



HM Treasury



HM Revenue
& Customs

Taxation of self-funded work- related training:

Consultation on the extension of tax
relief for training by employees and
the self-employed

March 2018

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Chapter 1

Introduction

- 1.1 A skilled workforce benefits both individuals and the wider UK economy. Higher skill levels lead to higher wages and stronger employment prospects, higher productivity and profits for businesses, and stronger growth rates. This, in turn, increases tax revenue for public services.
- 1.2 The government's Industrial Strategy¹ will support people to develop the skills needed for jobs of the future, responding to the opportunities that will be created by longer working lives, automation of low skilled labour and changes to the labour market. This is why the government is investing an additional £406m in maths, digital and technical skills in England. It will also introduce the National Retraining Scheme to equip the workforce with the skills they will need for the workplace of the future, as businesses adopt new technologies.
- 1.3 To further support investments in skills and the UK economy, some tax professionals and business organisations have called for changes to the tax system. The government is focused on creating an environment for individuals to develop their skills to boost aggregate productivity so Autumn Budget 2017² announced the government would consult on how it could extend the existing tax relief available for self-funded work-related training by employees and the self-employed. In particular, the government is interested in how any changes could focus on supporting those needing to upskill and retrain, particularly for those who want or need to change career.
- 1.4 The term "training" should be interpreted broadly in this consultation to include learning activities that impart, instil, improve or reinforce knowledge and skills. As outlined in Chapter 3, the meaning of work-related training is defined in s.251 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA 2003) and this has a wide definition covering training courses and other learning activities, including Continuing Professional Development.

Current tax rules for employees and the self-employed

- 1.5 Most employers fund the work-related training of their employees, although sometimes the employee might pay for the training themselves and subsequently have the costs reimbursed. The current rules mean **employers** can deduct these costs for tax purposes. **Employees** are not taxed on the

¹ Industrial Strategy: building a Britain fit for the future, HM Government, November 2017, www.gov.uk/government/publications/industrial-strategy-building-a-britain-fit-for-the-future

² Autumn Budget 2017, HM Treasury, November 2017, www.gov.uk/government/topical-events/autumn-budget-2017

benefit when their employer pays for, or reimburses them for, the cost of work-related training and certain associated costs. Tax relief is also available in certain circumstances when an employer funds retraining to help an employee find another job with a new employer or set up as self-employed.

- 1.6 However, some employees pay for work-related training and this is not reimbursed by their employer. Employees cannot currently receive tax relief other than in limited circumstances when the training is an intrinsic contractual duty of their existing employment. Responses to the call for evidence on employee expenses in 2017³ indicated that some feel this is unfair.
- 1.7 The **self-employed** can deduct the costs of training incurred “wholly and exclusively” for their business where it maintains or updates existing skills but not when it introduces new skills.

Number of individuals self-funding work-related training

- 1.8 HMRC’s analysis of the Labour Force Survey⁴ suggests around 860,000 **employees** self-funded work-related training in 2016. However, it is unclear whether this training related to existing employment, involved retraining for a future career, or had a recreational element. The vast majority of these employees would not have been able to deduct the costs of this training for tax purposes under the existing rules.
- 1.9 HMRC estimates suggest around 500,000 **self-employed** individuals self-funded work-related training in 2016 but the same caveats apply. The vast majority of these individuals could deduct at least some of the costs for tax purposes under the existing rules.
- 1.10 An estimated further 570,000 **non-workers and students** also self-funded work-related training in 2016.

Purpose of the consultation

- 1.11 The government recognises the importance of engaging fully and openly with individuals, businesses and other organisations on possible tax measures. Open and collaborative consultation ensures that stakeholders and the wider public understand the government’s objectives, that any policy changes are well targeted, and that the likely impacts are better understood. The move to a single fiscal event and new tax policy making cycle⁵ announced at Autumn Statement 2016 provides an opportunity to consult more frequently from an earlier stage of policy development.

³ Taxation of employee expenses call for evidence, HM Treasury, December 2017, www.gov.uk/government/consultations/taxation-of-employee-expenses-call-for-evidence.

⁴ The Labour Force Survey is a study of the employment circumstances of the UK population. It is the largest household study in the UK and provides the official measures of employment and unemployment, www.ons.gov.uk/surveys/informationforhouseholdsandindividuals/householdandindividualsurveys/labourforcesurveylfs

⁵ The new Budget timetable and the tax policy making process, HM Treasury, December 2017, [/www.gov.uk/government/publications/the-new-budget-timetable-and-the-tax-policy-making-process](http://www.gov.uk/government/publications/the-new-budget-timetable-and-the-tax-policy-making-process)

