



## **Employment Income, etc (clauses 7-17 and related schedules)**

### **Executive Summary**

#### **Clause 9: Benefits in kind: diesel cars**

We believe this legislation will achieve its aim, though we think it unlikely that any diesel cars will meet the required standard to avoid the diesel supplement until at least 2020.

#### **Clause 10: Termination payments: foreign service**

We are concerned that the net result of removing foreign service relief without replacing it will be that a termination award made to an individual that has largely worked overseas but ends his/her employment in the UK will be taxed more heavily than a 'normal' bonus.

#### **Clause 11 and Schedule 1: Employment income provided through third parties**

The Government are right to challenge and counter abusive tax avoidance schemes, such as those involving disguised remuneration. We do, though, have some concerns about the wide scope of this measure.

#### **Clause 12 and Schedule 2: Trading income provided through third parties**

We recommend amending the legislation to align the reporting deadline with the self-assessment return deadline, where a return has been issued.

#### **Clause 14: EIS, SEIS and VCT reliefs: risk to capital**

We welcome this attempt to simplify the legislation underpinning these reliefs. However, we have a number of concerns in relation to the supporting draft guidance and more widely on HMRC guidance on GOV.UK. Without detailed guidance, the withdrawal of advance assurance removes certainty and undermines the policy objective of supporting entrepreneurial businesses.

### **1. Clause 7: Deductions from seafarers' earnings**

#### *Overview*

- 1.1. Seafarers are entitled to a deduction of 100% in respect of earnings abroad during a qualifying period of at least 365 days. The deduction is available to UK residents and EU/EEA resident seafarers. A qualifying period is one consisting either wholly of days of absence from the UK or of days of absence, linked by UK visits, where those visits do not exceed 183 consecutive days and also do not in total exceed  $\frac{1}{2}$  of the days in the period.

- 1.2. This measure extends this existing deduction for seafarers' earnings to employees of the Royal Fleet Auxiliary, and puts on a statutory basis a concession that HMRC has previously operated (i.e. RFA employees have been claiming the deduction on a concessionary basis).

*CIOT comments*

- 1.3. We believe the legislation included in the Finance Bill will achieve its aim.

2. **Clause 8: Exemption for armed forces' accommodation allowances**

- 2.1. This clause was debated in Committee of the Whole House.

3. **Clause 9: Benefits in kind: diesel cars**

*Overview*

- 3.1. The benefit of private use of a car made available by reason of employment is charged to tax according to the price of the car, certain accessories and the 'appropriate percentage' based on the car's CO2 emissions figure. An additional charge is made in respect of car fuel provided for private use, which is also calculated by reference to the appropriate percentage.
- 3.2. The appropriate percentage is currently increased by 3% for diesel cars, subject to the overall maximum of 37%.
- 3.3. This measure increases the diesel supplement from 3% to 4% for cars registered from 1 January 1998 with effect from 6 April 2018. The diesel supplement does not apply to cars registered from 1 September 2017 that either meet or are certified against new standards for nitrogen oxide (NOx) emissions under the "real driving emissions" (RDE2) regime (known as "Euro 6d"), or which have a certified NOx emissions figure under RDE2 standards.

*CIOT comments*

- 3.4. We believe the legislation included in the Finance Bill will achieve its aim.
- 3.5. However, we understand that the emissions standard Euro 6d will ultimately be introduced in two stages. The first, referred to as Euro 6d-TEMP, will apply to new car type approvals from 1 September 2017 to the end of 2019. In this stage the test contains both NOx and particle number limits for road measurements—which may still be up to 2.1 times higher than the corresponding lab limits. In the second stage, emission standard Euro 6d will apply to new car type approvals from 1 January 2020 and to all new registrations from 1 January 2021; the factor for the deviation between road and lab limits will fall to 1.5. Consequently, as Euro 6d does not take full effect until 2020 it seems unlikely that any diesel cars will meet the required standard to avoid the diesel supplement until at least 2020.

4. **Clause 10: Termination payments: foreign service**

*Overview*

- 4.1. Lump sum payments received on termination of employment are taxed depending upon the exact nature of the payment. Some payments are completely exempt from tax, for example

those on accidental death in service, in respect of disability, or (currently) where the service has been predominantly abroad.

- 4.2. This measure removes foreign service relief (FSR) on termination payments, except for seafarers, for UK residents with effect from 6 April 2018.

