Appeal number: FTC/89/2010

[2011] UKUT 329 (TCC)

NATIONAL INSURANCE CONTRIBUTIONS — lump sum payments made to employees using own cars for business travel — whether "relevant motoring expenditure" — Social Security (Contributions) Regulations 2001 reg 22A — ITEPA s 229(2) — payments not linked to use and therefore not "relevant motoring expenditure" — appeal allowed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Appellants**

- and –

CHESHIRE EMPLOYER AND SKILLS DEVELOPMENT LIMITED (formerly TOTAL PEOPLE LIMITED) **Respondent**

Tribunal: Judge Colin Bishopp

Sitting in public in Manchester on 11 July 2011

Richard Adkinson, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Appellants

Grant Summers of Grant Thornton UK LLP for the Respondent

DECISION

Introduction

1. This is an appeal by the Commissioners for HM Revenue and Customs ("HMRC") against a decision ([2010] UKFTT 379 (TC)) of the Tax Chamber of the First-tier Tribunal (Judge Barlow and Mrs Crompton) by which they allowed the appeal of the respondent, Total People Limited (which has since changed its name to Cheshire Employer and Skills Development Limited and to which I shall refer as "CESDL"), against HMRC's refusal to make a repayment of Class 1 National Insurance Contributions ("NICs") which CESDL claimed it had overpaid in the tax years 2002-03 to 2005-06 inclusive. The amount in issue is in the order of £146,000. HMRC argue that the tribunal did not ask itself the right question and, as a result of so doing it came to the wrong conclusion. CESDL supports the tribunal's decision, saying that it was right for the right reasons, and contends in addition that the crucial finding was one of fact which is not susceptible of challenge on appeal.

2. Before me, as before the tribunal, HMRC were represented by Mr Richard Adkinson of counsel and CESDL by Mr Grant Summers, a partner in the accountants Grant Thornton UK LLP.

The facts

3. It is common ground that at the material time CESDL employed about 160 training advisers, each with a particular expertise. Their role was to visit the premises of employers in south-east Cheshire and in neighbouring counties in order to advise those employers and their trainees. They therefore spent most of their time away from CESDL's premises, and were required to undertake a significant amount of travel. Such travel, as the tribunal found, was practicable only if undertaken by car. The training advisers were expected to use their own cars, and were paid certain sums intended, as the tribunal accepted, to defray part of the cost of their doing so. In addition, payments described as being in respect of travelling expenses were made to some other employees undertaking different tasks but also travelling in their own cars on CESDL's business.

4. The tribunal found that there were two different schemes in operation. In one, the employee concerned was paid a rate per mile which it appears, although its decision reveals there was some uncertainty in the tribunal's mind, was of 40p per mile. In this scheme no lump sum allowance was paid. In the other scheme, the employee received a lower rate per mile, which the tribunal found to be initially 12p and later 13p per mile, plus a lump sum, expressed as an annual allowance but paid by equal monthly instalments. It was and is common ground that the payments of 12, 13 or 40p per mile did not attract NICs (and CESDL did not account for NICs on them). However, CESDL treated the lump sums as subject to NICs and accounted to HMRC for them. The issue is whether it should have done so: CESDL says not, with the consequence that it is now entitled to a refund; HMRC that it correctly accounted for the NICs, and that no refund is due.

5. Further relevant findings of fact appear at paras 17 to 24 of the tribunal's decision. For present purposes they can be summarised. It determined that, although CESDL's "Travel Policy", which formed part of its staff handbook, stated that an employee required to use his own car in the course of his duties could choose which scheme should apply to him, subject to agreement with the service director or chief executive on appointment or promotion, in practice those employees who covered large annual mileages on CESDL's business were not permitted to take only the 40p per mile payment, but were instead required to accept 12p or, later, 13p per mile plus the annual allowance. In the case of the training advisers the allowance was £3,600 per year, which increased to £3,700 during the relevant period: the increases in the rate per mile and the lump sum do not affect the principle. Employees expected to undertake relatively little business travel could elect to take the 40p per mile payments but no lump sum, and indeed the documents produced to the tribunal indicated that this was the only available course when the employee covered less than 2,500 miles per year. However, the tribunal found that the rule was not enforced strictly when an employee who had formerly driven more than 2,500 miles a year and had taken the reduced mileage payments plus the lump sum moved to a different role which required him to travel less than 2,500 miles a year. The lump sum payments were paid pro rata to part-time staff and to those who joined or left part-way through a tax year. A member of staff who took sick leave received the lump sum payments for 12 weeks, but then payment of the lump sum ceased, as did payment of the employee's salary.