- 1.12 This consultation is taking place at an early stage and does not set out specific options for how to extend the existing scope of tax relief for self-funded work-related training. The following chapters contain:
- a brief overview of training and skills in the UK
 - an explanation of the current tax rules
 - an overview of the lessons to be learned from previous tax initiatives to support training and international comparisons
 - the objectives and design criteria for an extension to the existing tax treatment
- 1.13 The government wants to gain an understanding of:
- how it can best learn the lessons from those previous initiatives, such as vocational training tax relief in the 1990s, and tax deductions for training in other countries
 - how it could design an extension to the existing tax relief that focuses on supporting good quality training for those wanting to upskill or retrain, particularly those who want or need to change career
 - how it could design an extension that prevents misuse on recreational activities, is sustainable for the public finances, and is simple to understand and administer
- 1.14 The government is not seeking views on whether to target any changes at a particular industry or set of skills. If the government does choose a targeted approach, it will be informed by work elsewhere. This consultation seeks to understand how any tax changes could apply whether or not they are targeted at a particular industry or set of skills.
- 1.15 Changes to the tax system for employers are also outside the scope of this consultation.
- 1.16 The deadline for responses is 8 June 2018.
- 1.17 The responses will inform policy development but the government has made no firm decisions about any of the issues set out in this document. The government will set out its intentions once it has considered the responses.

Chapter 2

Training and skills in the UK

2.1 Employment has risen to near record levels in the UK and the government has supported living standards through raising the income tax personal allowance and introducing the National Living Wage. However, raising wages over the long term requires improvements in productivity and continued investment in enhancing skills is an important element in ensuring the economy is fit for the future. Challenges need to be overcome to achieve this:

- The recent Institute for Public Policy Research study on skills noted that: “Those who could most benefit from learning opportunities are least likely to participate. Adults with lower levels of qualifications, in lower-paying occupations, in lower socioeconomic classes, and who left school at a younger age are all less likely to be participating in learning than the average adult. The number of adults in further education was down from around 4 million in 2005 to 2006 to under 2.5 million in 2015 to 2016.”¹
- The National Adult Learner Survey 2010² shows that the cost of training is the most commonly cited reason not to learn, with 58% of respondents highlighting it as an obstacle. There are also opportunity costs involved in training, such as lost earnings from time that could have been spent working.

2.2 The government is committed to supporting adults to secure meaningful and productive employment, and equipping them with the skills they need to maximise their earning potential. This is core to the Industrial Strategy as the UK seeks to take advantage of the opportunities from longer working lives, automation of low skilled labour and changes to the labour market:

- Artificial intelligence and data analytics will change jobs and businesses, and the government wants people to be able to capitalise on these opportunities. The Industrial Strategy builds on work to develop people’s skills, investing an additional £406 million in maths, digital and technical skills in England. This includes investing £84 million over the next five years to deliver a comprehensive programme to improve the teaching of computing and drive up participation in computer science.

¹ Another Lost Decade? Building a skills system for the economy of the 2030s, Institute for Public Policy Research, July 2017, www.ippr.org/research/publications/skills-2030-another-lost-decade

² National Adult Learner Survey 2010, Department for Business Innovation & Skills Research Paper Number 63, October 2012, www.gov.uk/government/uploads/system/uploads/attachment_data/file/34798/12-p164-national-adult-learner-survey-2010.pdf

- To increase adult learning and retraining, the government will introduce an ambitious National Retraining Scheme in England by the end of this Parliament. It will give individuals the skills they need to thrive and support employers to adapt as the economy changes. A high-level advisory group – the National Retraining Partnership – will bring together the government, businesses and workers, through the Confederation of British Industry and the Trades Union Congress, to set the strategic direction and oversee implementation of the scheme. The National Retraining Scheme will initially target skills shortages in key sectors, ensuring that the UK can develop much-needed digital and construction skills. A total of £30 million will be invested to test the use of artificial intelligence and innovative education technology in online digital skills courses so that students can benefit from this emerging technology.
- The National Retraining Scheme will be informed by £40 million to test innovative approaches to helping adults upskill and retrain. The pilots will help the government learn more about how to support and incentivise adults to learn skills that will help them, their local economies and national productivity. The government has already launched a Flexible Learning Fund, making available up to £10 million to support projects that design and test flexible, accessible ways of delivering learning to working adults with low or intermediate skills.

2.3 This builds on existing initiatives designed to support investments in skills and lifelong learning. These include:

- The apprenticeship levy is helping to deliver new apprenticeships and supports quality training. Apprenticeships provide people of all ages the opportunity to develop in work and life, giving people a clear route to success. Apprenticeships are paid jobs with training, allowing individuals to earn while they learn without having to pay for their training or qualifications. Designed by employers themselves, apprenticeships give individuals the transferable skills and knowledge that employers want.
- The Adult Education Budget (AEB) aims to engage adults and provide the skills and learning they need to equip them for work, an apprenticeship or further learning. It enables more flexible tailored programmes of learning to be made available, which may or may not require a qualification. The AEB funds core skills such as English and Maths, as well as English for Speakers of Other Languages (ESOL) and qualifications to get unemployed individuals into work.
- Adult learners can apply for grants and bursaries to help pay for courses and training. Usually, learners don't have to pay this money back.³
- Advanced Learner Loans support lifelong learning by reducing the upfront cost restraints on taking further education courses.⁴

³ www.gov.uk/grant-bursary-adult-learners

⁴ www.gov.uk/advanced-learner-loan

- Adult learners facing financial hardship while studying on Further Education courses can apply to receive Discretionary Learner Support.⁵ This could help to support learners with accommodation and travel expenses, the cost of course materials, or childcare.
- Part-time undergraduate students can take out tuition fee loans to help with the costs of study. From 2018 to 2019, part-time maintenance loans will be introduced, supporting the cost of living. Many part-time learners are mature students, or those with dependents. Supporting part-time learning also means supporting lifelong learning, enabling people to gain new skills or change career paths.

