

# **A summary of responses to National Minimum Wage workers:**

**travel and subsistence expenses schemes**



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# 1

## Introduction

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**1.1** The consultation *National Minimum Wage workers: Travel and subsistence expenses schemes* was published in February 2010. The consultation closed on 6 May 2010. This document summarises what the Government has learned through the consultation and sets out the Government's policy approach, as informed by the responses received.

**1.2** Workers paid at or near the National Minimum Wage (NMW) are able to participate in travel and subsistence schemes operated by some Employment Businesses<sup>1</sup> and umbrella companies. These schemes provide savings of tax and National Insurance Contributions (NICs), but because they involve a reduction in the amount of the worker's pay which is liable to NICs, this can impact adversely on his access to earnings-related contributory benefits.

**1.3** A potential solution to this problem was identified, which involves amendment to the NMW Regulations. The consultation set out the proposed amendment and invited comments. The objective of the consultation was to develop the best solution to this problem.

**1.4** The Government received a total of 54 responses. These were split very much into two groups: those very strongly in favour of action and those very strongly opposed. More than 20 of the responses were received from Employment Businesses and umbrella companies which seemed to have implemented, or which wanted to implement, a travel and subsistence scheme. The vast majority of these were against any action being taken to prevent NMW workers being able to participate in these schemes. However, other Employment Businesses, of which a few advised that they were of a significant size, placing in excess of 10,000 workers each week, together with some representative bodies, wholeheartedly agreed that action should be taken.

**1.5** The Government has considered carefully the responses from interested parties and on balance considers that action should be taken in relation to these arrangements where they involve NMW workers. Many of the responses received pointed out that these schemes do involve exploitation of the low paid, with the benefits skewed towards the Employment Business. There is also evidence, even from those opposed to the proposals, that these NMW workers, who represent some of the most vulnerable, do not understand the arrangements or their implications.

**1.6** The objective of the solution outlined in the consultation document was to ensure only that expenses paid to workers for travel (including associated subsistence costs)<sup>2</sup> to a temporary workplace would not count for the purposes of NMW. A number of respondents pointed out that the particular amendment to the NMW Regulations identified in the consultation had unintended consequences. This was because, if adopted, it would require employers to pay these travel expenses on top of NMW pay. It was not the intention that employers would be forced to pay these expenses and a revised proposed amendment to the NMW Regulations, which only serves to exclude the expenses, is set out at Annex A.

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<sup>1</sup> As defined in the Employment Agencies Act 1973, as amended by the Employment Relations Act 1999.

<sup>2</sup> Reference to travel expenses includes all other associated expenses which qualify for relief in accordance with ss337 and 338 ITEPA 2003 (DN:check reference)

1.7 Although the consultation document provided that any action would take effect from 1 October 2010, the proposed amendment will now take effect from 1 January 2011. This will allow employers to make the necessary changes to systems and processes.



# 2

## Background

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**2.1** Travel and subsistence schemes, operated by some Employment Businesses and umbrella companies, take advantage of the tax relief and the disregards that exist for the purposes of National Insurance Contributions (NICs) which relate to travel from home to a temporary workplace. By creating a single employment contract for each worker, these schemes convert what would otherwise be a series of permanent workplaces (for which there is no tax relief available on travel expenses) into temporary workplaces (for which tax relief on travel expenses is due). Workers agree that an amount of pay, which would otherwise be subject to tax and NICs, is replaced with expenses payments for travel to a temporary workplace. In this way, these schemes deliver tax and NICs savings for workers. Also, Employment Businesses or umbrella companies save employer's NICs on the pay which has been replaced with tax and NICs-free travel expenses.

**2.2** Workers paid at or near the NMW may participate in these schemes as the expenses paid for travel to a temporary workplace can count towards NMW pay.

**2.3** A number of problems arise as a result of NMW workers' participation in travel and subsistence schemes. Firstly, the reduction in their pay for tax and NICs purposes in return for the payment of travel expenses can adversely impact on NMW workers' access to earnings-related contributory benefits. The cases that HMRC have seen suggest a worker participating in a travel and subsistence scheme is only very slightly better off in terms of take home pay. In some schemes, it is the Employment Business or umbrella company employing the worker who retains the largest part of any financial benefits, with only a small proportion of these being passed on to the worker.

**2.4** Some businesses do not wish to implement travel and subsistence schemes for NMW workers as they consider that they involve profiting from low paid workers. Also, some businesses, for a number of reasons, are not able to implement such schemes. Such businesses suffer a competitive disadvantage compared to those businesses which do implement these schemes. The participation of NMW workers in these arrangements also gives rise to an Exchequer risk as not all NMW pay is subject to tax and NICs.

**2.5** The consultation document proposed that travel and subsistence expenses, which are allowable for tax and NICs purposes, do not count towards NMW pay. It concluded that the best way to do this was through amendment to the NMW Regulations, as this targets the particular issue of NMW workers participating in these schemes. It does not affect other workers. The solution also does not impact on the tax and NICs treatment of travel expenses.



# 3

## The consultation

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**3.1** The objective of the consultation was to develop the best solution to the problem. The Government welcomed views from interested parties on the consultation document and the impact assessment and particularly in relation to the questions set out at paragraph 5.1:

**Question 1:** The Government believes that amending the NMW Regulations to exclude expenses which relate to travel to a temporary workplace from counting towards NMW pay is the best approach in dealing with this problem. Are there alternative approaches which would achieve the same outcome and which you believe that the Government should consider? If so, then please give details of these.

**Question 2:** Will amending the Regulations in this way adversely impact on NMW workers in a way that we have not anticipated? If so, please provide details.

**Question 3:** What are your views on the potential implementation date of 1 October 2010, if the proposed changes to the Regulations are adopted?

