itself or because of difficulties in fitting various strands of the concession into the legislation in a coherent manner.

5.46 The extra-statutory concessions we have omitted because they are obsolete (or will be so by the time the Income Tax Bill is introduced) are:

A64 – External training courses – expenses borne by an employee
A90 – Jobmatch pilot scheme
A97 – Jobmatch Programme

5.47 The extra-statutory concessions we have omitted because they are of very limited application are:

A44 – Education allowances under Overseas Service Aid Scheme
A60 – Agricultural workers' board and lodging

5.48 The extra-statutory concessions we have omitted on grounds of complexity are:

A4 – Travelling expenses of directors and employees earning £8,500 a year or more

A37 – Tax treatment of directors' fees received by partnerships and other companies

A61 – Clergymen's heating and lighting, etc expenses

A68 – Payments out of a discretionary trust which are emoluments taxable under Schedule E

A81 – Termination payments and legal costs

5.49 We will rewrite Extra-Statutory Concession A85, transfers of assets by employees and directors to employers and others, in a later Exposure Draft.

The employment income clauses

Chapter 4.1 - Income taxed as employment income

5.50 This first chapter of Part 4 introduces the basic concepts to be used. Clause 4.1.1 identifies income charged to income tax under this chapter as employment income. It explains what is included as employment income and, within that, what is included as earnings from an employment. The charge to tax is made subject to the exemptions in Chapters 4.30 to 4.43. The following clause indicates that in charging employment income to income tax deductions may be allowed.

5.51 We have not republished the remainder of this chapter, but clauses 4.1.2 and 4.1.3 provide a non-exhaustive definition of "employment", explain that Part 4 applies equally to offices, and provide a non-exhaustive definition of "office".

5.52 Clause 4.1.4 provides for the remuneration of workers contracted to agencies, and who perform duties for agency clients, to be taxed as employment income. We are considering moving this clause to a less prominent position.

5.53 Clause 4.1.5 provides that employment income is charged to income tax only under Part 4. It therefore draws the boundary between employment income and other types of income.

Clause 4.1.1 Income taxed as employment income

5.54 This is a development of the clause that appeared in Exposure Draft No 6. It identifies the subject of the charge to income tax in Part 4 as employment income. Then it sets out what is covered by Part 4.

5.55 Employment income has two distinct strands. First, there are earnings from an employment. Secondly, there are other amounts charged to tax as employment income. This distinction is set out in subsection (2) and preserves the structural dichotomy of the current legislation.

5.56 Broadly, earnings from employment equate with emoluments under the current legislation. It is only "emoluments" that flow through the Cases of Schedule E and then into the receipts basis set out in sections 202A and 202B. So earnings from an employment have to be tested against the criteria of Chapter 4.50, chargeability and year of charge for earnings, to establish whether they are chargeable to income tax and, if so, the tax year in which they are charged to tax. Provisions relating to earnings are set out in a single block in Chapters 4.2 to 4.21.

5.57 "Other amounts charged to tax as employment income" covers the free-standing tax charges under Schedule E (see, for example, section 148 as discussed in Nichols v Gibson (1996) (68 TC 611)[2]. These amounts fall within the scope of section 19(1) paragraph 5. They do not currently feed through the Cases of Schedule E set out in section 19(1) paragraph 1. Accordingly, these amounts do not have to be tested against

[2] (CA)[1996] STC 1008

the criteria of Chapter 4.50. Provisions relating to these free-standing tax charges are also set out in a single block in Chapters 4.22 to 4.29.

5.58 In subsection (3) we list what falls within the category of earnings in this legislation.

5.59 As explained in Exposure Draft No 6, the use of the term "earnings" in this clause and elsewhere is a significant proposed rewrite change. Although we wanted to avoid the use of the word "emoluments" this did not prove entirely possible. There is a great deal of authority on the meaning of the word that it is important to retain. We were not able to find a wholly satisfactory alternative.

5.60 Nevertheless, we did not feel obliged to use "emoluments" quite as widely as it is used in the current legislation. At present, there are three groups of "emoluments". First, there are emoluments properly so called (broadly, those within the section 131 definition). Secondly, there are payments (actual and notional) that are treated as emoluments. Finally, there are amounts in respect of chargeable benefits that are treated as emoluments. We felt we only needed to retain "emoluments" for the first of those groups. However, if we retained the word only for this more restricted purpose, we had to adopt a new label to cover all three groups. We propose to use "earnings". However, we accept that this choice is not without its own difficulties.

5.61 There is a possible danger that the word "earnings" is not sufficiently colourless to be a label. It might carry connotations that are not accurate for these purposes. One such connotation might be that only rewards for past services fall within the term, whereas the case law (see, for example, Shilton v Wilmshurst (1991) 64 TC 78[3]) makes it clear that payments for becoming an employee may be within the charge. However, as "earnings" is only being used as a label it derives its meaning only from those matters that are said to fall within its scope.

5.62 Perhaps more significant is the point that, as the word is used in this context, the meaning of "earnings" will not coincide with the meaning of the same word in the context of National Insurance Contributions. It is not the role of the Rewrite to achieve greater synthesis between the two systems. This must be achieved by greater policy co-ordination. We therefore accept that we are proposing the use of a word that is used with different meanings in different contexts. We did consider alternatives, such as "remuneration", but they gave rise to similar difficulties.

5.63 As the word "earnings" has an exhaustive definition for these purposes, we consider the benefits of using a more modern word as a label outweigh the possible disadvantages. The great majority of the people who commented on Exposure Draft No 6 were in favour of (or accepted) our use of "earnings".

5.64 There are numerous exemption provisions which remove the charge to tax that would otherwise apply to particular types of employment income. We have collected the rewritten exemptions together in a block of chapters towards the end of Part 4. Subsection (4) makes it clear that where these exemptions apply, the relevant types of

[3] (HL) [1991] STC 88

income are outside the charge to income tax under Part 4. It also provides a helpful signpost to the exemptions themselves.

Clause 4.1.1A The amount of employment income charged

5.65 Subsection (1) of this clause appeared in Exposure Draft No 6 as clause 4.50.1(2). We have promoted it to Chapter 4.1, and expanded it, because it helps to make clear at an early stage that in charging earnings to income tax certain deductions are allowed. Some of the provisions under which deductions are allowed are included in Part 4. Others are in other parts of the Tax Acts.

5.66 We expect a similar provision will be needed for the non-earnings types of employment income. We have therefore included a marker in subsection (2). We will look at this further as we rewrite more of the free-standing Schedule E charges.

Chapter 4.9 – Taxable benefits: loans

5.67 Most of the provisions within this chapter were included in Exposure Draft No 6. We are publishing two new clauses for Chapter 4.9 in this Exposure Draft. These deal with reduced rate loans that an employer provides to an employee as bridging finance connected with a change of residence brought about by an employment change. The provision of such reduced rate loans is not exempt from the charge to tax, but these clauses provide for exceptions from, and reductions in, the tax that would otherwise be chargeable.

5.68 Where an employer reimburses the employee's expenses of such bridging finance, any potential charge to tax is removed by the exemption for removal benefits and expenses in Schedule 11A, now set out in Chapter 4.34. However, it is difficult to fit beneficial loans chargeable under section 160 into the scheme of Schedule 11A where a monetary cap of £8,000 applies to the exemption. This is because the calculation of the cash equivalent of the benefit is very different from that of most other emoluments.

5.69 The mechanism to offer some relief for such bridging loan finance is set out in section 191B. Basically an employee has to look first at all the other benefits and expenses connected with a removal brought about by an employment change to see whether or not there is any of the £8,000 exemption limit left unused. If so, that unused portion is converted into a number of days and the starting date for calculating benefit under section 160 is deferred by that number of days. Changes in the way that the £8,000 limit is calculated and applied are included in clause 4.34.15 and explained in paragraphs 5.597 to 5.599 below. These changes will feed through to clauses 4.9.17A and 4.9.17B, discussed below.

5.70 The following two clauses rewrite section 191B. We have also produced a slightly amended version of clause 4.9.19 (first published in Exposure Draft No 6) which now includes an additional subsection to deal with removal benefits.

Clause 4.9.17A Exception for certain bridging loans connected with employment moves

5.71 This clause rewrites those parts of section 191B that set out:

- what kind of loan is covered;
- the formula for working out the day by which the loan must be repaid if there is to be no charge to tax under section 160 (rewritten in Chapter 4.9 as published in Exposure Draft No 6); and
- interpretative provisions.

5.72 There is a consequential change to the law in clause 4.9.17A(1)(c) because of the revised basis on which the £8,000 limit on removal expenses is calculated in clause 4.34.15(2). This is a change to the law and policy. It is a change that, theoretically, is unfavourable to the taxpayer. For further comment on this see paragraph 5.597 of the

commentary on clause 4.34.15 where we invite comments on this proposed rewrite change.

5.73 We have made a slight change to the formula for working out the day by which the loan must be repaid if there is to be no charge to tax. The current formula in section 191B(10) uses A, B, C and D but in that formula B is always 365 (even in a leap year). We have therefore replaced B with the number 365 and moved the other elements of the formula up one place in the alphabet so that:

- "A" remains the unused amount of the exemption limit in Schedule 11A;
- "B" becomes the maximum amount of the loan outstanding; and
- "C" becomes the official rate of interest.

Clause 4.9.17B Other bridging loans connected with employment treated as made later

5.74 An employee who has a bridging loan that comes within section 191B may not repay that loan until after the day determined by the formula set out in section 191B(10), and so not come within the exception now set out in clause 4.9.17A. In such a case the employee's liability in respect of the beneficial loan under section 160 is worked out as if the loan had been made on the day determined by that formula.

5.75 This clause rewrites those parts of section 191B that achieve this reduction in chargeable benefit.

Clause 4.9.19 Claim for relief to take account of event after assessment

5.76 There may be an assessment to tax in respect of beneficial loan benefit under this chapter made before the "limitation day" specified in Chapter 4.34. Both clauses 4.9.17A and 4.9.17B include a provision to the effect that where this is the case, it should be assumed that there is no unused amount of the exemption limit.

5.77 However, after the limitation day it may be apparent that there is in fact an amount of the £8,000 exemption limit remaining unused.

5.78 We have added a subsection (4) to the version of clause 4.9.19 published in Exposure Draft No 6 to ensure that the benefit chargeable under this chapter is recalculated in such a case.

Chapter 4.12 – Taxable benefits: residual liability to charge

Clause 4.12.6A Power to exempt minor benefits

5.79 This clause rewrites section 155ZB, which allows regulations to be used to introduce minor exemptions from section 154 (rewritten in Chapter 4.12) where the benefits in question are generally available to all employees on similar terms. Before this provision was introduced by Finance Act 2000, all exemptions from section 154 had to be introduced through a Finance Act.

5.80 Subsection (3) provides for regulations to be made by statutory instrument subject to the negative resolution procedure. That will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Chapter 4.14 – Payments treated as earnings

Clause 4.14.4 Payments to non-approved personal pension arrangements

5.81 This clause treats as an employee's earnings an employer's payments to a non-approved personal pension arrangement made by the employee. The clause rewrites section 648.

5.82 It contrasts with clause 4.40.2, which exempts from income tax as the employee's earnings an employer's contributions to an **approved** personal pension arrangement made by the employee.

5.83 The contributions are not treated as earnings under this clause if they are treated otherwise as the employee's **earnings**. Subsection (2) contains a proposed rewrite change. Section 648 limits how it applies in terms of the employee's **income**. That may create doubt on the priority of section 648 over other charging provisions such as section 148 (a similar point is discussed in the introduction to the commentary on Chapter 4.22 at page 80). As section 648 treats these contributions as emoluments of the employment, ie "earnings" in the terms of this Exposure Draft, there is no need to limit priority other than against other earnings charges. This change establishes the priority of clause 4.14.4 over the charges on employment income other than earnings. It is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.84 Personal pension arrangements may be approved by the Board of Inland Revenue under section 631, in accordance with the rules of Chapter IV, Part XIV, ICTA. The rules for approval of pension scheme arrangements are not yet rewritten.

5.85 Subsection (3) provides for the relevant definitions from section 630(1) to apply.

Clause 4.14.5 Payments for restrictive undertakings

5.86 This and the following clause rewrite section 313. They deal with the payments made in return for restrictive undertakings.

5.87 Section 313 was first enacted as section 26 Finance Act 1950. At that time the charge was to surtax, rather than income tax. The giving of a restrictive undertaking was a device used to augment net income at a time of high rates of tax. The sum paid was characterised as capital and was not therefore chargeable to income tax. When surtax was abolished the charge (at that time in section 34 Income and Corporation Taxes Act 1970) survived as a charge to higher rates of income tax only. Section 73 Finance Act 1988 changed the basis on which the charge was made so that the sum paid was treated as emoluments from the employee's employment.

5.88 We have translated the sum described in section 313(1) as "an emolument of the office or employment" into "earnings from the employment" in clause 4.14.5(1). That reflects the changed definitions of "emoluments" and "earnings" used in Chapters 4.1 and 4.2 in Exposure Draft No 6.

5.89 In subsection (4) we have rewritten the words from the end of section 313(1) giving the timing provision for when income is chargeable. That provision will override the normal timing provisions relating to earnings that are in clause 4.50.9 in Exposure Draft No 6. When there is no employment at the time the payment is made the timing rule in clause 4.50.8 will operate.

5.90 By virtue of section 313(6)(a) liability only arises if the income is or would be chargeable under Case I or Case II of Schedule E. Subsection (7) reproduces that condition by reference to the relevant clauses in Chapter 4.50 in Exposure Draft No 6.

Clause 4.14.6 Valuable consideration given for restrictive undertakings

5.91 In this clause we have brought together the provisions that apply when the payment for the restrictive undertaking is in a non-monetary form. This is more logical and convenient than their present separation in section 313(4) and (6)(b).

Chapter 4.50 – Chargeability and year of charge for earnings

Clause 4.50.3 Earnings excepted from section 4.50.2

5.92 This clause was originally published in Exposure Draft 6. It rewrites the exclusion in section 192(1) from the Case I charge of the foreign emoluments of a non-domiciled employee, in employment with a foreign employer, where all of the duties are performed abroad. We have revisited this clause because our work on deductions has revealed ways in which the original clause could be improved.

5.93 The proposal to drop the label "foreign emoluments" and instead to focus on whether the employee of a "foreign employer" is domiciled in the United Kingdom is discussed in paragraphs 5.36 to 5.41 in the introductory commentary to the clauses at page 32.

5.94 In section 192(5) there is a list of deductions to be made in calculating the earnings which are excepted from the tax charge under Schedule E Case I (see clause 4.50.2 in Exposure Draft No 6). We have not been able to establish why that list does not include all the deductions allowed in charging emoluments to tax. The policy has always been to make all such deductions in calculating such excepted earnings. We believe any omissions are merely accidents of history.

5.95 Consequently in subsection (3) we have simply referred to "any deductions under this Part" and thus included all the deductions. This is a change to the law but not to policy. It is theoretically in favour of the Inland Revenue although, as it follows an existing practice, it will not in reality affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.96 Subsection (4) lists other deductions to be made in computing the excepted amount which we do not currently plan to rewrite in this Part. As our work progresses we will consider whether there are any other deductions which should be included in this list – for example under section 619(1), qualifying premiums or section 639, member's contributions to approved personal pension arrangements.

Chapter 4.16 – Deductions allowed from earnings: general rules

5.97 This is the first of six chapters dealing with deductions allowed in charging earnings to income tax. It sets out some general rules which are applicable to most of the deductions covered in the other five chapters.

5.98 The deductions in the current legislation are very difficult to unravel. Of course some individual provisions are straightforward. But collectively they interact in ways which are not always easy to follow. There are lots of connections between provisions and several fictions have been adopted to make the provisions work.

5.99 For example, consider some of the different ways in which section 198 is used by other provisions.

- Under section 156(8) the cost of a benefit provided is allowed as a deduction under section 198 (or other provisions) if it would be allowed as a deduction if paid out of emoluments.

- Under section 193(3) certain travel expenses are treated as having been necessarily incurred in the performance of the duties of an overseas employment for the purposes of section 198(1).

- Under section 193(7) references to section 198, and to deductions under section 198, are treated as including references to section 193(3), and to deductions under that subsection.

- Under section 200A(1) incidental overnight expenses are not regarded as emoluments if they would not be deductible under section 198.

5.100 Another major source of complexity is that there is a number of possible ways of meeting the expenses of an employee, taxed under different sections of the current legislation, and the mechanism for making a deduction is slightly different in each case.

5.101 For example, consider the position of a "higher-paid" employee making a train journey to attend a meeting. The table below shows some of the various ways in which the employer might fund the trip, how the employee would be taxed and how the employee might obtain a deduction in respect of the expenses of the train ticket.

Employer funds trip by	*Charging provision*	*Deduction allowable under*
• round sum allowance	section 19(1)1	Section 198
• specific expense payment	section 153	Section 198
• buying the ticket	section 141	Section 198 *via* section 141(3)
• providing credit card for employee to use on ticket	Section 142	Section 198 *via* section 142(3)

5.102 There are other possibilities. For example, if the same "higher-paid" employee travelled to the same meeting using private transport provided by the employer, the provision of the transport would be taxed under section 154 and a deduction allowable

under section 198 *via* section 156(8). If the trip involved foreign travel, there would be other deduction provisions involved.

5.103 We have tried to make it easier for the user to see whether any deduction is applicable by grouping the provisions in different chapters according to the type of deduction. So there are separate chapters for:

- deductions for employee's expenses (Chapter 4.17);
- deductions from benefit code earnings for costs which would have been deductible if they had been paid by the employee (Chapter 4.18);
- deductions for employee's expenses covered by fixed allowances (Chapter 4.19);
- deductions for earnings which represent expenses borne by the employer (Chapter 4.20); and
- deductions from seafarers' earnings (Chapter 4.21).

5.104 Within Chapters 4.17 and 4.20 we have then grouped the provisions according to the type of expense etc involved. For example, in Chapter 4,17, clauses 4.17.4 to 4.17.9 deal with travel expenses.

5.105 To make each individual deduction provision as simple as possible we have used this chapter to state some general propositions about deductions. This saves them having to be repeated in the individual provisions. So in the deductions clauses themselves we can concentrate on the rules applying for the particular deduction. The propositions are:

- deductions are allowed in charging earnings to tax;
- deductions are allowed only from the earnings of the employment in question;
- total deductions may not exceed earnings; and
- a deduction for a particular cost or expense is not allowed more than once.

5.106 We have also included some restrictions on the deductions which are allowable. The restrictions are

- deductions are not allowed for entertainment expenses or gifts (subject to certain exceptions), and
- there is a limit on the amount of deductions allowed for hiring cars.

Introductory

Clause 4.16.1 Deductions from earnings: general

5.107 This first clause of the chapter sets the scene by stating that in calculating the earnings from an employment that are chargeable in a tax year deductions are allowed under the following five chapters. It is the link between clause 4.1.1A(1), which indicates that tax is charged on total earnings subject to certain deductions being allowed, and the individual deduction provisions. It therefore points the way to the deductions for employee's expenses and for other matters.

5.108 Subsection (1) covers the deductions allowed under provisions in Part 4.

5.109 Subsection (2) points the way to other deductions from earnings which may be allowable. As our work progresses we will consider whether there are any other deductions which should be included in this list. Similarly, subsection (3) points the way to other more general deductions. Again, this subsection is just a marker until more work has been done on the deductions. Both these subsections will therefore be revisited when the relevant reliefs are considered in due course, both to see whether the provisions we have mentioned appear in the right subsection and whether other provisions should be mentioned.

General rules

Clause 4.16.2 The income from which deductions may be made

5.110 This clause is based on section 198(1), relief for necessary expenses, and other similar provisions which provides that expenses etc which are paid "out of the emoluments of the office or employment" may be deducted "from the emoluments to be assessed".

5.111 This clause starts by setting out the general proposition that deductions are allowed only from the earnings of the employment in question. Usually this is the employment in respect of which the relevant expenses etc are incurred, but in some cases like section 198(1B) and (3), section 192(3) and section 193(5) this may not be the case. We have therefore tried to make it clear in the clauses which employment is the "employment in question".

5.112 The only deduction we have found which does not fall within the general proposition set out in subsection (1) is in section 332(3), expenses of ministers of religion, which we have rewritten in clause 4.17.17. Subsection (2) covers this exception where the deduction may be allowed against the earnings of any employment as a minister and so may exceed the earnings of the particular employment.

5.113 As described in the commentary on clause 4.17.17, in separating the Schedule D and Schedule E aspects of deductions under section 332(3) we propose to allow deductions only from income of the appropriate class. The scope of subsection (2) is limited accordingly. See paragraph 5.212 of the commentary on clause 4.17.17 on page 60.

5.114 While the general proposition in subsection (1) holds good for virtually all the deduction provisions, it does not tell the whole story. Some deductions may only be made from earnings from the employment in question which are charged to tax under particular provisions. For example, under section 194(1), employee's travel expenses where duties performed abroad (rewritten in clause 4.20.2), a deduction may only be made from earnings which are taxed under Schedule E Case I. So subsection (3) sets out a further proposition for deductions which are limited in this way.

5.115 Subsection (4) sets out another similar proposition for expenses within section 199, expenses from official emoluments, which we have rewritten in clause 4.19.3. These expenses may only be deducted from those official emoluments.

Clause 4.16.3 Deductions from earnings not to exceed earnings

5.116 This clause sets out the general proposition that total deductions may not exceed the earnings of the employment in respect of which the relevant expenses etc are incurred.

5.117 This translation of the words in section 198(1), and other deduction provisions, requiring the employee to have paid the expenses from the emoluments of the employment is one of the proposed rewrite changes with a wide-ranging effect. It is described in detail in paragraphs 5.20 to 5.22.

5.118 Users are likely to wonder what happens to the excess where the potential deductions do in fact exceed the earnings. So subsection (2) provides a link to the loss relief provisions in section 380. It is quite clear from section 380 that there can be Schedule E losses which may be set against other income of the year or carried back to previous years. As deductions normally cannot exceed the earnings from which they are made it is less obvious how those losses may arise. We have identified three ways so far.

- As indicated above, the deduction for expenses of ministers of religion is not restricted to any particular employment.
- Capital allowances may exceed the earnings from which they may be deducted.
- A loss may be made as a result of certain conditions of employment (for example, where an employee is remunerated by a percentage of profits but is responsible for a corresponding percentage of any losses).

Clause 4.16.4 Order for making deductions

5.119 In general there is no order of priority for allowing deductions. Apart from some relatively uncommon situations, deductions may be allowed in any order. This clause ensures that the general provisions in section 835, about deductions being allowed in the order which is most advantageous for the individual concerned, are taken into account.

5.120 In subsection (2), we have also provided signposts to particular provisions under which deductions are allowed in a particular order.

Clause 4.16.5 Prevention of double deductions

5.121 This clause starts by setting out the general proposition that a deduction for a particular cost or expense is not allowed more than once. So an employee may not deduct something under one provision and then again under another. This proposition may be derived from a number of specific provisions. But we believe it is true generally, even where it is not articulated in the current legislation.

5.122 In some instances the amount of the deduction may not be computed by reference to an actual amount of expenditure (for example, the deductions for expenses borne by the employer which are treated as earnings covered in Chapter 4.20). Nevertheless, we believe the term "costs or expenses" is sufficient to cover all potential Part 4 deductions.

5.123 Under Extra-Statutory Concession A1, flat rate allowances for cost of tools and special clothing (clause 4.19.2 in this Exposure Draft), and section 199, expenses from official emoluments (clause 4.19.3 in this Exposure Draft), an employee is allowed a deduction for particular flat rate expenses. The employee may also be allowed a deduction for the **actual** expense incurred under, for example, section 198. We have taken the opportunity here to make clear how these fixed allowances work in relation to deductions for actual expenses. Subsection (2) indicates that the employee is allowed to make only one of the deductions. In effect, the employee may choose whether to deduct the fixed allowance or the expense actually incurred.

5.124 This reflects the position under Extra-Statutory Concession A1. But under section 199 the position is slightly different.

5.125 Under section 199(2) an employee who is entitled to deduct a fixed allowance is only entitled to deduct the expense actually incurred if that expense is greater than the fixed allowance. In fact, however, some people prefer to make a deduction for the expense actually incurred even if it is **less** than the fixed allowance. And in practice the Inland Revenue does not prevent them doing this. Subsection (2) is drafted to allow this practice to continue. This brings section 199 into line with Extra-Statutory Concession A1.

5.126 Allowing the employee to choose which deduction to make, regardless of which is greater, is a change to the law. But as the Inland Revenue practice is to allow people to make whichever deduction they choose it is not a change to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Rules restricting deductions of particular kinds

Clause 4.16.6 Disallowance of business entertainment and gifts

5.127 This is the first of three clauses which rewrite the Schedule E aspects of section 577. The Schedule D aspects were rewritten in clauses 3.3.7 to 3.3.9 in Exposure Draft

No 10. The capital allowances aspects have been rewritten in clause 269 of the Capital Allowances Bill. The remaining aspects of section 577, relating to investment companies, will be rewritten as part of the rewrite of the corporation tax provisions. We believe that by separating the various aspects we have made their application to each of the areas affected clearer and more specific.