2.4 A mix of complementary policies involving direct spending and taxation will help ensure individuals can access the skills necessary for the future. As a result, the government is consulting on how it could make changes to the tax system for self-funded work-related training by employees and the self-employed.

⁵ www.gov.uk/discretionary-learner-support

Chapter 3

Overview of the current rules for the taxation of work-related training

- 3.1 Many employees incur expenses as part of doing their job. Some employers pay for business expenses directly, while others reimburse their employees for business costs they incur. Some employees pay business expenses themselves without reimbursement.

Training funded by employers

Current or related employment

- 3.2 Most employers fund their employees' work-related training, although sometimes the employee might pay for the training themselves and subsequently have the costs reimbursed.
- 3.3 Employers can deduct this expenditure as a business expense and employees do not pay tax or National Insurance contributions on the benefit because there is a wide statutory exemption for payments or reimbursements of expenditure on the provision of work-related training.¹
- 3.4 In this context, work-related training is training for an employee's current employment or a "related employment". It is defined as any training course or other activity which is designed to impart, instil, improve or reinforce any knowledge, skills, or personal qualities which:
- are, or are likely to prove, useful to the employee when performing the duties of the employment or related employment
 - will qualify or better qualify the employee to perform the duties of the employment or
 - will qualify or better qualify the employee to participate in charitable or voluntary activities performed in association with the employment or related employment
- 3.5 A "related employment" is:
- any office or employment held with the employer or which is to be held with the employer or a connected person

¹ Employment income: further education and training costs (Sections 250-254 ITEPA 2003), www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim01200

- any such office or employment to which the employee has or can realistically expect to have a serious opportunity of being appointed
- 3.6 The objective of the exemption is to include all genuine training, in a range of competencies, which the employee would need to advance their career, or to achieve a career move with their employer.
- 3.7 The rules include the following features:
- the exemption applies to both internal and external courses
 - there is no territorial limitation on the location at which training is undertaken
 - the exemption extends to a range of training materials
 - the exemption applies not only to the cost of providing qualifying training, but also extends to related costs, such as the cost of additional childcare and the travelling and subsistence costs of the employee
 - the definition of work-related training includes training which is linked to charitable and voluntary activities
 - incidental overnight expenses can be paid tax-free to employees on training courses in the same way as such expenses can be paid tax-free when an employee is away on business
- 3.8 However, any payment or reimbursement of training costs will remain taxable when it has as its purpose:
- an intention to reward the employee
 - the provision to the employee of an employment inducement, including to take up a new job
 - enabling the employee to enjoy the facilities or benefits provided for entertainment or recreational purposes unconnected with work-related training

Retraining for a new employment

- 3.9 There is a tax exemption for costs met by an employer for an employee who is about to leave, or has left within the previous year, to attend certain courses of retraining intended to help them get another job or set up a business.² It applies to courses which:
- are designed to teach or improve skills or knowledge which will help the employee to find new work and are entirely devoted to those objectives
 - last no more than 2 years
- 3.10 The exemption is only available if the employee has been in the employment of the employer for at least 2 years up to the time the course begins or at the time the employment ceased. He or she must leave within 2 years after

² Employment income: retraining expenses paid by employer: exemption from tax (Section 311 ITEPA 2003), www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim05005

finishing the course if the employee has not left by the time it starts. The exemption is withdrawn if the employee is re-employed by the same employer in the 2 years following the end of the course.

3.11 The opportunity to attend the course must have been given to all employees in a similar position. The expenses which are exempt are:

- fees for the course
- fees for examinations taken during or at the end of the course
- the cost of essential books
- the costs of travelling and subsistence to the extent that they exceed the costs normally incurred by the employee in travelling between home and normal place of work (or former place of work if the employee has left)

Non-reimbursed costs of self-funded training by employees

3.12 Some employees pay for training and this is not reimbursed by their employer. This might be because the training is unrelated to their employment, including where the employee is seeking to change career or learn a new skill to undertake a hobby. In other cases, it might be because the employer chooses not to reimburse the costs of work-related training.

3.13 The general overarching rule on tax deductions for employees' expenses is longstanding and subject to a large body of case law.³ Deductions are allowed for an expense if:

- the employee is obliged to incur and pay it as a holder of the employment
- the amount is incurred wholly, exclusively and necessarily in the performance of the duties of the employment; it is not sufficient that the expense is incurred to enable the employee to either prepare for his duties or to improve his ability to perform those duties

3.14 This means no deduction is normally permitted for non-reimbursed expenses incurred by an employee for training. This includes where the subject of the training is closely relevant to the nature of the employment and where training forms part of a Continuing Professional Development programme. The expenses are not deductible because they are not incurred in the performance of the duties of the employment.