**Question 4:** What would be the impact of changes to Regulations on administrative processes and costs to business?

**Question 5:** Do you have any comments on the accompanying Impact Assessment?

**3.2** The consultation was launched on 11 February 2010 and closed on 6 May 2010. A wide range of organisations and individuals responded to the consultation. Most of the responses reflected the views of Employment Businesses, but professional and representative bodies, together with the Equality and Human Rights Commission, the Gangmasters Licensing Authority and the Low Pay Commission also responded.



# 4

## Overall view of the proposals

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**4.1** The vast majority of respondents were either strongly for or strongly against the proposals, with only one or two of the responses not coming down firmly on one side or the other. The overall themes emerging from the responses are summarised below.

### Exploitation

**4.2** Those responses that considered the issue of possible exploitation of NMW workers agreed that any action seeking to prevent this could only be positive. However, some disagreed that these arrangements gave rise to the exploitation of workers, with others believing that this was clearly the case.

**4.3** The consultation document suggested at paragraph 3.33 that workers might have little choice about participating in travel and subsistence schemes. A number of respondents disagreed with this view, confirming that, in their opinion, workers freely entered into these arrangements and furthermore have the ability to opt out subsequently if they so wish. On the other hand, some respondents were very concerned that in reality workers were not given a true choice as to whether to participate or not, with one respondent commenting that in their experience any worker who refuses to sign up will not be given work.

**4.4** Some of those respondents who were not in favour of the proposal did acknowledge that invariably employees are asked to opt-out of the arrangements, rather than opt-in. They admit that, if this is not properly explained to the workers, this process opens up the question as to whether they truly know what they are getting into.

**4.5** The consultation document made reference to the disproportionate savings being made by the Employment Business compared to the worker. In examples seen by HMRC, the Employment Business benefits financially by 4 or 5 times more than the worker. One of the respondents in favour of preserving the status quo commented that the significant savings made by the Employment Business meant that in the current economic climate, this was a way of saving jobs. Another commented that Employment Businesses should not be begrudged benefiting themselves in return for providing workers with access to savings of tax and National Insurance Contributions (NICs) savings. One Employment Business, which said that it was reluctantly driven by commercial pressures to introduce a travel and subsistence scheme, confirmed that the majority of the benefits fall to the Employment Business and not the worker and also that workers do not understand the schemes.

**4.6** Most of those in favour of the proposal expressed concern that the benefits of the scheme are very much skewed in favour of the Employment Business. One respondent commented that from the evidence that they had seen, the worker benefits by £5 per week, but the Employment Business by between £30 and £45 per week.

**4.7** Another respondent, commenting on the savings being made by the Employment Business, suggested that the consultation document assumed these workers are naïve. The respondent went on to say that these workers would in fact be fully aware of the level of savings being made by the Employment Business. This is because the workers would clearly be capable of seeing from their payslip that there is a difference between the amount of salary that they were sacrificing and the amount of expenses that were being paid to them. Some respondents asked

that HMRC should consider making it a condition of issuing an expenses dispensation, which is key to these schemes, that the tax and NICs savings which relate to the worker have to be passed on to the worker. Also, there was a request that HMRC provide guidance for workers on these schemes or again, as a condition of issuing a dispensation, require that employers provide full guidance to workers.

## The Government response

**4.8** The way in which travel and subsistence schemes operate is complex. Workers paid at or near the NMW include some of the most vulnerable in society, e.g. migrants for whom English is not their first language and those who are unqualified, without good numeracy and literacy skills. It is reasonable to presume that these workers may not fully understand how these schemes work, nor that they have the ability to opt out.

**4.9** Also, there is evidence to support that presumption. The report on the Inquiry into recruitment and employment in the meat and poultry processing sector carried out by the Equality and Human Rights Commission looked at agency workers within this sector. It reported that 70% of these workers are migrant workers and over one-third of those interviewed did not understand the contents of the documentation that their Employment Business had given them, but felt under pressure to sign up to it. Some had tried to get the documents translated but none had refused to sign them beforehand.

**4.10** In addition, over the last 5 years HMRC compliance teams have interviewed an estimated 400 to 500 workers, the majority of whom were paid at or near the NMW. Virtually none of these workers understood in any meaningful way the contractual terms of their engagement. Although they may understand that if they are in a scheme they can earn £5 or so a week more, but how that is achieved is not explained nor are the consequences of what that might mean for benefits.

**4.11** HMRC has received a number of emails from workers expressing concern about travel and subsistence schemes – examples of which are set out below.

### **Box 4.A: Examples of emails HMRC has received:**

**“We are a group of polish people and are very worried about our taxes.** Our employer tell everything is ok but we don’t pay tax. We earn 5.8 an hour and we take it all home. (sic)”

“I am a temporary worker for xxxx. I have my pay slips weekly, but I discovered that agency is deducting subsistence payments from my wage (sic). I did not agree this with the agency.”

**4.12** In 2006, the Low Pay Commission (LPC) looked at salary sacrifice arrangements and NMW, in particular in relation to substituting cash salary for benefits in kind, such as childcare vouchers. They recommended that salary sacrifice schemes should not count towards NMW pay. Their report in 2006 stated “we strongly believe that the minimum wage should be as simple as possible for employers and workers to understand....It is clear to us that allowing salary sacrifice schemes to count towards the minimum wage would depart from the principle..” The report went on to say that although the LPC knew that some employers would put in place measures to ensure that their workers understood fully the implications of participation in a salary sacrifice scheme, including the potential impact on entitlement to state benefits, they were concerned that others may not ensure that their employees were able to take such a fully informed decision. The LPC said “we believe that low-paid workers are more vulnerable to exploitation by unscrupulous employers and more at risk of reducing their entitlement to state benefits”.

**4.13** From the responses received to the consultation, there is a widespread acceptance by even those who are against the proposals that the Employment Businesses gain more from the scheme than the worker. One respondent remarked that there is no legal definition of “exploitation”, but that it is widely understood as describing the position where one party unfairly uses another party to their own advantage. As there is evidence that most of the workers interviewed do not understand these arrangements, it is reasonable to conclude that the benefit obtained by some Employment Business is indeed unfair and, based on this definition, that some of the schemes are exploitative.