5.128 Section 577 was enacted as section 15 Finance Act 1965, to counter what was perceived as a growing abuse of "expense account living". Business proprietors (and their more senior employees on the employer's behalf) were entertaining, sometimes on a lavish scale, those with whom they came into contact through their business. Those entertained were not always customers of the business, although there was generally some connection with the business so that the claim could be made that the expenditure was "for the purposes of the trade etc". An element of reciprocity between those providing and those benefiting from the entertainment had also evolved.

5.129 The extended definition of "trade" in section 577(7)(b) applies in section 577(5), which defines "business entertainment". That latter term is used in section 577(1)(a) to which section 577(1)(b) refers back. Thus, particularly where the employee has an appointment that can be described as a profession or vocation, section 577(1)(b) could operate to deny a deduction to such an employee, despite the intention to the contrary. The Inland Revenue has not applied section 577 in that way. We have made it clear in clause 4.16.6(1) that the trade, business, profession or vocation to which the business entertainment expenses relate is the trade etc of the employer. This is arguably a change to the law but not to policy. It does not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change to clarify the scope of the disallowance for employees pursuing a profession or vocation.**

Clause 4.16.7 Business entertainment and gifts: exception where employer's expenses disallowed

5.130 When Finance Bill 1965 was passing through Parliament the then Chancellor of the Exchequer said that there was no intention to disallow the same expenditure on both the employer and the employee through whom it was made. Where the amount of the expenditure on business entertainment could be identified without any doubt, the disallowance would be borne by the employer and the employee would be excluded from the disallowance provisions.

5.131 However, where a round sum allowance is provided for the employee to meet a variety of expenses, some of which might be business entertainment, such identification is not possible. In those circumstances the disallowance applies to the employee and not the employer.

5.132 This clause brings together the elements in section 577 that prevent the operation of clause 4.16.6(1) as far as the employee is concerned where the employer has borne the disallowance of the business entertainment expenses. Subsections (2) and (3) refer in descriptive terms to the conditions that have to be met for the clause to apply, rather than referring to specific legislation, as section 577(3)(b) does. This is a change to the law but not to policy. It will only rarely affect anyone's liability to

income tax and when it does so it will be in the taxpayer's favour. **We welcome comments on this proposed rewrite change.**

5.133 As originally enacted, section 15 Finance Act 1965 allowed a deduction for the cost of entertainment expenditure that related to overseas customers (but not suppliers) of the business. Section 72 Finance Act 1988 removed that saving, so that from then on all business entertainment expenses were covered by section 577 (as the provision had by then become).

5.134 In subsection (1) we have removed the reference currently in section 577(5) to "bona fide" because we do not believe that it adds anything to "members of staff". This follows the line taken in clause 269(3) in the Capital Allowances Bill.

5.135 Section 577(3)(b) refers to a sum (of expenses) being "disallowed in whole or in part". We do not believe that it is possible for a sum to be disallowed "in part" since the change made in 1988. The sum is either disallowed or allowed in its entirety in the employer's tax computation. Depending upon which happens, the sum is either potentially allowable as a deduction for the employee or not. The employee will only be able to get a deduction if the expense meets the conditions for a deduction to be allowed in section 198 (rewritten in Chapter 4.17) or section 332 (rewritten in clause 4.17.16). In subsections (2) and (3) we have not reproduced the reference to "in whole or in part". This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on the proposal to remove this phrase.**

Clause 4.16.8 Business entertainment and gifts: other exceptions

5.136 This clause provides exceptions for other types of expenses that the employee might incur which, but for the provisions it contains, would be disallowed by clause 4.16.6.

5.137 In subsection (1) we have removed the reference in section 577(5) to "bona fide" for the same reason as given in 5.130 above. This follows the line taken in clause 269(3) in the Capital Allowances Bill.

5.138 We propose changing the word "donor" towards the end of the introduction to section 577(8) to "employer" in clause 4.16.8(3). We think that the conspicuous advertisement that is referred to will be for the employer and not, necessarily, the donor who might well be an employee of the employer. We do not think the same considerations apply to the use of the word "donor" in section 577(8)(b) and therefore do not propose to make any change there. This is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.139 The exception from the general principles of section 577 in section 577(8) is principally directed at the employer rather than the employee. However, because it permits the employer to deduct an amount spent for a particular purpose, when combined with section 577(3)(b) it prevents the employee getting a deduction for that amount. Thus the employee might well be charged to tax on the amount involved but would not be allowed a deduction against that charge. We do not believe that is the

intended result. We have included subsection (3) to remove any doubt that there might be about whether employees are excepted from the prohibition in clause 4.16.6. This reflects how the Inland Revenue currently operates the provisions of section 577. The proposal is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.16.9 Car hire

5.140 This clause restricts the amount allowed as a deduction for car hire charges, when the retail price of the car when new exceeds £12,000. It is a partial rewrite of sections 578A and 578B, which will be inserted in ICTA 1988 by the Capital Allowances Bill. Those new sections themselves derived from sections 35 and 36 of the Capital Allowances Act 1990.

5.141 The restrictions on allowable car hire charges for expensive cars, in calculating trade profits or deductions against employment income, were added to the original capital allowances restrictions to prevent them being circumvented by car hire instead of purchase. In rewriting the capital allowances legislation, the opportunity was taken to move what are in fact income tax rules to a more appropriate location.

5.142 This clause rewrites sections 578A and 578B to the extent that they apply to deductions allowable against employment income. The impact of the restriction in sections 35 and 36 of the 1990 Act has not been changed either by the clauses inserted in ICTA or by the rewrite in this clause.

5.143 Subsections (1) and (2) repeat the relevant parts of section 578A (1) to (3). They introduce the term "qualifying hire car" which is then defined at subsection (4). The restriction is now calculated using a simple fraction (rather than through descriptive words as in the 1990 Act).

5.144 Subsections (3) to (5) rewrite section 578B(1) to (3).

5.145 In the definition of "qualifying hire car" at subsection (4), subsection (4)(a)(i) is new and covers the case where purchase of the car under the terms of the hire agreement is not subject to an option. This is a change to the law but not to policy. It is in the taxpayer's favour, as it excludes more cars from the restricted deduction rules. This change mirrors the change proposed in Exposure Draft 10: Trading Income of Individuals, Part 3, clause 3.3.10. **We welcome comments on this proposed rewrite change.**

5.146 The amount (£12,000) in subsections (1) and (2) is subject to amendment by Treasury order. This power is contained in clause 4.48.1.

Chapter 4.17 – Deductions for employee's expenses

5.147 This chapter deals with the most familiar situation in which deductions from earnings are allowed – where the employee has paid an expense of the employment. It also extends to the situation where someone else (usually the employer) pays the expense on the employee's behalf. It therefore covers section 198, the related provisions in Schedule 12A, and a number of other provisions which allow deductions for particular expenses paid by the employee.

5.148 We have grouped the clauses according to the type of expense involved. For example, clauses 4.17.4 to 4.17.9 deal with travel expenses.

5.149 The following chapters deal with other situations in which deductions from earnings are allowed.

Introductory

Clause 4.17.1 Scope of this Chapter: expenses paid by the employee

5.150 This is the first of two introductory clauses in this chapter. It sets out the general proposition that, for a deduction to be allowed under the provisions in this chapter, the expense has to be paid by the employee. This reflects various forms of expression in section 198 and other provisions which indicate that the employee must "incur and defray" the expense.

5.151 A deduction is also allowed under most of the provisions in the chapter where the employee has incurred the expense but the actual liability has been met by someone else, usually the employer. The current legislation does not state that explicitly. But subsection (2) makes the position very much clearer by stating that the employee is treated as paying the expense where the actual liability is met by someone else and constitutes earnings of the employee. This is one of the proposed rewrite changes with wide-ranging effect. It is described in more detail in paragraphs 5.23 and 5.24.

5.152 To be allowed a deduction under Chapter 4.17, the employee must satisfy subsection (1), read, if necessary, with subsection (2). With two exceptions, dealt with in subsection (3) – both of those conditions are capable of being satisfied for each of the deduction provisions in this chapter, although there are some provisions where it is perhaps unlikely that subsection (2) will apply.

5.153 Including these provisions here saves us having to say something to the same effect in each of the individual deduction provisions in the chapter.

5.154 In subsection (4) we have also included a signpost to the following chapter. This deals with deductions from benefits code earnings for costs that would have been deductible if the employee had paid them. (It therefore covers situations where an expense is met by the employer in the form of a taxable benefit.)

Clause 4.17.2 Effect of reimbursement etc.

5.155 This second introductory clause deals with the position where the employee is reimbursed for an amount that has been paid. The issues arising in connection with this point have been discussed in paragraphs 5.25 and 5.26 of the introductory commentary on the clauses at page 30.

5.156 This clause also includes wording designed to ensure that the provisions of this chapter apply where a payment is made to the employee in respect of the expenses in question, and that payment is included in the employee's earnings. This guards against the argument that, in such a case, it is the person making the payment to the employee who pays the amount question, rather than the employee.

Basic rule for deduction of employee's expenses

Clause 4.17.3 Deductions for expenses: the basic rule

5.157 Subsection (1) of this clause derives from section 198(1)(b) and states the basic rule relating to deductions from earnings from an employment.

5.158 We have omitted the part of section 198(1)(b) which provides that this provision does not apply to qualifying travelling expenses. These words have the effect that a taxpayer first needs to consider whether a particular deduction constitutes a qualifying travelling expense. Only if it does not so qualify would the taxpayer then have to consider whether the basic rule applies. We think that this order is illogical. It seems better to ask the taxpayer to consider the basic rule stated in this clause first before going on to consider whether a deduction may be obtained on the basis that there has been a qualifying travelling expense. This will constitute a change to the law but not to policy. The deductions that a taxpayer can obtain will remain entirely unaltered. **We welcome comments on this proposed rewrite change.**

5.159 Subsection (2) of this clause relates the basic rule stated in subsection (1) to the provision made for other deductions in subsequent clauses of this chapter.

Travel expenses

Clause 4.17.4 Travel in performance of duties

5.160 This is the first of two clauses rewriting the proposition, contained in section 198(1)(a), that a deduction is allowed for qualifying travelling expenses. This clause rewrites the part of the definition of qualifying travelling expenses to be found in section 198(1A)(a).

5.161 The label "qualifying travelling expenses" is introduced in section 198(1)(a), but is used only at the beginning of section 198(1A). We have dispensed with this label in the rewritten legislation.

Clause 4.17.5 Travel for necessary attendance

5.162 This is the second of the two clauses referred to in paragraph 5.160 above. Subsection (1) of this clause rewrites the part of the definition of qualifying travelling expenses to be found in section 198(1A)(b)(i).

5.163 The deduction for which subsection (1) provides is not available if the travel is "ordinary commuting" or "private travel". These expressions are mentioned in section 198(1A)(b)(ii). But it is necessary to turn to Schedule 12A for detailed definitions of these terms.

5.164 We have reorganised the statutory material so that the definitions of "ordinary commuting" or "private travel" are now placed near the proposition they qualify - in subsections (2) and (4) of this clause. These subsections also deal with the gloss on these expressions to be found in paragraph 3 of Schedule 12A.

Clause 4.17.6 Meaning of "workplace" and "temporary workplace"

5.165 The definitions of "ordinary commuting " and "private travel" in clause 4.17.5 use the expressions "workplace and "permanent workplace". This clause explains what those expressions mean, rewriting provisions currently in Schedule 12A.

Clause 4.17.7 Travel between group employments

5.166 This clause rewrites section 198(1B), a subsection that applies where an employee, who has employments with more than one company in the same group, travels from a place of employment with one group company to another place of employment with another group company. Section 198(1B) operates through section 198(1) and (1A). We propose to rewrite it independently from those subsections for the reasons set out in paragraphs 5.27 to 5.30 of the introductory commentary to the clauses.

5.167 As explained in paragraph 5.28 we propose to state for each rewritten provision exactly what particular conditions need to be fulfilled. We have not reproduced the condition from section 198(1) that it is the holder of the employment who is obliged to incur and defray the expenses.

5.168 In subsection (3), we have been able to abbreviate the definition of the word "group" given in the second sentence of section 198(1B)

Clause 4.17.8 Travel at start or finish of overseas employment

5.169 This clause rewrites section 193(2) and (3), which allow a deduction for travelling and subsistence expenses when an employee travels from the United Kingdom to take up an overseas employment or travels back to the United Kingdom after it ceases. Section 193(2) and (3) operate through section 198(1). We propose to rewrite them independently from section 198(1) for the reasons set out in paragraphs 5.27 to 5.30 of the introductory commentary to the clauses.

5.170 As explained in paragraph 5.28 we propose to state for each rewritten provision exactly what particular conditions need to be fulfilled. We have not reproduced the condition from section 198(1) that the holder of the employment is obliged to incur and defray the expenses.

5.171 The decision to drop the term "foreign emoluments" and instead to focus on whether the employee of a "foreign employer" is domiciled in the United Kingdom is discussed in paragraphs 5.36 to 5.41 in the introductory commentary to the clauses at page 32.

5.172 In subsection (1), the new labels "starting travel expenses" and "finishing travel expenses", which are defined in subsection (3), describe travel to take up an overseas employment and travel home after it has finished.

Clause 4.17.9 Travel between employments where duties performed abroad

5.173 This clause rewrites section 193(5) and (6), which allow a deduction for travelling and subsistence expenses where an employee with more than one employment travels between them, outside the United Kingdom. The deduction depends on the individual being resident and ordinarily resident in the United Kingdom. And the deduction is made from the earnings of the employment which is being travelled to, so long as they are not what are currently described as "foreign emoluments". Section 193(5) and (6) operate through section 198(1). We propose to rewrite them independently from section 198(1) for the reasons set out in paragraphs 5.27 to 5.30 of the introductory commentary to the clauses.

5.174 As explained in paragraph 5.28 we propose to state for each rewritten provision exactly what particular conditions need to be fulfilled. We have not reproduced the condition from section 198(1) that the holder of the employment is obliged to incur and defray the expenses.

5.175 The decision to drop the reference in section 192(1) to "foreign emoluments" and instead to focus on whether the employee of a foreign employer" is domiciled in the United Kingdom is discussed in paragraphs 5.36 to 5.41 in the introductory commentary to the clauses at page 32.

Fees and subscriptions

Clauses 4.17.10 to 4.17.12 Introduction

5.176 The following three clauses rewrite section 201, which was originally enacted as section 16 Finance Act 1958. There had been strong pressure for legislation to allow deductions for a range of fees and subscriptions following the publication in June 1955 of the final report of the Royal Commission on the Taxation of Income and Profits (Cmd. 9474). That report criticised the restrictive rule in what is now section 198(1)(b) that, to be allowed as a deduction, an expense had to be expended "wholly, exclusively and necessarily in the performance of the duties of the office or employment".

5.177 The sorts of fees and contributions covered by section 201(2) have to be paid before an employee can (lawfully) begin to practise the particular profession to which the fees relate. They would not therefore meet the "in the performance of the duties" test in section 198. The subscriptions covered by section 201(3) are voluntary in nature (in the sense that employees do not have to join the body concerned) and so would not meet the "necessarily" test in section 198.

5.178 There is another distinction between the expenses allowable under those two subsections. Subsection (2) lists those bodies to which fees paid qualify for deduction. Subsection (3) gives a general description of the sorts of bodies that are eligible to apply to the Board of Inland Revenue for approval under that subsection, by reference to their character and the activities they pursue.

5.179 The names of the bodies that the Board approves are published in a booklet called "Fees and subscriptions paid to Professional Bodies and Learned Societies (List 3)", which we refer to as "List 3" for convenience. It has been updated every six months or so and will shortly be published on the Inland Revenue's web site. The vast majority of the bodies in List 3 have been approved under subsection (3). Where fees paid to a body qualify for deduction under subsection (2) their entry in List 3 records that fact.

5.180 It seems odd that these two different rules exist. Under the current approach, it is only possible to amend the list in section 201(2) by means of primary legislation and there is no statutory requirement for the Board to publish details of the bodies that it approves under section 201(3). Furthermore, there seems to be something of a breakdown in that approach - List 3 shows some deductions as available under section 201(2) where there is no mention of the body in question in the section 201(2) list, for example retention fees paid to the Hearing Aid Council.

A new approach

5.181 We think it would be better to move to a common system where the Board maintains two registers. One would list those bodies currently dealt with under section 201(2) and the other those under section 201(3). This is similar to the approach previously adopted in section 376A for "qualifying lenders" within the MIRAS (mortgage interest relief at source) provisions. The suggested approach would provide a faster and more flexible way of dealing with changes in the bodies within the scope of section 201(2).

5.182 The approach is likely to be of wider application for bodies within section 201(3) but we think it has something to offer in relation to section 201(2) as well. List 3 is a prototype register from which the actual registers can be built.

5.183 We expect that the registers would be published on the same regular basis as the current List 3.

5.184 We have included in clause 4.17.10(5), as part of the proposed registration process, a new requirement that the Board should give a body written notice of its decision on the body's application for inclusion in a register.

5.185 We have included machinery in these clauses to allow the Board to remove bodies from the registers. In the commentary on clause 4.17.12 below, we seek views as to whether there should be a requirement for approved bodies to notify the Board if there is a change in their circumstances which might affect their approval or listed entry in the published register.

5.186 For the moment we have only drafted legislation for the "steady state" situation that assumes that the register exists. If people like this approach we will need to draw up some transitional provisions:

- to transfer to the professional body register those bodies already listed in section 201(2);
- to include in the professional body register those bodies identified in List 3 as within section 201(2) that do not currently appear in that subsection; and
- to transfer to the second register the bodies in List 3 that are currently approved under section 201(3).

5.187 Moving to a registration system would be is a change to the law and policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.17.10 Deduction for professional membership fees

5.188 Clause 4.17.10 deals with professional fees paid to bodies currently listed under section 201(2). Instead of listing the relevant professional bodies it requires the Board to maintain and publish a list of those professional bodies, and sets out how a body may come to be included in the register. Clause 4.17.12 sets out how a body may be removed from the register.

5.189 We have moved the introductory words in section 201(1) to the introductory and general rules clauses in Chapters 4.16 and 4.17. The reasons for doing that are described in the commentary on those clauses.

5.190 Subsections (1) and (2) rewrite section 201(5). Subsection (2) redefines the essential characteristic of a professional fee that presently qualifies under section 201(2). Instead of listing the various fees individually, it refers to amounts payable under "an enactment". This is a general term to cover the various statutes that contain the requirement for employees' names to appear in a roll or record before they can pursue their employment. This is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

5.191 Subsection (4) sets out the criteria that a body must meet if it is to be included in the register and allows the Board to register a body if it does meet them.

5.192 We have adapted the second leg of section 201(6), relating to the date from which approval is effective, to a registration system. While doing that we have made it clear that a fee or subscription paid in any year between that in which the body seeks

approval and that in which approval is granted is also allowable as a deduction in the year in which it is paid. This is reflected in clauses 4.17.10(6) and 4.17.11(8) and simply reproduces the treatment currently applied by the Inland Revenue. This is a change to the law but not to policy. **We welcome comments on this proposed rewrite change.**

Clause 4.17.11 Deduction for annual subscriptions

5.193 This clause rewrites those parts of section 201 dealing with annual subscriptions to bodies approved under section 201(3). These include the Board's power under section 201(4) to determine what part (if not all) of such an annual subscription may be allowed as a deduction.

5.194 The proposed new scheme outlined above involves a new requirement for the Board to notify its decisions in writing. The corresponding requirement in this clause to notify the Board's decision on an application in writing simply enacts current practice. This is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.17.12 Decisions of the Board

5.195 This clause adapts the first leg of section 201(6) to fit with the registration system. It also rewrites the provisions in section 201(7) in a clearer way, by splitting out the ideas within it.

5.196 The Board is currently not required to notify in writing a decision to remove approval or vary a determination. It seems sensible to include such a requirement in the proposed registration system.

5.197 The Board is only likely to learn of an event that might cause it to review a body's registration status from the body itself. There is presently no requirement that a body should do that. We have not proposed any legislation to deal with this point and we recognise that there would be a small regulatory cost associated with such a requirement. **We welcome comments on whether such a requirement should be included.**

5.198 A new power for the Board to cancel a registration under clause 4.17.10 is an administrative consequence of the move to a registration system. To achieve the same effect with the current legislation would need an amendment to the bodies listed in section 201(2), and would require primary legislation. The proposal is arguably unfriendly towards the taxpayer in that the Board can now take a decision that previously required the approval of Parliament. However, we do not believe that any taxpayers will be disadvantaged by this proposed change, particularly as they will have the right of appeal to the Special Commissioners. We have asked for comments on the move to a registration system in paragraph 5.187.

Employee liabilities and indemnity insurance

Clause 4.17.13 Deduction for employee liabilities

5.199 This is the first of four clauses that rewrite section 201AA. Introduced by section 91 Finance Act 1995, section 201AA allows deductions for costs or expenses related to the sorts of liability covered by directors' and officers' liability insurance. This clause rewrites the provisions relating to employee liabilities.

5.200 We have replaced the concept of a "qualifying liability" with that of an "employment-related liability", which we define in subsection (2). We have not reproduced the reference in section 201AA(2) to the liability being "imposed". Section 201AA does not give any more information about how the liability might have been imposed. We have rewritten the provisions describing other characteristics that the liabilities must have. We do not, therefore, see this slight difference in approach as a proposed rewrite change.

5.201 We have brought forward to subsection (3) the prime requirement that the liabilities can lawfully be insured against. Users now meet it much earlier than they did in section 201AA(8).

5.202 Section 92 Finance Act 1995 introduced similar provisions for liabilities that arise in the six years after the tax year in which someone ceases to hold the employment to which a liability relates. It might seem natural to include the rewrite of that extension alongside this clause. However, we have not rewritten section 92 for the moment as it provides for a deduction from total income and does not relate directly to employment income. When we rewrite section 92 we will consider and invite comment on where it is best to locate it.

Clause 4.17.14 Deduction for indemnity insurance

5.203 We have separated out the provisions in section 201AA relating to indemnity insurance. We deal with them in this and the next two clauses.

5.204 Employees can get a deduction for premiums paid personally or for the amount assessed on them if their employer has taken out an insurance policy that covers an individual or a group of employees. (See clause 4.17.1(2)).

5.205 Section 201AA(9) explains the broad meaning of "premium". That is because, particularly in the field of mutual insurance, several different terms, such as "subscription", "contribution" or "call", are used to describe payments. The definition was included to make it clear that section 201AA would cover all such payments. We have retained the definition. **We welcome comments, particularly from those in the insurance sector, on whether it is still necessary to define "premium".**

Clause 4.17.15 Meaning of "qualifying insurance contract"

5.206 In this clause we have rewritten and reordered the material that was in section 201AA (3) and (4).

5.207 In clause 4.17.15(2)(d) we have not reproduced the phrase in parentheses in section 201AA(4)(d). We do not believe it adds anything to the rest of the paragraph.

Clause 4.17.16 Connected contracts

5.208 This clause reproduces the elements within section 201AA(6) which prevent section 201AA being used for purposes other than those for which it was intended. We have separated out and reordered the various elements of the provision to make them easier to follow.

Expenses of ministers of religion

Clause 4.17.17 Expenses of ministers of religion

5.209 This clause rewrites those parts of section 332 that relate to Schedule E deductions for the expenses of ministers of religion. Those parts of section 332 that relate to exemptions from tax under Schedule E for ministers of religion are covered in clause 4.35.1.

5.210 Section 332(3) sets out the deductions that a minister can make from "any profits, fees or emoluments" of his profession or vocation. Where the minister is chargeable to tax on profits or fees under Schedule D, the available deductions are set out in clause 3.9.7 of Exposure Draft No 10.

5.211 This clause therefore only allows deductions from emoluments – rewritten here as "earnings".

5.212 Currently, deductions under section 332(3) are available against income earned as a minister that is assessable either under Schedule D or Schedule E. In separating the Schedule D and Schedule E aspects of the deduction we have restricted the deductions to one particular class of income. As explained in relation to clause 3.9.7 of Exposure Draft No 10, this is a change to the law and policy. However we feel it is logical, administratively convenient and will simplify the law. Theoretically the change is in favour of the Inland Revenue, but we do not believe it will have any practical consequences. If the deduction of expenses creates a loss that loss will be available against other income. **We welcome comments on this proposed rewrite change.**

5.213 This clause allows a deduction for any expenditure that meets the requirements. It makes no distinction between capital and revenue expenditure. This is different from the rule for ministers chargeable under Schedule D, set out in clause 3.9.7 of Exposure Draft No 10. In that case the current wording of section 332(3) could only possibly have application for capital expenditure and the clause only mentions capital expenditure.

5.214 Subsection (2) of this clause rewrites subsection 332(3)(b). This allows a deduction for "such part of the rent (not exceeding one quarter) as the inspector by whom the assessment is made may allow". The inspector's decision is subject to appeal to the General or Special Commissioners. These rules do not fit with Self Assessment. We have therefore rewritten the provision to make the deduction available without reference to the inspector, on a just and reasonable apportionment basis. There is then

no need for the special appeal mechanism. This is a change to the law and policy. We do not believe it will affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.215 We have rewritten section 332(3)(c) in clearer terms. First, we have outlined the nature of the deduction available in respect of maintenance, repair, insurance and management of premises in subsection (3). Second, we explain in subsection (4) how to calculate the amount of deduction allowed.