6. The tribunal also found that the rules for more senior employees and directors were different. The payments were not merely reimbursement for the cost of travelling, but were described in CESDL's documents as "additional", and as "part of the recruitment package". Some of the more senior staff received a lump sum of £4,100, later increased to £4,200, per annum, and CESDL's two directors received £7,100, which increased to £7,200, per annum. Whatever their amount, the lump sum payments were all made by equal monthly instalments. The senior employees and the directors, I deduce, also received 12p or 13p per mile travelled on CESDL's business, although the tribunal's decision contains no specific finding to that effect.

7. The tribunal found that although the contracts of employment used by CESDL mentioned the payments which were available to those using their cars on CESDL's business, they did so in a different paragraph from that in which the employee's salary was identified, and in no case was the lump sum element, where payable, included within the salary. It was common ground that the lump sums were not taken into account in the calculation of employees' pensionable pay.

8. The decision says very little about the numbers of miles covered on CESDL's business by different members, or classes of members, of its staff, though it is apparent from material produced to the tribunal and made available to me—and not in dispute—that the training advisers generally travelled quite large distances, while the senior staff and the directors, or most of them, travelled comparatively modest distances, in some cases less than the 2,500 miles used, or purportedly used, as the demarcation between the two schemes. The tribunal

accepted the evidence of CESDL's managing director about his rationale for structuring the scheme as he did, namely that he considered allowing all staff to claim 40p per mile could have the effect of encouraging them to profit from that allowance, while the payment of a lump sum by monthly instalments gave them some certainty of being able to meet hire purchase or similar commitments incurred in the acquisition of cars of a reasonable standard: it recorded that such a requirement, imposed in order that CESDL's image was not impaired, was spelt out in the staff handbook. Despite the absence of specific findings, it is apparent from the tribunal's decision that there was no real correlation between the lump sum and the mileage covered by an individual employee. As Mr Summers accepted, the payment was made at a fixed flat rate, dependent on the employee's grade, and did not vary by reference to the miles actually covered.

9. The tribunal also found that the salaries paid by CESDL increased over the relevant years by, typically, 3 or 4%, whereas there was only one increase in the lump sum (and in the lower rate of mileage payment). It concluded from this difference that the increase in the travel allowance (as it described the aggregate of the mileage payment and the lump sum) was not linked to the salary increases. It viewed that as an important finding, as is plain from paras 25 and 26, in which the tribunal set out its reasons for determining the appeal as it did:

> "25. Clearly there are indications, if taken separately, that could lead to a conclusion either that the lump sum payments were additions to salary or that they were paid as motoring expenditure but we have decided that, taking all the evidence into account, they were the latter. The most important single piece of evidence is the absence of a link between the increase in salary and the increase in the motoring allowances. [CESDL's] rationale for structuring the payments as it did is also significant.
>
> 26. Accordingly we find that the payments in question were not paid as earnings and so the appeal is allowed."

The law

10. The relevant law is to be found in reg 22A of the Social Security (Contributions) Regulations 2001, as amended by the Social Security (Contributions) (Amendment No 2) Regulations 2002. The regulation, as so amended and as it was in force throughout the relevant period, was as follows:

> "(1) To the extent that it would not otherwise be earnings, the amount specified in paragraph (2) shall be so treated.
>
> (2) The amount is that produced by the formula—
>
> **RME - QA**
>
> Here—
>
> **RME** is the aggregate of relevant motoring expenditure within the meaning of paragraph (3) in the earnings period; and
>
> **QA** is the qualifying amount calculated in accordance with paragraph (4).
>
> (3) A payment is relevant motoring expenditure if—
>
> (a) it is a mileage allowance payment within the meaning of section 229(2) of ITEPA 2003;

(b) it would be such a payment but for the fact that it is paid to another for the benefit of the employee; or

(c) it is any other form of payment, except a payment in kind, made by or on behalf of the employer, and made to, or for the benefit of, the employee in respect of the use by the employee of a qualifying vehicle.