## **Competitive disadvantage**

**4.14** Paragraph 3.35 of the consultation document made the point that some Employment Businesses are unwilling to offer these schemes to workers as they believe them to involve profiting from low paid workers. As a result, such businesses would be put at a competitive disadvantage. One respondent commented that it could not be accepted that any company could rationally or sensibly take this view. Others also strongly disagreed that these arrangements resulted in any form of competitive disadvantage within the temporary labour market. This is because the Employment Business makes a commercial decision as to whether to implement the arrangements or not – they could, for example, pass on all the savings to the worker.

**4.15** Those Employment Businesses supportive of the proposals disagreed, saying that they believed the schemes were unfair and unethical. They made the point that these arrangements were only implemented by Employment Businesses with the sole objective of maximising profit and that these profits have then been used to compete unfairly. One representative body advised that during the recession, there has been acute pressure to cut margins, especially at the lower paid end of the market where there is plenty of supply. This has led to huge differences in the cost of supply of these workers, depending on whether a travel and subsistence scheme is being operated, resulting in market distortions.

## **The Government response**

**4.16** The responses to the consultation show that some Employment Businesses do hold the view that travel and subsistence schemes involve the business in profiting from low paid workers. The Government’s conclusion at paragraph 4.13 above, that some of the schemes are exploitative, demonstrate that this view, held by some Employment Businesses is not unreasonable. The unwillingness of some Employment Businesses to offer these arrangements does, as a matter of fact, put them at a competitive disadvantage compared to those businesses which do offer them.

## **Discriminating against low paid workers**

**4.17** All the respondents opposed to the proposal made the point that this would result in those paid at or near NMW being excluded from travel and subsistence schemes but those who are more highly paid being able to continue to benefit. They believe this to be completely unfair and discriminatory as the low paid have most need of the financial benefits that these schemes offer.

**4.18** Those who were in favour of the proposals did not see this a problem – the negatives of the proposals were outweighed by the positives.

## **The Government response**

**4.19** Reference to the LPC 2006 report is again relevant here. The LPC said that they wanted to ensure that the value of the NMW is protected. As a result, their recommendation was that workers paid at or near the NMW should not be able to participate in salary sacrifice

arrangements for childcare vouchers, bikes to work etc, if any salary sacrifice would take their earnings below the NMW. As the LPC reported, this preserves simplicity in the NMW rules, which they believe is why the NMW has been effective as a wage floor. They believe that it is important that workers know what they are entitled to employers or engagers are easily able to demonstrate that they have met their legal obligations. HMRC should be put in the position of being able to enforce the NMW effectively and simplicity in the arrangements is key to this.

**4.20** The LPC also reported that any negative consequences of opening up the definition of minimum wage pay to accommodate salary sacrifice schemes would fall hardest on the lowest-paid. So, by not allowing workers paid at or near the NMW to participate in salary sacrifice arrangements relating to travel and subsistence expenses, the Government is ensuring that, with the exception of accommodation, there is a consistent approach on salary sacrifice in relation to NMW workers.

## **Wider impact than those paid at or near NMW**

**4.21** A number of responses stated that the impact of the proposals was wider than that envisaged by the consultation document and would impact workers earning up to a rate of £9 per hour. This is because as a result of the proposed changes, a worker earning £9 per hour would not be able to enter into a salary sacrifice in return for the payment of travel and subsistence expenses which took his hourly rate below the level of the NMW, currently £5.80.

## **The Government response**

**4.22** The consultation document did refer to workers paid at or near the NMW and the Government recognises that those earning above the NMW level will be affected by the proposals.

**4.23** In terms of workers earning up to £9 per hour, such a worker could continue to sacrifice up to £3.20 per hour (at current NMW rates) and be unaffected by the proposal (providing that the expenses paid to the worker are properly incurred). £3.20 per hour represents more than one-third of the worker's gross pay for tax and NICs purposes and in a 40-hour working week, the worker would be giving up £128. (The pre-sacrifice net pay would be £286.) Assuming, as seems likely that the expenses paid to the worker are lower than the amount sacrificed, say £100, then this means that the worker would have to spend more than 35% of their pre-sacrifice net pay in getting to work in order to be affected by the proposal. The amount of expenses which would properly qualify for tax relief and be disregarded for NICs will depend on the facts, but the Government questions whether it is credible that many workers with a net take home pay of £286 would be spending more than £100 per week in getting to their place of work.

## **Impact on earnings-related contributory benefits**

**4.24** All those opposed to the proposals strongly believe that the impact on earnings-related contributory benefits was overstated in the consultation document. Their view was that, providing the pay after salary sacrifice is at least the amount of the Lower Earnings Level<sup>3</sup> (LEL), workers would be unaffected. They advised that most properly run schemes should ensure that earnings do not fall below the LEL as otherwise there are no tax or NICs savings to be made and this is sufficient to preserve entitlement to contributory benefits. Many thought that requiring employers to ensure that any reduction in pay did not take the worker below the LEL would be sufficient.

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<sup>3</sup> The LEL is set at £97 for 2010/11. If a worker's earnings reach or exceed this level, but do not exceed the Earnings Threshold (£110 per week for 2010/11), he will not pay NICs but will be treated as having paid them for the purposes of benefit entitlement.



**4.25** In relation to achieving the “qualifying earnings factor”<sup>4</sup>(QEF), many of these respondents thought that this would be achieved because the worker would be eligible for NICs credits if claiming Jobseeker’s Allowance (JSA) or Working Tax Credits (WTC). A few respondents thought that some workers, mostly the young and migrant workers would not in any case be concerned about securing a UK State Pension. Others made the point that if the QEF is not achieved, income based benefits would be available to the worker and that the consultation document had overlooked this. Some thought that if these workers had concerns about their benefit position, they could in any case pay Class 3 NICs, which are voluntary contributions.

**4.26** Those in favour of the proposals believed that the short-term financial gains that workers receive would not benefit them in the long term. They also thought it likely that the workers themselves did not understand the impact on their benefit entitlement, as this would not have been explained to them.