5.216 In Part 4 we have separated out the provisions on exemptions from those on deductions. This means that we describe the relevant premises both here and in clause 4.35.1, exemption for accommodation benefits of ministers of religion. We think that this duplication is worthwhile in that it makes the legislation easier to use.

5.217 In clause 3.9.7 of Exposure Draft No 10 there is a proposed rewrite change (see paragraph 5.418) where we have replaced the word "borne" used in section 332(3)(c) with "incurred". This change is appropriate in the Schedule D context, where deductions are generally made when incurred. However, it does not fit with the general pattern of deductions from employment income, which are generally made only when actually paid.

5.218 The deduction in respect of maintenance, repair, insurance and management of premises is only available in the case of premises owned by a charity or ecclesiastical corporation. For ease of use, this clause includes a definition of "charity", drawn from section 506(1), although this definition does not currently apply for section 332(3). This is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Agency fees paid by entertainers

Clause 4.17.18 Limited deduction for agency fees paid by entertainers

5.219 This clause rewrites section 201A, which was enacted by section 77 Finance Act 1990. Section 69 Finance Act 1991 introduced amendments to deal with payments to co-operative societies with retrospective effect from 6 April 1990.

5.220 Section 201A was necessary to allow entertainers who were in employment, to get relief for the fees they pay to their agents for finding them work. Such fees would not be deductible under the general rule in section 198(1) for the deduction of expenses for two reasons. First, they are paid to put the performer in the position to earn from the employment. They are not, therefore, expended "in the performance of the duties of the employment". Second, as not every entertainer uses the services of an agent, the expense does not pass the "necessarily" test.

5.221 We have removed much of the repetition in section 201A that arises from the two-stage enactment of section 201A referred to in paragraph 5.219.

5.222 We have removed the qualifier "bona fide" from "co-operative society". We do not think it adds anything to what is still, in clause 4.17.18(4), a closely defined term.

5.223 We have not reproduced section 201A(6) which contains the commencement date on the ground that it is now spent. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.224 The requirements in sections 201A(2)(e) and 201A(2A)(c) that the fees be paid out of the emoluments of the employment are now expressed in the general rule for earnings in clause 4.16.3.

5.225 We had difficulty rewriting section 201A. That stemmed particularly from the references in subsections (2)(e), (2A)(c) and (4) to emoluments falling to be to be charged to tax "for" the year concerned. It is possible for earnings to be chargeable to tax "for" one tax year because of the contract of employment under which they arise but to be chargeable to tax "in" a later tax year because of the receipts basis of assessment. It is not clear which of these is "the year concerned".

5.226 In most instances the two will be the same. If they are not then there is uncertainty about which earnings are relevant and this is particularly acute for the calculation of the 17.5% limit. We propose to remove any uncertainty by rewriting the legislation so that the limit is computed by reference to the earnings chargeable to tax "in" a tax year. That is the figure that will be shown on forms P60. It is also the figure that taxpayers will report on self-assessment tax returns. Furthermore it is a figure that is readily available to the Inland Revenue from employers' returns and it has the advantage of requiring no further calculation. For those reasons, and despite what the legislation says, this is the figure used at present.

5.227 This is a change to the law but not to policy. We cannot tell, taking one tax year at a time, whether or not it would be in favour of the taxpayer. However, we think that over the period of the employment there will be no net effect. **We welcome comments on this proposed rewrite change.**

Special rules for earnings with a foreign element

Clause 4.17.19 Deductions from earnings charged on remittance

5.228 This is the first of two clauses which rewrite section 198(2) and (3).

5.229 Section 198(2) applies where there are earnings that "do not fall within Case I or II of Schedule E". It follows, accordingly, that such earnings are either chargeable under the present Case III of Schedule E or are not chargeable to income tax at all.

5.230 This clause deals with the earnings chargeable under the present Case III of Schedule E. Deductions are allowed from those earnings only in limited circumstances.

5.231 In subsection (2), paragraph (a) refers both to expenses paid by the employee out of the relevant earnings and to expenses paid on the employee's behalf by another person and included in those earnings. This wording does not appear in the present legislation, but it corresponds to the wording used in clause 4.17.1(1) and (2). This is a change to the law but not to policy. **We welcome comments on this proposed rewrite change.**

5.232 In subsection (3), the reference to "sections 4.17.3 to 4.17.9" derives from the reference to "subsection (1)" in section 198(3). Clauses 4.17.8 and 4.17.9 do not derive directly from section 198(1), but these have been included in the new reference because the provisions they rewrite (section 193(3) and (6)) operate through section 198(1).

5.233 One of the cases in which this section needs to be considered is where the earnings from an employment consist in part of earnings within clause 4.50.3 and in part of other earnings. If that is the case, then deductions must be made from the other earnings before determining the amount of the earnings within clause 4.50.3; but a deduction for the same costs or expenses must not be made twice. Subsection (4) of the clause deals with these two points.

Clause 4.17.20 Restriction on deductions under ss 4.17.3 to 4.17.7 from other earnings

5.234 This is the second of two clauses which rewrite section 198(2) and (3). This clause deals with part of section 198(2).

5.235 One set of circumstances in which section 198(2) applies is where the income from an employment falls into two categories, so that there are:

- earnings that are chargeable under the present Case III of Schedule E or are not chargeable to income tax at all; and
- "other" earnings (ie earnings that are chargeable under the present Case I or II of Schedule E).

5.236 This clause is concerned with such circumstances, and with earnings in the second category. The clause prevents a deduction relating to earnings in the first category from being given against earnings in the second category.

Example

5.237 Suppose that F, a Frenchman, is resident and ordinarily resident in France. He performs most of the duties of his employment in France where he receives the earnings for those duties. F does not remit any of those earnings to the United Kingdom, so they are not chargeable to income tax in the United Kingdom. As the holder of his employment, F is also obliged, while in France, to incur expenditure wholly, exclusively and necessarily in the performance of his duties there. **But** F also performs a minority of the duties of his employment in the United Kingdom where he receives earnings for these other duties. These earnings are chargeable to income tax in the United Kingdom under the present Case II of Schedule E. This clause prohibits F from deducting the expenditure incurred in France from the income chargeable to tax in the United Kingdom.

5.238 This clause does not deal with the part of section 198(2) that relates to capital allowances. That part is dealt with in clause 20 of the Capital Allowances Bill and

paragraph 25 Schedule 2 and Schedule 4 to that Bill repeal the relevant words in section 198(2).

Clause 4.17.21 Deductions for corresponding payments by non-domiciled employees with foreign employers

5.239 This clause rewrites section 192(3) which allows relief for payments made out of "foreign emoluments" (as defined in section 192(1)) in circumstances corresponding to those in which a deduction would have been available for such payments if the emoluments were not "foreign emoluments". For example, it applies to a contribution to a foreign retirement benefits scheme which would have been deductible if it had been made to an approved scheme in the United Kingdom.

5.240 The proposal to drop the label "foreign emoluments" and instead to focus on whether the employee of a "foreign employer" is domiciled in the United Kingdom is discussed in paragraphs 5.36 to 5.41 in the introductory commentary to the clauses at page 32.

5.241 The discretionary nature of the provision enables relief to be given for payments normally deductible from total income rather than just from emoluments of the employment. Payments that might be relieved under this provision include interest payments under a foreign loan agreement or payments under a foreign court order.

5.242 At present, the relief under section 192(3) is given "in computing the amount of the emoluments". While it is not expressed explicitly as an exemption, the relief operates in much the same way as an exemption because it reduces the amount that is taken into account as emoluments, before any deductions are given.

5.243 We have not identified any policy reason why such relief is given in this way rather than by allowing a deduction in charging the earnings to tax.

5.244 We therefore propose to rewrite the relief as a deduction. This will affect the order, but not the result, of the calculation for testing whether the employee has earnings of more than £8,500 per annum for the purposes of section 167. We will make any appropriate changes to clause 4.13.3 when it is next re-published. This is a proposed rewrite change to the law and policy. It will not affect anyone's liability to income tax. **We welcome views on this proposed rewrite change.**

Excluded expenses: accommodation expenses of MPs etc.

Clause 4.17.22 Exclusion of accommodation expenses of MPs and other representatives

5.245 This clause rewrites section 198(4). This prevents MPs and other representatives from obtaining a deduction from earnings for residential or overnight accommodation. Section 198(4) is the counterpart to provisions contained in sections 200 and 200ZA, which are rewritten at clauses 4.35.3 and 4.35.4. Those clauses provide that allowances for residential or overnight accommodation are exempt from income tax on earnings from an employment. This clause therefore provides that no deduction is allowed for the accommodation expenses in respect of which the allowances are paid.

5.246 Section 198(4) provides that no deduction shall be made "under this section". But subsection (1) of this clause provides that no deduction from earnings is allowed "under this Chapter". We think this is less confusing for the reader than listing all the provisions that rewrite section 198 and the sections construed with it or operating through it. We have considered whether we have changed the effect of the present legislation. A change could arise in either of two ways–

- Chapter 4.17 includes material that has no connection with the present section 198, so this clause may operate to disallow a deduction that ought not to be disallowed.
- Material that is to be construed with section 198 has been rewritten elsewhere than in Chapter 4.17, so this clause may not operate to disallow a deduction that ought to be disallowed.

5.247 On the first point, we do not believe that, in practice, this clause will operate to disallow any deduction that is currently allowable.

5.248 On the second point, section 195(7), which has to be construed with section 198 (see section 195(11)), has now been rewritten at clause 4.20.5. There is an argument that a deduction under this provision, which was previously disqualified, is now allowable. However, we think it highly unlikely that clause 4.20.5 and this clause will ever both be applicable to any one case.

5.249 This is a change to the law but not to policy. We do not believe that it will have any effect upon the way in which this provision applies, so it will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Chapter 4.18 – Deductions from benefits code earnings

5.250 The clauses in this chapter allow deductions where goods or services are provided, which are within the scope of the benefits code and deductions would have been allowed if the goods or services had been paid for by the employee. They rewrite sections 141(3), 142(2), 145(3) and 156(8).

5.251 These provisions were previously dealt with in Exposure Draft No 6 as clauses 4.6.17, 4.7.17 and 4.12.7. We have now brought them together and put them alongside all the other deductions clauses. We have also changed them so that they work in the same way as those clauses.

5.252 In the current legislation these deductions are limited by being deductible only from the income brought into charge by the section. For example the deduction under section 141(3) is made against the amount taxable under section 141(1).

5.253 That does not fit very well with the general approach for deductions. Under clauses 4.16.2 and 4.16.3, deductions are normally allowed from any earnings from the relevant employment, but total deductions may not exceed those earnings.

5.254 We have not therefore limited these deductions so that they may only be made from the corresponding income brought into charge. Instead, we have limited **the amount** of the deduction. That fits better with our overall limit on deductions. As long as the amount of the deduction is limited in this way it will produce the same result.

5.255 Limiting the amount of these deductions is a change to the law and policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.256 Each of the provisions rewritten here refers to amounts that would have been deductible under specific provisions. In clauses 4.18.2 to 4.18.4 we have referred to amounts that would have been deductible under Chapter 4.17, deductions for employee's expenses. We think it is easier for the reader than listing all the specific provisions, especially as different deductions provisions are mentioned in the original provisions rewritten in this chapter. In theory, this general reference goes wider than the current legislation. In practice, however, we believe it will make no difference.

5.257 This is a change to the law but not to policy. We do not think it will affect anyone's liability to income tax, but if it did so it would be in the taxpayer's favour. **We welcome comments on this proposed rewrite change.**

Introductory

Clause 4.18.1 Scope of this Chapter: costs of benefits deductible as if paid by employee

5.258 This introductory clause sets out the general proposition for a deduction to be allowed under this chapter. A person's earnings must include an amount treated as earnings under the relevant parts of the benefits code and a deduction must have been allowable if he or she had paid the cost of the goods or services.

Deductions where amounts treated as earnings under the benefits code

Clause 4.18.2 Deductions where non-cash voucher or credit-token provided

5.259 This clause applies where the goods or services are provided using a non-cash voucher or a credit-token. The benefit is treated as earnings under Chapter 4.6. Since the employee is not paying for the goods or services, no deduction is allowed under the deduction provisions relating to expenses (sections 198, 201, 201AA and 332(3)).

5.260 If the employee would have been allowed a deduction under the provisions in Chapter 4.17, deductions for employee's expenses, if he or she had paid for the goods or services, a deduction is allowed under this clause.

5.261 Although the current legislation provides only for deductions to be made from the corresponding income brought into charge, we have taken a different approach. This clause allows the deduction to be made from any earnings from the employment but limits the amount of the deduction allowed.

Clause 4.18.3 Deductions where living accommodation provided

5.262 This clause applies where the benefit provided is living accommodation. The benefit is treated as earnings under provisions in Chapter 4.7. If the employee is not paying for the accommodation, there can be no deduction under the provisions relating to such expenses (sections 198 and 332(3)).

5.263 If the employee would have been allowed a deduction under any relevant provisions in Chapter 4.17, deductions for employee's expenses, if he or she had paid for the accommodation, a deduction is allowed under this clause.

5.264 Although the current legislation provides only for deductions to be made from the corresponding income brought into charge, we have taken a different approach. This clause allows the deduction to be made from any earnings from the employment but limits the amount of the deduction allowed.

5.265 When this clause appeared in Exposure Draft No 6 as clause 4.7.17, it included a proposed rewrite change. Section 145(3) allows a deduction for the amount that would have been deductible if the accommodation had been paid for by the employee out of emoluments. The amount of the deduction is then limited because it is deductible only from the income brought into charge. But the legislation does not explicitly prevent deductions being based on the commercial rent. Clause 4.7.17 allowed a deduction for an amount equal to the cash equivalent of the benefit provided. This clearly prevents deductions being based on the commercial rent where the cash equivalent is obviously lower and accords with current practice.

5.266 People who commented on the proposed change were in favour and no one objected. We have retained the change in this new version of the provision. It is a change to the law but not to policy. We believe it will not affect anyone's liability to income tax. **We welcome any further comments on this proposed rewrite change.**

Clause 4.18.4 Deductions where benefits taxable under Chapter 4.12 provided

5.267 This clause applies where an unspecified benefit is provided. The benefit is treated as earnings under Chapter 4.12. But the employee is clearly not paying for the goods or services, so no deduction is allowed under the provisions relating to expenses (sections 198, 201, 201AA and 332(3)).

5.268 If the employee would have been allowed a deduction under any relevant provisions in Chapter 4.17, deductions for employee's expenses, if he or she had paid for the benefit, a deduction is allowed under this clause.

5.269 Although the current legislation provides only for deductions to be made from the corresponding income brought into charge, we have taken a different approach. This clause allows the deduction to be made from any earnings from the employment but limits the amount of the deduction allowed.

5.270 The limit on the deduction is either the amount treated as earnings or the amount that would have been deductible had the employee paid the cost of the benefit, whichever is less. These amounts will usually be the same, but if the employee makes good an amount to the provider of the benefit, the cost of the benefit which would be deductible (if the employee paid it) is greater than the amount treated as earnings.

Chapter 4.19 Fixed allowances for employee's expenses

Introductory

Clause 4.19.1 Scope of this Chapter: amounts fixed by Treasury

5.271 This clause introduces the two following clauses which allow deductions for amounts fixed by the Treasury.

Fixed sum deductions

Clause 4.19.2 Fixed sum deductions for repairing and maintaining work equipment

5.272 This clause enacts Extra-Statutory Concession A1 (flat rate allowances for cost of tools and special clothing).

5.273 The concession reflects the long-standing practice under which employees who bear the cost of maintaining tools and special clothing are entitled to a fixed sum deduction negotiated with the unions concerned. This avoids the negotiation of large numbers of individual deductions.

5.274 The enactment of this concession is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposals to legislate this extra-statutory concession.**

5.275 Under subsections (1) and (2) the Treasury may set a fixed sum for deduction where it is the custom for employees to bear the costs of all or part of the maintenance of tools and special clothing ("work equipment" at subsection (5)) and the costs would be deductible under clause 4.17.3, deductions for expenses: the basic rule. The Inland Revenue recommends to the Treasury the sums to be fixed.

5.276 Under subsection (3) the full fixed sum deduction is only available if the employee is obliged to meet the relevant costs in full.

5.277 Under subsection (4) the fixed sum deduction is reduced where the employer meets part of the costs that the fixed sum deduction is intended to cover. The amount of the reduction is the cost met by the employer.

5.278 An employee can still, under the general deduction rule in clause 4.17.3, deduct the actual amount spent if it is greater than the fixed rate allowance (or, should the employee so choose, a smaller sum). But two deductions for the same expense are disallowed under the general provision to prevent double deductions. Subsection (6) cross-refers to the appropriate provision (clause 4.16.5(2)).

Clause 4.19.3 Fixed sum deductions from earnings payable out of public revenue

5.279 A deduction in respect of expenses is normally allowed by section 198. This clause rewrites section 199 under which a fixed sum, set by the Treasury, is allowed as a deduction for persons paid out of the public revenue instead of the amount of expenses incurred. Many of these might prefer to opt for the fixed sum allowances

rather than having the burden of having to keep track of expenses and retain receipts etc.

5.280 Only those for whom a fixed sum allowance is agreed are entitled to a deduction under this section. They may still choose instead to have a deduction under provisions in Chapters 4.16 to 4.18, if that would allow a larger deduction than the fixed sum.

5.281 In clause 4.16.5(2) we have a provision which prevents double deductions, so we have not rewritten this aspect of section 199 in this clause. Consequently, the employee may instead have a deduction under clause 4.17.1 even if that would allow a **smaller** deduction than the fixed sum. We seek comments on this proposed rewrite change in the commentary to clause 4.16.5 at paragraph 5.126 on page 48.

Chapter 4.20 – Deductions for earnings representing benefits or reimbursed expenses

5.282 This chapter deals with cases where the employer, or a third party, bears the cost of something that is taken into account as part of the employee's earnings, but the employee is entitled to a deduction from those earnings. The effect of the deduction is therefore similar to an exemption for the amount in question.

5.283 This chapter does not deal with a deduction for expenses incurred and paid by the employee without any reimbursement. That kind of deduction is covered in Chapter 4.17.

5.284 As in Chapter 4.17, we have grouped the clauses according to the type of expense involved. For example, clauses 4.20.2 to 4.20.4 deal with travel expenses where the duties of the employment are performed abroad.

5.285 The amounts which form part of the employee's chargeable earnings may take a number of forms. For example, they may take the form of:

- cash reimbursement;
- cash equivalents for the provision of non-cash vouchers or the use of credit-tokens; or
- cash equivalents of benefits-in-kind.

5.286 In addition, the costs or expenses actually incurred by the employer or third party in the relevant tax year may bear no relation to the amount which is chargeable as part of the employee's earnings, particularly in the case of benefits in kind. "Costs" or "expenses" are therefore perhaps slightly misleading terms for the amounts in such cases. A deduction under these provisions may only be made where the benefit provided or expense reimbursed is chargeable as part of the employee's earnings and the amount of the deduction is limited to the amount so charged. We have therefore used the term "the included amount" to cover all possible forms of chargeable provision.

5.287 This change in terminology is also discussed in paragraphs 5.34 and 5.35 in the introductory commentary on the clauses.

5.288 A common thread throughout the provisions rewritten in this chapter is that the amounts included in the employee's earnings are expressed in terms of provision "by or on behalf of the employer" or similar.

5.289 In each case, we have been unable to establish the original policy reasons for limiting the scope of the relief to provision by or on behalf of the employer. There may be circumstances where the provision is by or on behalf of someone other than the employer and the amount is still chargeable as part of the employee's earnings.

5.290 As long as all the other conditions for the deductions are satisfied, we can see no reason why they should exclude provision by persons other than the employer or someone on his behalf. We therefore propose to omit the references to "by or on behalf of the employer". This is a change to the law and policy. If there is any tax effect, it will be in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Introductory

Clause 4.20.1 Scope of this Chapter: earnings representing benefits or reimbursed expenses

5.291 This is an introductory clause. It sets out the general proposition that for a deduction to be allowed under this chapter an amount has to be included in the earnings of the employee either because a particular benefit has been provided or because a particular expense has been reimbursed. Here, and throughout the chapter, the amount included in the employee's earnings is referred to as "the included amount".

5.292 Including this proposition here saves us having to say something to the same effect in each of the individual deduction provisions in the chapter.

5.293 There is some overlap between this chapter and Chapter 4.18, which deals with deductions from benefit code earnings for costs which would have been deductible if they had been paid by the employee. We have therefore included a signpost to Chapter 4.18.

Travel costs and expenses where duties performed abroad

5.294 The next three clauses rewrite section 194 which provides deductions for what are currently described as "foreign travel expenses". We have separated out into three clauses the rules which apply to the expenses of the employee's own travel, those which apply to the travel expenses of employee's family and the special rules for deciding where seafarers' duties are performed.

5.295 The proposition contained in section 194(9), which prevents a double deduction in respect of the same costs or expenses, now appears in clause 4.16.5(1).

Clause 4.20.2 Travel costs and expenses where duties performed abroad: employee's travel

5.296 This clause sets out the rules for the deduction of travel costs of the employee.

5.297 Subsection (3) rewrites the deduction provided by section 194(5) and (6). This covers the travel costs of return visits to the United Kingdom of an employee who is working abroad for extended periods. It applies to both employments where only a part of the duties are performed abroad and to those where all of the duties are performed

abroad, as long as they do not give rise to foreign emoluments as defined section 192(2).

5.298 Subsection (4) rewrites the deduction provided by section 194(3) and (4). This only covers the situation where part of the duties of an employment are performed abroad. The deduction is in respect of the travel costs for the journey from the United Kingdom to the place abroad where the employment is performed and for the return journey.

5.299 At first sight, and apart from the fact that the journeys are in reverse, there seems to be an overlap between the deductions provided by section 194(3) and (4) and 194(5) and (6) in respect of employments where the duties are performed partly abroad.

5.300 This overlap was recognised when these provisions were introduced in 1977. The provisions now in section 194(3) and (4) were intended to make clear that a deduction was also allowed for the cost of travel to the point of departure from the United Kingdom (eg the airport or port) as well as the cost of the onward fare.

5.301 This provision also extended relief to cover the cost of any such journeys starting from a place other than the employee's normal workplace, for example, a journey commenced from the employee's home or from a place where the employee was on holiday.

5.302 A double deduction was prevented by section 194(9) which we have rewritten as part of clause 4.16.5(1).

5.303 The rules for a deduction under section 194(3) and (4) work differently where duties are performed on a vessel. We have set out the deduction as it applies where the duties are not performed on a vessel in subsection (4) of this clause, and have set out the deduction as it applies where duties are performed on a vessel in subsection (5). Please also see clause 4.20.4.

Clause 4.20.3 Travel costs and expenses where duties performed abroad: visiting spouse's or child's travel

5.304 This clause sets out the rules of the deduction for the travel costs of members of an employee's family.

Clause 4.20.4 Where seafarers' duties are performed

5.305 This clause rewrites section 194(7) which modifies the rule in section 132(4)(b) (rewritten as clause 4.50.15(2) in Exposure Draft No 6) for determining the place where a seafarer's duties are treated as being performed. This modified rule applies for deductions under both clauses 4.20.2 and 4.20.3.

Travel costs and expenses of non-domiciled employees where duties performed in UK

5.306 The next three clauses rewrite section 195(1) to (10) which provides deductions for travel expenses of employees who are not domiciled in the United Kingdom.

5.307 We have not rewritten section 195(13) as it is spent. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.20.5 Non-domiciled employee's travel costs and expenses where duties performed in UK

5.308 In subsection (3), we have updated "usual place of abode" to "the country outside the United Kingdom in which the employee normally lives".

5.309 Subsection (6) contains a new definition of "remittance earnings" to describe emoluments which are currently chargeable under Case III of Schedule E. In Exposure Draft No 6 these are earnings chargeable under clauses 4.50.3 and 4.50.5(3).

Clause 4.20.6 Non-domiciled employee's spouse's or child's travel costs and expenses where duties performed in UK

5.310 This clause sets out the rules of the deduction for the travel costs of members of an employee's family.

5.311 Again, as in clause 4.20.4, we have replaced the words "usual place of abode" with "the country outside the United Kingdom in which the employee normally lives" in subsection (3).

Clause 4.20.7 Date of arrival condition

5.312 This clause sets out the rules for calculating the start and end of the five year qualifying period for which the deductions under clauses 4.20.5 and 4.20.6 are allowed.

5.313 Currently, the deductions are available for five years beginning with a qualifying arrival date. However, the current legislation is opaque as to when the qualifying period ends because it is stated in terms of the section "applying" for five years from when the employee arrives in the United Kingdom to take up the employment. For example, the employee might make a journey at the four years and 11 month date, but the costs might not in fact be "paid" by the employer until after the expiry of the five-year qualifying period. It is not clear in such as case whether or not the section "applies" because the journey takes place during the five-year period but the costs are paid after it has ended.

5.314 Consequently, in order to try and make the rules for the end of the five-year period clearer, we have, in subsection (1) incorporated the Inland Revenue practice –

published in SE35060 – of looking at the date when the journey was undertaken, rather than at the date when the expenditure was incurred.

5.315 This is a change to the law but not to policy. As it simply follows an existing practice, we believe it will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.316 In some circumstances the conditions in section 195(3) and (4) may be satisfied more than once in respect of the same employment or the individual may come to the United Kingdom to carry on the duties of more than one employment. Consequently, there may be a number of qualifying arrival dates and the relief may extend to more than one employment.