Here 'qualifying vehicle' means a vehicle to which section 235 of ITEPA 2003 applies, but does not include a cycle within the meaning of section 192(1) of the Road Traffic Act 1988.

(4) The qualifying amount is the product of the formula—

M × R

Here—

M is the sum of—

(a) the number of miles of business travel undertaken, at or before the time when the payment is made—

(i) in respect of which the payment is made, and

(ii) in respect of which no other payment has been made; and

(b) the number of miles of business travel undertaken—

(i) since the last payment of relevant motoring expenditure was made, or, if there has been no such payment, since the employment began, and

(ii) for which no payment has been, or is to be, made; and

R is the rate applicable to the vehicle in question, at the time when the payment is made, in accordance with section 230(2) of ITEPA 2003 and, if more than one rate is applicable to the class of vehicle in question, is the higher or highest of those rates."

11. Section 229(2) of ITEPA 2003 (the Income Tax (Earnings and Pensions) Act 2003) came into force on 6 April 2004. It re-enacted, without significant amendment, provisions of the Income and Corporation Taxes Act 1988 to which the 2001 Regulations previously referred. For present purposes, therefore, it is sufficient to consider the ITEPA provisions. Section 229(2) defines a "mileage allowance payment" as "amounts … paid to an employee for expenses related to the employee's use of … a vehicle for business travel". Other provisions impose various conditions, of no relevance in this case. I shall return to the significance of this definition. It is and was common ground that the sums paid by reference to the miles actually driven fall within reg 22A(3)(a), that reg 22A(3)(b) is not in point, and that the issue before me is whether the lump sum payments fall within reg 22A(3)(c). It is also common ground that the employees' cars were all qualifying vehicles within s 235 of ITEPA.

12. The effect of reg 22A is that mileage allowance payments are to be treated as earnings save to the extent, first, that they amount to "relevant motoring expenditure" not exceeding the prescribed qualifying amount and, second, they are not earnings for some other reason. The first proviso allows for some payments up to a certain threshold to be excluded from being treated as earnings,

the second is designed to avoid double counting. The threshold for the first proviso is found, as reg 22A(4) shows, by multiplying the number of miles of business travel undertaken by the rate per mile prescribed by s 230(2) of ITEPA. It was accepted that the rates of allowance per mile paid by CESDL came within s 229(2) and did not exceed the rate prescribed by s 230(2) in any case, and it was for that reason that those payments were not to be treated as earnings and did not attract NICs. CESDL has always accepted that only so much of the lump sums as do not exceed the amounts determined in accordance with reg 22A(4) (when added to the mileage payments made to the employees) may be exempt from NICs, and it has limited its claim accordingly. HMRC accept that if a refund is due at all, the claim has been correctly calculated.

HMRC's case

13. The essence of Mr Adkinson's argument was that although the tribunal had identified as the first issue whether the lump sum payments were earnings in any event, and had decided they were not, it had not gone on to consider whether they represented relevant motoring expenditure within the meaning of reg 22A(3). It had instead decided the appeal on the footing that if the payments were not earnings they must be motoring expenditure: so much was apparent from para 25 of the decision, set out above. The question the tribunal had asked did not properly address the legislative test. Moreover, in addressing the question it had asked itself, it had ignored, or had failed to take into account, the facts that there was a contractual entitlement to the lump sums, that the amount paid differed depending on the grade of employee rather than the grade of car, that there was no correlation between the amount paid and the distance travelled and that the payments were (according to the rather scant evidence adduced by CESDL) determined by reference to the estimated running costs of a single model of car covering 15,000 miles a year of which half were assumed to be for business purposes, regardless of the fact that employees might run almost any car they chose. In addition it failed to police the scheme properly by withdrawing the lump sum from employees whose annual business mileage fell below 2,500, and its treatment of employees on sick leave was illogical, since the payments were made for 12 weeks even though the employee undertook no business travel, and was then withdrawn even though the cost of acquiring the car, the supposed rationale behind the payments, would still have been incurred by the employee.