3.15 The only exception is where the external education is an integral part of the contractual duties of the employment.⁴ Typically, these cases will be employments which involve research or an employee who is undertaking a training phase of their career, during which the attendance at external courses represents an intrinsic part of the duties of the employment.

³ The general rule for employees' expenses (Section 336 ITEPA 2003), www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim31620

⁴ Education and training: where education is part of the duties of the employment, www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim32535

3.16 The following must apply for the expense from training to be allowable:

- Each and every holder of the employment must be obliged to incur the expenses in carrying out the duties of the job and the amount must be incurred wholly, exclusively and necessarily in the performance of the duties
- Training is an intrinsic part of the contractual duties of the employment
- All other duties are being undertaken as part of the training process. They constitute the practical aspects of the training process and are intended to complement the theoretical aspects of the training, which include the externally provided training
- There is a mandatory requirement for the employee to undertake the external training as an intrinsic part of the duties of the employment
- Failure to complete the training and obtain the qualification will mean that the employee will not be able to continue in employment with the employer in the role that would otherwise have been available to them after qualification

Box 3.A: Examples of how the current rules apply to employees for non-reimbursed self-funding training

An employee is a salesman for a company with a major export trade to France. He enrolls in a night school course for one evening each week to improve his French. He asks for a deduction for the cost of the course.

No deduction is due. The employee's duties as a salesman do not extend to learning French at night school.⁵

A scientist is employed by a University department to carry out basic research in polymer chemistry. As part of her continuing research she attends a presentation at a different university of the findings of a scientist working in the same field. She is required to attend such presentations as part of the programme of research for which she is employed. The subject matter of the presentation directly influences the content and direction of her own research.

The duties of this employment include research. In this case attendance at the presentation is an integral part of the research process and so is one of the duties of the employment. The costs of travel to the presentation are deductible.⁶

A trainee doctor employed as a registrar on a training contract is required, as a stated contractual duty of the employment, to attend various external training courses. As part of the duties of the employment there is a mandatory

⁵ The general rule for employees' expenses: in the performance of the duties, www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim31653

⁶ Other expenses: education and training: where education is part of the duties of the employment, www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim32545

requirement to maintain a national training number by attending a series of training courses and events. Failure to complete the course and obtain the qualification will mean that he cannot proceed to the next stage of his chosen profession.

Attendance at the training events is an intrinsic part of the employment and one of the duties of the employment. The costs of travel to the events, course fees and other associated costs met by the employee are deductible.⁷

Self-funded work-related training by the self-employed

3.17 Expenditure by someone who is self-employed is generally allowable in computing profits for the purposes of tax and National Insurance contributions provided it is:

- wholly and exclusively for the purposes of the business
- not capital expenditure
- not specifically disallowed by statute

3.18 A training course to update expertise, knowledge or skills already possessed will normally be regarded as revenue expenditure. However, expenditure on a training course for a business owner that is intended to provide new expertise, knowledge or skills brings into existence an intangible asset, which will have an enduring benefit for the business. It is therefore of a capital nature so does not qualify for tax relief.⁸

Box 3.B: Example case showing how the current rules apply to the self-employed

In *Dass v Special Commissioner and others* [2006] EWHC2491 (Ch), the taxpayer traded as a tutor in English and as a legal consultant. He took a course which would have led to a diploma in law (LL Dip) qualification and claimed a deduction for re-sit examination fees (having missed the original examinations due to illness). The Special Commissioner decided that the fees were capital in nature:

'I agree with HMRC that the particular course was one to equip Mr Dass with a new qualification that would have enabled him to venture into new areas of practice, and it was not merely a "refresher" in relation to his existing expertise. This seems to me to be a correct way of distinguishing between the costs (in relation to courses) that constituted capital as distinct from revenue

⁷ Other expenses: education and training where education is part of the duties of the employment, www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim32546

⁸ Intangible assets: proprietor's training courses, www.gov.uk/hmrc-internal-manuals/business-income-manual/bim35660

expenditure ... I think that HMRC applied the test correctly and, I was told, in a manner consistently with the treatment of all other taxpayers.'

In the High Court Lightman J upheld the Special Commissioner's decision on the capital/revenue distinction.⁹

⁹ Capital/revenue divide: intangible assets, www.gov.uk/hmrc-internal-manuals/business-income-manual/bim35660

Chapter 4

Learning lessons

- 4.1 The government is keen to learn from previous attempts in the UK to use the tax system to support individuals undertaking training. It also wants to learn the lessons from experiences in other countries to ensure it understands the challenges and opportunities from potential reform.