5.317 Section 195(1) sets out the sort of employments to which it applies and it is clear from section 195(6) that the person may have more than one such employment. We therefore think that the reference in section 192(2) (the five-year rule) to the date of "the employment" is unclear. In subsection (2)(2) of this clause we have expanded the reference so as to refer to any employment to which the section applies.

Foreign accommodation and subsistence costs and expenses

Clause 4.20.8 Foreign accommodation and subsistence costs and expenses (overseas employments)

5.318 This clause rewrites the rules in section 193(4) which allow a deduction for the provision of board and lodging while an employee is working abroad.

5.319 The decision to drop the label "foreign emoluments" and instead to focus on whether the employee of a "foreign employer" is domiciled in the United Kingdom is discussed in paragraphs 5.36 to 5.41 in the introductory commentary to the clauses at page 32.

5.320 We found that "board and lodging" has a variety of definitions in dictionaries, but usually means the provision of **both** board and lodging. The original intention was to provide a deduction from amounts included in the employee's earnings for the cost of accommodation (including living accommodation for the purposes of sections 145 and 146 – Chapter 4.7 in Exposure Draft No 6) and meals. We think that "accommodation and subsistence" (in the title of this clause) is a more accurate reflection of the subject of the deduction. It is not necessary for both elements to be present for the deduction to be available.

5.321 This provision was partly rewritten in Exposure Draft No 6 as clause 4.7.17(2) and (3) so far as it provided a deduction against amounts chargeable under that Chapter. Now that the whole of section 193(4) has been rewritten here, clause 4.7.17 will be dropped.

Personal security assets and services

Clause 4.20.9 Costs and expenses in respect of personal security assets and services

5.322 This clause rewrites sections 50 to 52 Finance Act 1989, which provide a deduction in respect of the provision of security assets and services.

5.323 In subsection (8) we have not replicated the section 52(3)(b) Finance Act 1989 reference to "living accommodation" on the basis that "dwelling" already encompasses it. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.324 Under section 52(2) Finance Act 1989 the fact that an asset or service also improves the personal physical security of any member of the employee's family or household, does not prevent a deduction being made.

5.325 The test in section 50(6) Finance Act 1989 that the whole or main benefit should be an improvement in the **employee's** personal physical security only applies to the provision of security **services.** The primary test in respect of the provision of security **assets** in section 50(7) Finance Act 1989 depends solely on the intention of the provider. Consequently, the benefit test in section 52(2) Finance Act 1989 has no relevance to the provision of security **assets**.

5.326 Subsection (7) – which rewrites section 52(2) Finance Act 1989 – therefore only refers to the provision of security services. This is a removal of unnecessary material. It should not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Chapter 4.21 – Deductions from seafarers' earnings

5.327 This chapter rewrites section 192A and Schedule 12. These provide the Foreign Earnings Deduction (FED) for seafarers against earnings chargeable under Schedule E Case I (see clause 4.50.2 in Exposure Draft No 6). This deduction, like those under Chapter 4.20, has something of the flavour of an exemption in that the amount deductible is equal to an amount of earnings rather than any costs or expenses incurred.

Clause 4.21.1 Deduction from seafarers' earnings: eligibility

5.328 This clause sets out the conditions for eligibility for the FED. Broadly speaking, seafarers must spend no less than half of a qualifying period of at least 365 days outside the United Kingdom and not more than 183 consecutive days in the United Kingdom during the qualifying period.

5.329 It is possible to combine various periods of absence from the United Kingdom to determine whether the test has been satisfied. Currently, paragraph 3 Schedule 12 deals with by using the terms "qualifying period", "relevant periods", "a single qualifying period", "the last qualifying period" and the "intervening period". We did not find these concepts and their various combinations easy to follow.

5.330 So, in subsection (2), we have referred to an "eligible period", which consists of either a period of absence from the United Kingdom or a "combined period" (as defined in subsection (3)). We believe that this is a clearer way of explaining these rules.

Clause 4.21.2 Calculating the deduction

5.331 This clause sets out the amount of the FED which may be allowed from the earnings attributable to the eligible period.

5.332 Subsection (2) rewrites the rule in paragraph 3(3) Schedule 12 about earnings for a period of leave immediately following an eligible period. That rule says that the emoluments for such a period of leave may be taken as attributable to the qualifying period, but only to the extent that this would not mean having to treat any emoluments for one tax year as belonging to a different tax year. Essentially this rule allows emoluments for a period of leave to be attributed to the qualifying period to the extent that they are emoluments for the tax year during which the qualifying period ends. We have rephrased the rule accordingly, and in terms of "earnings" and the "eligible period".

Clause 4.21.3 Limit on deduction where UK duties etc. make amount unreasonable

5.333 This clause rewrites paragraph 2 Schedule 12. This contains anti-avoidance provisions against attempts to manipulate the amount of the earnings to take advantage of the relief.

5.334 The rules in paragraph 2(3) of Schedule 12 for determining associated employments end with the words "but paragraph (b) above shall not be construed as requiring an individual to be treated in any circumstances as under the control of another person". We have been unable to establish any policy or practical purpose for

these words. We no not propose to rewrite them. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.21.4 Taking account of other deductions

5.335 This clause contains the rules for calculating the amount of the earnings for the purposes of this chapter. It is derived from paragraph 1A Schedule 12.

5.336 All the other employment income deductions are allowed against the full amount of earnings from the employment for the tax year in question. However, the FED is only allowed in respect of the earnings from the employment which are attributable to an eligible period.

5.337 This means that in some circumstances only a part of a seafarer's earnings for a year may be eligible for the FED. If the FED was computed and allowed by reference to the gross earnings for the eligible period, this would displace any other employment income deductions, with the effect that those other deductions, which were for a full year, would be allowed against the earnings for only part of the year.

5.338 To prevent this, the clause requires that the amount of the earnings for the eligible period is to be computed by first deducting all of the employment income deductions and any capital allowances from the gross earnings of the employment for the year. The net product of this calculation is then apportioned to find the earnings for both the eligible and non-eligible periods.

5.339 Paragraph 1A of Schedule 12 lists the deductions which are to be taken into account in determining the earnings for the purposes of the FED. However, this list is not complete. For example, it does not refer to deductions under sections 201AA, 201A or 202, or under sections 50 to 52 Finance Act 1989.

5.340 This appears to be unintended. In practice, all the other employment income deductions and capital allowances are taken into account when calculating the earnings eligible for the FED.

5.341 Accordingly, we have extended the list to include all those which may be made under Chapters 4.17 to 4.20. This is a change to the law but not to policy. It is theoretically in favour of the Inland Revenue although, as it follows an existing practice, it will not in reality affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.342 Subsection (2) lists other deductions to be made in calculating earnings for the purposes of FED which we do not currently plan to rewrite in this Part. As our work progresses we will consider whether there are any other deductions which should be included in this list – for example under section 619(1), qualifying premiums or section 639, member's contributions to approved personal pension arrangements.

Clause 4.21.5 Duties on board ship

5.343 This clause determines whether duties performed on particular voyages are regarded as having been performed in or outside the United Kingdom. It is derived from paragraph 5 Schedule 12.

5.344 This modifies the rules in section 132(4)(b), rewritten in Exposure Draft No 6 as clause 4.50.15, but only for the specific purpose of identifying the duties and earnings which are eligible for the FED. For all other purposes, the rules in clause 4.50.15 are unaffected by this clause.

Clause 4.21.6 Place of performance of incidental duties

5.345 This clause sets out the rules, which apply only to the FED, regarding the performance of duties which are incidental to the main duties of the employment. Subsection (1) is derived from paragraph 6 of Schedule 12 and determines the place of performance where the main duties are performed in the United Kingdom.

5.346 Under section 132(2), if the duties of an employment are mainly performed outside the United Kingdom, any duties incidental to those performed in the United Kingdom are treated as being performed outside the United Kingdom. However, this rule does not apply when deciding whether or not a seafarer is absent from the United Kingdom to determine entitlement to FED. This exception to the section 132(2) rule is currently in section 132(3) and rewritten in subsection (2) of this clause.

5.347 This rule was originally rewritten in Exposure Draft No 6 as clause 4.50.14(2). However, as it is only relevant to the FED, we now think it is better to include it in Chapter 4.21.

Clause 4.21.7 Meaning of employment "as a seafarer"

5.348 This clause defines what this means.

Clause 4.21.8 Meaning of "ship"

5.349 "Ship" takes its everyday meaning, subject to the exception in respect of an "offshore installation" as defined by the Mineral Workings (Offshore Installations) Act 1971.

Chapter 4.22 – Other employment income: payments to non-approved pension schemes

Introduction

5.350 This chapter sets out the charge to tax, currently in section 595, on an employee whose employer makes payments to non-approved pension schemes. It is one of the free-standing Schedule E charges covered by paragraph 5 of section 19(1).

5.351 Chapter 4.23 deals with another such free-standing charge – section 148.

5.352 The charges under section 595(1) and 148(1) are both expressed in terms of being "tail-end batsmen" in relation to the employment income charge. That is:

- section 595(1) - "if not otherwise chargeable to income tax as income of the employee…" and;
- section 148(1) - "payments and other benefits not otherwise chargeable to tax…".

5.353 We did not find an explicit "tie-breaker" in the legislation.

5.354 In an effort to make all this clearer, we considered the basis of the charges under sections 595 and 148 from first principles. The key points which helped us reach a conclusion are as follows.

5.355 First, the charge under section 595 is intended to catch any payments which are not otherwise chargeable to tax as income. Therefore, the charge does not depend on the payment being "for" or "by reason of the employment". In other words, the payment has only to be "with a view to the provision of any relevant benefits…" under a non-approved retirement benefit scheme for it to be chargeable. Therefore it bites on payments which escape a charge as emoluments.

5.356 Secondly, the definition of "an employee" in section 612(1) extends to past and future employees, including directors. To that extent section 595 "sweeps up" any amounts which are not chargeable as emoluments.

5.357 Thirdly, the charge under section 148 can cover payments which might also be within the section 595 charge, where the amounts are connected either with a significant change in the terms or conditions of an employment or its termination.

5.358 Fourthly, the charge under section 148 can apply to capital payments which escape a charge to tax as emoluments under section 19(1) paragraph 1. In other words, section 148 can catch amounts which would never have been chargeable either as emoluments or under section 595.

5.359 That seemed the decisive factor in concluding that, in terms of employment income, the charge under section 595 takes priority over section 148.

5.360 We have acted on this conclusion in two ways. First, we have rewritten section 148 as Chapter 4.23 to reflect the fact that the section 595 charge has priority.

5.361 Secondly, we have tried to make the order of priority clear in clause 4.22.1(3). We could not express the relationship in terms of amounts being chargeable because the first £30,000 of any amounts falling through to Chapter 4.23 are not charged to tax. Instead, we have focused on "on a payment to which Chapter 4.23 would apply". The introduction of this "order of priority" clause is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change and on the proposed ordering of these provisions.**

Clause 4.22.1 Payments into non-approved retirement benefits schemes treated as employment income

5.362 This clause sets out the charge to tax, currently in section 595(1), on an employee where the employer makes certain payments to non-approved pension ("retirement benefits") schemes. It is a free-standing charge to tax and the charging rules are set out in section 595. In terms of the rewritten employment income rules the charge is on "other amounts charged to tax as employment income" in clause 4.1.1(2)(b).

5.363 Subsection (3) is new and is discussed in paragraph 5.355.

5.364 The other provisions in Chapter I Part XIV ICTA are not exclusively relevant to employment income and will be rewritten at a later stage. Therefore, subsection (4) applies the definitions of "employee" and "director" which are in section 612(1).

5.365 Section 595(1)(b) provides relief where the payment by the employer is made under an insurance or contract covered by section 266 and which is not otherwise allowable. As the relief is given under section 266, we have not rewritten section 595(1)(b) here. It will either not be repealed or section 266 will be amended to give effect to it.

Clause 4.22.2 Meaning of "non-approved retirement benefits scheme"

5.366 This clause defines such a scheme.

Clause 4.22.3 Apportionment of payments in respect of more than one employee

5.367 Where a single payment is made to a non-approved scheme in respect of more than one employee, it is apportioned between the employees. Each is taxed only on an appropriate share of the payment.

5.368 In subsection (2) we have dealt with such apportionments by the use of a formula. **Do people find this helpful?**

Clause 4.22.4 Exception: employment where earnings charged on remittance

5.369 This clause provides an exception from the charge where the employee's earnings are chargeable under what is currently Case III of Schedule E. That charge is dealt with in clauses 4.50.3 and 4.50.5(3) in Exposure Draft No 6.

Clause 4.22.5 Exception: non-domiciled employees with foreign employers

5.370 This clause provides a further exception from the charge under clause 4.22.1. This is where the earnings are (in current terms) "foreign emoluments" and the payment is to a retirement benefits scheme which corresponds to approved or relevant statutory schemes etc. As explained in paragraphs 5.36 to 5.41 we have dropped the term "foreign emoluments", instead setting out the relevant circumstances in each case, and we have followed that approach here.

Clause 4.22.6 Exception: seafarers with overseas earnings

5.371 This clause legislates the Inland Revenue's practice (set out in SE15050) of excepting payments from the charge under section 595, rewritten as clause 4.22.1, when they are made to seafarers who have no net chargeable earnings from the employment in question for the year as a result of the foreign earnings deduction which is rewritten in Chapter 4.21.

5.372 Legislating this practice is a change to the law, but not to policy. It is in the taxpayer's favour. **We welcome views on this proposed rewrite change.**

Clause 4.22.7 Relief where no benefits paid or payable

5.373 This clause rewrites those parts of section 596 that allow an application for relief where the relevant benefits are not subsequently received from the scheme.

5.374 At present, the legislation provides for an application for relief only from the employee. However, some benefits might not be due until after the employee has died. In practice the Inland Revenue have always accepted applications by the employee's personal representatives.

5.375 We now propose to legislate that practice in subsection (1). This is a change to the law but not to policy. It is in the taxpayer's favour. **We welcome comments on this proposed rewrite change.**

5.376 We have taken it that section 595(5), which extends (for section 595) the meaning of provision for an employee of relevant benefits to include provision for dependants etc was also intended to apply to section 596.

Chapter 4.23 – Other employment income: payments and benefits on termination of employment

5.377 This chapter contains another of the free-standing Schedule E charges covered by paragraph 5 of section 19(1). It brings together section 148 and Schedule 11. Combining these has enabled some restructuring and useful pruning. **We welcome comments on the structure we have used.**

5.378 We have not yet rewritten the reporting requirements at paragraph 15 Schedule 11 as they belong with section 203(2). We will pick these up in rewriting the enabling provisions for the PAYE regulations.

5.379 We have not rewritten section 148(5) as it does not say anything substantive. We believe this removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Termination payments and benefits treated as employment income

Clause 4.23.1 Termination payments and benefits treated as employment income

5.380 This clause contains the charge to tax on termination payments and benefits where they exceed the £30,000 threshold. Subsection (1) sets out the basis of the charge and the threshold. The charge under section 148 is not subject to the Cases of Schedule E, it is an free-standing charge and the charging rules are set out within the section. The charge is on "other amounts charged to tax as employment income" in clause 4.1.1(2)(b).

5.381 Clause 4.23.1(2) indicates the scope of the charge.

5.382 The use of "relative" in subsection (2) in conjunction with the use of "spouse" is taken by the Inland Revenue to mean blood relatives only, and thus to exclude relatives by marriage. Elsewhere in Part 4 "relative" is defined to include both spouses and blood relatives, for example see clause 4.9.20 in Exposure Draft No 6. We have not introduced another definition here to avoid confusion. **We would welcome comments as to whether "relative" should be defined in this chapter.**

5.383 Subsection (3) brings within the scope of the potential charge a payment or benefit which the employee or former employee diverts elsewhere. It treats them as received by the employee or former employee.

5.384 The meaning of the word "benefit" in this chapter is much wider than "benefits" in the benefits code (see Chapters 4.4 to 4.13 in Exposure Draft No 6). It excludes the right to receive benefits in the future. This exclusion is currently in section 148(3). We have moved it to the clause which defines benefits, because the right to receive something is a benefit not a payment.

5.385 In section 148(3) the exclusion is "for this purpose" which relates to the charge for the year of receipt. We have not confined the proposition in this way, but have

made it chapter-wide by putting it into the definition of benefit. This is a change to the law and policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.386 Throughout the Chapter references to "emoluments" have been changed to "earnings" where this is appropriate. This follows Exposure Draft No 6. In the terms of clause 4.1.1, this brings in all amounts which would be within clause 4.1.1(3). This is the case even if there is an exemption which would otherwise apply to the benefit in question. Any exemption which removes chargeability under the benefits code in Exposure Draft No 6, or chargeability as an emolument under clause 4.1.1(3)(a), is ignored and the value of the benefit will form part of the total receipts in this chapter. There is, however, an ambiguity regarding a small number of exemptions which we have not been able to resolve in relation to clause 4.23.1(4)(a)(ii). For these, the exemption is expressed "shall not be regarded as emoluments of the office or employment for any purpose of Schedule E". Clause 4.43.2 states this exemption and lists the rewritten sections in which those words are used. The commentary on that section sets out the problem in relation to the free-standing charges such as this. It is not clear whether the benefits exempted by these provisions are to be included in the charge under Chapter 4.23, or the words "for any purpose of Schedule E" exclude them. We are still working on this, and hope to be able to make the position clear in the Employment Income Bill. In the meantime we have preserved the ambiguity.

Clause 4.23.2 Charge to tax in year of receipt

5.387 This clause sets out the rules for the timing of the charge to tax. The rules are similar to the receipts basis for earnings. In cases where payments are made over a period of time, or benefits are provided for some time after the employment has terminated, once the £30,000 threshold has been exceeded, there will be continuing liability as long as payments continue to be made or benefits provided.

5.388 The fact that payments may be made or benefits provided over a considerable period inevitably raises the question of residence status for a year of assessment in which such payments or benefits are received. As the charge is independent of the residence status rules which apply to earnings, tax is chargeable on amounts over the £30,00 threshold even if the employee or former employee is neither resident nor ordinarily resident in the United Kingdom. We considered whether we should make this plain in this chapter. But we decided that such matters are best left to case law or the part of the rewrite which deals with residence issues. **We welcome comments on our decision in this case.**

Clause 4.23.3 The person chargeable

5.389 This clause sets out who is chargeable to tax. Subsection (1) emphasises the fact that it does not matter who receives the payments or benefits, it is the employee or former employee who is chargeable.

5.390 Subsection (2) then deals with the case where the employee has died, and payments and benefits are received after death. In such a case, where tax is chargeable because of the termination of, or change in, employment there is no charge to tax until

the amount is paid or due, or at the end of the year in which the benefit is used. The persons chargeable in that case are the personal representatives and the tax is due and payable from the estate. If payments or benefits are made to any of the persons in clause 4.23.1(2) or (3) there could be a continuing liability for the estate.

Clause 4.23.4 How the £30,000 threshold applies

5.391 This clause deals with two aspects of the £30,000 threshold. The first concerns the payments and other benefits that are to be aggregated. The second concerns the way the £30,000 is to be allocated between payments and benefits received at different times. We have rearranged paragraphs 7 and 8 of Schedule 11 to reflect this. Subsections (1) to (3) deal with the first aspect, and subsections (4) and (5) relate to the second. **We welcome comments of whether this rearrangement makes it easier to follow.**

5.392 Subsection (1)(c) sets out the circumstances in which the payments and benefits from more than one employer are aggregated. Only one sum of £30,000 is available in respect of an employment, different employments with the same employer and employments with employers who are associated.

5.393 It is only necessary to consider whether employers are associated if there is more than one event producing a potential charge under this chapter. If that happens it is necessary to look at the time of each event to see whether the payments and benefits need to be aggregated.

Example

5.394 Employers A, B and C are all controlled by D successively. An employee receives payments for a change in or termination of employment from employer A on 1 January 2000, and from employer C on 1 January 2010

- on 1 January 2000 D controls both A and B (but not C)
- on 1 January 2010 D controls B and C (but not A).

As D controlled A on the first date, and controlled C on the second date, the employers are associated and the employments are treated as if they were with the same employer. If any of the £30,000 is unused after the 1 January 2000 event the balance is available against the amount for the 1 January 2010 event. If it has all been used, the whole of the second event amount is chargeable. It is therefore possible for someone to be caught by this legislation even though they had no idea that a later employer had any connection with the employer who made a payment to which this chapter applies. That is an unfortunate consequence of these anti-avoidance rules the purpose of which are to prevent an employee obtaining a series of payments and benefits from connected companies, which they may control or influence.

5.395 Subsection (3) sets out the meaning of "control" for the purposes of this clause. It rewrites paragraph 8(2) Schedule 11. The meaning of control for this purpose is the

same as in section 840. This is further extended by subsection (3)(b), which treats the successors to the employer or the person looked at to determine control as if they were the original employer or person. Successors are not defined anywhere in the Tax Acts so the normal meaning applies, being someone who takes the place of another person to perform a like role and duties.

Exceptions

Clause 4.23.5 Exception for death or disability payments and benefits

5.396 Having set out the basis of the charge in clauses 4.23.1 to 4.23.4 we set out the exceptions to the charge in clauses 4.23.5 to 4.23.10.

5.397 This clause provides an exception where the payment or benefit is due to death, injury or disability.

Clause 4.23.6 Exception for payments and benefits under tax-exempt pension schemes

5.398 This clause provides an exception where the payment is made or benefit provided through certain pension schemes and is due to a change in or termination of employment owing to ill-health.

5.399 The payment or benefit referred to in subsection (1)(b) is a commutation calculated by reference to past service. This is exempt from tax by virtue of the provisions dealing with exempt pension schemes. It is therefore necessary to preserve the exemption.

5.400 The current legislation refers to "any such scheme or fund … as is described in section 596(1). In subsection (2)(a) we have specified these schemes as we believe this will help users. **We welcome comments on whether this is helpful.**

Clause 4.23.7 Exception for employee liabilities indemnity insurance payments and benefits

5.401 This clause does not derive from section 148 and Schedule 11 but from section 92(10) Finance Act 1995. As it is the only case in which an exception is located separately from the charging provisions we thought it should be brought in so that all the exceptions are together. **We welcome comments on whether it is appropriate to make this addition.**

5.402 Section 92 Finance Act 1995 allows for a deduction from total income of a former employee for the cost of a premium for insurance against claims which might be made as a result of the period of employment, so long as the former employee personally bears that cost.

5.403 Where payments or benefits for a change in or termination of employment include cash or non-cash benefits intended to provide the indemnity insurance, the amount which would otherwise be chargeable is excepted from the charge under

section 148. This covers the situation where the former employee does not personally bear the cost of the premium, but would have been entitled to a section 92 deduction if he did so.

5.404 The exception in this clause includes both the case where the personal representatives are the recipients of the benefit and the case where the personal representatives bear the cost of a premium.

5.405 In this clause we have changed the references to executors and administrators, and used the term "personal representatives" instead. This term is defined in clause 4.48.2. We invite comment on the proposed rewrite change involved in paragraph 5.793 of the commentary on that clause. This brings the provision into line with the rest of this chapter, since "personal representatives" is the expression used in paragraphs 2(1) and 14(2) of Schedule 11 and it follows the line taken in previous Exposure Drafts.

Clause 4.23.8 Exception for certain payments and benefits for forces

5.406 This clause provides an exception for certain payments and benefits for members of the armed forces. It is derived from paragraph 5 Schedule 11.

Clause 4.23.9 Exception for certain payments and benefits provided by foreign governments etc.

5.407 This clause provides an exception which is limited to those employed by foreign governments and to particular circumstances. In some cases the employment may have been within clause 4.50.7 (in Exposure Draft No 6) by virtue of clause 4.50.6(b) and not excepted by subsections (5) and (6) of that clause. The employment would not then come within the "foreign service" exception at clause 4.23.10.

Clause 4.23.10 Exception in certain cases of foreign service

5.408 This clause provides an exception for payments made in certain cases of "foreign service". The exception depends on the length of the foreign service up to the date of the termination of or change in employment, compared with the whole period of service.

5.409 As the period involved exceeds 20 years it is necessary to define "foreign service" in a number of different ways because of the changes in the Schedule E charge over that period. We deal first (in subsection (2)(a)) with the period in which the rewritten legislation will have effect. Then (in subsection (2)(b)) we deal with the period in which the "foreign earnings deduction" (in sections 192A or 193(1)) is applicable. Finally (in subsection (2)(c)) we deal with the period before the foreign earnings deduction became available and before the Cases of Schedule E were introduced.

Clause 4.23.11 Reduction in certain cases of foreign service

5.410 The exception for foreign service in clause 4.23.10 may not apply because the length of service is insufficient. If so, the amount charged to tax may be reduced under

this clause, which is derived from paragraphs 9 and 11 Schedule 11. The amount of the reduction depends on the length of foreign service compared with the total length of service.

5.411 The reduction is applied to the amount which remains above the £30,000 threshold.

5.412 There is, however, a limitation to the reduction. This is intended to ensure that where tax is deducted from a payment – for example a gift aid payment – enough tax remains in charge to satisfy the tax on the payment. Subsection (4) provides that any personal reliefs and the reduction added together must not bring the income of the person chargeable to tax below an amount which would ensure that tax payable is equal to the tax on the gift aid payment.