*CIOT comments*

- 4.3. We have raised with HMRC our concerns about the interaction of the removal of FSR on termination awards and the rules normally applied to attribute general earnings between UK and non-UK duties. We remain concerned that the net result of removing FSR without replacing it will be that a termination award made to an individual that has largely worked overseas but ends his/her employment in the UK will be taxed more heavily than a 'normal' bonus. We do not believe this will provide certainty or clarity, especially where a bonus is received at a time when an employment is being terminated.
- 4.4. For example, an individual works 19 tax years outside the UK when non-resident and 1 tax year at the end of the employment in the UK when UK resident. The employment is terminated and a £40,000 termination award under section 401, ITEPA 03 (payments and benefits on termination of employment) is received. Under the existing rules there would be full FSR. Under the new rules there will be no FSR with £10,000 taxable under section 401 after accounting for the £30,000 exemption.
- 4.5. Compare this situation to that of an assignee returning to the UK and then receiving a bonus for past services. This would be taxable as earnings under section 62, ITEPA 03 and sourcing rules would mean that, using the above example, the bonus would be apportioned over the 20 years and as 19/20ths are attributable to non-UK duties, on a just and reasonable basis, only 5% or £2,000 would be taxable in the UK. In other words a materially lesser amount than will result following the abolition of FSR.
- 4.6. It seems to us that if termination payments do not follow the same sourcing rules as apply to general earnings, there is an incentive created to pay sums as bonuses rather than termination payments in some cases.
- 4.7. Additionally, the legislation provides for FSR where an individual is non-UK resident for the tax year in which the employment terminates, with residence status being determined under the SRT. However, residence status is generally determined at the end of the tax year, when all the facts are known by the individual.
- 4.8. This may mean that, for example, the ex-employer makes a 'tax-free' termination payment at a time when the ex-employee is outside of the UK but the individual subsequently returns to the UK and becomes tax resident for the year. As a consequence the payment becomes taxable even though all the service may have been performed outside the UK.
- 4.9. Conversely, the termination payment may be paid after the ex-employee has returned to the UK in which case the ex-employer is likely to subject the payment to tax on the assumption the individual will be UK tax resident that year. But if, for example, the individual finds new employment overseas he/she could be non-UK resident that tax year.
- 4.10. Consequently, it seems to us that taxing the termination payment based on the individual's UK residence status in the tax year of termination results in arbitrary taxation and that it would

be fairer if the same sourcing rules as apply to general earnings applied to termination payments too.

## 5. **Clause 11 and Schedule 1: Employment income provided through third parties**

### *Overview*

- 5.1. The 'disguised remuneration' (DR) legislation is aimed at employees, directors and employers who use arrangements involving trusts and other vehicles to avoid, reduce or defer income tax (and NIC) liabilities on rewards of employment, or to avoid restrictions on pensions tax relief.
- 5.2. This measure has four main objectives:
  - To put beyond doubt that Part 7A applies regardless of whether contributions to DR schemes should previously have been taxed as employment income.
  - To introduce a 'close company gateway' (CCG) intended to put beyond doubt when Part 7A applies to the remuneration of owners of close companies. This is to take effect from 6 April 2018.
  - To impose a requirement to provide information on those subject to the loan charge by 1 October 2019.
  - To amend section 689 ITEPA 2003 to enable the tax liability to be collected from employees of non-UK employers and who provided services to a UK end client where the non-UK employer is unable to meet the liability or no longer exists.

### *CIOT comments*

- 5.3. The Government are right to challenge and counter abusive tax avoidance schemes, such as those involving disguised remuneration. We do, though, have some concerns about the wide scope of this measure.
- 5.4. We have no comments on the amendments to section 554A of ITEPA 2003, which are aimed at clarifying the application of Part 7A by putting beyond doubt that an income tax charge on a payment of earnings does not prevent a subsequent Part 7A charge arising as a result of a later relevant step.
- 5.5. We welcome the introduction of a 3-year condition (i.e. the employment must have existed within the preceding three years of the relevant transaction) into the CCG. However, we have raised with HMRC concerns that the CCG is too widely drafted, such that it could potentially apply to ordinary commercial transactions and other benign arrangements that are not tax avoidance. It only has certain exclusions (such as for distributions, e.g. dividends) in new section 554AC. Although changes have been made to the draft legislation published last September our concerns about the scope of the CCG remain. We would therefore like HMRC to clarify the intended scope of this measure in guidance.
- 5.6. We think the new duty on individuals to provide loan charge information to HMRC by 1 October 2019 will achieve its purpose. However, we are concerned that the transactions to which the 5 April 2019 loan charge applies will often have taken place many years ago and, at the time, were not contentious from HMRC's perspective. As the employee may have left the relevant employment some time ago they may not appreciate that a loan charge arises, and if he/she has moved since, the former employer or trustees of the Employee Benefit Trust may not be able to contact the individual. Consequently, the former employee may not be aware

that a report has to be made, or may not have all the relevant information in his/her possession (or know from whom to obtain such information) to provide all the information required by HMRC. Consequently, while HMRC's undertaking that it will contact all individuals it is aware of to inform them of their obligation is welcome, how effective this will be remains to be seen. In the circumstances, we think it is essential that HMRC applies a light touch to the imposition of penalties for failure to provide information, e.g. where the individual, reasonably, is unaware that a return is required, and for the provision of incorrect information, e.g. where the individual has provided information in good faith.