## The Government response

**4.27** The Government agrees that it is difficult to predict with any certainty what impact participation in a travel and subsistence expenses scheme will have on a worker’s access to earnings-related contributory benefits. This is because there are so many variables to take into account, such as work history etc. The consultation document made clear that participation in such schemes **could** impact on benefit entitlement. By participating in travel and subsistence schemes, NMW workers reduce their pay, on which NICs is paid. This, depending on how many weeks they are able to work for, puts at risk their ability to achieve the QEF. This is most likely to be the case in relation to eligibility for both basic and additional State Pension.

**4.28** The most significant impact of these schemes on benefit entitlement relates to the additional State Pension. The additional State Pension builds up in each year between age 16 and State Pension age for which NICs on earnings at or above the QEF have been paid. (Not all NICs credits count towards the additional State Pension for this purpose.) So, an individual who spends some of the year working and some time unemployed may not be able to patch together a qualifying year. If the worker loses out on a qualifying year, the loss of benefit here is enduring; the worker would lose out on income throughout his retirement. Whether or not workers who are young or who are migrants are interested in securing a pension is not relevant here; if their earnings for NICs purposes are sufficient to meet the contribution conditions, then they are eligible to receive the relevant pension.

**4.29** Payment of voluntary Class 3 NICs may not be appropriate for these workers. The cost of Class 3 NICs is currently £12.05 per week and they only count towards basic State Pension and bereavement benefits, not JSA or Employment and Support Allowance. The cost of Class 3 NICs will be significant for those earning at or near NMW and may be greater than their uplift in take home pay.

**4.30** The Government does not agree that legislating to require employers to maintain earnings for workers who participate in these schemes at or above the LEL is an effective solution. The impact of these schemes on the worker’s ability to achieve the QEF has also to be taken into account.

**4.31** Respondents pointed out that income related benefits may be available for workers, in place of earnings-related contributory benefits. The contributory principle is one of the key elements of our welfare system. People pay contributions while they are working and receive benefits when they are unable to work. Income-related benefits exist as a safety net for those who may not, for whatever reason, have entitlement to contributory benefits, and entitlement

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<sup>4</sup> In order to achieve the qualifying earnings factor, the worker must have qualifying earnings (or in some cases credits) of at least 52 x the LEL

depends on the personal circumstances of the individual, and, where relevant, their partner. As income-related benefits are funded from taxation, it may be perceived as unfair that an individual qualifies for payment as a result of arrangements which have been put in place with the objective of reducing the amount of tax and NICs payable by that individual and his employer.

# 5

## Responses to the consultation questions

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**Question 1:** The Government believes that amending the NMW Regulations to exclude expenses which relate to travel to a temporary workplace from counting towards NMW pay is the best approach in dealing with this problem. Are there alternative approaches which would achieve the same outcome and which you believe that the Government should consider? If so, then please give details of these.

**5.1** Those respondents who are in favour of the proposals believed that excluding these expenses from counting towards NMW is the best approach. However, some of these respondents and others against the proposals highlighted that the potential approach set out at paragraph 4.2 of the consultation document, i.e. an amendment to Regulation 34 of the NMW Regulations has an unintended consequence. Amending the NMW Regulations in this way would mean that they would require the employer to pay these expenses in addition to NMW pay and the employer would have no choice about paying them.

**5.2** Some believed that the Government should consider the proposal more widely, i.e. that the issue of the savings of tax and National Insurance Contributions (NICs) being made on these expenses should be considered in relation to all workers and not just those paid at or near the NMW. Also, some thought that dispensations should only be granted where the scheme required that receipts were provided for all travel and subsistence expenditure that workers incur.

**5.3** Those not in favour of the proposal believed that it was only necessary to stop schemes where pay is sacrificed to a level below the LEL, as discussed at paragraph 4.24. These respondents believe that the problem relates only to aggressive and abusive schemes. They suggested that the solution to this is greater compliance activity by HMRC to ensure enforcement of the existing rules. Also HMRC should issue clear guidance as to how these schemes should be operated. Some also believed that when issuing an expenses dispensation, HMRC should attach conditions to this which would then prevent many of the abuses from occurring.

### The Government response

**5.4** The Government's intention was only to exclude the payment of expenses for travel to a temporary workplace from counting as pay for NMW purposes; it is not the intention to require the employer to pay these expenses in addition to NMW pay. After further consideration, the solution set out in the consultation document may not be appropriate. For this reason, an alternative amendment to the NMW Regulations is proposed which is outlined at Annex A.

**5.5** Following the 2008 consultation on travel and subsistence schemes and tax and NICs, which confirmed that there were poor levels of compliance in this area, HMRC refocused its efforts to ensure that the current regime is properly applied. The point was made that if compliance did not improve, the Government might return to this at a later date. This refocused, ongoing compliance activity highlights continuing levels of non-compliance. This includes Employment Businesses operating as if dispensations have been issued when they have not and poor control being exercised over expenses paid to workers.

**5.6** In terms of the role that HMRC plays in agreeing a dispensation, HMRC are not able to prescribe or influence what types of expenses payments an employer may pay or reimburse their staff or the level of such payments; these are matters for employers to decide. It is, however, HMRC's function to determine the tax and NICs implications of payments made by employers and to advise employers accordingly.

**5.7** HMRC continues to enforce the existing rules and take action against arrangements that contravene legislation, whether or not these involve workers paid at or near the NMW. However, the particular problem that the Government wishes to tackle here is not one of contravention of the rules but whether the rules should allow NMW to be able to participate in travel and subsistence schemes.

**Question 2:** Will amending the Regulations in this way adversely impact on NMW workers in a way that we have not anticipated? If so, please provide details.

**5.8** Those respondents who are not in favour of the proposals strongly believed that the consultation document had underestimated the impact of the reduction in take home pay that the worker would suffer as a result of the proposals. Many referred to Example A in the consultation document which illustrated that the worker could be better off by as much as £1,500 per year, in support of their position. Others in favour of the proposals accepted that workers may be slightly worse off each week in terms of take home pay, but this would be in the range of £5 to £10.