5.413 In rewriting the limitation of the relief at paragraph 11(3) Schedule 11 we found a technical error. The limit on the relief applies where it would "reduce the amount of **income** on which he is chargeable below the amount of **income tax** which he is entitled" to charge or deduct. The intention was as set out in paragraph 5.412 above. We have corrected this. It is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

General and supplementary provisions

Clause 4.23.12 Valuation of benefits

5.414 This clause sets out how to value the benefits chargeable under this chapter. We have made changes to paragraph 12 Schedule 11 so that the valuation rules relate to the benefits code as set out in Exposure Draft No 6. We have also avoided, as far as possible, references to legislation that will not be within Part 4, employment income.

5.415 Paragraph 12 Schedule 11 uses the valuation provisions of section 596B. We do not intend to rewrite that section in Part 4 as we have rules for benefits in the benefits code chapters of Part 4.

5.416 We have therefore rewritten the valuation of benefits provisions in terms of the benefits code. This enables us to apply clauses 4.4.2 and 4.7.18 from Exposure Draft No 6 (relationship between emoluments and amounts treated as emoluments in the benefits code). The amount of any emoluments is considered first, and the cash equivalent under the benefits code "tops up" the emolument with the excess. The use of the benefits code is a change to the law but not to policy. We do not think it will affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.417 Sub-paragraphs (3) to (7) of this clause modify the valuation provisions used in the benefits code so that they can apply properly to work out the valuation of benefits brought into the charge to tax under this chapter.

5.418 One problem with using the benefits code occurs when the person who receives the benefit is not the employee and the recipient, "makes good". To overcome this we have introduced clause 4.23.12(4) which allows the valuation of the cash equivalent to be made by reference to the person chargeable or the recipient of the benefit. As the provisions on the calculation of the cash equivalent all provide for deduction of the amount made good this allows the deduction in all circumstances. Clause 4.23.1(3), which treats the employee as the recipient in certain circumstances, then has to be disapplied for valuation purposes. This is a change to the law and policy. We do not think it will affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.419 Other problems arise because there are references to the employer throughout the benefits code. If an employment which has ceased the employer becomes a former employer. Under subsection (5) the benefits code provisions are read with that meaning substituted.

5.420 In addition, the section 596B provisions differ in two ways from the benefits code provisions in Chapter 4.7. In clause 4.7.12 in Exposure Draft No 6 only rent paid by the employee is taken into account in calculating the cash equivalent. In section 596B(8) the whole of any amount made good by the recipient of the accommodation is taken into account. Clause 4.7.13 substitutes market value for original cost where the property was first used as provided accommodation after 31 March 1983, and an interest in it was held for more than 6 years prior to that. Section 596B(6) applies without the requirement that it was first occupied after that date. Subsections (6) and (7) allow for these small differences.

Clause 4.23.13 Notional interest treated as paid if amount charged for beneficial loan

5.421 This clause is the equivalent of clause 4.9.12,in Exposure Draft No 6, interest treated as paid, in the benefits code and is written in the same terms.

5.422 When there is a chargeable benefit under Chapter 4.9 because the interest paid on a loan is less than the official rate, the cash equivalent of the benefit is not interest paid. Tax relief would not be available even if the loan were for a qualifying purpose because interest has to be paid for the relief to be due. This clause treats the cash equivalent as if it were interest paid so that relief can be obtained, but prevents it from being treated as income of the lender. The reference in clause 4.23.13(4)(b) to section 369 is to prevent the interest from being treated as real interest paid under deduction of tax. Section 369 now only applies to interest paid on loans to purchase life annuities in certain circumstances. Clause 4.23.13(4)(b) will be reviewed when the Employment Income Bill is drafted to establish whether it can be omitted at that time.

5.423 Some or all of the cash equivalent might fall within the £30,000 threshold so that there is no amount charged, or the amount on which tax is charged is less than the amount of notional interest. If so the relief is limited to the amount which is charged.

Chapter 4.30 – Exemptions: transport, travel and subsistence

5.424 This is the first of several chapters dealing with the many exemption provisions, which apply for employment income. These are currently to be found in various places in the Tax Acts. We have collected these here, together with some extra-statutory concessions which we propose to legislate.

5.425 We have arranged the individual exemptions according to subject. We hope that this will make it easier for users to find out whether a particular kind of employment income is exempt. We have also replaced "place of work" used in some sections, for example section 155(1A) and section 197A, rewritten at 4.30.1, with "workplace". A general definition of this term is in clause 4.48.2.

5.426 This chapter deals with the exemption of certain benefits connected with travel and subsistence.

Clause 4.30.1 Parking provision and expenses

5.427 This clause brings together the provisions in sections 197A and 155(1A), which remove the charge to tax in respect of the provision of car parking, with the exemptions for motor cycle parking and facilities for parking bicycles, in section 49(2) Finance Act 1999. It only applies to parking places at the place of work.

5.428 The exemption covers the charge to tax as earnings under clause 4.1.1(3)(a), expenses treated as earnings under Chapter 4.5 and the benefits charge under Chapter 4.12. There is a corresponding exemption for parking places provided by non-cash vouchers or credit-tokens in clauses 4.33.1 and 4.33.2.

5.429 The exemption in subsection (1) is currently written as an exception from the charge under section 154. The form of the exemption in subsection (2) has been changed to exemption from income tax as earnings in place of "not… an emolument… for any purpose of Schedule E". This follows the wide-ranging proposed rewrite change discussed in paragraph 5.43 of the introductory commentary on page 33. See also the commentary on clause 4.43.2 at paragraph 5.783 on page 138.

5.430 There are definitions of "motor cycle" and "cycle" in section 49(2) Finance Act 1999. But there is no definition of "car" in sections 155(1A) or 197A. We felt that as the subject of the exemption is a parking space, definitions of what might be put in it did not add anything, so we have not reproduced them here. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome views on this proposed rewrite change.**

Clause 4.30.2 Modest private use of heavy goods vehicles

5.431 This clause rewrites the exception in section 159AC that prevents a benefit being chargeable where there is minor private use of a heavy goods vehicle.

5.432 The exemptions in section 159AC(2)(b), (3)(a) and (3)(c), dealing with expenses in connection with the vehicle, are dealt with in clause 4.30.3.

Clause 4.30.3 Payments and benefits connected with taxable cars and vans and exempt heavy goods vehicles

5.433 When an employee is chargeable to tax under the provisions in Chapter 4.8 in respect of a car or van that charge is intended to cover all the expenses in connection with the vehicle, other than the provision of a driver or fuel. This clause exempts payments from being charged to tax under clause 4.1.1(3)(a), Chapter 4.5 or Chapter 4.12. The exemptions are derived from sections 157(3) and 159AA(3).

5.434 If a heavy goods vehicle, which is not used wholly or mainly for private use, is exempted from the Chapter 4.12 charge by clause 4.30.2 it is also exempt in respect of expenses connected with it under section 159AC(3).

5.435 As both exemptions are currently expressed in the same terms, we have brought them together in this clause as a single exemption. The use of "taxable" car or van, and "exempt" heavy goods vehicle are labels to assist in identifying the basis on which the exemption is due.

5.436 Subsections (1) to (4) state the exemptions in respect of the various ways in which a charge might arise. For non-cash vouchers or credit-tokens the exemption is in clause 4.33.4.

5.437 Currently the exemption for the discharge of liability and certain expense payments in connection with an exempt heavy goods vehicle only applies in a case where there would otherwise have been a charge to tax under Chapter II of Part V of ICTA – applicable only to employees earning £8,500 or more and directors. We propose, in subsection (7), to extend the exemption to the lower-paid. This is a change to the law and policy. While it is unlikely that such a charge will arise in many cases, this change corrects an anomaly and is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Clause 4.30.4 Incidental overnight expenses and benefits

5.438 This clause rewrites the exemption for incidental overnight expenses currently in section 200A. That provision covers the exemption in so far as it relates to the charges under Chapter 4.1 (emoluments) and Chapter 4.5 (expenses). This clause also provides for an exemption from a charge to tax under Chapter 4.12. This part of the exemption is derived from section 155(1B).

5.439 The exemptions in respect of the provision of non-cash vouchers and credit-tokens relating to overnight absences in the same circumstances are dealt with in clause 4.33.3.

5.440 Sums paid by way of incidental overnight expenses are not eligible for the exemption in subsection (1) if the employee is already allowed a deduction under one of the provisions listed in section 200A(1)(b). We think that list includes all the provisions under which a deduction may be available. However, the current approach of listing all the references is long-winded and not necessarily easy to follow. It is simpler to say in subsections (1)(c) and (2)(b) "would not be deductible under this Part".

This is a change to the law and policy. It will not affect anyone's liability to income tax. **We welcome views on this proposed rewrite change.**

5.441 In subsection (1)(b) we have used a new label of "the overnight stay conditions" to describe the conditions which have to be satisfied in identifying a "qualifying period". Those conditions are explained in subsection (4).

5.442 Subsection (2) exempts the charge on benefits under Chapter 4.12 where relief for the cost of the benefit could not be obtained under clause 4.18.4, if the employee had paid for it. Subsection (2) rewrites section 155(1B).

5.443 In setting out the condition about deductibility of travelling costs, the current legislation, at section 200A(3)(b)(i), contains a list of deduction provisions which are regarded as satisfying the test. Subsection (5)(a) replaces this list and instead refers to expenses "deductible under this Part (otherwise than under any of the excepted foreign travel provisions)". We have listed the "excepted foreign travel provisions" in subsection (6).

Clause 4.30.5 Incidental overnight expenses and benefits: overall exemption limit

5.444 The exemption for incidental overnight expenses is a limited exemption. This clause sets out the limit on the exemption and how it is applied. The cap on the exemption applies to the sum of the expenses and benefits exempted under clause 4.30.4 and the amount exempted for non-cash vouchers and credit-tokens under clause 4.33.3. We use the label "the exemption provisions total" in subsection (2) to refer to the aggregate total eligible for exemption under both of these clauses.

5.445 Subsection (3) sets out "the permitted amount" for each qualifying period. The "permitted amount" is a new label for the amount described as the "authorised maximum" in section 200A(4).

Clause 4.30.6 Works bus services

5.446 This clause rewrites most of section 197AA. This excludes from the charge to tax under section 154 benefits arising from the provision of a works bus service for employees. The only part of section 197AA we have not rewritten in this clause is subsection (6). This deals with the exemption from the charge to tax under section 141 (non-cash vouchers) where the employee is given a non-cash voucher to evidence entitlement to use the works bus service. That exemption is covered in clause 4.33.1.

Clause 4.30.7 Support for public bus services

5.447 This clause rewrites section 197AB. This excludes from section 154 benefits arising from any financial or other support provided by one or more employers for a public bus service that their employees use for journeys to and from the workplace, or between workplaces.

Clause 4.30.8 Cycles and cyclist's safety equipment

5.448 This clause rewrites the exception in section 197AC. This prevents an employee being chargeable to income tax in respect of the provision of a cycle or associated safety equipment. The part of section 197AC dealing with the provision of a voucher entitling the employee to use a cycle or safety equipment is covered in clause 4.33.1.

5.449 The exception only applies where the employer provides the cycle or safety equipment for the employee's use rather than transferring it to him. If the cycle or equipment is given to the employee to keep, the benefit arising is still chargeable to tax in the normal way (see clauses 4.2.2, 4.4.2 and 4.12.1 in Exposure Draft No 6).

5.450 Section 197AC(6) includes an interpretation of "employment". We have not rewritten this because the term "employment" is defined for the whole of Part 4 in clause 4.1.2.

Clause 4.30.9 Exemption of travelling and subsistence during public transport strikes

5.451 This clause legislates Extra-Statutory Concession A58. This exempts travelling and subsistence when there is a disruption in public transport. This is a proposed rewrite change to the law but not to policy. It is in the taxpayer's favour. **We welcome comments on the proposals to legislate this extra-statutory concession.**

5.452 The concession provides an exemption for payments and benefits provided to employees to ensure they are able to get to work when there is a public transport strike. In the normal way when the employer pays the cost of, or provides transport for, "ordinary commuting" it would in most cases be chargeable to tax and no deduction would be allowed. Nor would deductions be allowed for accommodation and subsistence paid for or provided near to the permanent workplace.

5.453 If the employee is working at a temporary workplace, or on a training course, the provision of transport, accommodation and subsistence is not exempt, but a deduction is allowed under Chapter 4.17.

5.454 The concession states that no entries are needed on the P11D or P9D in respect of the benefits covered by it. We would not want the legislation of the extra-statutory concession to impose any new compliance burden. The clause therefore expressly exempts provision of transport, accommodation and subsistence in respect of which there is an amount included in earnings, and for which a deduction would not be due under Chapter 4.17.

Clause 4.30.10 Exemption of transport to work for disabled employees

5.455 This clause legislates Extra-Statutory Concession A59, some current practice as stated in the Inland Revenue Schedule E Manual at SE23600, and an unpublished practice which will shortly be published.

5.456 The original Extra-Statutory Concession covered payments made by the Ministry of Labour to employees of what became Remploy. It benefited severely and

permanently disabled people. A revised concession was published in June 2000 which provided a very much wider exemption for any provision of transport to and from the workplace, or contributions towards the cost of such journeys, for a disabled person.

5.457 The concession does not exempt the provision of a car which is chargeable under section 157, or, if it is adapted so that it no longer counts as a car, under section 154. But in practice the provision of a car for a disabled employee is not taxed where it can only be used – and is used only – for "ordinary commuting".

5.458 Initially this practice applied only to specially adapted cars. It has recently been extended to a car which has automatic transmission, if the employee cannot use a geared car because of the disability.

5.459 The clause puts these practices onto a legislative footing.

5.460 Legislating this extra-statutory concession and these practices is a proposed rewrite change to the law but not to policy. It is in the taxpayer's favour. **We welcome comments on the proposals to legislate this extra-statutory concession and to incorporate the Inland Revenue practices.**

Clause 4.30.11 Transport home: late night working and failure of car-sharing arrangements

5.461 This clause legislates Extra-Statutory Concession A66. The concession is in two parts - late night working and failure of car sharing.

5.462 The concession is limited to 60 occasions under either one part or both parts together. For each occasion after the sixtieth there is chargeability as normal.

5.463 The journeys concerned are from work to home only. We have not, therefore, used the term "ordinary commuting" as this would indicate journeys from home to work as well.

5.464 The conditions for the concession require judgements about when it is "not…reasonable to expect" an employee to use public transport – subsection (2)(c)(ii), and what are "unforeseen and exceptional circumstances". It is not possible to define these questions of judgement further.

5.465 Legislating this extra-statutory concession is a proposed rewrite change to the law but not to policy. It is in the taxpayer's favour. **We welcome comments on the proposals to legislate this extra-statutory concession**

Chapter 4.31 – Exemptions: education and training

5.466 This chapter contains tax exemptions for expenditure incurred by others in providing education and training for an employee. The first group of clauses deals with work-related training, and rewrite sections 200B to 200D. The second group of clauses deals with certain types of education and training defined by reference to the Learning and Skills Act 2000. These rewrite sections 200E to 200J.

5.467 Sections 200E to 200J were enacted in Finance Act 2000. Although they are in many ways similar to sections 200B to 200D, they contain some small but significant differences. We have dealt separately with the two groups of provisions. This involves some repetition, but we think the legislation would be less clear, and less easy to use, if we amalgamated the two groups.

5.468 Within each group of clauses we first describe the expenditure to which the clauses apply. We then define the type of training or education with which the clauses are concerned. Finally we set out circumstances in which exemption from tax will not apply.

Work-related training

Clause 4.31.1 Exemption of work-related training provision

5.469 This clause sets out what is exempt from tax. It is derived from sections 200B and 200D.

5.470 Section 200B deals with expenditure by the employer. Section 200D then provides the same consequences for expenditure by someone other than the employer. We have amalgamated these provisions, and refer to expenditure by a person other than the employee.

5.471 This requires a proposed rewrite change. Section 200D was intended to ensure that training funded by a third party would be exempt to the same extent as that funded by the employer. It has consistently been interpreted in that way. But it is not certain that the wording of section 200D achieves the intention. Section 200D refers only to a benefit, whereas section 200B refers both to expenditure and to the benefit of the training thereby provided. We believe our approach removes the doubt. To that extent it is a change to the law but not to policy. It is in favour of the taxpayer.

5.472 Sections 200B(4) and 200C(2) relate to the payment or reimbursement of travelling and subsistence expenses incidental to work-related training. The combined effect of these provisions is that the payment or reimbursement is exempt from tax only if the expenses are incurred wholly, exclusively and necessarily in undertaking the training. That is more restrictive than the test applied to travelling expenses in sections 588 to 589B, which deal with the provision of retraining and outplacement services when an employment ends. The test in sections 200B to 200D was never intended to be more restrictive. It has not in practice been applied more restrictively. The intention in all these provisions was to require amounts to be necessarily expended on travelling and subsistence. Clause 4.31.1(3)(d) achieves that intention. It brings Chapter 4.31 into

line with Chapter 4.41, in which sections 588 to 589B are rewritten. It is a change to the law but not to policy. It is in favour of the taxpayer.

5.473 Section 200C(2) refers to travelling and subsistence expenses that would have been deductible under a specific provision, section 198. In this clause, we have instead referred to amounts that would have been deductible "under this Part". This general reference clearly goes wider than the current specific reference. In practice, however, we believe it will make no difference. The current reference already imports deductions under a number of other provisions, such as sections 193 to 195, which operate through, or are included in references to, section 198. (Further information on the interaction of those rewritten provisions can be found at, for example, paragraphs 5.27 to 5.30 of the introductory commentary to the clauses.) It remains that extended scope of section 198, as rewritten across a number of chapters, which will be relevant. Referring to this Part as a whole, rather than to a specific provision, is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.474 **We welcome comments on these three proposed rewrite changes.**

Clause 4.31.2 Meaning of "work-related training"

5.475 This clause defines "work-related training".

Clause 4.31.3 Exception where provision for excluded purposes etc.

5.476 This clause deals with expenditure for which the exemption in clause 4.31.1 does not apply.

5.477 Section 200C(4) says that section 200B does not apply to expenditure that is exempt under section 588. Section 588 deals with retraining courses undertaken when an employment ceases and has been rewritten in Chapter 4.41. We believe section 200C(4) is unnecessary and we have omitted it. It is possible for an employee to be exempt from tax under both section 200B and section 588 in respect of expenditure on training. As the exemption is only given once it is not necessary to say that one section has priority over the other.

5.478 Section 200C(5) excludes from the exemption expenditure eligible for relief under section 32 Finance Act 1991 (vocational training). That relief was repealed by Finance Act 1999, with effect from 1 September 2000 (SI 2000 No 2004, Finance Act 1999, Section 59(3)(b), (Appointed Day) Order). There is little likelihood of the exclusion in section 200C(5) being applicable to any expenditure by the time the rewritten clauses come into effect. We have therefore not rewritten section 200C(5).

5.479 These omissions remove unnecessary material and we do not think they will affect anyone's liability to income tax. **We welcome comments on these two proposed rewrite changes.**

Clause 4.31.4 Exception where unrelated assets are provided

5.480 This clause deals with a further type of expenditure for which the exemption in clause 4.31.1 does not apply.

5.481 We have amended the definition of "training materials" in section 200C(7) so that the items listed in clause 4.31.4(3) are now illustrative, rather than representing an exhaustive list. An exhaustive list would become too restrictive as new means of delivering training are developed. We cannot predict what form they will take.

5.482 This more flexible approach is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Individual learning account training

Clause 4.31.5 Exemption for contributions to individual learning account training

5.483 This clause sets out what is exempt from tax. We have used the term "individual learning account training" because the trainee concerned must hold an account that meets conditions specified in the Learning and Skills Act 2000, or in regulations made under that Act. The clause rewrites sections 200E and 200J.

5.484 Section 200E deals with expenditure by an employee's employer or former employer. Section 200J then provides the same consequences for expenditure by someone other than the employer or former employer. We have amalgamated these provisions. Our approach is to refer to expenditure by a person other than the employee.

5.485 This requires a proposed rewrite change similar to that described in paragraphs 5.470 and 5.471 of the commentary on clause 4.31.1 above. Section 200J is intended to ensure that training funded by a third party is exempt to the same extent as that funded by the employer or former employer. We believe that our approach ensures that the rewritten legislation has the intended effect. To that extent it is a change to the law but not to policy. It is in favour of the taxpayer.

5.486 Section 200F(2), which relates to the payment or reimbursement of travelling and subsistence expenses, is intended to work in the same way as section 200C(2). Apart from some extra words in section 200F(2), to deal with the case of a person whose employment has ceased, the two provisions are identical. Paragraph 5.472 of the commentary to clause 4.31.1 above describes the current mismatch between policy and statute in these provisions and the proposed rewrite change. This change keeps Chapter 4.31 in line with Chapter 4.41. This is a change to the law but not to policy, and is in favour of the taxpayer.

5.487 Section 200F(2) refers to travelling and subsistence expenses that would have been deductible under a specific provision, section 198. In this clause, we have instead referred to amounts that would have been deductible "under this Part". Reasons for the change are set out in paragraph 5.473 of the commentary on clause 4.31.1 above. It is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.488 We have invited comments on these three proposed rewrite changes in paragraph 5.474.

Clause 4.31.6 Meaning of "individual learning account training"

5.489 This clause defines "individual learning account training".

Clause 4.31.7 Exception where provision for excluded purposes

5.490 This clause deals with expenditure for which the exemption in clause 4.31.5 does not apply.

5.491 As noted in the commentary on clause 4.31.3 above, where earnings are exempt under two separate provisions it is not necessary to give priority to one of those provisions. For that reason we have not rewritten section 200H. That section says that section 200E does not apply to expenditure to the extent that either section 200B or section 588(1) has effect.

5.492 This removes unnecessary material and as such we do not think it will adversely affect anyone's liability to income tax. We invite comments on this proposed rewrite change at 5.479 of the commentary on clause 4.31.3.

Clause 4.31.8 Exception where unrelated assets are provided

5.493 This clause deals with a further type of expenditure for which the exemption in clause 4.31.5 does not apply.

5.494 The definition of "training materials" in this clause is the same as in clause 4.31.4. We have again used an illustrative definition rather than the exhaustive one in section 200F(5). This allows for a more flexible interpretation as new means of delivering training are developed.

5.495 This is a change to the law but not to policy. It is in favour of the taxpayer. We have invited comments on this proposed rewrite change in paragraph 5.482 of the commentary on clause 4.31.4 at page 97.

Clause 4.31.9 Exception where training not generally available to staff

5.496 This clause deals with the requirement for individual learning account training to be generally available to an employer's staff. It rewrites sections 200G and 200J. A contribution to an employee's education or training is not exempt from tax if made under arrangements that allow for discrimination in favour of particular employees or groups of employees.

5.497 The relevant arrangements must provide for contributions to be generally available, on similar terms, to all employees. That is the case whether the contribution is made by the employer or by someone else. We think the rewritten clause brings out this requirement more clearly than the current legislation. That legislation deals with expenditure by someone other than the employer as a separate case in section 200J. We have amalgamated the two sections in this respect as in clause 4.31.5. We have also changed the reference to arrangements to cover those in place at the time, whoever agrees to incur the expenditure (not simply where the employer agrees). We believe that our approach ensures that the rewritten legislation has the intended effect. To that

extent it is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change**

5.498 Clause 4.31.9(2) allows the Treasury to make regulations. In subsection (5) the clause sets out the method for making the regulations – statutory instrument subject to the negative resolution procedure. This will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Chapter 4.32 – Exemptions: recreational benefits

Recreational facilities

5.499 The first three clauses in this chapter deal with an exemption where an employer provides certain sporting or recreational facilities for employees. All the clauses are derived from section 197G.

5.500 We have reordered the material in section 197G. First we describe benefits to which the exemption applies. Then we set out the conditions which must be met for the exemption to apply to those benefits. Finally we list those benefits to which it does not apply.

5.501 **We welcome comments on whether the structure we have used makes the provision easier to follow.**

5.502 In this chapter we have used "facilities" in the plural throughout to denote that it is the tangible facilities which are meant and not the opportunity to use them. This replaces "facility" used in section 197G(3)(c)-(f) and section 197G(4) opening words and (b).

5.503 **We welcome comments on whether these changes are appropriate, and whether they make the legislation easier to understand.**

Clause 4.32.1 Exemption of recreational benefits

5.504 Subsection (1) provides the exemption from income tax. Subsection (2) makes it clear that both the use of the facilities and the right or opportunity to use them are within the exemption. Subsection (1)(b) acknowledges the fact that a right to use something can itself be a benefit. The availability and use of the facilities must meet the conditions set out in subsection (3) for the benefit to be exempt.

5.505 An employer may provide a non-cash voucher which the employee must present to use the facilities provided. If the facilities meet all the conditions set out, and the voucher can only be used for that purpose, there is no chargeability on the cost of provision of the voucher by Chapter 4.6 of Exposure Draft No 6. The provision giving the voucher exemption is in clause 4.33.1(4). This is part of the restructuring, as outlined in the introduction to the commentary, which places the exemption from chargeability in respect of the provision of a voucher in Chapter 4.33.

5.506 The simplest case where this exemption can apply is that of a single employer. If all the conditions in subsection (3) are met, the exemption applies. In that case "the employer in question" is the single employer.