CESDL's case

14. Mr Summers argued that the tribunal's conclusion was a straightforward finding of fact, and was not irrational, such that it might be disturbed on appeal in accordance with the principles described in *Edwards (Inspector of Taxes) v Bairstow* [1956] AC 14. He relied on the principle that both the income tax and the national insurance legislative provisions were drawn in ways, even if not identical, which had the same aim, that is of allowing relief for both tax and NIC purposes on payments made to reimburse travelling expenses, up to prescribed limits. The legislation should be construed purposively, and how the arrangements were structured was irrelevant, as long as the purpose and the limits were not offended. He referred me to the observation of Lord Nicholls of Birkenhead in

Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes) [2005] 1 AC 684 at [36], to the effect that one must take

> "the two steps which are necessary in the application of any statutory provision: first, to decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, to decide whether the transaction in question does so. As Ribeiro PJ said in *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46, para 35:
>
> > 'the driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically.'"

Although both *Barclays Mercantile* and *Arrowtown Assets* were cases about avoidance arrangements, which this case was not, the principles to be applied were the same.

15. The purpose of making the payments in this case was to reimburse to the employees, within the statutory maxima, the cost of the motoring expenses they incurred on their employer's business. The fact that payment was made in a lump sum, or in fact as a monthly payment, was an administrative simplification which did not affect the underlying principle. The First-tier Tribunal addressed the correct question and came to the correct answer.

16. Moreover, the First-tier Tribunal's decision was consistent with HMRC's own published guidance, which expressly recognised that payments might be made by way of lump sum allowance. Payment by way of lump sum rather than on a mile-by-mile basis did not involve any loss to the Exchequer because of the statutory maxima, which CESDL had respected in calculating its claim. That CESDL had structured its payments in one way rather than another was rightly viewed by the First-tier Tribunal as immaterial.

Discussion and conclusions

17. I accept Mr Summers' argument that it is not essential that payments be made on a mile-by-mile basis, and that payment by round-sum allowance may be permissible. So much is apparent from the wording of reg 22A itself, which does no more than prescribe the manner in which the calculations of the qualifying amount and the residue of relevant motoring expenditure, to be treated as earnings, are to be calculated. That prescription carries with it no implication about the permissible approaches to the determination of the payment itself. For similar reasons it seems to me that the various other factors identified by Mr Adkinson, though not irrelevant, are in reality supplementary details supporting his principal argument that the First-tier Tribunal asked itself the wrong question, an argument which in my judgment is irresistible. I add for completeness that I do not consider it significant that the lump sums were calculated by reference to a single vehicle; if round sum payments are permissible at all, some degree of arbitrariness is almost inevitable (just as the maximum amount per mile of 40p allowed by ITEPA s 230(2) is arbitrary). I also read little into the fact that payments continued for a period to those on sick leave. Though that fact lends

some support to HMRC's argument, it might equally be regarded as no more than a sympathetic gesture by a responsible employer.

18. It is plain from para 25 of its decision that the First-tier Tribunal was drawing a distinction between earnings, in the shape of additions to salary, and motoring expenditure. Despite Mr Adkinson's criticisms, I see no great difficulty in characterising the lump sums as payments in respect of motoring expenses. But it is not enough that the payments represent, or are intended as, reimbursement of motoring expenditure; they must be of "relevant motoring expenditure" within the meaning of reg 22A(3), which in turn requires that the payment satisfies one of the three prescribed conditions. Although it is agreed that the only relevant condition is (c), it is in my view necessary to examine also what is said in (a) and (b).

19. Condition (a) brings a payment within the definition of "relevant motoring expenditure" if it is a "mileage allowance payment" as defined by s 229(2) of ITEPA. I set the definition out again for convenience: it encompasses "amounts … paid to an employee for expenses related to the employee's use of … a vehicle for business travel". The essence of the definition is clearly the link between the payment and the *use* of the vehicle. The draftsman's use of the phrase "mileage allowance payment" makes it quite clear that there must be some link between the payment and the miles driven.

20. Condition (b) does no more than include within the definition those payments which would come within (a) but for the fact that they are paid to a third party. An employee might, for example, be able to obtain fuel while travelling on business by using a payment card, the employer bearing the cost.