## 6. **Clause 12 and Schedule 2: Trading income provided through third parties**

### *Overview*

- 6.1. This is 'disguised trading income' legislation which applies from 6 April 2017 and is aimed at preventing trading profits being disguised as other receipts and escaping a tax charge. The legislation prevents arrangements involving an individual which result in a deduction from income, or exclusion of earnings, where that deduction or those earnings are used to provide a payment, loan, transfer of money's worth or other benefit to the individual or anyone connected to them.
- 6.2. Loans made before 6 April 2017 and after 5 April 1999 are also caught and if such loans remain outstanding at 5 April 2019 a loan charge arises. This is similar to the loan charge legislation for disguised employment income except that the charge can be postponed for certain qualifying commercial loans approved by HMRC.
- 6.3. This measure introduces a requirement for self-employed individuals in the scope of the loan charge to provide additional information to HMRC about the loans they have received by 1 October 2019. This is similar to the requirement being imposed on employed individuals that have received loans under disguised remuneration schemes.

### *CIOT comments*

- 6.4. We think the new duty on individuals to provide loan charge information to HMRC by 1 October 2019 will achieve its purpose. Given that almost all of the individuals concerned will be in receipt of a Self-Assessment (SA) return, we would expect that such information as HMRC require could be included in that return. However, the proposed reporting deadline of 1 October 2019 is earlier than that for SA and so, as things stand, this would seem not to be possible. Hence, we would recommend amending the legislation to align the reporting deadline with the SA return deadline, where a return has been issued.

## 7. **Clause 13 and Schedule 3: Pension schemes**

### *Overview*

- 7.1. This measure amends Finance Act 2004, as it relates to the registration of pension schemes for UK tax reliefs. The changes (i) allow HMRC to align the pension scheme tax registration process with the Pension Regulator's authorisation and supervision regime for Master Trust schemes and (ii) allow HMRC to refuse to register or to de-register a pension scheme where one of the sponsoring employers is a dormant company.

### *CIOT comments*

- 7.2. We have no comments on the new legislation, which we understand is being introduced as part of the government's response to pension scams (i.e. the changes tighten HMRC rules to stop scammers opening fraudulent pension schemes).

## 8. **Clause 14: EIS, SEIS and VCT reliefs: risk to capital**

### *Context*

- 8.1. Clause 14 introduces a new principles-based 'risk to capital' test for EIS, SEIS and VCTs. HMRC will no longer provide advance assurance for investments that would appear not to meet the terms of the new rule. If the new test proves effective in simplifying the conditions, this approach may be used to simplify further aspects of the venture capital schemes legislation.

### *CIOT comments*

- 8.2. We welcome initiatives for simplifying the legislation underpinning these reliefs. The current complexity of the legislation (both in terms of substantive law and the layout of the provisions) makes it difficult for businesses and advisers to establish the qualifying conditions with certainty and to avoid some of the bear traps. At a time when a start-up company is cash poor and needs to retain seed capital for business development, it has to use funds for professional advice to work through the complex legislation. This conundrum may prove fatal to the success of a claim where limited or no advice is taken.
- 8.3. One of the consequences of using a principles-based approach is the need for supplemental guidance to set out HMRC's interpretation of the application of the wide starting principle. We have a number of concerns in relation to HMRC guidance on GOV.UK, including the time it can take for guidance to be published or updated, the accuracy of the guidance, and the extent to which guidance, in its various forms, can be relied upon. If a principles-based approach to drafting legislation is to be adopted more widely, the case for addressing these concerns is even more urgent.
- 8.4. While we recognise that the advance assurance service is under pressure causing significant delays, the withdrawal of advance assurance in relation to the new test will potentially undermine certainty and practicability unless there is detailed guidance that provides examples of its application in difficult or 'grey' areas, as well as in more commonplace scenarios. The current draft guidance<sup>1</sup> includes only four examples all focusing on relatively straightforward areas. Could consideration be given to including a number of anonymised examples drawn from HMRC's extensive experience of the advance assurance process?
- 8.5. It is important that investors and advisers can place reliance on the guidance because of the very serious consequences of contravening the conditions for the relief in terms of loss of tax reliefs. There is a risk that if application of the relief is unclear, and no advance assurance process is available, that the policy intention will not be fulfilled.
- 8.6. We have commented publicly on our concerns with HMRC's approach to this issue (see CIOT response to the Treasury Committee Inquiry into the 2017 Autumn Budget<sup>2</sup> and our response

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<sup>1</sup> <https://www.gov.uk/hmrc-internal-manuals/venture-capital-schemes-manual/vcm8500>

<sup>2</sup> <https://www.tax.org.uk/sites/default/files/171130%20Treasury%20Committee%20submission%20FINAL.pdf>

to HM Treasury's Patient Capital Review where we focussed our comments on 'Financing Growth in Innovative Firms'<sup>3</sup>).

8.7. We have no comments on clauses 15-17.

## 9. The Chartered Institute of Taxation

9.1. The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

9.2. The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

9.3. The CIOT's 18,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation  
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