The UK

Vocational training tax relief

- 4.2 Vocational training tax relief was introduced in the early 1990s and withdrawn when Individual Learning Accounts were introduced in 2000 to 2001. It was available to individuals who paid for certain costs of their own training.¹ Courses qualified for relief if certain conditions were met:
- Relief was due if the course led to a National Vocational Qualification or Scottish Vocational Qualification (NVQ or SVQ) and the trainee was at least 16 years old and, if under 19 years old, not in full time education in a school.
 - Relief was also due for non NVQ or SVQ linked training provided the course provided skills or knowledge which were relevant to, and were intended to be used in, paid employment or self-employment. The trainee had to be 30 or more years old at the time of the payment and the course had to be full time, lasting for at least four weeks but no more than a year. All teaching and practical applications had to take place in the UK.
- 4.3 To qualify for the relief, trainees also had to be resident in the UK, not be in receipt of any other form of tax relief for the fees and not be receiving, or entitled to receive, public financial assistance for the course. Trainees had to fund the training themselves and not be undertaking the course either wholly or mainly for recreational purposes or as a leisure activity.
- 4.4 Most trainees received relief at source by deducting an amount equal to income tax at the basic rate from the fees they paid to UK training providers. Training providers then reclaimed that amount directly from the Inland Revenue. Higher-rate taxpayers could claim higher rate relief from their local tax offices or in their Self-Assessment returns, although higher rate relief was removed in 1999 to ensure that public support was targeted on those who needed it most.

¹ The Vocational Training (Tax Relief) Regulations 1992.

- 4.5 Around 200,000 individuals claimed the relief each year but it proved very difficult to create a system that delivered the intention behind the rules. For example, more than a quarter of the £36 million tax relief given in 1997 to 1998 related to claims for flying and diving. Horse riding and cookery courses were also popular, with the relief criticised for funding expensive hobbies.

Application of existing tax treatment for work-related training

- 4.6 HMRC assesses claims for a tax deduction based on their individual merits and the facts in each case. HMRC has to deal with attempts to stretch the definition of work-related training in order to claim a deduction for other activities. The examples below refer to cases when the employer has paid for the activities:
- Businesses taking their employees on holidays all over the world in the name of training and research because they visited locations in the destinations with some relevance to the trade
 - Businesses in the food supply industry claiming they are sampling products at restaurants for research purposes when they are simply going out to lunch or dinner
 - Some business owners attempting to claim tax deductions for business entertainment by arguing it improves their knowledge under the rules for training expenditure
- 4.7 This demonstrates the need to ensure any tax changes for employees and the self-employed are closely defined so that individuals are clear about what they can and cannot claim. Misuse and error create risks to the Exchequer and other costs to taxpayers because of the increased compliance activity required by HMRC.

International experiences

The Organisation for Economic Co-operation and Development (OECD) study of taxation and skills

- 4.8 The OECD published a study in April 2017² to assess how taxes and other policy levers impact on investments in skills. The study found governments provide many tax reliefs to support investment in skills and good design is important in ensuring their effectiveness. The study found:
- 21 of 30 countries provide tax relief for training through deductions from taxable income. In 19 of the 21 countries, the deduction is only available where the training concerned is related to, or even necessary for a worker's current employment.
 - In 7 of the 21 countries, caps exist which limit the amount of skills expenditure that can be deducted from taxable income. In 2 countries, thresholds also exist below which skills expenditures cannot be deducted from taxable income.

² OECD Tax Policy Studies: Taxation and Skills, OECD, April 2017, www.oecd.org/ctp/taxation-and-skills-9789264269385-en.htm

- In 6 of the 30 countries, tax credits are provided, although these tend to offset the cost of university or basic education rather than reduce the costs of career-related education. Tax credits can be more beneficial to those on the lowest incomes because those who don't have a tax liability, or a large enough tax liability, for the credit to be offset against can sometimes receive a refund.

4.9 The OECD study highlighted some of the insights and general lessons to learn from the use of tax incentives to support work-related training and how these should interact with other approaches. The OECD conclude:

- the optimal mix of policies, involving loans, spending, and taxes, will depend on a country's circumstances
- the incentive for individuals to invest in skills is higher in countries with both lower income taxes and higher levels of skills spending
- tax policies should aim to increase skills investments and the subsequent use of those skills in the labour market
- tax reliefs are often more complex to administer and for taxpayers to understand than direct spending on skills investment
- existing skills tax reliefs are often only available for training connected to a workers' current employment, and may be ineffective in assisting workers who need or want to change careers
- many tax incentives are only of value to those who earn taxable income
- tax incentives can encourage training but also involve significant deadweight losses, providing subsidies to skills investments that would occur even in the absence of government support
- tax incentives may provide larger benefits to those on higher incomes, to those in secure jobs, and to those with higher existing skills
- income contingent loans can be more effective than tax deductions, which are less effective supporting those with liquidity constraints because the costs are incurred during the tax year and the benefit of the tax deduction is not felt until later
- low skill, low-income taxpayers are more likely to not claim or misunderstand what they are entitled to claim

4.10 The government is also aware that international tax authorities need to undertake significant activity to check compliance with the rules. This can sometimes include contacting employers to check whether the training being claimed for by an employee is genuinely work-related.

4.11 The issues above demonstrate a selection of the practical challenges associated with extending the scope of tax relief for self-funded work-related training. It is important for these issues to be considered and the lessons to be learned when considering the options.