**5.9** Many thought that the impact of the proposals on tax credits had also not been properly considered, i.e. that by participating in a scheme, potentially the worker benefits from an entitlement to an increased amount of Tax Credits. These respondents believed that these increased tax credits are a significant benefit of these schemes. Similarly, some respondents pointed out that participation in these schemes could also affect the level of other benefits that workers might access where those are determined by reference to gross pay for tax and NICs purposes, such as housing benefit.

**5.10** However, others, including those against the proposals, believe that there is unfairness in the Tax Credit position which results from these schemes. At present, where a worker participates in a travel scheme, he could receive more in tax credits than a permanent employee even though his gross pay, before salary sacrifice, may have been the same as that permanent employee and that his cash take home pay as a result of participating in the scheme will be slightly higher.

**5.11** Some respondents also raised the issue of employment rights. If a worker does not participate in a travel and subsistence scheme, then he will be engaged as an agency worker and will not be an employee of the Employment Business or the end client. By being in a travel and subsistence scheme, the worker is engaged under an overarching contract of employment. Respondents pointed out that as workers had to be employed by the Employment Business in order for the scheme to operate effectively, implementation of the proposal would mean that these schemes become ineffective and there would be no point in Employment Businesses entering into employment contracts with these workers. As a consequence, workers would lose out as they will have reduced protection in terms of their employment rights. On the other hand, some thought that the employment contracts were contrived, offering a guaranteed minimum hours of only 336 hours per year, or 6 hours per week and that workers could lose hours for refusing an assignment or being unavailable at short notice. One respondent expressed the view that the employment contracts are "not worth the paper they are written on".

## The Government response

**5.12** The Government accepts that, by implementing this proposal, workers participating in these schemes may see a reduction in their take home pay. The Government believes it unlikely that workers could lose out by as much as £1,500 per year. Example A in the consultation document was only used to illustrate how these schemes work and involved replacing the amount of pay sacrificed with exactly the same amount of expenses. This example is not at all representative of the cases that HMRC has seen, which are more in line with Example D in the consultation document, where the worker benefits by £6.45 per week. This was borne out by the responses to the consultation; many referred to the worker being only slightly better off, by about £5 per week and certainly no more than £10 per week. Furthermore, those Employment Businesses who argued that workers could be up to £1,500 per year worse off, referred only to the example in the consultation document in support of this and no real-life examples were cited in support of this.

**5.13** The Government understands the implications of the proposals on those who participate in these schemes and who claim Tax Credits. Tax Credits generally, and the WTC in particular, are intended to help make work pay for those on lower incomes. They ensure that families in the same circumstances receive the same level of support. They are not intended to provide support where arrangements have been introduced by employers which reduce the amount of employer and employee contribution to the Exchequer. Also, the Government is concerned about the unfairness that these schemes create, as those workers who participate benefit artificially from enhanced eligibility for Tax Credits, compared to other workers, with similar levels of income who do not or cannot participate.

**5.14** In relation to employment rights, based on some of the responses received to the consultation, the Government is doubtful that the overarching employment contracts do indeed confer tangible benefits for workers. Furthermore, the report of the Equality and Human Rights Commission into the Inquiry into recruitment and employment in the meat and poultry processing sector states “none of the migrant agency workers we interviewed had any idea whether they were working under a contract for services or as an employee of the agency”.

**5.15** It is also worth noting that expenses, which NMW workers incur in travelling from home to their temporary workplace, can still be met in full or in part by employers and, providing the relevant conditions are met, these would be free of tax and NICs. It is just that, as these expenses will not count towards NMW pay, they will need to be paid on top of this pay.

**Question 3:** What are your views on the potential implementation date of 1 October 2010, if the proposed changes to the Regulations are adopted?

**5.16** Those in favour of the proposals believed that this should be done at the earliest opportunity. Some believed that the implementation date should be earlier than 1 October 2010 but some thought that it may be preferable to introduce the proposals from the start of a tax year as they will affect the tax and NICs position of the employee.

**5.17** Those respondents who do not support the proposals thought that, if the proposals were to be implemented, 1 October 2010 was too early as some consultation with workers as well as changes to processes would be required. Others thought the proposals should come into effect when the labour market and economy in general is in a stronger position. One respondent thought that implementation should be phased in over 3 to 4 years.

## The Government Response

**5.18** The Government wishes to introduce the proposed change to the regulations to prevent home to work travel expenses counting towards NMW pay as soon as is practicable. The Government has reviewed the consultation responses and it has determined that this date

should now be 1 January 2011. This will allow employers sufficient time to make the appropriate changes to systems and processes.

#### **Question 4: What would be the impact of changes to Regulations on administrative processes and costs to business?**

**5.19** Some respondents believed that as workers who participate in these schemes have employment contracts, these contracts would have to be re-negotiated. Several Employment Businesses expressed that implementing changes would be costly for those businesses operating these schemes – involving changes to policy and procedures and the need for possible changes to software.

**5.20** Others thought that the impact of changes would be minimal in terms of administrative costs. Some considered that operators of the schemes would suffer a drop in profitability and where those margins are shared with end clients, this will mean an increase in costs for those clients. But, they believe that those operating ethically will see the barrier to fair competition removed. One Employment Business commented that the additional tax and NICs paid as a result of the proposed changes would reduce the burden on those who comply with the system and reduce the time that it takes for the UK to emerge from the current economic crisis.

### **The Government response**

**5.21** The Government accepts that there will be some changes to process for those operating these schemes. There will no longer be a need to process salary sacrifice arrangements through the payroll. Other changes will depend on the precise model adopted by the Employment Business and will largely result in either reversion to a standard payroll model operated by many Employment Businesses (where workers are no longer engaged under contracts of employment), or a slightly modified version of existing arrangements (where workers continue to be engaged under contracts of employment and some expenses are paid in addition to the NMW).

