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To: Selection and Member Services Committee – 9 July 2013
Member Remuneration Panel – 10 July 2013

Subject: Members' Travel Expenses

Summary: To consider options to mitigate the impact of a recent ruling by Her Majesty's Revenue & Customs (HMRC) on taxing Members' home to office travel claims

1. Background

- (1) Members may claim travel expenses when representing the Council on official business, subject to certain provisions¹. The taxation aspects are set out on the HMRC website².
- (2) The current mileage rate for a Member undertaking KCC business is 45p per mile for the first 10,000 miles and 25p per mile thereafter (in any one tax year), which is the maximum permitted by HMRC without being subject to income tax. Public transport costs can be fully reimbursed for business travel.
- (3) As office holders, Elected Members are normally regarded as having two places of work: their own home and the strategic headquarters of the authority, which is why Members (unlike officers) can claim the cost of mileage between their own home and County Hall. However, HMRC has recently reiterated that reimbursement of travel from home to County Hall is subject to the deduction of income tax and National Insurance Contributions (NICs), unless the Member routinely sees constituents in their own home. According to HMRC, the fact that a Member might read Council papers or complete correspondence at home does not make that home a distinct place of work for the purposes of claiming tax relief on travel expenses.
- (4) Reimbursement of travel expenses from a Member's home to other KCC offices or other places when representing the Council on official business is not subject to tax. However:
 - Members must be able to show that attendance at the particular place was necessary to perform their representative duties; and
 - If such a journey is substantially the same as travel from home to County Hall, then HMRC will not accept that it qualifies as a business journey³.

¹ In accordance with (1) the Members' Allowances Scheme adopted by the County Council and (2) paragraphs 16-19 of New Council Constitutions: Guidance on Regulation for Local Authority Allowances (DCLG): (<http://minutes.southend.gov.uk/akssouthend/images/att3790.pdf>)

² <http://www.hmrc.gov.uk/manuals/eimanual/eim65960.htm>

2. Negotiations with HMRC

- (1) The Council has made numerous representation to the HMRC with regard to their interpretation of these rules since 2011. The Council has sought to argue that the rules are arbitrary, outdated and impractical for the following reasons:
- KCC has one of the largest local authority areas in the UK; some Members travel in excess of 12,000 miles per year and deducting tax from those expenses penalises individuals and could deter others from serving the public by being or becoming an elected representative. In this respect, the rules penalise large County areas, compared to small District or London Borough areas, which are often significantly smaller and have excellent public transport links.
 - There are 'double standards' in the legislation in that members of the UK Parliament, the Welsh National Assembly, the Scottish Parliament and the Northern Ireland Assembly, in defined circumstances, are all able to claim tax relief on constituency to Parliament mileage claims whereas local government councillors cannot claim tax relief on home to office claims.
 - A commonsense approach to health and safety means that it is not appropriate for elected Members to routinely open up their own homes to members of the public not known to them, which is particularly relevant for Members who live alone.
 - Advances in technology since HMRC's rules were introduced mean that elected Members are able to 'meet' with constituents in many different ways as effectively as meeting in person, e.g. via social media, video-conferencing and Skype, and a number of Members use these new technologies to deal with constituents' enquiries.
 - The public cost of administering the rules will increase even after taking into account the additional revenue raised and the complexity of the rules will almost certainly result in inadvertently incorrect submissions.
- (2) All of these arguments have been rejected by HMRC as being irrelevant and in March 2013, HMRC wrote to KCC confirming that they did not agree that Members can treat their own home as a workplace if they do not routinely see constituents there. It is clear from this letter that KCC must apply the relevant HMRC regulations relating to home to office mileage, which for most Members will mean that such journeys are subject to deductions for income tax and National Insurance.
- (3) Whilst HMRC's guidance may seem to be arbitrary, outdated and impractical, it nevertheless represents the current legal requirements, and a failure to comply with it would expose the Council and individual Members to fines and liability for tax arrears.

³ HMRC will normally regard such journeys as normal commuting unless the extra distance involved is ten miles or more each way.

3. Current Position

- (1) Having not succeeded in persuading HMRC to amend or disapply their rules, KCC had prepared to implement the rules with effect from 1 May 2013. However, at the Selection and Member Services Committee meeting on 5 June, Members asked officers to delay the implementation whilst a further approach was made to HMRC at the most senior level. The Committee also asked officers to prepare a detailed report for consideration by the Member Remuneration Panel, setting out proposals for Members' mileage expenses that will enable the County Council to comply with all necessary legal obligations whilst ensuring, as far as possible, that the financial implications for Members are cost-neutral.
- (2) It should be reiterated that if members do regularly see constituents in their own homes, they should declare this and consequently there would be no tax liability on home to office travel claims.
- (3) Going forward, the options available to the Council appear to be as follows:

Steps / Options	Impact
Step 1. Comply with the HMRC rules and deduct tax from home to office mileage claims unless the Member routinely sees constituents in their own home	<ul style="list-style-type: none"> ● We have to do this, regardless of any other options we consider. This will make us legally compliant ● Compliance with the rules will cost KCC an estimated additional £12k for employer Class 1 NICs
Or; Do not apply the rules	<ul style="list-style-type: none"> ● Not an option, as this would be unlawful and would result in fines, backdated liabilities and criminal prosecution
Option 1. Do not mitigate the impact of the tax and NICs deductions	<ul style="list-style-type: none"> ● This will increase the cost of being an elected representative, particularly for those who travel long distances to County Hall and may deter some people from seeking election/re-election ● The maximum impact on any Member, based on 2012/13 travel claims, would result in a reduction of their 'take home' amount, including their basic allowance, of 12% ● The average impact (although no one Member fits the 'average') for an individual on basic rate tax and in receipt of the full personal tax allowance, would result in a reduction of their 'take home' amount, including their basic allowance, of 2.7%

	<ul style="list-style-type: none"> ● It would have a nil impact on a handful of Members
Option 2. Increase the mileage rate for those journeys that are subject to deductions for tax under HMRC rules (i.e. home to office journeys) to compensate for the basic rate tax and NICs (even where the individual Members doesn't pay NICs)	<ul style="list-style-type: none"> ● As close to cost-neutral as possible for Members (without multiple rates and huge complexity) but greater cost for the Council (approximately £45k in addition to Step 1) ● More complicated to administer as there will be two different rates for mileage ● More complicated system prone to inadvertent error
Option 3. Subject to HMRC approval, introduce a flat-rate allowance for home to office travel, based upon geographical zones and perhaps a separate multiplier depending on a Member's Council role	<ul style="list-style-type: none"> ● Could work out as cost-neutral for the Council, but would have some winners and many losers at the individual Member level ● Would need different rates for those Members who need to attend County Hall more frequently than others; potentially three bands ● Potentially more difficult to administer both for Members and the Council ● Could inadvertently lead to increased costs for the Council

4. Financial implications

- (1) Calculating the financial implications to a precise figure is impossible. This is because:
- a) We have 38 new Members of the Council in respect of whom we have no travel history on which to base future costs
 - b) Without examining every Member's travel claim for every month, home to office mileage is not known with precise accuracy
 - c) The new rules may change travel behaviour
 - d) The age of the Member claiming travel affects their deductions
 - e) The marginal rate of tax individual Members are liable to pay is either 20%, 40% or 45%

The following figures should therefore be seen in the context of a best estimate.

- (2) Step 1 above is a 'must-do', the estimated cost of which is £12k, comprising the additional employer Class 1 National Insurance contributions the Council will have to make. This cost is unavoidable whichever other option is adopted.

- (3) Ignoring Step 1 is not an option, as should we fail to administer a compliant scheme, the financial cost be in the hundreds of thousands of pounds.
- (4) Option 1 would have no cost to the Council other than the £12k shown at Step 1, but would cost individual Members an aggregate of around £45k, ranging at a personal level from zero to potentially £2,800.
- (5) Option 2 shows an estimated additional cost of £45k. This is based on the following calculation:
 - 2012/13 travel claim = £138k
 - Assume 65% of these claims are home to office journeys = £89k
 - For the tax and NICs to have nil impact on Members who pay basic rate tax and are under state retirement age, the rate per mile would need to increase from £0.45 to £0.662, an increase of 47%. This rate is based upon the basic rate of tax, and would only apply to home to office mileage, not business mileage. Claims for public transport would need to be uplifted in line with this
- (6) Option 3 could be worked to have a cost neutral position to either the Council or to Members, but not both. Almost all Members would either win or lose, although this may result in a change of travel behaviour. If the Member Remuneration Panel recommended this option, officers would work through options based on the overall funding pot set, and the differing levels proposed, e.g. Cabinet Member gets double the flat-rate home to office allowance, Committee Chairmen and/or members of particular committees get 1.25 of the flat-rate allowance, and all other Members get the flat-rate allowance. At the core of this option would be the geographical distance. An illustrative example is shown at **Appendix 1**.

5. Conclusions

This report has identified that:

- a) we must comply with legislation and therefore the necessary deductions for tax and NICs from Members' travel claims must be made with effect from [insert date]
- b) this will adversely impact on most Members' net 'take home' sums
- c) there are options available that could mitigate the impact of 2) above, although the complexity of our tax system means we cannot make this entirely neutral for every single Member and will incur additional costs for the Council
- d) Members of the Remuneration Panel should be asked to consider the options set out in this paper

Background Papers:

None

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