Questions

- 1 Do you agree with the lessons that need to be learned from experiences in the UK and overseas?

Chapter 5

Objectives and design criteria

5.1 Consistent with the tax-policy making process, the government is setting out the intended objectives and using this consultation to help identify the most effective options. It will listen carefully to the views of stakeholders and the government is open to innovative suggestions but these must provide value for money for the Exchequer, meet the intended objectives, and address the lessons needing to be learned in the previous chapter.

High-level objectives and design principles

5.2 As outlined in Chapter 2, the government is focused on creating an environment for people to develop their skills. This will help individuals compete in today's evolving market place, improve their earnings, and ensure the economy is fit for the future. Any tax changes for work-related training should therefore focus on supporting individuals:

- needing to upskill or retrain, particularly for those who want or need to change career, to progress in the work place and improve their earnings
- undertaking training with approved providers and leading to qualifications

5.3 The design of any extension should also:

- ensure relief is not available for expenditure on recreational activities or other personal purposes so that the scope for misuse of the relief is minimised
- be sustainable and affordable for the public finances
- be as simple as possible to understand and administer so that take-up is maximised and errors are minimised

5.4 The government has an open mind on whether tax relief and/or tax credits would be the most appropriate approach to achieving these objectives. It is also open to other alternative approaches to supporting self-funded work-related training through the tax system if they meet these objectives and design criteria.

Questions

- 2 Do you agree with the high-level objectives? Are there any others you think are as or more important?
- 3 Do you agree with the high-level design principles? Are there any others you think are as or more important?

Meeting the high-level objectives

Supporting those needing to retrain or upskill, particularly for those who want or need to change career

- 5.5 Individuals undertake training to:
- maintain or update existing skills or qualifications
 - learn new skills or acquire new qualifications
- 5.6 The government recognises the case for ensuring tax relief is available for maintaining or updating existing skills. It does not rule this out but the government is particularly focused on ensuring individuals can respond to changes in the labour market and wants to ensure any change focuses firstly on supporting those needing to retrain or upskill. Retraining refers to skills that can be used to move into a new employment or trade. Upskilling refers to the employee or self-employed individual seeking new expertise or skills in the same employment or trade. There are different policy issues to address in both.

Retraining for employees and the self-employed to move into a new employment or trade

- 5.7 The OECD study highlighted that existing skills tax reliefs around the world are often only available for training connected to an individual's current employment or trade, and may be ineffective in assisting workers who need or want to change careers. There may be several practical reasons for this, including ensuring tax reliefs aren't misused for recreational purposes. For example, a plumber could participate in a cooking course with the intention to use the skills for a new employment or trade but it would be very difficult to distinguish between those who participate to learn skills for other reasons.
- 5.8 The existing tax rules mean an employee does not pay tax when an employer pays for a course that is designed to teach or improve skills which will help the employee to find new work or set up a business and is entirely devoted to those objectives. He or she must leave their employment within 2 years after finishing the course if they have not left by the time it starts. This caters for particular circumstances but in many cases an employer will not fund retraining to support an employee to find new work. The employee may be self-funding the training to provide themselves with the option of job opportunities elsewhere or a change of career.
- 5.9 One option to address this might be to allow the expenditure to be carried forward and set against the profits or earnings of the new trade or employment. This would need to be within a specified and reasonable timeframe after the training has been completed. This would ensure the relief can only be applied when the individual starts a new business or employment rather than being based on the intention to do so. This would have the advantage of potentially supporting those who retrain but do not pay tax because they are not in work or earn less than the income tax personal allowance at the time of the training. It also addresses the OECD's observations that tax policies should seek to increase skills investments and

the subsequent use of those skills in the labour market. However, there may be alternative approaches that could be more effective and the government welcomes views.

The self-employed and upskilling for an existing trade

- 5.10 The current tax rules for the self-employed mean expenditure on training intended to provide new expertise, knowledge or skills for their existing trade does not qualify for a tax deduction. It is instead treated as capital expenditure because it creates an enduring benefit to the business. Reforming the rules so that the self-employed can deduct expenditure in these circumstances would support those learning new skills to expand their business. This would also be more consistent with the existing rules for employees, which allow a deduction if an employee is reimbursed for expenditure on training based on whether it is to “impart, instil, improve or reinforce any knowledge, skills, or personal qualities”.¹
- 5.11 The government would welcome views on how it could change the tax rules to address this issue. For example, a deduction could be provided for such expenditure subject to the general condition that it is wholly and exclusively for the purposes of the trade.

Employees and upskilling for an existing employment

- 5.12 Employees do not pay income tax on the benefit when an employer pays for training to upskill for an existing employment or where it could lead to another job with the same employer. However, if the employee needs to self-fund training to improve existing skills or learn new skills for their existing employment then it does not qualify for tax relief. The government is particularly focused on ensuring employees can prepare for the jobs of the future but recognises there is a case for ensuring tax relief is available for maintaining and improving existing skills too if there is any change to the rules.