**5.22** Respondents to the consultation have not raised any concerns relating to administrative processes and costs to business which the Government was not aware of.

#### **Question 5: Do you have any comments on the accompanying Impact Assessment?**

**5.23** Not all respondents commented on the Impact Assessment. The responses that did comment ranged from those believing that the Impact Assessment was fair, to those who believed that it was flawed or insufficiently detailed. Those who believed that it was flawed referred specifically to the equality impact assessment, as they believe that the Government has not properly considered the impact on migrant workers, who make up a large proportion of temporary workers paid at or near NMW. Some believed that the proposals could be discriminatory because of their impact on migrant workers and the low paid in general. Some also believed that the likely increase in illegal and “cash in hand” working had also not been considered.

### **The Government response**

**5.24** The Government has now conducted a full Impact Assessment and this is set out at Annex C to this document. The Government believes that on balance the responses to the consultation document support its decision to take action to prevent NMW workers participating in these schemes.

# A

## Amendment to the NMW Regulations

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**A.1** Regulation 31 of the National Minimum Wage Regulations 1999(SI. 1999/584) sets out a list of reductions from the total remuneration payable in a pay reference period that counts towards the National Minimum Wage. The intention is to insert at Regulation 31(1) a further such reduction:

“(j) any money payments paid by the employer to a worker in the pay reference period in respect of expenses, subsistence or accommodation that are allowed as deductions from earnings under section 338 Income Tax (Earnings and Pensions) Act 2003.”





# B

## Consultation respondents

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### Representative bodies

Recruitment and Employment Confederation (REC)  
Association of Labour Providers (ALP)  
National Farmers Union (NFU)  
Freelancer and Contractor Services Association (FCSA)  
Trade Union Congress (TUC)

### Statutory bodies

The Low Pay Commission  
The Equalities and Human Rights Commission  
The Gangmasters Licensing Authority

### Professional Associations

Institute of Chartered Accountants in England and Wales  
Low Incomes Tax Reform Group  
Institute of Directors

### Other

27 Employment Businesses  
2 Umbrella Companies  
3 Accountancy firms  
A firm of solicitors  
A barrister  
8 Other businesses, advisers or individuals  
Unite the Union





# Final Impact Assessment

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The Final Impact Assessment follows overleaf

## Summary: Intervention & Options

Department /Agency:  
**HM Revenue and Customs**

Title:  
**Impact Assessment of Travel & Subsistence Schemes for Low Paid Workers**

Stage: Final

Version: Final

Date: July 2010

**Related Publications:** National Minimum Wage workers: Travel and subsistence expenses schemes – February 2010 and consultation stage Impact Assessment

**Available to view or download at:**

<http://www.hmrc.gov.uk>

**Contact for enquiries:** Robin Wythes

**Telephone:** 020 7147 2511

### What is the problem under consideration? Why is government intervention necessary?

Temporary workers paid at or near the National Minimum Wage (NMW) can participate in travel and subsistence schemes, operated by some Employment Businesses and umbrella companies. These are designed to provide tax and NICs savings while complying with NMW rules. Many of these schemes are exploitative as the employer retains most of the financial benefits and the workers have little or no knowledge of how these schemes work. Also, participation may adversely affect workers' access to earnings-related social security benefits. Those businesses not wishing to operate these schemes for NMW workers suffer a competitive disadvantage, leading to market distortion. These schemes also give rise to an Exchequer loss.

### What are the policy objectives and the intended effects?

The Government's objectives are to prevent exploitation, allow full access to earnings-related social security benefits, create a level playing field for businesses engaging temporary NMW workers, and protect the Exchequer. The amendment to the NMW Regulations should protect the contributory benefit position of low paid workers currently participating in these schemes and stop others being potentially prejudiced. It should also result in a fairer market as there would be competition on more equal terms. Expenses for travel to a temporary workplace would no longer count as NMW pay, so more NMW pay would be subject to tax and NICs, increasing the amount paid to the Exchequer.

### What policy options have been considered? Please justify any preferred option.

The options that have been considered are:

- no change - continue with the status quo; or
- amend the NMW Regulations so that expenses paid to a worker for travel to a temporary workplace, as defined for tax and NICs purposes, will not count towards their NMW pay.

In February 2010 the Government consulted on this and in the light of the responses will proceed with option 2. This will address the issue of exploitation and the potential adverse impact on workers' access to social security benefits and will create a level playing field for Employment Businesses.

### When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?

For all policy changes, compliance costs are routinely reviewed one to three years after implementation.

### **Ministerial Sign-off** For final proposal/implementation stage Impact Assessments:

***I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.***

Signed by the responsible Minister:



Date: 26 July 2010

## Summary: Analysis & Evidence

Policy Option: 2

Description: Amend the National Minimum Wage Regulations.

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' Employment Businesses and umbrella companies may have to change the control parameters in their current payroll system or revert to the standard payroll system to secure the NMW of some workers. This is estimated to be negligible.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	<b>£ NEG</b>		
	<b>Average Annual Cost</b> (excluding one-off)		
	<b>£ 0</b>		<b>Total Cost (PV)</b> <b>£ NEG</b>
Other <b>key non-monetised costs</b> by 'main affected groups' NONE			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' NONE
	<b>One-off</b>	<b>Yrs</b>	
	<b>£ 0</b>		
	<b>Average Annual Benefit</b> (excluding one-off)		
	<b>£ 0</b>		<b>Total Benefit (PV)</b> <b>£ 0</b>
Other <b>key non-monetised benefits</b> by 'main affected groups' Amending the Regulations removes a tax distortion in the labour market and increases the availability of earnings-related contributory benefits to workers receiving at or around National Minimum Wage.			

### Key Assumptions/Sensitivities/Risks

This option is expected to increase the amount of tax and NICs collected by £20m in 2010-11 and £90m for 2011 onwards due to the reduction of workers using travel and subsistence schemes. This additional revenue will be collected from Employment Businesses and workers using such schemes.