5.507 Two or more employers may provide facilities jointly. In such a case each employer is looked at separately. The condition in subsection (3)(a) requires that the facilities must be available to all the employees of that employer – the "employer in question". If one employer restricts the availability to certain employees, none of the employees of **that** employer can claim the exemption.

5.508 The use of these words "public generally" in subsection (3)(b) is to indicate that the exemption cannot apply to facilities available for public use. If an employer buys time in public facilities, or pays for employees to use them, the exemption does not apply. If there are in-house facilities made available to the "public generally", the exemption does not apply. However, in-house facilities made available for use to a particular sector of "the public", meaning people other than employees, such as a local school allowed to have swimming lessons does not prevent the exemption from applying provided the condition in clause 4.32.1(3)(c) is met.

5.509 The test at subsection (3)(c) looks at actual use of the facilities rather than the people to whom they are made available. There are several different things taken into account here. To simplify this we have used the expression "employment-related" and then defined what we mean by that in the next subsection.

5.510 The word "mainly" in subsection (3)(c) is used to permit some use by those for whom it is not employment-related without the condition being breached.

5.511 The words in brackets in subsection (3)(c) are to indicate that where there is provision for the employees of more than one employer all users must be considered. Use by former employees and their families is included, provided the employer has made the facilities available to all employees. If an employer has restricted use, so that the test at subsection (3)(a) fails for that employer, it does not prevent the use test being satisfied for other employers. Provided the restricting employer has only small numbers actually using the facilities, the "mainly" test is satisfied. This can best be explained using an example.

5.512 Example. Suppose a facility is:

- available to a few of A's employees; and
- available to all of B's employees; but
- not available to the public generally.

The exemption does not apply to A's employees because the condition in subsection (3)(a) is not satisfied. Subsection (3)(a) is satisfied for B's employees.

The opportunity to use the facilities may be employment-related for B's employees but not for A's. If B's employees who use the facilities substantially outnumber the employees of A who use it, it will be used mainly by employees whose opportunity to use it is employment-related. The condition in subsection (3)(c) is then satisfied for B's employees, and the exemption will apply for them.

Clause 4.32.2 Excluded benefits

5.513 Subsection (1) sets out the benefits which are not within the exemption.

Clause 4.32.3 Power to alter benefits to which s. 4.32.1 applies

5.514 This clause gives the Treasury a power to limit or extend the scope of the exemption. Subsection (2) provides that regulations are made by statutory instrument subject to the negative resolution procedure. This will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Annual parties and functions

Clause 4.32.4 Annual parties and functions

5.515 This clause legislates Extra-Statutory Concession A70B (Staff Christmas parties). This is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposal to legislate this extra-statutory concession**.

5.516 Although the heading to the concession is "Staff Christmas Parties", the extension of the original concession to other parties indicates that it refers to annual functions in general, so we have used the heading "Annual parties and functions".

5.517 As the concession is in terms that no tax will be charged on the benefit, subject to the monetary limits, it is legislated here as an exemption from income tax.

5.518 When an extra-statutory concession contains monetary limits, the amount can be changed by press release or by republishing it with different amounts. This is not possible for legislation. There are a number of exemptions in current legislation in which an amount is fixed by the Treasury. We have adopted the same approach for rewritten concessions and have drafted a general power for the Treasury to increase the amounts at clause 4.48.1. This provision is listed there.

5.519 In most cases where an exemption applies to provision by way of a non-cash voucher or credit-token we have placed that exemption in Chapter 4.33. A ticket for entry to a function is a voucher. But as this may not be generally recognised, we thought it would be more appropriate to keep the exemption in this section.

5.520 **We welcome comments on whether the non-cash voucher exemption for annual parties should be left in this section or moved to Chapter 4.33.**

Entertainment

Clause 4.32.5 Third party entertainment

5.521 This clause rewrites the exemption at section 155(7). The provision of the benefit in this case is 'by reason of the employment' and is therefore within the terms of Chapter 4.12. But it is not provided by the employer, and the cost of it is not borne by the employer. This presents a compliance problem because neither the employer nor the employee might know the cost to the provider. The exemption is therefore deregulatory.

5.522 The conditions laid down make it clear that the reason for the entertainment must be gratuitous, and not in any way a reward for past or future services, nor from

anyone connected with the employer. If these conditions are not met, there is no exemption.

5.523 If the provision of the entertainment is by way of a non-cash voucher or a credit-token, there are corresponding exemptions at sections 141(6B) and 142(3B) which have been included in the general exemptions from Chapter 4.6 in clauses 4.33.1 and 4.33.2.

Chapter 4.33 – Exemptions: non-cash vouchers and credit-tokens

Introduction

5.524 Chapter 4.6 of Exposure Draft No 6, included some exceptions for non-cash vouchers and credit-tokens. In the course of rewriting the more general exemption provisions, other exceptions and exemptions came to light which, if we followed the same pattern as in Exposure Draft No 6, would be within Chapter 4.6. In some cases these reflected an exemption from a benefits charge under Chapter 4.12, and in others a more general exemption. The exemptions for non-cash vouchers and credit-tokens depend on what is bought with them.

5.525 We have brought together in Chapter 4.33 almost all the exemptions which apply to non-cash vouchers and credit-tokens. This is one of the proposed rewrite changes with wide-ranging application discussed in the introductory commentary on the clauses. We invite comment on this approach in paragraph 5.44. Broadly speaking, anything which is not in this chapter is not exempt if provided by way of a non-cash voucher or credit-token. It therefore remains chargeable, even if it would be exempt if provided direct. This chapter also incorporates the extra-statutory concessions which give exemptions, and which are proposed rewrite changes already listed under the main exemption sections.

5.526 We have reorganised these exemptions into one chapter because we felt that people are more likely to look for exemptions specifically relating to non-cash vouchers and credit-tokens, rather than for references to the use to which the voucher or credit-token is put. (The exceptions to this approach are clause 4.32.4(4), tickets for annual parties or functions, and clause 4.35.7, armed forces' travel warrants.) When all the employment income provisions are brought together, the Chapter 4.6 charging provisions will contain a cross-reference to this chapter.

5.527 The other possibilities were either to put all the voucher and credit-token exemptions into Chapter 4.6, or to write them with the related main exemption, where there is one.

5.528 **We welcome comments on whether it is better to have the exemptions in one chapter dealing only with non-cash vouchers and credit-tokens or as part of the main exemption clause, or in Chapter 4.6.**

Clause 4.33.1 Exemption of non-cash vouchers for exempt benefits

5.529 Subsections (1) and (2) provide the general terms of the exemption and then list where each individual exemption is found in full.

5.530 Subsection (3) provides exemption for two cases which operate in a different way.

5.531 Subsection (4) imposes a further restriction which applies for non-cash vouchers used to obtain specific things.

5.532 Subsection (5) makes it clear that, although some of these general exemptions apply only to a charge which would fall on someone who is not in lower paid employment, the voucher can be exempt even if the employee is in such employment. This is necessary because chargeability for non-cash vouchers and credit-tokens applies to all employees, unlike other benefits charges.

5.533 **We welcome comments on whether the use of a general clause of this type is helpful.**

5.534 Self-assessment poses a timing problem with regard to the use of a non-cash voucher to which an exemption applies. The voucher is chargeable for the tax year when the cost of it is incurred, or when it is received by the employee. If it is not used in that year and it is charged to tax, the self-assessment may be amended to give effect to the exemption within the period up to 31 January following the latest filing date.

Clause 4.33.2 Exemption for credit-tokens used for exempt benefits

5.535 This clause is the equivalent to clause 4.33.1 (vouchers) and works in the same way.

5.536 In the case of a credit-token, chargeability arises at the time it is used to obtain something and not at the time of its issue. There is therefore no timing problem here.

5.537 The list of benefits which could be obtained using a credit-token does not contain all those listed for non-cash vouchers. This is because some of the things in that list could not be obtained by use of a credit-token in such a way as to be exempt.

5.538 **We welcome comments on whether the use of a general clause of this type is helpful.**

Clause 4.33.3 Exemption for incidental overnight expenses

5.539 It is not possible to put this exemption in clauses 4.33.1 and 4.33.2 because of the particular conditions which apply. The general exemption for incidental overnight expenses is in clause 4.30.4.

5.540 This clause was published in Exposure Draft No 6 as clause 4.6.13. It has been amended to bring it into line with clause 4.30.4, and with the structure of the deductions clauses. It also corrects some errors in the original draft.

5.541 Clause 4.6.13(a) wrongly gave exemption to the extent that the "authorised maximum" was not exceeded: in fact the exemption does not apply at all if the "authorised maximum" is exceeded. Also, we realised that goods and services obtained by use of the voucher or token needed different treatment from money. Subsections (2) and (3) make the necessary changes.

5.542 In subsection (4) we have referred to amounts that would not be deductible under clause 4.18.2. That clause is a new version of clause 4.6.7 as published in Exposure Draft No 6. It contains a proposed rewrite change in that it refers to Chapter

4.17 as a whole, rather than the specific provisions mentioned in sections 141(3) and 142(2).

5.543 Subsections (5) and (6) import the limitation of the amount and the terms used from clauses 4.30.4 and 4.30.5.

Clause 4.33.4 Exception where benefits or money obtained in connection with taxable car or van or exempt heavy goods vehicle

5.544 This clause replaces 4.6.14 in Exposure Draft No 6. It expands the scope of the original draft by extending the exemption to use of the voucher or credit token for expenditure on vans and heavy goods vehicles as well as cars.

5.545 The exemption from chargeability as earnings is in clause 4.30.3.

5.546 The commentary regarding clause 4.30.3 applies to this clause. The proposed rewrite change in that clause at subsection (7) is the same as in this clause at subsection (3)(b).

Clause 4.33.5 Exception for small gifts from third parties

5.547 This clause legislates the part of Extra-Statutory Concession A70A which deals with gifts are in the form of non-cash vouchers or credit-tokens. The exemption from chargeability as earnings is in clause 4.42.11.

5.548 The exemption could not be included in clauses 4.33.1 and 4.33.2 because there are restrictions as to the reason for the gift, the nature of the voucher or token and the amount for the exemption to apply. The restrictions as set out in clause 4.42.11 apply to this clause.

5.549 The concession is confined to the obtaining of goods and so excludes services or money. The amount which can be exempt in any tax year is a total of £150 from the same donor, being the total cost of any goods and the cost of the voucher.

5.550 Legislating this extra-statutory concession is a proposed rewrite change as explained in the commentary on clause 4.42.11 in paragraphs 5.768 to 5.770, where we invite comment on the proposed rewrite change involved.

Chapter 4.34 – Exemptions: removal benefits and expenses

5.551 Section 191A gives effect to Schedule 11A, which provides an exemption for removal expenses and benefits.

5.552 Schedule 11A covers general removal expenses in paragraphs 3 and 7 to 14 and benefits in paragraphs 4 and 16 to 22. There is a good deal of duplication in these paragraphs. In this chapter we have dealt with benefits and reimbursed expenses together wherever possible.

5.553 The provisions in paragraphs 8 to 14 and 17 to 22 of Schedule 11A all start with a similar phrase, ending in every case with the words "if (and only if)". We have not reproduced the words in brackets when rewriting these provisions in clauses 4.34.5 to 4.34.13 as they to not seem to add anything to the conditions.

5.554 The commencement provisions for Schedule 11A in paragraph 29 are now spent.

Exemption of removal benefits and expenses

Clause 4.34.1 Exemption for removal benefits and expenses: general

5.555 This clause sets out the general proposition that any removal benefits or reimbursed removal expenses listed in this chapter are exempt from income tax, up to the limit set out in clause 4.34.15.

5.556 Subsections (1) and (2) of this clause rewrite paragraph 1 of Schedule 11A, which exempts the benefits and expenses in question from income tax under Case I or II of Schedule E.

5.557 The charging provisions from which Chapter 4.34 gives exemption are described in subsection (2).

5.558 We have not rewritten the opening words of paragraph 1(1) of Schedule 11A, "where by reason of a person's employment". We do not think these words are necessary because there is no tax charge in respect of benefits or reimbursed expenses unless they arise "by reason of a person's employment" – see, for example, clause 4.12.1 in Exposure Draft No 6. The exemptions in this chapter only apply where there is the possibility of a charge.

5.559 Paragraph 2 of Schedule 11A ensures that the exemption from charge under Cases I and II does not result in them being chargeable under Case III as a result of section 131(2). Under the rewritten provisions concerning chargeability in Chapter 4.50 it is no longer possible for tax to be chargeable under more than one of the clauses in Chapter 4.50.

Clause 4.34.2 Benefits and expenses to which this Chapter applies

5.560 This clause lists all the benefits and reimbursed expenses potentially within the scope of the limited exemption set out in clause 4.34.1. It also details the overriding

conditions that must be satisfied. It is derived from paragraphs 3, 4, 7 and 16 of Schedule 11A.

5.561 One of the overriding conditions is that the benefits must be provided or that the reimbursed expenses must be incurred on or before a particular day. In the current legislation that day is called the "relevant day" and defined in paragraph 6 of Schedule 11A. In this Exposure Draft we have called it "the limitation day" and defined it in clause 4.34.4.

Clause 4.34.3 Conditions applicable to change of residence

5.562 This clause rewrites paragraph 5 of Schedule 11A, which describes the conditions that apply to a change in residence.

5.563 We have not reproduced the words in brackets in paragraphs 5(1)(b) and (c) as they to not seem to add anything. This removes unnecessary material. It does not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.564 A number of the later paragraphs in Schedule 11A refer to the circumstances set out in paragraph 5(1). We have referred to a change of residence within paragraph 5(1) as being "the employment change" to make those references more straightforward.

Clause 4.34.4 Meaning of "the limitation day"

5.565 This clause defines "the limitation day" and effectively rewrites paragraph 6 using a reference to "the employment change" defined in clause 4.34.3(3).

5.566 The concept of "the limitation day" is also relevant to clauses 4.9.17A and 4.9.17B which reduce the charge to tax in respect of employment-related loans that satisfy the bridging loan conditions.

Benefits and expenses within this Chapter

Clause 4.34.5 Acquisition benefits and expenses

5.567 This clause sets out the acquisition benefits and expenses that come within the chapter. It combines paragraphs 9 (expenses) and 18 (benefits) of Schedule 11A so cutting out unnecessary duplication. We have also followed this approach in a number of the following clauses combining the rules for expenses and benefits.

Clause 4.34.6 Abortive acquisition benefits and expenses

5.568 This clause combines paragraphs 10 (expenses) and 19 (benefits) of Schedule 11A, so bringing the expenses and benefits connected with an abortive acquisition of a new residence together into one clause.

Clause 4.34.7 Disposal benefits and expenses

5.569 This clause combines paragraphs 8 (expenses) and 17 (benefits) of Schedule 11A, so bringing the expenses and benefits connected with the disposal of the employee's former residence together into one clause.

5.570 Paragraph 8(4) of Schedule 11A, to which paragraph 17(3) also refers, describes loans that relate to a residence. The loan must satisfy either the condition that it was raised to obtain an interest in the residence, or the condition that an interest in the residence forms security for the loan, or both. If "or both" refers to a loan which satisfies both conditions it is redundant. So it is probably intended to cover the situation where part of the loan satisfies one condition and part of it satisfies the other condition.

5.571 We have replaced the "or both" in this clause with a provision enabling a loan to meet the test where different parts each meet one of the conditions. This is a change to the law, but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Clause 4.34.8 Benefits and expenses connected with transporting belongings

5.572 This clause combines paragraphs 11 (expenses) and 20 (benefits) of Schedule 11A, so bringing the expenses and benefits connected with the transportation of belongings together within one clause.

5.573 Subsection (3) sets out the meaning of "domestic belongings" and "transportation", currently in paragraph 11(2) and (3) of Schedule 11A.

Clause 4.34.9 Benefits and expenses connected with travelling and subsistence

5.574 This clause combines paragraphs 12 (expenses) and 21 (benefits) of Schedule 11A, so bringing the expenses and benefits connected with travelling and subsistence together within one clause.

5.575 Subsection (1)(g) covers travel facilities for a child who is a member of the employee's family. It applies where, in order to secure continuity of education, the child does not move to the new area at the same time as the employee and has to undertake extra travelling as a result.

5.576 The current legislation in paragraphs 12(1)(i) and 21(1)(i) of Schedule 11A does not include travel by such a child to and from temporary living accommodation of the employee. We do not know whether this is intentional or an oversight.

5.577 It is difficult to see why there should be this difference in treatment. If the employee has to use temporary accommodation, that would be the child's "home" until the employee moved into permanent accommodation. This problem seems quite likely to arise during the period covered by the exemption.

5.578 We therefore propose to extend the exemption to cover a child's journeys to and from the employee's temporary accommodation. This is a change to the law and to

policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

5.579 Subsection (4) defines "new duties", "former area", "new area", "relevant child", currently in paragraph 12(2) of Schedule 11A and "subsistence", currently in paragraph 28 of Schedule 11A.

Clause 4.34.10 Exclusion where benefits or expenses deductible

5.580 If a deduction under sections 193 to 195 is available to the employee in respect of a removal benefit or expense, that benefit or expense is outside the exemption set out in Schedule 11A. This is currently in paragraphs 12(4) and 21 (7) of Schedule 11A. This clause rewrites those provisions.

5.581 A deduction might be allowed for only part of a benefit provided. So the other part of the benefit might still be exempt under paragraph 21(8) of Schedule 11A. This provision is rewritten in subsection (3).

Clause 4.34.11 Exclusion where car and van benefits otherwise taxable

5.582 The exemption in paragraph 1 of Schedule 11A does not apply to car or van benefits. They are excluded by paragraphs 21(2) and (4) to (6) of Schedule 11A.

5.583 In rewriting those provisions, we considered the phrase "any relevant time" that appears in paragraph 21(2) and is defined in paragraph 21(6). In theory the current wording could apply to the provision of a company car used by the employee in a previous tax year, but given up before the start of the tax year in which he or she moved to the new area. We do not know whether this has ever arisen in practice.

5.584 We have rewritten this rule so that it can only apply if the vehicle is provided for private use (other than in connection with the move) in the same tax year that the employment change takes place. This is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Clause 4.34.12 Bridging loan expenses

5.585 This clause rewrites paragraph 13 of Schedule 11A. This deals with bridging loan expenses (interest) connected with an employee's change of residence resulting from an employment change.

5.586 We have combined the first two conditions that the bridging loan must satisfy, currently in paragraph 13(1)(a) and (b), in subsection (1)(a). Subsections (1)(b) and (c) list the other conditions.

5.587 The purpose for which the loan must be used is currently set out in paragraphs 13(4) and (5). Again we have combined those provisions without any change in effect, in subsection (2). We have replaced "or both" in 4.34.12(2)(iii) with wording to enable a loan to meet the test where different parts of it each meet one of the conditions. This is the same change as set out in paragraphs 5.570 to 5.571 above in relation to clause 4.34.7, where we invited comment on this proposed rewrite change.

5.588 The exemption is limited to the interest paid on a loan equal to the market value of the employee's former residence.

5.589 The current legislation does not specify how to allocate the total loan interest between exempt and non-exempt where paragraph 13(3) and (4) both apply. We have therefore included in subsection (4) a method statement to explain how to allocate the interest. This new feature is a change to the law, but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.590 Paragraph 13(7) of Schedule 11A extends the meaning of interest payable by an employee to cases where it is payable by any members of the employee's family or household, whether or not jointly with the employee. Paragraph 13(8) applies a parallel extension in meaning to references to a loan being raised by the employee. These provisions are combined in subsection (5).

Clause 4.34.13 Replacement of domestic goods

5.591 This clause combines paragraphs 14 (expenses) and 22 (benefits) of Schedule 11A, and brings the expenses and benefits connected with replacing domestic goods together into one clause.

5.592 We have changed the heading of this provision. The current heading, "duplicate expenses" does not really describe what this provision is about.

5.593 Under paragraph 14(2) if an employee sells any of the domestic goods replaced by the new goods covered by paragraph 14, the sale proceeds have to be deducted from the amount qualifying under this paragraph. However, there is no similar requirement to deduct sale proceeds of the replaced domestic goods in a case where the employer provides the new goods (dealt with in paragraph 22). We think it is right and logical to apply the same rule both where the employer reimburses and where the employer provides those goods direct. We therefore propose to remove the requirement to deduct sale proceeds of replaced domestic goods currently in paragraph 14(2). This is a change to the law and policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Clause 4.34.14 Power to amend ss.4.34.5 to 4.34.13

5.594 Under this clause, the Treasury may make regulations to extend clauses 4.34.5 to 4.34.13 to bring within their scope benefits or expenses not otherwise covered. This clause combines paragraphs 15 (expenses) and 23 (benefits) of Schedule 11A, so bringing the provisions dealing with the Treasury's regulation-making power together into one clause.

5.595 Subsection (5) sets out the method for making the regulations – a statutory instrument subject to the negative resolution procedure. This will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Limit on exemption

Clause 4.34.15 Limit on exemption

5.596 Paragraph 24 of Schedule 11A sets out the limit on the total amount of the exemption available under this chapter.

5.597 We propose a rewrite change in that the current legislation does not explicitly include in the list of expenses and benefits that count towards the £8,000 limit any items that have been funded by the use of non-cash vouchers or credit-tokens. There is no logical justification for this inconsistent treatment and it does not sit comfortably with the idea of a cohesive benefits code. We therefore propose to include in the list of items counting towards the £8,000 limit any benefits within this chapter that are treated as earnings under the benefits code. This will have the effect of including benefits treated as earnings under Chapter 4.6 (taxable benefits: vouchers and credit-tokens) in Exposure Draft No 6. This is a change to the law and policy. It is a change theoretically unfavourable to the taxpayer. We do not think that this change will have any significant effect **in practice** as it seems unlikely that the major elements of removal expenses and benefits would be so funded. This being the case, we consider the change is worth making because it will mean that the law will be easier to follow. It is instinctively logical that if an item is potentially exempt under this chapter, then it should count towards the limit. **We welcome comments on this proposed rewrite change.**

5.598 There is a second proposed change in respect of the way in which we apply the limit to benefits. The current treatment of such benefits is dealt with in paragraph 24(3) to (8) of Schedule 11A. There is something of an anomaly in the way these provisions currently hang together. If a benefit is chargeable to tax under section 154 (the reference to Chapter II in paragraph 24(3)) only the amount that would be chargeable under that section counts towards the exemption. However, that same benefit could be chargeable on a larger amount under section 19. For example, if an asset is transferred to the employee the amount chargeable under section 19 as "money's worth" might be, say, £5,000 whereas the amount chargeable under section 154 might be only £3,000 as the cost of the asset to the employer. If that asset is connected with the employee's change of residence, it may be exempt but only up to the section 154 amount of £3,000. The remaining £2,000 of the section 19(1) would remain outside the exemption. We have therefore recast the provisions setting out the amount that counts towards the £8,000 limit in terms of the amounts that are treated as earnings (under whatever section that may be). This is a change to the law and policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

5.599 The current provisions also go into great detail about how to quantify the amount of benefit relating to the provision of living accommodation in paragraph 24(4) to (8). We have amalgamated all of this into subsection (5). It brings together all the various permutations for the computation of amounts chargeable in such cases. This formulation also sweeps up the consequential effect of legislating Extra-Statutory Concession A91(b) (living accommodation provided by reason of employment) in clause 4.7.8, published in Exposure Draft No 6. It therefore forms part of a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

Supplementary provisions

Clause 4.34.16 Meaning of "residence" etc.

5.600 This clause rewrites paragraph 25 of Schedule 11A. We think there is no need to refer to an employee's sole or main residence. Instead we explain which residence we are talking about if the employee has more than one residence.

Clause 4.34.17 Meaning of "members of the employee's family or household"

5.601 This clause rewrites paragraph 26 of Schedule 11A, listing the people included in an employee's family or household rather than, as currently, interpreting the phrase in negative terms.

Chapter 4.35 – Exemptions: special kinds of employees

Ministers of religion

Clause 4.35.1 Accommodation benefits of ministers of religion

5.602 This clause rewrites those parts of section 332 which provide exemptions from tax under Schedule E for ministers of religion. The parts of section 332 that allow deductions for the expenses of ministers of religion are covered in clause 4.17.17.

5.603 This clause applies to benefits in respect of accommodation occupied by a minister of religion in premises owned by a charity or ecclesiastical corporation. These benefits are exempt if they are:

- amounts paid on behalf of or reimbursed to the minister;
- statutory deductions reimbursed to the minister; and
- expenses reimbursed to a minister who is in "lower-paid employment".

5.604 We have rewritten the exemption as applying to a full-time minister and defined the term. That includes both categories of person mentioned in section 332(1)(a) and (b).

5.605 Section 332(2)(a) and (c) include the phrase "in consequence of his being the holder of his office". We think this can safely be removed without altering the sense of the provisions.

5.606 In Part 4 we have separated out the provisions on exemptions from those on deductions. This means that we describe the relevant premises both here and in clause 4.17.17. We think that this duplication is worthwhile in that it makes the legislation easier to use.

5.607 The premises must be owned by a charity or ecclesiastical corporation. This clause includes a definition of "charity", drawn from section 506(1). Since that definition does not currently apply for this purpose, this is a change to the law, but not to policy. It will not affect anyone's liability to income tax. We have invited comments on this proposed change in paragraph 5.218.