Questions

- 4 How could the rules be reformed to allow a tax deduction for self-funded retraining subsequently used in a new employment or self-employment? Do you think a time-limited carry forward would be the best approach and how could this work in practice?
- 5 How could the rules be reformed to allow a tax deduction when the self-employed fund training on upskilling for their existing business?
- 6 How could the rules be reformed to allow a tax deduction when an employee funds training on upskilling for their current employment?
- 7 To what extent would reforms to tax relief change behaviour so individuals are incentivised to undertake more work-related training? Please explain.

¹ Employment income: further education and training costs (Section 251 ITEPA 2003), www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim01200

- 8 Do you think the tax system would be the most effective lever to support employees and the self-employed who want or need to upskill, retrain, and take part in career learning? Please explain.

Supporting those undertaking training with approved providers and leading to qualifications

- 5.13 There is a wide spectrum of training available from a wide range of learning providers in the UK. It will be important to deliver value for money from any extension to the existing tax treatment and ensure the training is delivering benefits to individuals and the UK economy. The government is particularly focused on supporting individuals securing skilled work. Focusing on training leading to recognised qualifications is likely to incentivise activity that delivers the skills needed for that work and is recognised by employers.
- 5.14 The government recognises the importance of all forms of training, including learning that does not lead to qualifications. However, tax changes will have a cost to the Exchequer and the government must consider focusing on providing incentives where they can offer demonstrable benefits. The government would like to know how businesses might usefully identify genuinely valuable training.
- 5.15 Focusing on support for training provided by approved providers offering formal qualifications is consistent with the government's approach elsewhere in the system. For example, Advanced Learner Loans in England are only available if the course is a Level 3, 4, 5 or 6 qualification² at an approved college or training provider. These qualifications appear on the Register of Regulated Qualifications³ and providers are approved by the Education and Skills Funding Agency. This ensures the provider is a legitimate training business with a track record of trading and delivering learning. Qualifications and providers are accredited differently across the different countries of the UK. This creates a challenge but the government would seek to ensure comparable treatment across England, Scotland, Wales and Northern Ireland.
- 5.16 This approach would ensure that tax relief supports those individuals undertaking training with approved providers but would exclude courses for a range of formal non-regulated qualifications offered by professional organisations. One option might be to allow tax relief for formal qualifications offered by professional organisations approved by HMRC for the purposes of tax deductions related to fees and subscriptions⁴ but the government is open to alternative approaches.

Questions

- 9 How could the government target work-related training leading to valued qualifications through approved providers and professional organisations?

² www.gov.uk/what-different-qualification-levels-mean/list-of-qualification-levels

³ <https://register.ofqual.gov.uk/>

⁴ Professional bodies approved for tax relief (list 3), www.gov.uk/government/publications/professional-bodies-approved-for-tax-relief-list-3

Meeting the high-level design principles

- 5.17 The government wants to ensure the design of any extension meets certain criteria to ensure it is effective, affordable, and is not open to misuse.

Ensure relief is not available for expenditure on recreational activities or other personal purposes so that the scope for misuse of the relief is minimised

- 5.18 Many individuals undertake training activities that are either wholly or mainly recreational. The government is clear that the cost of these activities should not be borne by all taxpayers in any changes to the current system.
- 5.19 The lessons learned from the introduction of the vocational training tax relief demonstrate the practical challenges and significant scope for ambiguity. This could cause genuine confusion for individuals about what is allowable. It would also allow individuals to argue that mostly recreational activities have work-related benefits. For example, an individual could participate in an acting course and argue its purpose is to improve their public speaking for work rather than for recreational purposes. This could be true but it would be difficult to distinguish between different cases and make enforcement very difficult. Although the vocational training tax relief rules in the 1990s explicitly excluded any course that was undertaken either “wholly or mainly for recreational purposes or as a leisure activity”, the relief was widely criticised for supporting those with expensive hobbies and eventually withdrawn.
- 5.20 In particular, the government would welcome views on whether there are any effective objective tests that could be introduced to show the training is genuinely work-related. This could make the system clearer for individuals to understand, reduce the scope for misuse, and make enforcement less resource-intensive.

Questions

- 10 How can the scope for misuse be minimised, particularly claims related to recreational activities, and the rules be made enforceable in practice without being resource-intensive for individuals or HMRC?

Be sustainable and affordable for the public finances

- 5.21 The government must ensure that the cost of existing and new tax reliefs are sustainable and affordable for the public finances. The cost of training courses and activities can vary significantly, ranging from hundreds to tens of thousands of pounds. Some other countries have an annual cap on the level of expenditure on training that can qualify for a deduction and the government will need to consider this option carefully. For example, a £500 cap would provide a basic rate taxpayer with £100 in income tax relief even if the individual paid a total of £1,000 for the training course.
- 5.22 A cap could ensure any extension to the existing tax relief is affordable and help target limited resources. For example, there is evidence from the use of the deduction in Australia that those with higher incomes tend to claim

larger amounts.⁵ A cap would also recognise there is a significant private benefit involved in training because it can lead to better career prospects, higher wages for an employee or increased profits for a self-employed individual. A cap could also reduce the incentive to misuse the relief and could then be modified in the future once the government has been able to assess the operation of the relief in practice.