21. Condition (c) appears at first sight to be of wider application, by including "any other payment", but again one sees the phrase "in respect of the use by the employee" of the vehicle. It is in my view impossible to accept, as Mr Summers' argument requires, that the draftsman took care in conditions (a) and (b) to restrict the types of payment which fall within the definition, and then in condition (c) relaxed the very same restriction. In my judgment condition (a) sets the scene; the purpose of (b) and (c) is to bring within the definition payments which might not fit within (a), but which are of the same character.

22. At para 9 of its decision the First-tier Tribunal first made the point that it was necessary to decide whether the payments in question were earnings because, if they were, there was nothing more to determine: NICs would be due on them, however the employer and employee chose to describe them. It decided that point in favour of CESDL and HMRC do not, in terms, attack that finding. In the same paragraph the tribunal identified the need next to determine whether the payments were of relevant motoring expenditure, but in my judgment it then failed to make that determination. It may well have been side-tracked by its understanding, recorded at para 13, that "[i]f the lump sums were not earnings the respondents accept that they would then be part of the RME", a concession which, Mr Adkinson told me, he had not made and which, it seems to me, HMRC are most unlikely to have made since it is inconsistent with the thrust of their argument, as it is set out in their statement of case. Critically, in my view, there is nothing in

the decision which suggests that the link between the payments and the use of the vehicles was considered by the tribunal.

23. Unfortunately for CESDL, its own evidence shows that the link is absent. The managing director's explanation of the schemes which I have mentioned above indicated that the payments were made, not to defray the cost of use, but to defray the cost of acquisition or ownership. The sums paid bore no relation, save by chance, to the scale of the use made by the employee of his car for CESDL's purposes; as Mr Adkinson argued, and I agree, it is difficult to see how a payment which is made irrespective of the number of miles covered can properly be said to be related to use, even leaving aside what I have said about the drafting of s 229(2). The fact that senior employees using their cars very little received more than junior employees using their cars extensively, too, is inconsistent with a link between payment and use. Moreover, Mr Summers' argument that the lump sum represented a payment in respect of standing charges while the 12p or 13p per mile covered the marginal costs seems to me to support HMRC's rather than his own case: standing charges are a consequence of ownership, or of possession, rather than of use. It is true that (as I understand the findings of fact) only those employees who made some use of their cars for CESDL's business received any payment, but for the reasons I have given it is in my view clear that the necessary link is with the degree, rather than the mere fact, of use. I am unable to read s 229(2) in any other way.

24. It is no answer that reg 22A(4) limits the amount allowable. The calculation required by that paragraph must be related back to para (2): their combined effect is not simply to restrict the amount which is eligible for exemption from NICs, but to restrict the amount of relevant motoring expenditure which is so eligible. In other words, if the payment is not of relevant motoring expenditure, no relief is available. Nor does it help CESDL's case that a purposive construction is necessary, since the plain purpose of the legislation, as I read it, is to restrict the relief to the qualifying amount determined in accordance with the same provisions.

25. Mr Summers argued that the tribunal's finding was one of fact, and it seems to me from the manner in which para 25 is worded that the tribunal took the same view. Mr Adkinson argued that it was a finding of law, alternatively that if it was a finding of fact it was perverse. It will be apparent from what has gone before that in my judgment the tribunal reached its finding, whether it is characterised as one of fact or of law, after asking itself the wrong question or, at least, an inadequate question, and that the answer given was based on an error of law, with the consequence that it is open to me to disturb it if I am satisfied it was wrong. I am so satisfied: the payments were not of relevant motoring expenditure because they were not paid by reference to, or with regard to, the use by the employees of their cars on CESDL's business. The appeal must therefore be allowed.

26. Mr Adkinson accepted that if I allowed the appeal I might remit the matter to the First-tier Tribunal for re-determination, but his preferred course was that I re-make the decision myself. Mr Summers urged me to remit to the First-tier Tribunal. Remission would be the appropriate course if I had concluded that the facts should be found again, or further facts should be found. I am, however,

satisfied in this case that there is no need for that to be done. The facts already found are adequate to enable me to re-make the decision, and I adopt that course. The payments were not of relevant motoring expenditure and they were accordingly emoluments of employment liable for NICs. CESDL's claim for reimbursement must fail.

Colin Bishopp

Upper Tribunal Judge

Re-released in amended form: 25 November 2011

Formatted: No underline