Price Base Year 2010	Time Period Years 5	<b>Net Benefit Range (NPV)</b> <b>£ NEG</b>	<b>NET BENEFIT (NPV Best estimate)</b> <b>£ NEG</b>
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	1 January 2011			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	£ NEG			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	N/A			
What is the value of the proposed offsetting measure per year?	£ 0			
What is the value of changes in greenhouse gas emissions?	£ 0			
Will the proposal have a significant impact on competition?	Yes			
Annual cost (£-£) per organisation (excluding one-off)	Micro £0	Small £0	Medium £0	Large £0
Are any of these organisations exempt?	No	No	No	No

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)	
Increase of	£ 0	Decrease of	£ 0
<b>Net Impact</b>			<b>£ 0</b>

Key: Annual costs and benefits: (Net) Present

## Evidence Base (for summary sheets)

### 1. Background

Traditionally, temporary workers placed with end clients by Employment Businesses have been engaged under “agency contracts”. This means that each placement is considered to be a permanent place of employment for tax and National Insurance Contributions (NICs) purposes. As a consequence, the cost of the worker’s travel to the end client and any associated subsistence costs are not eligible for tax relief as this is home to work travel.

In recent years there has been a growth in travel and subsistence schemes operated by some Employment Businesses and umbrella companies. These schemes involve the engagement of workers under an overarching employment contract. This changes what would otherwise be home to work travel into travel to a temporary workplace. The cost of travel to a temporary workplace and associated subsistence costs are eligible for tax relief and are disregarded for NICs purposes.

Many travel and subsistence schemes use salary sacrifice arrangements. This means the worker sacrifices from his gross pay for tax purposes, a sum equivalent to, or (in many cases involving NMW workers) greater than, the travel and subsistence payments which are paid by the Employment Business or umbrella company. Providing the arrangements are implemented correctly, no PAYE and NICs are payable on the salary sacrificed, nor on the travel and subsistence expenses paid.

Workers who are paid at or around the National Minimum Wage (NMW) rates are not able to participate in salary sacrifice arrangements if the amount sacrificed would reduce their pay below NMW rates. Where a salary sacrifice arrangement is entered into, it is a matter of looking at all the payments made to, and deductions made from, the worker to consider whether the worker has been paid at least the NMW. The NMW legislation and the expenses rules for income tax and NICs treat expenses paid by the employer for travel to a temporary workplace in different ways. For NMW purposes, these expenses are treated as not being “in connection” with the worker’s employment and so are classed as pay for NMW purposes. This is in contrast to the tax and NICs position, where these travel and subsistence expenses do not count as pay for tax and NICs purposes, as they are eligible for tax relief and are disregarded for NICs.

The availability of tax relief for travel expenses (and for the expenses to be disregarded for NICs) and whether there is compliance with the NMW Regulations depends on the way that these travel and subsistence scheme arrangements are implemented. In some cases that HMRC have seen the arrangements are not fully compliant. Where non-compliance is identified, HMRC will take enforcement action.

In many cases, travel and subsistence schemes result in the NMW worker taking home only slightly more each week in his pay packet than a worker not in a scheme. This small uplift in pay, which is important to a low paid worker, is emphasised strongly to the worker by the Employment Business or umbrella company. However, it is usually the Employment Business or umbrella company which benefits the most from the scheme by retaining most of the financial benefits – a fact the worker may be unaware of. The worker is not usually advised that participation in such a scheme could impact on eligibility for earnings-related social security benefits.

In cases that HMRC has seen, workers paid at the NMW, currently £5.80 per hour for those aged 22 or more (equivalent to £232 for a 40 hour week) and using travel and subsistence schemes can be sacrificing as much as 40% of their wages in return for the payment of travel and subsistence expenses. Access to earnings-related contributory benefits is based on a worker attaining the “qualifying earnings factor” (QEF), which is equivalent to 52 times the LEL for NICs purposes (£5,044 in 2010/11), to have access to certain benefits. By participating in travel and subsistence schemes, NMW workers reduce their pay, on which NICs is paid. This,

depending on how many weeks they are able to work for, puts at risk their ability to achieve the QEF. This is most likely to affect eligibility for both basic and additional State Pension.

It is also important to note that where a worker participates in a travel and subsistence scheme, the reduction in his gross pay for tax purposes may mean that the amount of Working Tax Credits which he is entitled to claim may increase, compared to a NMW worker who does not participate in such a scheme. The Government is concerned about the unfairness that these schemes create as workers who participate artificially benefit from enhanced eligibility for Tax Credits, compared to other workers, with similar levels of income who do not or cannot participate.

The Government has received a number of complaints from businesses in connection with these schemes. Some of those Employment Businesses which have implemented these arrangements have used the savings to cut margins which has led to a difference in the cost of supply of workers. This results in a competitive disadvantage for those which have not implemented these schemes

## **2. Policy Objectives**

The Government is committed to tackling the problem of NMW workers being able to participate in travel and subsistence schemes, which exploit low paid workers. The Government's objective is threefold:

- 1) To prevent exploitation and to ensure that the contributory benefit position of temporary workers paid at or near the NMW is not prejudiced by the reduction of earnings liable to Class 1 NICs;
- 2) To ensure that Employment Businesses and umbrella companies do not gain an unfair competitive advantage through the use of travel and subsistence schemes for these temporary workers: and
- 3) To protect the Exchequer.

## **3. The Options**

Option 1: Do nothing.

Leave the existing NMW Regulations unchanged allowing temporary workers to continue to use travel and subsistence schemes not counting this expense when calculating their pay for NMW purposes.

Option 2: Amend the National Minimum Wage Regulations .

The Government has decided to proceed with this option – to amend the NMW Regulations so that expenses paid to an employee for the cost of travel from home to a temporary workplace along with associated subsistence costs will not count as pay for NMW purposes.