- 5.23 The government is mindful of the need to find a balance if it introduced a cap on the level of expenditure eligible for a tax deduction. It will need to consider this in the context of the wider public finances and is also interested in other approaches that could ensure the Exchequer cost of any extension is affordable. For example, learning the lessons from the introduction of vocational training tax relief, the government could seek to target any extension at lower earners. As outlined in Chapter 1, the consultation does not consider targeting particular industries or skills.

Questions

- 11 **If it is necessary, at what level would any cap on expenditure eligible for tax relief need to be set to make a meaningful difference to the choices made by individuals? Please explain.**
- 12 **Are there complementary or alternative approaches that could ensure any extension is affordable but would still meets its objectives?**

Be as simple as possible to understand and administer so that take-up is maximised and errors are minimised

- 5.24 The government aims to simplify the tax system where possible, ensuring the UK remains an attractive environment for enterprise and individuals can understand their tax obligations. It is important, as far as possible, that any extension to the existing tax relief available to employees and the self-employed is easy to understand and apply. This helps to minimise error and reduce the operational costs for HMRC in administering the system.
- 5.25 Employees currently claim tax relief on eligible non-reimbursed expenses in a number of ways:
- by completing a form (P87) through their Personal Tax Account
 - a paper form (P87)
 - by phone
 - by giving details in a letter
 - submitting a self-assessment return
- 5.26 The self-employed enter details on their self-assessment. These are established processes and are the starting point for the administration of any extensions to tax relief in this area. However, the government is open to workable alternatives if they could improve take-up and reduce inaccurate claims.

⁵ Reform to deductions for education expenses, Discussion Paper, Australian Treasury, May 2013.

Questions

- 13 How could any changes be administered so that take-up is maximised, errors are minimised, and the system is not resource-intensive for either individuals or HMRC? Is the existing system involving submitting a paper or online form via the Personal Tax Account and self-assessment appropriate?

Other tax issues

- 5.27 The government is interested in any issues with the current rules for employees and the self-employed that need to be resolved.

Questions

- 14 Are there any issues with the current rules or administration of the existing tax relief for work-related training by employees and the self-employed that need to be resolved?

Chapter 6

Summary of consultation questions

6.1 The questions apply to employees and the self-employed unless otherwise stated. Please outline if your answer is different for each group.

Lessons learned

- 1 Do you agree with the lessons that need to be learned from the UK and overseas?

Objectives and design criteria

- 2 Do you agree with the high-level objectives? Are there any others you think are as or more important?
- 3 Do you agree with the high-level design principles? Are there any others you think are as or more important?
- 4 How could the rules be reformed to allow a tax deduction for self-funded retraining subsequently used in a new employment or self-employment? Do you think a time-limited carry forward would be the best approach and how could this work in practice?
- 5 How could the rules be reformed to allow a tax deduction when the self-employed fund training on upskilling for their existing business?
- 6 How could the rules be reformed to allow a tax deduction when an employee funds training on upskilling for their current employment?
- 7 To what extent would reforms to tax relief change behaviour so individuals are incentivised to undertake more work-related training? Please explain.
- 8 Do you think the tax system would be the most effective lever to support employees and the self-employed who want or need to upskill, retrain, and take part in career learning? Please explain.
- 9 How could the government target work-related training leading to valued qualifications through approved providers and professional organisations?
- 10 How can the scope for misuse be minimised, particularly claims related to recreational activities, and the rules be made enforceable in practice without being resource-intensive for individuals or HMRC?

- 11 If it is necessary, at what level would any cap on expenditure eligible for tax relief need to be set to make a meaningful difference to the choices made by individuals? Please explain.
- 12 Are there complementary or alternative approaches that could ensure any extension is affordable but would still meets its objectives?
- 13 How could any changes be administered so that take-up is maximised, errors are minimised, and the system is not resource-intensive for either individuals or HMRC? Is the existing system involving submitting a paper or online form via the Personal Tax Account and self-assessment appropriate?
- 14 Are there any issues with the current rules or administration of the existing tax relief for work-related training by employees and the self-employed that need to be resolved?

Chapter 7

Next steps

- 7.1 The deadline for responses to this call for evidence is 8 June 2018. Representations by email are preferable and should be sent to employeebenefitsandexpenses@hmtreasury.gsi.gov.uk.
- 7.2 Alternatively, hard copies can be sent to:
- Taxation of self-funded work-related training
Personal Tax Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ
- 7.3 Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from GOV.UK. All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.
- 7.4 When responding please say if you are a business, consultancy, individual or representative body. Please provide demographics of your organisation; in the case of representative bodies, please provide information on the number and nature of people you represent.
- 7.5 This consultation will inform future policy development but the government has made no firm decisions about the issues set out in this document. The government will set out its intentions once it has considered the responses received.

Confidentiality

- 7.6 Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.
- 7.7 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we

will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury or HM Revenue & Customs.

- 7.8 HM Treasury and HM Revenue & Customs will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

HM Treasury contacts

This document can be downloaded from
www.gov.uk

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