5.608 We have also made the definitions of "statutory amount" and "statutory deduction" more specific. This is a change in approach but not in the underlying law. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

MPs, government ministers and others

Clause 4.35.2 Termination payments to MPs and others ceasing to hold office

5.609 This clause rewrites section 190. It refers to Acts that give MPs, MEPs and certain other political office holders an entitlement to termination payments. That entitlement, established prior to termination, makes the payments chargeable to tax as earnings. The payments are in fact compensation for loss of office. If it were not for the predetermined entitlement they would normally fall within section 148 and tax would be chargeable on an amount above the £30,000 threshold.

5.610 This clause ensures that such payments are not treated as earnings and are taxed as termination payments under Chapter 4.23, subject to the threshold set out in that chapter.

5.611 Section 190(3) applies to "grants and payments if they are not pension payments". The reference to pension payments is unnecessary because section 190 applies to "emoluments" and pension payments are not taxed as emoluments. We have not included the reference to pension payments in the rewritten clause because they are not taxed as employment income.

5.612 We have omitted the reference to the Parliamentary Pensions Act 1984 as it was repealed by the Ministerial and other Pensions and Salaries Act 1991 and would only apply where the loss of office was before 28 February 1991. It is now spent. This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.613 The meaning of "a relevant office" is set out in section 4(6) Ministerial and Other Pensions and Salaries Act 1991. Broadly it covers all Government Ministers, Opposition Leaders and Whips, the Chairman and Deputy Chairman of Ways and Means, and the Chairman and Deputy Chairman of Committees of the House of Lords.

Clause 4.35.3 Overnight expenses allowances of MPs

5.614 This clause rewrites part of section 200. It provides an exemption from income tax for certain allowances paid to Members of Parliament. Without it, the allowances would be chargeable to tax as earnings.

5.615 Section 200 says that the allowances "shall not be regarded as income for any purpose of the Income Tax Acts". We have simplified this formula to say that such an allowance is "exempt from income tax". The rest of the proposition is dealt with in clause 4.43.1.

5.616 The allowances that qualify are those provided for by a resolution of the House of Commons covering the overnight expenses set out in the clause, where an MP has to stay away from home overnight either in London or in the constituency in order to carry out Parliamentary duties.

5.617 We have rearranged the material in sections 200 and 200ZA. Overnight expense allowances to members of the House of Commons are dealt with in this clause.

Those paid to members of the Scottish Parliament, the National Assembly for Wales and the Northern Ireland Assembly are covered in clause 4.35.4. Travel by members to European Union institutions or to the parliament of another Member state is dealt with in clause 4.35.5. **We welcome comments on whether this rearrangement makes the legislation easier to use.**

5.618 Although the allowances are exempt from tax this clause does not prohibit a deduction for an MP's expenses in respect of which the allowances are paid. That prohibition is in section 198(4), which is rewritten as clause 4.17.22.

Clause 4.35.4 Overnight expenses of other elected representatives

5.619 This clause rewrites the overnight expenses part of section 200ZA in respect of elected representatives of the Scottish Parliament, the National Assembly for Wales and the Northern Ireland Assembly.

5.620 We have not combined this exemption with the similar one for members of the House of Commons because the detailed rules are different. We felt it would be clearer if they were kept separate. Again, this clause is supplemented by clause 4.43.1.

Clause 4.35.5 EU travel expenses of MPs and other representatives

5.621 This clause brings together the exemption for European Union travelling expenses paid to members of the House of Commons, the Scottish Parliament, the National Assembly for Wales and the Northern Ireland Assembly.

5.622 The definition of European Union travel expenses is the same in both section 200 and section 200ZA. Combining the relevant parts of the two sections cuts out duplication. Again this clause is supplemented by clause 4.43.1.

Clause 4.35.6 Transport and subsistence for Government ministers etc.

5.623 This clause provides an exemption in respect of transport or subsistence provided for certain Government office-holders (mainly Ministers) and members of their families or households. The exemption also covers payments and reimbursements of travel and subsistence expenses if they are made by or on behalf of the Crown.

5.624 The exemption was extended in Finance Act 1999 to apply to Ministers and similar office-holders serving in the Scottish Parliament, the National Assembly for Wales and the Northern Ireland Assembly.

5.625 For the purposes of this exemption, the provision of transport includes the provision of a car, which would otherwise give rise to a charge to tax under Chapter 4.8, taxable benefits: cars, vans and related benefits, in Exposure Draft No 6. The current legislation applies the exemption specifically to cars, but then goes on to define a car as "any mechanically propelled road vehicle" – a phrase which could include, for example, a van or a motorbike. We have removed this slight incongruity by applying the exemption to the provision of a "vehicle", and defining "vehicle" in the same way as "car" is defined in the current legislation.

Armed Forces

Clause 4.35.7 Armed forces' leave travel facilities

5.626 This clause exempts armed forces' leave travel facilities from income tax. It rewrites section 197.

5.627 The original provision was introduced by Finance Act 1977 to exempt from tax the various travel warrants and allowances, including allowances for the use of private cars, made available to service personnel. Section 197(2) amplifies the exemption at section 197(1) with a list of the tax provisions being removed and examples of the leave travel facilities within the exemption.

5.628 We have substituted "the armed forces of the Crown" for "the naval, military or air forces of the Crown". That allows the same term to be used in this clause and in clause 4.35.8 for the same body of taxpayers. The two terms are construed as having the same meaning and include all United Kingdom service personnel, both members of a regular force and members of a reserve force. References to the "armed forces" now also include the women's services (which was not the position in 1977 when the original provision was introduced).

5.629 The approach taken in this clause is to exempt from income tax the provision of "travel facilities" for, and payments made in respect of, leave travel.

5.630 Travel facilities are not defined, limited or illustrated, except that:

- the exemption specifically includes a "transport voucher" within the meaning given in clause 4.6.5; and
- the exemption excludes the provision of a vehicle for leave travel (because charges under section 157, car benefits, are not within the scope of section 197).

Clause 4.35.8 Armed forces' food, drink and mess allowances

5.631 This is the first of two clauses rewriting parts of section 316.

5.632 The legislation in section 316 originally derives from a number of different provisions enacted between 1946 and 1951. Those provisions were consolidated first as section 457 ITA 1952 and then as section 366 ICTA 1970 before becoming section 316. In the case of Lush (HM Inspector of Taxes) v Coles (1967) 44 TC 169[4], Stamp J described them as containing "something of a hotchpot" (at 172G).

5.633 Section 316 has five subsections, which may be divided into three categories.

- Subsections (1), (2) and (5) all deal with re-enlistment bounties and gratuities. These subsections are discussed in paragraph 5.634 below, and we are not proposing to rewrite them.

[4] [1967] 2 All E.R. 585

- Subsection (3) covers food and mess allowances. This subsection is rewritten in this clause and in clause 4.43.1.

- Subsection (4) covers training expenses allowances. This subsection is rewritten in clause 4.35.9 and in clause 4.43.1.

5.634 Subsections (1), (2) and (5) deal with re-enlistment bounties and gratuities under schemes set up in 1946 and 1950 for certain categories of military personnel who had seen active service, either during the second world war or in the years immediately following it. So far as we can discover, these schemes all came to an end many years ago. We have consulted with the Ministry of Defence who agree that these provisions should not be retained. We propose to leave out these subsections on the grounds that they are obsolete. Removing this unnecessary material will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.635 Subsection (3) confers exemption on two different categories of allowance, and in this clause we have found it helpful to deal with the two categories separately.

Clause 4.35.9 Reserve and auxiliary forces' training allowances

5.636 This is the second of two clauses rewriting provisions contained in section 316. This clause rewrites subsection (4) of that section. It is supplemented by clause 4.43.1.

5.637 This provision was litigated in Lush (HM Inspector of Taxes) v Coles (1967) 44 TC 169[5], where the taxpayer was an officer in the Civil Defence Corps who received a training bounty of £15 from local authority funds. The General Commissioners upheld the his appeal against an assessment under Schedule E on the grounds that the bounty fell within what is now section 316(4). But the Inspector's appeal to the High Court was successful, because Stamp J held that a sum paid out of local authority funds could not be described as being paid "out of the public revenue".

Crown Employees

Clause 4.35.10 Crown employees' foreign service allowances

5.638 This clause exempts allowances paid to Crown employees working abroad as compensation for the extra cost of having to live outside the United Kingdom. It rewrites section 319.

5.639 An allowance is exempt only if a certificate as to its purpose has been given by the Treasury or by an appropriate Minister. Subsection (3) lists the Ministers who, in addition to the Treasury, may give such a certificate. That list derives from the Transfer of Functions (Foreign Service Allowance) Order, SI 1996 No 313. It was varied by the Transfer of Functions (Lord Advocate and Secretary of State) Order, SI 1999 No 678 with effect from 19 May 1999.

5.640 When the legislation for this exemption was enacted in 1943 it was not intended that a foreign service allowance should in any way affect the recipient's liability to tax.

[5] [1967] 2 All E.R. 585

This is now dealt with in clause 4.43.1 - (General disregard of some exempted earnings for income tax purposes).

Consuls, foreign agents etc.

Clause 4.35.11 Consuls

5.641 This clause rewrites those parts of section 321 that relate to consuls of a foreign state. It ensures that any employment income earned as such a consul is exempt from tax. The clause reproduces the current definition of "consul".

5.642 The remainder of section 321 relates to other official agents of a foreign state, and is rewritten in clause 4.35.12. The exemption has fewer conditions for consuls than for other official agents. It therefore seems sensible to deal with the two categories separately.

Clause 4.35.12 Official agents

5.643 This clause rewrites the remaining parts of section 321, relating to official agents of a foreign state other than consuls.

5.644 Official agents of a foreign state are exempt from tax on their earnings in that capacity, unless they are Commonwealth citizens or citizens of the Republic of Ireland. The exemption does not apply if the employment is connected with any undertaking carried on for the purposes of profit.

5.645 The current definition of "official agent" has been restated in expanded terms in subsections (3) and (4).

Clause 4.35.13 Consular employees

5.646 Other consular employees of a foreign state are also exempt from tax on their earnings in that capacity if they satisfy certain conditions. This clause rewrites section 322(2) to (5).

5.647 Section 322 currently refers to consular officers and employees. We have dropped the reference to officers as they are outside subsections (2) to (5) rewritten in this clause.

5.648 Both the foreign state and the employee have to satisfy conditions for the exemption to apply.

5.649 First, the exemption only applies where Her Majesty names the foreign state by Order in Council as one with which the UK has a reciprocal arrangement. "Reciprocal arrangement" is a new term, defined in subsection (3). It describes an agreement between a foreign state and the UK to treat each other's consular employees similarly for tax purposes, ie as set out in this clause.

5.650 Second, the employee has to satisfy nationality conditions as set out in subsection (2).

5.651 The material in this Clause has been rearranged so that the conditions for exemption appear first, followed by the relevant definitions, with the mechanics of the Orders in Council completing the picture.

Visiting forces and staff of designated allied headquarters

Clause 4.35.14 Visiting forces and staff of designated allied headquarters

5.652 This clause rewrites part of section 323, which confers income tax benefits upon visiting forces and NATO staff.

5.653 Section 323 confers two income tax benefits:

- earnings paid by the government of a designated country or by a designated allied headquarters are exempt from income tax; and
- an individual to whom the section applies is not treated as resident in the United Kingdom by reason solely of being a member of a visiting force or of being attached to, or an employee of, a designated allied headquarters.

5.654 This clause deals with the first income tax benefit. We propose to deal with the second benefit in another Part of the rewritten legislation.

5.655 The exemption from income tax applies for several different descriptions of individuals:

- members of a visiting force of a designated country (see subsection (1));
- members of a civilian component of a visiting force of a designated country (see subsection (1));
- members of the armed forces of a designated country attached to a designated allied headquarters (see subsection (2)(a));
- members of a civilian component of the armed forces of a designated country attached to a designated allied headquarters (see subsection (2)(b)); and
- employees of a designated allied headquarters who come within a description agreed between the government and the other members of the NATO Council (see subsection (3)).

5.656 Two definitions needed for this clause are contained in Part I of the Visiting Forces Act 1952. These are the definitions of a visiting force (in section 12(1) of that Act) and of a member of a civilian component of a visiting force (in section 10 of that Act). We have not attempted to set out those definitions in this clause – partly for reasons of length and partly because we do not wish to lose the explicit link between this clause and the 1952 Act.

5.657 Section 323 is entitled "Visiting forces". The clause has a longer, more informative title.

5.658 We propose to amend the current cross-references to the Visiting Forces Act 1952. Subsection (5) of the clause contains a reference to "**Part I of** the Visiting Forces Act 1952" as opposed to the reference to "the Visiting Forces Act 1952" in section 323(4). The additional words were in section 367(3) of the Income and Corporation Taxes Act 1970 (the predecessor of section 323(4)). We have reinstated those words because the two most important interpretative provisions for present purposes, are in Part I of the 1952 Act and apply for the purposes of that Part. These are the definitions of a member of a civilian component of a visiting force and of a visiting force

5.659 Subsection (5) of the draft clause also corrects another minor drafting error in section 323(4). The present legislation refers to subsections (1) and (2) of section 323, and it is then stated that "**those subsections** shall be construed as one with the Visiting Forces Act 1952". However, the reference to a "civilian component" of a visiting force depends entirely upon subsection (4) itself; and no requirement is imposed to construe subsection (4) as one with the 1952 Act. We do not think there can be any doubt that the provisions of section 10 of the Visiting Forces Act 1952 must be applicable; and we have rewritten the provision on this basis. This is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.660 Section 323 is one of a number of provisions that confer tax benefits to visiting forces and NATO staff. Other provisions are:

- section 11(1) of the Taxation of Chargeable Gains Act 1992 (for capital gains tax);
- section 155 of the Inheritance Tax Act 1984 (for inheritance tax); and
- section 74 of the Finance Act 1960 (for stamp duty).

Detached national experts

Clause 4.35.15 Experts seconded to European Commission

5.661 This clause legislates Extra-Statutory Concession A84. It exempts from tax daily subsistence allowances paid by the European Commission to "detached national experts".

5.662 Detached national experts are people seconded to the Commission for periods from three months to three years, under a scheme introduced on 26 July 1988. They are experts in a particular field who advise and assist Commission officials.

5.663 To identify the people to whom the clause applies we refer in subsection (2) to the scheme established by the Commission on 26 July 1988. We have provided for the exemption from tax to continue in the event that the scheme is replaced by a new scheme having broadly the same effect.

5.664 The enactment of this concession is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposals to legislate this extra-statutory concession.**

Offshore oil and gas workers

Clause 4.35.16 Offshore oil and gas workers: mainland transfers

5.665 This clause legislates Extra-Statutory Concession A65. It applies to a limited number of employees who work on offshore oil or gas installations. Those whose "permanent workplace", as defined in clause 4.17.6, is the installation, would be chargeable to tax in respect of any transport, accommodation and subsistence provided. That is because the travel to that workplace would be travel between home and work, so no deduction could be claimed under Chapter 4.17 for that or for any associated accommodation and subsistence. Under Extra-Statutory Concession A65 such benefits are not charged to tax.

5.666 The concession states that no entries are needed on the P11D or P9D in respect of the benefits covered by it. Rewriting the concession as an exemption from income tax ensures there is no compliance burden attached to this provision.

5.667 The provision of transport exempted by this clause is confined to that part of the journey between home and work which starts at the mainland departure point from which the oil and gas rig workers are normally transported to the offshore installation. Apart from travel from the nearby overnight accommodation, it does not provide exemption for travel between the mainland departure point and a place other than the offshore installation.

5.668 If the employee has a permanent workplace on the mainland, the provision of transport to the installation is not exempt, but a deduction under Chapter 4.17 would be available. The same applies to the accommodation and subsistence in connection with such travel. This position is preserved in subsection (5)(b). This makes it clear that the exemption only applies to provision of transport, accommodation and subsistence where the travel is "ordinary commuting", or is part of an "ordinary commuting" trip, so that no deduction under Chapter 4.17 would be available in respect of it.

5.669 Legislating this extra-statutory concession is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments the proposal to legislate this extra-statutory concession.**

Miners etc.

Clause 4.35.17 Miners etc: coal and allowances in lieu of coal

5.670 This clause legislates Extra-Statutory Concession A6 which exempts from income tax cash payments to miners in lieu of free coal which they would have been entitled to receive by reason of their employment.

5.671 In practice, the Concession is also applied to retired miners and miners' widows. That aspect will be legislated in due course in the rewritten provisions for pension income.

5.672 It is Inland Revenue practice to extend the concession to the provision of smokeless fuel in place of coal. (This happens where the miners concerned live in a smoke control area). This practice is reflected by the inclusion of smokeless fuel in this clause.

5.673 It is Inland Revenue practice to interpret "miners" as meaning:

- all manual workers at a colliery on the surface or below ground, including those employed on screening and washing plant, haulage etc; and
- officials (overmen, deputies and shot firers) and weekly paid industrial staff.

The Inland Revenue practice (at SE 66695) specifically excludes clerical, administrative and technical staff, together with workers at coke ovens and brickworks etc.

5.674 In this clause we have brought together the various kinds of workers accepted under this practice as coming within the concession under the term "colliery worker". We have defined this in subsection (2).

5.675 Legislating this concession is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposals to legislate this extra-statutory concession.**

Chapter 4.39 – Exemptions: Priority share allocations

Introduction

5.676 This chapter rewrites section 68 Finance Act 1988. This exempts the benefit derived by directors and employees from a priority allocation of shares.

5.677 The legislation starts by granting a complete exemption from the charge as earnings in respect of any benefit derived from an entitlement to a priority allocation of shares. This points to the rewritten clauses being included in the chapters covering the exemptions from the charge as earnings.

5.678 However, in some circumstances the legislation brings back into charge the discount enjoyed by employees. It does so by excluding the relevant amount from the initial exemption. The rules for calculating this amount are different from the normal rules for calculating emoluments.

5.679 We considered putting the charge on the discount somewhere among Chapters 4.2 to 4.12 containing other charges as earnings. We could not easily do so because the charge is essentially a limit on the exemption. We have therefore included it alongside all the other material relating to priority allocations of shares so that all such material is in one place.

5.680 **We welcome views on this proposed approach.**

5.681 When section 68 Finance Act 1988 was enacted, it only dealt with relatively straightforward offers where there was a single public offer under which both members of the public and directors and other employees applied for shares including any priority shares.

5.682 Successive amendments catered for more complex share offers. These included offers where, because of legal and other technical issues, the priority shares for directors and employees were subject to a separate employee offer. Each new tranche of legislation was "bolted on" to what had gone before. This was done by imposing the fiction that the separate public and employee offers were in fact a single offer – "the offer".

5.683 This has led to some rather dense and convoluted legislation – particularly in the rules for the limits on the number of priority shares and the "similar terms" condition. In order to try to make the provisions easier to understand, we have abandoned that fiction and adopted the following structure:

- clauses 4.39.1 and 4.39.2 deal with single share offers;
- clauses 4.39.3 and 4.39.4 deal with share offers with separate public and employee offers; and
- clauses 4.39.5 to 4.39.8 deal with supplementary material, which is common to both.

We welcome views on the proposed re-structuring of the legislation.

5.684 We have not rewritten section 68(4) Finance Act 1988. That deals with the capital gains aspects. This will either not be repealed, or will be incorporated into the Capital Gains Tax Act.

5.685 We have not rewritten Section 68(6) Finance Act 1988, the original commencement provision, on the grounds that it is spent. This removal of unnecessary material will have no effect on anyone's liability to income tax. **We welcome comments on this proposed rewrite change**.

Exemption where single offer made to public and employees

Clause 4.39.1 Exemption: single offer to public and employees

5.686 As indicated in the introductory commentary to this chapter, clauses 4.39.1 and 4.39.2 deal with single share offers. This clause sets out the exemption.

5.687 The exemption in section 68(1) is expressed in terms of any benefit not being treated as an emolument. We have rewritten this as "is exempt from income tax as earnings". We believe that this is clearer and has the same effect. This is an example of one of the proposed rewrite changes with wide-ranging effect, see paragraphs 5.42 and 5.43 at page 33 in the introductory commentary to the clauses.

5.688 In subsection (1)(a), we have substituted "genuine" for "bona fide".

5.689 Subsections (3), (4) and (5) contain the conditions that have to be met before the benefit is exempt. In contrast to the current legislation, dealing with the conditions one by one should be clearer.

Clause 4.39.2 Discount not covered by exemption

5.690 This clause excludes from the exemption in clause 4.39.1 the benefit of any discount enjoyed by a director or employee in acquiring the priority shares. The discount therefore remains taxable as earnings.

Exemption where offer to employees separate from public offer

Clause 4.39.3 Exemption: offer to employees separate from public offer

5.691 As indicated in the introductory commentary to this chapter, clauses 4.39.3 and 4.39.4 deal with the situation where there are separate public and employee share offers. This clause sets out the exemption.

5.692 In subsection (1)(a), we have again substituted "genuine" for "bona fide".

5.693 In subsection (2), we have again expressed the exemption as "exempt from income tax as earnings". This is another example of one the proposed rewrite changes with wide-ranging effect. See paragraphs 5.42 and 5.43 at page 33 in the introductory commentary to the clauses.

5.694 Subsection (3) requires the case of each company whose shares are subject to the employee offer to be considered. The present fiction that the public offer and the employee offer are a single offer means that, reading subsections 68(2)(a) and 68(2C) Finance Act 1988 together, a company whose shares are **only** subject to the public offer also has to be considered. In such a case, the limit on the number of shares allocated to employees, imposed by section 68(2)(a), will never be exceeded. In re-writing, we have not mentioned these companies. This is a proposed rewrite change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.39.4 Discount not covered by exemption

5.695 This clause excludes from the exemption in clause 4.39.3 the benefit of any discount enjoyed by a director or employee in acquiring the priority shares. The discount therefore remains taxable as earnings.

5.696 Subsection (4) deals with the situation where the aggregate "notional price" of all the shares is different from the actual fixed price or the lowest tendered price. In those circumstances it is necessary to calculate the "appropriate notional price" for the shares in question. We have used a formula to try to make the basis of the calculation clearer.

Supplementary provisions

Clause 4.39.5 Meaning of being entitled "on similar terms"

5.697 This clause explains the condition that entitlement to a priority allocation of shares should be on "similar terms".

5.698 Subsections (4) to (6) only apply where the allocation of shares in a company for directors and employees of the company is different from the allocations for directors and employees of other companies.

Clause 4.39.6 Meaning and amount or value of "registrant discount"

5.699 The opportunity to acquire shares at a discount to the fixed price or lowest tendered price, subject to certain conditions, is a feature of many public share offers. This clause contains the definition of such a discount and retains the label of "registrant discount". It also describes how to calculate its amount or value.

5.700 In subsections (1)(c) and (2) we have used the label "subscribing employee" to describe those directors and employees who subscribe for shares under the offers and who comply with the same registration requirements as members of the public.

Clause 4.39.7 Application to directors and other office holders

5.701 To avoid the need to refer to both a director and an employee throughout this chapter, subsections (1) and (2) apply the legislation to a director as it applies to an employee. **We welcome comments on whether this is helpful or whether the approach of the current legislation is preferable.**

5.702 Section 68 Finance Act 1988 is unusual among the provisions dealing with employment-related shares in that it does not define "director". In subsection (3) we have, for the time being, used the definition of "director" from section 136(5)(b), which applies in relation to the grant of share options. Including this definition is a change to the law, but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.703 We intend to revisit this point when we consider the various definitions of "directors" and "employees" for other provisions dealing with employment-related shares.

Clause 4.39.8 Minor definitions

5.704 This clause contains the minor definitions used in Chapter 4.39.

5.705 Section 68 Finance Act 1988 is unusual among the provisions dealing with employment-related shares in that it does not define "shares". We have established that it is not intended to extend to public offers of securities. Consequently, we have used the definition of "shares" which appears in section 288 of the Taxation of Chargeable Gains Act 1992. Including this definition is a change to the law but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.706 We intend to revisit this point after we have considered the various definitions of shares (and stock and securities) used for the other provisions dealing with employment-related shares legislation.

Chapter 4.40 – Exemptions: payments to approved personal pension arrangements

Clause 4.40.1 Death or retirement benefit provision

5.707 This clause combines the exemptions currently available under section 155(4) and under Extra-Statutory Concession A72. The latter widens the scope of section 155(4), which only applies to death etc benefits payable to an employee's spouse, children or dependants. The concession covers death etc benefits payable to other members of the employee's family or household as defined in section 168(4).

5.708 An employee normally nominates to whom any death benefits should be paid. The exemption only applies if that recipient remains a member of the employee's family or household.

5.709 To the extent that this clause legislates Extra-Statutory Concession A72 it is a change to the law, but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposal to legislate this extra-statutory concession.**

Clause 4.40.2 Exemption of contributions to approved personal pension arrangements

5.710 This clause deals with contributions by an employer under the employee's approved personal pension arrangements. It rewrites the exemption at section 643(1). Such contributions are exempt from income tax as earnings of the employee.

5.711 Personal pension arrangements may be approved by the Board of Inland Revenue under section 631, in accordance with the rules of Chapter IV, Part XIV, ICTA 1988. The rules for approval of pension scheme arrangements are not yet rewritten.

