Finding the right route

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Marion Hodgkiss and *Michael Steed* look at where the travel and subsistence rules went wrong, and what might be done to fix them

Key Points

What is the issue?

Unclear and unnecessarily complicated legislation that needs redrafting, especially in the face of changing work practices

What does it mean to me?

Just how difficult it is to advise clients in this common, but complex area

What can I take away?

The suggested solution is revised legislation and merged concepts for both self-employed and employed people

Imagine the following scenario: Stuart and Jean are married and live in York. Stuart is self-employed and works from home traveling to clients in his capacity as a consulting engineer. None of his travel is regular and he responds to client requests for his services.

Jean is employed and works locally. Both have been offered the opportunity to work in London for 12 months in their separate professional lives.

Their working week for the work in London is as follows: they both get up very early on a Monday morning and they drive down to London. They stay in a modest B&B, eating out in the evening and then after work on Friday, they retrace their footsteps back to their home.

The question, simply put, is – what is all of this for tax relief purposes? – what can they claim and what is disallowed?

The basic shape of the legislation

The obvious point to make is that there are two separate sets of rules for what is essentially the same bit of travel and subsistence – the self-employed rules with its own vocabulary and the different employed rules with its own lexicon.

Let’s start with Stuart. He is principally bound by the iron grip of ITTOIA 2005, s34, which provides that he will only get relief for expenditure ‘wholly and exclusively’ incurred for a business purpose.

We do not propose to walk through the principles and case law here, beyond noting that although it trips off the tongue quickly, we all know how difficult it is in practice to apply the ‘wholly and exclusively’ rule and to be able to separate a business purpose from a private purpose.

Do Stuart’s accommodation costs meet that test?

Case law, such as *Tim Healy v HMRC* [2015] TC04425, *Newsom v Robertson* [1952] 33 TC 452 and *Horton v Young* [1971] 47 TC 60, all suggest that there are some core principles that must not be offended. The *Newsom* logic (an elegant Lord Denning judgement) is that where you live and the 'base' from which you start your trade are in many, if not most, circumstances, different places and the upshot of this is that travel and subsistence costs are not allowable between home and the base. Costs beyond the base are generally allowable. In this regard, we also note that the rise of live/work units would actually simplify this!

So, back to Stuart; if Stuart's work pattern was that he worked in many parts of the country for contracts of say a few weeks and that this pattern was unpredictable and in response to client demand, then to our eyes, the decided cases suggest, but do not definitively say, that he is an itinerant worker (using *Horton v Young* logic), whereby all his travel would be allowable.

But there is an immediate problem. The cases do not allow us to identify a time beyond which the itinerant rules will no longer apply; to be able to say, for example, that a contract length of three months is fine and you will still be an itinerant worker, but any longer and you will acquire a base where you work.

Case law does, however, address extreme examples, so in *Hanlin v HMRC* [2011] UKFTT 213 (TC) the taxpayer claimed, inter alia, overnight accommodation costs of £4,800 for staying in Dungeness during the week (48 weeks, four nights each week, £25 per night) while maintaining a home in Coventry. The taxpayer had been working on a particular contract in Dungeness for some seven or eight years. Not surprisingly, the FTT found that the accommodation expenses were not deductible. The taxpayer had chosen to live away from his base of operation (we make no comment about whether in this case, the taxpayer was self-employed in the first place).

So there seems to be a cut-off beyond which a person will no longer be an itinerant worker and will acquire a base of work. But the legislation is silent on when this is and we think that there is a case for changing this – see our conclusions below.

What if Stuart decided to stay in a hotel, or a club? Why should that make a difference? And yet it does – you only have to re-read the *Healy and Elwood (Elwood (H M Inspector of Taxes) v Utitz* (1965) 42 TC 482), judgements to see that.

The reasons for this are simple. The wholly and exclusively rule allows for some stretch, but not too much.

Section 34(2) allows for an identifiable part of dual business/private expenditure to be extracted and allowable (this is useful for say car expenses that are used for both business and private use), but more subtly still, and on decided case law (such as *Elwood*) allows for some incidental private use to be allowed to stand and not to contaminate the 'wholly and exclusively' principle.

Therefore, in *Elwood*, staying in a club, which according to the Revenue 'afforded extra advantages' that would kill the wholly and exclusively requirement, the court rejected that assertion and allowed a stay at a London Club when visiting London on business as an alternative to staying in a hotel.

Elwood also allows us to conclude that staying in a hotel is generally allowable, but staying in a club potentially pushes a taxpayer over the line, unless the 'extra advantages' are incidental and can be allowed to stand.

So for Tim Healy, not staying in a hotel and choosing an apartment instead placed himself in harm's way and into the jaws of the fatal duality of purpose. His fate was sealed by asserting that he wanted the apartment to entertain his family and friends.

Our conclusions and comment

On the basis of the above cases, it seems likely that Stuart would struggle to claim tax relief for his travel costs to London, given the length of the assignment.