5.712 Subsection (2) sets out the relevant definitions from section 630(1).

Chapter 4.41 – Exemptions: termination of employment

Redundancy payments

Clause 4.41.1 Limited exemption for statutory redundancy payments

5.713 This clause rewrites the parts of sections 579 and 580 relevant for employment income. The parts that are relevant for trading income have been rewritten at clauses 3.4.16 to 3.4.20 of Exposure Draft No 10, Trading Income of Individuals: Part 3. The clause provides an exemption for statutory redundancy payments and certain approved contractual termination payments, provided they do not exceed the amount of statutory redundancy payment that would otherwise have been made.

5.714 We have followed clause 3.4.16 in Exposure Draft No 10 in drafting by reference to an "approved contractual payment" as opposed to the "corresponding amount of any other employer's payment" – the expression currently to be found in section 579(1). We consider that the new expression makes the legislation easier to follow.

5.715 We have also introduced the expression "statutory payment" to describe the sum specified in section 579(6). Here too we consider that the new expression makes the legislation easier to follow. The introduction of this expression has also enabled us to dispense with the definition of "the Minister" in section 580(1)(c).

Outplacement benefits

Clause 4.41.2 Counselling and other outplacement services

5.716 This clause exempts from income tax the provision of counselling and other services in connection with the cessation of a person's employment. It rewrites sections 589A and 589B as they relate to an employee. The provisions that allow an employer to deduct expenditure in computing profits are rewritten in clauses 3.4.11 and 3.4.15 in Exposure Draft No 10 (*Trading Income of Individuals: Part 3*).

5.717 The exemption is subject to several conditions. One is that the employee has been employed by the employer for a continuous period of at least two years (section 589B(2)(c)). Under the Employment Rights Act 1996 some events that involve a change in the identity of the employer are treated as not breaking the continuity of employment. The Inland Revenue follows that approach in its interpretation of section 589B(2)(c). In subsection (3)(c) we say that the two year requirement relates to the employment that is ceasing, not to employment by the employer. It is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.718 Section 589B(4) limits travelling expenses to those which would be deductible under section 198 on the assumption that receipt of the services is one of the duties of the employment. The assumption is necessary because relief under section 198 is for amounts expended in the performance of the duties of the employment. Section 198 also requires that the expenses are incurred and defrayed by the employee out of the emoluments of the employment. An assumption that expenses are so incurred and defrayed ought to have been included in section 589B(4) for that provision to work as

intended, in the same way that it was included in section 200C(2)(b). Our practice has been to make that assumption in applying the exemption.

5.719 We have included such an assumption in subsection (3)(e)(ii). This is a change to the law but not to policy. It is in favour of the taxpayer.

5.720 Section 589(6) refers to travelling and subsistence expenses that would have been deductible under a specific provision, section 198. In this clause, we have instead referred to amounts that would have been deductible "under this Part". This general reference clearly goes wider than the current specific reference. In practice, however, we believe it will make no difference. The current reference already imports deductions under a number of other provisions, such as sections 193 to 195, which operate through, or are included in references to, section 198. (Further information on the interaction of those rewritten provisions can be found at, for example, paragraphs 5.27 to 5.30 of the introductory commentary to the clauses.) It remains that extended scope of section 198, as rewritten across a number of chapters, which will be relevant. Referring to this Part as a whole, rather than to a specific provision, is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.721 **We welcome comments on these three proposed rewrite changes.**

Clause 4.41.3 Retraining courses

5.722 This clause deals with the exemption from income tax of training course expenses for people whose employment has ceased or is expected to cease. It rewrites sections 588 and 589 as they relate to an employee. The provisions that allow an employer to deduct expenditure in computing profits are rewritten in Clauses 3.4.11 to 3.4.13 in Exposure Draft No 10, Trading Income of Individuals: Part 3.

5.723 Section 588(1)(b) requires a course to be undertaken with a view to retraining. That is, strictly speaking, a condition to be satisfied independently of section 589(3) and (4). Those subsections set out several conditions that must be satisfied if a course is to be regarded as undertaken with a view to retraining. Section 588(1)(b) implies a need to enquire into a person's reasons for undertaking a course. In practice such an enquiry is not made. A course is regarded as a qualifying course undertaken with a view to retraining if the conditions in section 589 are satisfied. We have therefore not reproduced the condition in section 588(1)(b). This has allowed us to group the other conditions more logically. It is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on this proposed rewrite change.**

5.724 In subsection (5) we have added an assumption that needs to be made about travel expenses. The same assumption is added, for the same reasons, in clause 4.41.2(3)(e)(ii). Reasons for the change are set out in paragraphs 5.718 and 5.719 of the commentary on clause 4.41.2. It is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.725 Section 589B(4) refers to travelling expenses that would have been deductible under a specific provision, section 198. In this clause, we have instead referred to amounts that would have been deductible "under this Part". Reasons for the change are

set out in paragraph 5.720 of the commentary on clause 4.41.2. It is a change to the law but not to policy. It will not affect anyone's liability to income tax.

5.726 We invite comments on these two proposed rewrite changes in paragraph 5.721.

Clause 4.41.4 Recovery of tax

5.727 In some circumstances the exemption provided by section 588 depends on future events. This clause rewrites, as regards the employee, the provisions that enable the exemption to be withdrawn if those events do not happen. They are essentially administrative rules that could be located with the other administrative rules we shall be rewriting. We believe it is more helpful to place them alongside the provisions relating to the exemption. **We welcome views as to whether it is helpful to include the rules here.**

5.728 The reference in section 588(5) to an assessment under section 29(1) of the Taxes Management Act 1970 applies only to an assessment for 1996/7 or a later year. The operative provision for an earlier year is section 29(3) as it stood before it was amended by sections 191 and 199 Finance Act 1994. We think that by the time the rewritten provisions are included in a Bill there will be no need to make provision for an assessment for an earlier year. If that is not correct an appropriate transitional provision will be included.

Chapter 4.42 – Miscellaneous exemptions

Clause 4.42.1 Accommodation, supplies and services used in employment duties

5.729 This clause rewrites section 155ZA which excludes from section 154 benefits arising from the provision of accommodation, supplies and services mainly used to perform an employee's duties of the employment, but also used to a minor degree for other purposes.

5.730 In subsection (7) the clause sets out the method for making the regulations provided for in subsections (4) and (5) – statutory instrument subject to the negative resolution procedure. This will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Clause 4.42.2 Subsidised meals

5.731 This clause combines the exemption for the provision of meals in a staff canteen currently in section 155(5) with Extra-Statutory Concession A74. The latter provides an exemption for the provision of any free or subsidised meals on the employer's premises where all the employer's employees are able to obtain such meals or have vouchers or tokens enabling them to obtain such meals, regardless of where those meals are obtained.

5.732 To the extent that this clause legislates Extra-Statutory Concession A74, it is a change to the law, but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposals to legislate this extra-statutory concession.**

Clause 4.42.3 Mobile telephones

5.733 This clause rewrites section 155AA, which excludes from section 154 the benefit arising from the provision of a mobile telephone. It is no longer necessary to make any special mention of mobile phones provided in connection with a taxable car, van or exempt heavy goods vehicle, as benefits provided in connection with such vehicles are adequately covered by clause 4.30.3. So we do not propose to rewrite section 155AA(3). This removes unnecessary material. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.42.4 Limited exemption for computer equipment

5.734 This clause rewrites section 156A, which provides a limited exemption in respect of computer equipment provided to employees or members of their families or households.

5.735 The exemption only applies where the employer provides the computer equipment for the use of the employee (or members of his or her family etc) rather than transferring it to him or her. In a case where the computer is given to the employee to keep, the benefit arising is still chargeable to tax in the normal way (see clauses 4.2.2, 4.4.2 and 4.12.1 in Exposure Draft No 6).

5.736 The exemption is not available in cases where the arrangements to provide computer equipment particularly favour directors. This does not mean that where an employer has coincidentally only provided computer equipment for directors or their families that the exemption cannot apply. The employer's provision of computer equipment has to be deliberately restricted to directors and their families for the exemption to be withheld. This is covered in section 156A(2), rewritten in this clause as subsection (4).

Clause 4.42.5 Overseas medical treatment

5.737 This clause rewrites section 155(6). It originated as an extra-statutory concession which was enacted in Finance Act 1981. There are two aspects of the exemption:

- the provision of medical treatment; and
- the provision of insurance against the cost of medical treatment.

5.738 As far as the first aspect is concerned, the exemption only applies where the provision of the medical treatment falls within the terms of Chapter 4.12 (currently section 154). There is no exemption if the payment for the treatment is handled in such a way that chargeability arises under clause 4.1.1(3)(a) (currently section 19(1) paragraph 1 and section 131), Chapter 4.5 (currently section 153) or Chapter 4.6 (currently sections 141 and 142).

5.739 The same applies to the provision of insurance. It is only direct provision which is exempt, so it does not cover reimbursement of the employee's premium for overseas medical insurance.

5.740 The reference to in-patient treatment is applicable to the whole section. This is to clarify that the insurance may also provide cover for in-patient treatment.

Clause 4.42.6 Care for children

5.741 Care facilities provided for the children of employees normally give rise to an employment-related benefit. The benefit of "workplace nurseries" is exempt from tax as a benefit if the facilities satisfy certain conditions. This clause rewrites section 155A. It contains the exemption and sets out the relevant conditions.

5.742 The conditions are grouped in the order:

- conditions applying to the child;
- conditions applying to the premises; and
- conditions applying to the employer.

5.743 Section 155A(3)(a) uses the term "parental responsibility". The definition of that term in section 155A(8) is a cross-reference to the Children Act 1989. In the rewritten clause we have used the definition in the Children Act and eliminated the cross-reference.

5.744 We have eliminated the reference in section 155A(6)(a) to the Nurseries and Child-Minders Regulation Act 1948. That Act was repealed by the Children Act 1989.

Clause 4.42.7 Repairs and alterations to living accommodation

5.745 This clause rewrites section 155(3). It only applies in the case of provided accommodation which falls within Chapter 4.7 published in Exposure Draft No 6. It was introduced by Finance Act 1977 when section 145 (rewritten in Chapter 4.7) was enacted, as that change affected the treatment of expenditure in connection with accommodation.

5.746 In the case of alteration and additions to the property within subsection (1)(a), the cost would sometimes result in an increase in the cash equivalent under Chapter 4.7. In order to prevent a double charge to tax it is necessary to exempt the cost of the alterations and additions which fall through to Chapter 4.12 because the cost of provision was "not otherwise chargeable to tax".

5.747 The second part of this exemption at subsection (1)(b) refers to landlord's repairs, the definition of which prevents it extending to tenant's repairs, or improvements disguised as repairs.

Clause 4.42.8 Suggestion awards

5.748 This clause together with clause 4.42.9 legislates Extra-Statutory Concession A57, (suggestion scheme awards). The concession originated during the last war. It exempts from tax certain awards, up to specified limits, which are made to employees for suggestions that result in improvements to efficiency or have some other intrinsic merit. Such awards would normally represent emoluments of an employment.

5.749 Legislating this concession is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposals to legislate this extra-statutory concession.**

5.750 Subsection (1) exempts the suggestion award from tax. Subsections (2) to (5) explain, by a series of definitions, what is meant by a "suggestion award" and in this way provide all the conditions that must be satisfied for the exemption to apply. The monetary limits are dealt within the following clause 4.42.9. We consider both these approaches provide greater clarity than the list of conditions in the extra-statutory concession.

5.751 Subsection (2) distinguishes two types of award, defined at subsection (4), and requires that both must be made under a suggestion scheme, itself defined at subsection (5).

5.752 Subsection (3) sets out the conditions that both types of suggestions must meet. These conditions are found in paragraph (b) of the extra-statutory concession. Broadly the suggestion must be outside the scope of the employee's normal duties. The obvious, but important, condition at subsection (3)(a) is considered self-evident in the extra-statutory concession.

5.753 Subsection (5) is a refinement of the present requirement that a suggestion scheme should be open to "all employees". This subsection recognises that schemes may be open to only a division, either vertical or horizontal, of a workforce. The important factor is that all employees within that division should compete on equal terms. The extra-statutory concession requires that the scheme should be "formally constituted". We believe that the word "scheme" is sufficient to cover this requirement.

5.754 The extra-statutory concession includes a proviso that the exemption does not apply to any tax liability on sums derived from the exploitation or disposal of rights in something that the employee has invented. We have not reproduced that proviso as we consider the exemption from income tax "under this Part" (in subsection (1)) makes it sufficiently clear that only employment income is affected.

Clause 4.42.9 Suggestion awards: "the permitted maximum"

5.755 This clause provides the monetary limits for exempting awards which satisfy the conditions in the previous clause. The limit in each case is called "the permitted maximum".

5.756 Subsection (1) provides the permitted maximum for an encouragement award while the remainder of the clause deals with profit-related awards.

5.757 Under subsection (4) the overall permitted maximum for profit-related awards is £5,000 or, if less, an amount linked directly to the financial benefits that arise from the suggestion.

5.758 Where more than one award is made for the same suggestion on the same occasion, the overall permitted maximum is shared out proportionally - subsection (2). Under subsection (3), awards made on a later occasion attract any of the overall permitted maximum remaining after allocation among previous recipients.

5.759 When an extra-statutory concession contains monetary limits, the amount can be changed by press release or by republishing it with different amounts. This is not possible for legislation. There are a number of exemptions in current legislation in which an amount is fixed by the Treasury. We have adopted this approach for rewritten concessions and have drafted a general power for the Treasury to increase the amounts at clause 4.48.1. This provision is listed there.

5.760 Subsection (5) defines the terms used in subsections (2) to (4).

Clause 4.42.10 Long service awards

5.761 This clause legislates Extra-Statutory Concession A22 (long service awards). The concession was introduced in the mid-1970s when employers had begun to give employees long service gifts other than the traditional clock or watch. It was restricted to tangible articles or shares of a defined kind to prevent cash payments that would properly be charged under section 19(1) paragraph 1 being dressed up as long service awards.

5.762 Subject to the permitted maximum amount, the concession exempts the award from income tax.

5.763 When an extra-statutory concession contains monetary limits, the amount can be changed by press release or by republishing it with different amounts. This is not possible for legislation. There are a number of exemptions in current legislation in which an amount is fixed by Treasury order. We have adopted that approach for rewritten concessions and have drafted a general power for the Treasury to increase the amounts at clause 4.48.1. This provision is listed there.

5.764 In practice, the concession is applied more liberally than a strict interpretation of it would permit. For example, the provision by the employer of a holiday or a life membership to (say) the National Trust as a long service award would be treated as covered by the concession. We believe that we have brought within the scope of this clause all the types of award currently treated as being within the concession.

5.765 The concession does not restrict qualifying service to "the same employer" in the same way as the definition of a long service award in subsection (2). However, in practice the concession is applied so that the service must be with the same employer unless there has been a change of employer of the kind described in subsection (5).

5.766 The definition of "group" adopted means that the minimum possible group relationship will enable the exemption to apply.

5.767 The proposal to legislate the concession is a change to the law but not to policy. Is it in favour of the taxpayer. It will not affect anyone's liability to income tax. **We welcome comments on the proposal to legislate this extra-statutory concession.**

Clause 4.42.11 Small gifts from third parties

5.768 This clause legislates Extra-Statutory Concession A70A. The conditions for the exemption are in similar terms to the entertainment exemption at clause 4.32.5. The reasons for it are the same, namely to remove the compliance problems if the conditions in subsection (4) are met. Those conditions include a limit on value and a restriction to gifts of goods.

5.769 The concession also extends to non-cash vouchers and credit-tokens. That aspect is dealt with in clause 4.33.5.

5.770 This is a change to the law but not to policy. It is in favour of the taxpayer. **We welcome comments on the proposal to legislate this extra-statutory concession.**

Clause 4.42.12 Interpretation of Chapter 4.42

5.771 The phrases "members of the employee's family" and "family or household" appear in various places in this chapter. This clause uses the definition of those phrases in clause 4.4.5.

Chapter 4.43 Exemptions: supplementary provisions

Clause 4.43.1 General disregard of some exempted earnings for income tax purposes

5.772 This clause ensures, in appropriate cases, that the income concerned is not only exempt from tax but is also disregarded for all other income tax purposes.

5.773 Exemptions from income tax for employment income are currently expressed in a number of ways. For example:

- "shall not be regarded as income for any purpose of the Income Tax Acts" – section 200(1) (expenses of Members of Parliament);
- "shall be exempt from income tax" section 322(2) – (income from employment, consular officers and employees);
- "no charge to tax under Schedule E shall arise in respect of" – section 589A(4) (counselling services for employees);
- the employee "shall not be taxable under Schedule E" – section 157(3) (cars available for private use);
- "shall be exempt from income tax under Schedule E as emoluments" – section 190(1) (payments to MPs and others);
- "shall not be regarded as emoluments of the office or employment for any purpose of Schedule E" – section 200A(1) (incidental overnight expenses); and
- "the emoluments of the employee from the office or employment shall not be taken to include …" – section 200B(2) (work-related training provided by employers).

5.774 Broadly, the current forms of expression fall into two categories. One provides for the income to be disregarded for tax purposes. The other simply confers an exemption from income tax. As explained in previous Exposure Drafts we have tried to introduce some much-needed consistency by using only the clearest and most straightforward form of expression – "is exempt from income tax". (See paragraphs 5.42 and 5.43 of the introductory commentary to the clauses).

5.775 This form of words obviously exempts income from the direct charge to tax. It also exempts income from an indirect charge to tax, allowing it to be left out in computing profits chargeable to income tax and losses. See Hughes v Bank of New Zealand (CA 1936) 21 TC 472[6]. In addition, the income may be ignored for the purposes of notifying chargeability and making income tax returns.

5.776 However, the income is only exempt from income tax. Unlike, for example, expenses of Members of Parliament as exempted by section 200(1), it continues to be income. And it is not disregarded for any other income tax purposes.

[6] (HL)[1938] A.C. 366

5.777 For the provisions listed in this clause which derive from legislation the current form of the relevant exemption goes further than a simple exemption from the charge to tax. It also disregards the income in question for all purposes of income tax.

5.778 Some of the provisions listed are rewritten extra-statutory concessions. We have included them here because in practice the income they cover is disregarded for all tax purposes. They are parts of the changes under which we propose to enact Extra-Statutory Concessions A6, A22, A57, A58, A59, A65, A66, A70A, A70B and A84.

Clause 4.43.2 Exempted amounts not to be treated as earnings or emoluments

5.779 As explained above, exemptions from income tax for employment income are currently expressed in a number of ways. Subsections (1) and (2) of this clause deal with a collection of exemptions which are limited in scope. The types of income in question are not totally exempt from income tax. For example, the income may only be exempt from income tax "as an emolument of the office or employment" (section 197A, car parking facilities). Consequently it may be taxable in some other way: the income tax charge under Schedule E includes a number of free-standing charges as well as the three Cases applying for emoluments.

5.780 Under section 190, certain grants and payments made to MPs etc when they leave Parliament are "exempt from income tax under Schedule E as emoluments". The legislation then makes it clear that this does not prevent tax being charged under section 148, payments in connection with termination of employment. Unfortunately other provisions are not so helpful and it is difficult to tell whether other tax charges are intended to apply.

5.781 If no other tax charges do apply we would like to say simply that the income "is exempt from income tax" – there is no point in preserving the appearance of another tax charge being applicable if there is no such tax charge. But obviously we cannot say that where other tax charges do apply. So we need to do more work to discover the exact scope of these limited exemptions.

5.782 At the moment, subsection (1) exempts the income concerned from tax as earnings for all Schedule E purposes. This would prevent other tax charges applying. But we do not yet know the actual effect of the words used in each particular exemption. We have not yet rewritten most of the free-standing Schedule E charges. Until we do that we will not be able to determine the relevance of these charges for each of these exemptions.

5.783 Subsection (1) also stops the income concerned from being treated as earnings for all other Schedule E purposes. We have not yet rewritten all aspects of Schedule E. Until we are nearer the end of our work on employment income we will not be able to determine whether there would be any other Schedule E consequences of extending the scope of these exemptions. And we also need to consider whether there would be any wider consequences – for example, for National Insurance Contributions or for reliefs relating to pension contributions.

5.784 In the meantime, subsections (1) and (2) are markers.

5.785 Subsections (3) and (4) deal with exemptions which are limited in a slightly different way. Paragraph 1 Schedule 11A covers various removal benefits and expenses and says "the employee shall not … be regarded as receiving emoluments of the employment for any purposes of Case I or Case II of Schedule E".

5.786 Again, we need to do more work to discover just what effect these exemptions may have. In the meantime, subsection (3) reproduces the current position.

Chapter 4.48 – Supplementary provisions

Clause 4.48.1 Alteration of amounts by Treasury order

5.787 This clause bring together several separate powers for the Treasury to upgrade certain monetary amounts which are specified in the statute without having to go through a Finance Bill.

5.788 The powers relating to the following provisions are new:

- section 4.32.4(2) and (3), annual parties and functions;
- section 4.42.9(1) and (4), suggestion awards: "the permitted maximum";
- section 4.42.10(2), long service awards; and
- section 4.42.11(2), small gifts from third parties.

5.789 They are part of the changes under which we are enacting Extra-Statutory Concessions A22, A57, A70A and A70B.

5.790 The other powers appear in current legislation.

5.791 In subsections (1) and (5) the clause sets out the method for making the regulations – statutory instrument subject to the negative resolution procedure. This will not be required if a provision equivalent to section 828 is included in the Income Tax Act.

Clause 4.48.2 Interpretation of this Part

5.792 This clause sets out definitions for terms that have a common meaning and are used throughout the provisions rewritten so far.

5.793 We have used the same definition of "personal representatives" as first appeared in clause 6.4.28 in Exposure Draft No 2. Current legislation uses different definitions for different purposes. (See, for example, sections 229(1) and 701(4) and section 111(3) Finance Act 1989.) This definition simplifies the vocabulary, does not include references to other (non-tax) legislation, and can be applied to different jurisdictions (within and outside the United Kingdom). It also replaces references to "executors and administrators" in some clauses (for example clause 4.23.7). See paragraph 5.405 of the commentary on page 87. It is a change in the law but not policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

5.794 "Workplace", as defined in this clause is a term used in a number of the exemptions particularly those in Chapter 4.30. The current legislation for most of those exemptions does not have such a definition. The introduction of the definition is therefore a change to the law, but not to policy. It will not affect anyone's liability to income tax. **We welcome comments on this proposed rewrite change.**

Clause 4.48.3 Index of defined expressions

5.795 This clause provides a list of defined expressions.

Updated Framework For Income Tax For Individuals

Part	Description
General provisions	
1	CORE PROVISIONS
2	MAIN OBLIGATIONS AND RIGHTS
Income subject to tax (computational rules)	
3	TRADING INCOME
4	EMPLOYMENT INCOME
5	PROPERTY INCOME
6	SAVINGS & INVESTMENT INCOME
7	PENSION INCOME
8	SOCIAL SECURITY INCOME
9	FOREIGN INCOME
10	MISCELLANEOUS INCOME
Exemptions and reliefs	
11	EXEMPT INCOME
12	LOSSES AND RELIEFS (against general income)
13	PERSONAL ALLOWANCES (against total income)
14	RELIEFS GIVEN AT SOURCE
15	DOUBLE TAXATION
Other rules	
16	TAX AVOIDANCE
17	SPECIAL TYPES OF INDIVIDUAL
18	ADMINISTRATIVE PROVISIONS
19	MISCELLANEOUS

Income Tax Bill

Part 1 – Core provisions

Chapter 1.1 – Overview of Act

Plan of Chapter

1.1.1	General scope of Act
1.1.2	Charge of income tax for tax years
1.1.3	Administration of income tax
1.1.4	Main obligations of individual taxpayers
1.1.5	Income charged to income tax

1.1.1 General scope of Act

This Act is about income tax and contains provisions relating to the obligations and rights of individuals in connection with that tax.

Defined terms:

Origin: drafting

1.1.2 Charge of income tax for tax years

(1) Income tax is charged for any tax year for which Parliament so determines.

(2) A ***tax year*** means a year beginning with 6th April and ending with the following 5th April.

References to ***the tax year 2001-2002***, and similar references, are to the tax year beginning on 6th April in the year first mentioned.

Defined terms:

Origin: subs.(1) – ICTA s.1(2), drafting; subs.(2) – ICTA s.832(1) “the year 1988-89”.

1.1.3 Administration of income tax

Income tax is under the care and management of the Board of Inland Revenue, referred to in this Act as ***the Board***.

Functions of ***the Inland Revenue*** may be exercised by any officer of the Board.

Defined terms:

Origin: TMA s.1(1), drafting.

1.1.4 Main obligations of individual taxpayers

Part 2 makes provision about the main obligations of individual taxpayers.

These include provisions about:

keeping and preserving records,

making a return,

self-assessment, and

payment.

Defined terms:

Origin: drafting.

1.1.5 Income charged to income tax

(1) Income tax is charged in accordance with this Act on all amounts charged to income tax under the provisions of this Act or any other enactment.

Unless otherwise provided, references in this Act to ***income*** include anything that is or may be the subject of a charge to income tax.

(2) Parts 3 to 10 of this Act deal with the following kinds of income:

Part 3: trading income

Part 4: employment income

Part 5: income from land

Part 6: savings and investment income

Part 7: pension income

Part 8: social security income

Part 9: foreign income

Part 10: miscellaneous income.

Defined terms:

Origin: subs.(1) – ICTA s.1(1), drafting; subs.(2) – drafting.