Ironically, he may fare better by incorporating and claiming under the temporary workplace rules discussed below.

But we return again to the uncertainty in this common and important area of giving advice. The cases are infinitely variable.

A better way may be to suggest say a three month limit on itinerant status, beyond which the itinerant status is lost? This has the merits of certainty, equity and clarity.

Perhaps a more fundamental adjustment to the legislation is required.

Given the uncertainty that the s 34 test has engendered, dare we slaughter sacred cows and suggest that the phrase could be scrapped and replaced by a ‘solely’ test with a legislative easing for ‘incidental’ private use?

We are also struck by the judgments in *Dr Samadian v HMRC* [2014] UKUT 0013 (TCC) and *Dr David Jones* (TC4643) and indeed for any sole trader who does as least some of his or her work at home, and would offer for discussion a homeworking allowance along the lines of the ITEPA 2003, s 316A allowances of £4 per week for employed people, that would be a sensible way forward to cover homeworking costs.

So what about Stuart’s subsistence?

For years the *Caillebotte v Quinn logic* [1975] 50 TC 222, ruled, and applied the wholly and exclusively logic to self-employed taxpayers who ate and drank in the course of their self-employment.

The *Caillebotte* logic specifically covered a building contractor’s daily lunchtime sandwich, so advisers were still struggling with an evening meal.

In 2009, the ITTOIA legislation was modified with the insertion of s 57A, which codified and slightly ameliorated the harsh logic of the *Caillebotte* decision and now specifically allows for subsistence costs (reasonable expenses on food and drink), where travel is occasional and outside of normal travel patterns, or for itinerant trades.

So, the courts have generally accepted that if travel is allowable, the reasonable food costs say for evening eating is also allowable (see also BIM47705).

This effectively tells us that if Stuart is struggling to get a deduction for his travel, then he will also struggle with his subsistence costs, and even if the circumstances were such that he could claim travel and subsistence costs, travelling and staying with Jean raises the spectre of duality of purpose (the pleasure of her company in the same B&B) and even whether they could both claim tax relief for effectively the same travel.

We are always surprised by how diversely deductibility of subsistence costs is interpreted by practitioners and we regularly hear at conferences for example, that some advisers will allow alcohol and some will not – perhaps the Temperance movement has come to tax.

Certainly we cannot find any legislative suggestion that alcohol is a pleasure and therefore next to sin and therefore taxable. So have a drink on the Chancellor (see also BIM47705)!

We also wonder if in the name of simplicity sole traders should be allowed to have flat rate deductions for food and drink that are available for employees.

So, we cannot but conclude that in the absence of an effort to redraft the legislation in clearer terms for the self-employed, the rules will remain a box of sundered fragments.

The employed travel and subsistence rules

So, now let's turn to Jean.

Jean is clearly employed, so we drop all references to the language of self-employed. We shift to ITEPA, ss336 to 339) and the core rule that distinguishes a permanent workplace and a temporary workplace.

This distinction has been around for years now and it's probably fair to say that it works on most days of the week for simple situations where an employed worker has one permanent workplace and occasionally travels to temporary workplaces.

In the absence of any contravening facts, it would seem that Jean is travelling to a temporary workplace (TW) and so home to the TW travel expenses are allowable. HMRC extend the travel expenses concept to include subsistence expenditure – accommodation and meals (see HMRC Guide 490 – Employee travel, Chapter 5.4).

But that is far from being the whole story. Workplace patterns are changing and there is fairly widespread agreement that the rules are struggling to keep up with modern more flexible work practices for employees.

This was the reason that the OTS in its 2014 report suggested a review of the employed rules for travel and subsistence.

Following this, the government published a discussion document aimed at modernising the tax rules for travel and subsistence in 2015.

Perhaps surprisingly, in Budget 2016, the government announced that it had analysed the responses and concluded, that: 'although complex in parts, the rules

are generally well understood and work effectively for the majority of employees and has decided not to make further changes at this time’ (Budget Red Book 2.38) It has however revised HMRC Guide 490 in August 2015.

We do not entirely agree that the rules are generally well understood. It is clear from talking to our clients that this is an area that causes problems, especially as work patterns are changing.

We regard this as unfinished business and needs to be revisited to assist clarity and practical application.

We also offer as a basis for discussion the possibility of trying to bring the two dictionaries, self-employed and employed, closer together.

Perhaps the concept of the base and the workplace could be merged?

Travel costs and employment intermediaries

The government did, however, decide in 2015 that there would be changes to the deduction rules for employment intermediaries, a part of the crackdown on contractor (IR35) companies.

FB 2016, Clause 14 provides the draft legislation.

Although we understand the reasons for targeting employment intermediaries, we do think that determining whether a worker is subject to supervision, or direction or control, will in practice cause further uncertainty, notwithstanding that HMRC has published guidance on the issue.

On this point, we also wonder whether a simpler metric of disallowing home to work travel for contractor companies after say three months would reach the same point by a simpler route.