## **4. Consultation**

The Government has consulted on option 2 and the consultation closed on 6 May 2010. 54 responses were received. These were split very much into two groups: those very strongly in favour of action and those very strongly opposed. Nearly half of the responses were received from Employment Businesses who had implemented or who wanted to implement a travel and subsistence scheme. The vast majority of these were against any action being taken to prevent NMW workers being able to participate in these schemes. However, other Employment Businesses, together with some representative bodies and statutory bodies wholeheartedly agreed that action should be taken.

The precise behavioural effects of option 2 have been better informed by the consultation process which has enabled stakeholders to comment in detail on the specific proposal.

## 5. The Risks and Expected Impacts

### *Option 1: Do nothing.*

If the existing Regulations are left unchanged then temporary workers will continue to be paid through travel and subsistence schemes, reducing their pay for tax and NICs purposes with consequential potential prejudice to their contributory benefit entitlement.

HMRC compliance staff have been asked by Employment Businesses how they can set up their own travel and subsistence schemes and others have complained that they are being undercut by users of such schemes. HMRC continue to receive complaints from Employment Businesses that schemes are resulting in an unfair competitive advantage for scheme users. Scheme promoters emphasise the financial benefits of such schemes to prospective clients and scheme users emphasise the financial benefits to prospective workers (although not the disadvantages). There is evidence that these arrangements are exploitative. Some responses to the consultation confirmed that the Employment Business benefits significantly – by as much as 4 or 5 times as much as the worker. Also, there is evidence that workers do not understand these arrangements and in reality workers are not given a true choice as to whether to participate or not. There is no evidence that the potential effect of these schemes on the workers' contributory benefits is ever explained.

There is a risk that these schemes will become more widely used by Employment Businesses or umbrella companies to secure an unfair competitive advantage over those not using such schemes. This is achieved both by being able to entice workers away from competitors with the promise of greater take home pay and by using some of the financial savings to undercut competitors. Some respondents commented that these schemes have distorted the temporary labour market and, if no action is taken, will continue to do so.

### *Option 2: Amend the National Minimum Wage Regulations.*

Changing the NMW Regulations will mean that those NMW workers currently participating in travel and subsistence schemes would see an increase in their gross pay and a small reduction in their weekly take home pay. The change will increase the PAYE and NICs payable to the Exchequer. It will also ensure that temporary workers' pay on which NICs is payable and which may be relevant in determining entitlement to earnings-related contributory benefit purposes, cannot be reduced below the NMW rate in return for the payment of travel expenses.

By not allowing salary sacrifice arrangements for travel expenses to count towards NMW, this preserves simplicity in the NMW rules, which has been effective as a wage floor. In this way, workers will be clear as to what they are entitled to, employers and engagers are easily able to show that they have met their legal obligations and HMRC is able to enforce NMW effectively.

Workers may have reduced entitlement to Tax Credits and other benefits such as housing benefit, as the reduction in gross pay for tax purposes which occurs as a result of participation in these schemes increases eligibility for these benefits. However, the Government believes that this option restores fairness amongst workers – those with the same gross pay have the same access to benefits.

This will ensure that, generally speaking, workers participating in travel schemes will be treated in the same way as those engaged by Employment Businesses not using such schemes. The Government believes that this is equitable, and that equal treatment of workers will restore the level playing field in the market place ensuring Employment Businesses tendering for work are doing so broadly on the same terms. Where workers are incurring travel and subsistence costs in attending work, it will be for individual Employment Businesses to determine how such costs are addressed when agreeing terms with workers.

Employment Businesses currently paying workers through travel and subsistence schemes may behave in a number of different ways as a result of changes to NMW Regulations. The Government believes the following scenarios are the two most likely:



- Some may revert to engaging workers through agency contracts meaning that any travelling costs to the client's premises and associated subsistence costs would not be eligible for tax relief;
- Some may continue to engage workers through overarching employment contracts and may pay tax free expenses in addition to NMW pay.

It should be emphasised that that the proposed change is unlikely to result in a uniform reaction across all scheme users because of the nature of temporary labour provision. Different supply and demand issues in different sectors will influence responses, as will the size and underlying business plans of scheme users.

## **6. Costs and Benefits**

*Option 1: Do nothing.*

### Costs & Administrative Burdens

None for businesses directly. It is possible that cognisant of reputational damage, end clients will not wish to be associated with Employment Businesses using travel and subsistence schemes which exploit low paid workers. HMRC may need to deploy more compliance resources to address the growth in the schemes.

### Benefits

None

### Revenue Effects

The expected growth in travel and subsistence schemes available to temporary workers will lead to a reduction in the amount of tax and NICs payable to HMRC. The Government estimates that this will result in an erosion of Exchequer receipts.

*Option 2: Amend the National Minimum Wage Regulations.*

### Costs & Administrative Burdens

Employment Businesses and umbrella companies involved directly or indirectly in placing low-paid temporary workers across all sectors will be affected by this option. HMRC has received, and continues to receive, complaints from a number of Employment Businesses not using travel and subsistence schemes that competitors using such schemes are undercutting them.

As a result, it is possible that in some instances this option will increase costs to end clients. However, since many Employment Businesses and temporary workers are currently operating without the financial advantages of such schemes, it is unlikely to have a profound affect on the average cost of labour to end users.

Some of the responses to the consultation have indicated that the impact of the measure could be greater than those workers paid at or near the NMW, suggesting that it could impact workers paid up to £9 per hour. The Government agrees that workers paid more than NMW will be affected, depending on the level of expenses which the worker incurs in travelling to his workplace. However, in order to be affected by the measure, a worker earning £9 per hour would have to sacrifice in excess of £3.20 per hour, i.e. more than one-third of his gross pay. Although the expenses paid to the worker are likely to be less than the amount of the salary sacrifice, it does not seem credible that many workers earning £9 per hour would be spending such a significant proportion of their earnings in getting to work.

Where Employment Businesses and umbrella companies specialise in the low paid labour market, it may not be viable to continue with their current business model due to a reduction in their profit margin. This may result in either a change of business model or in a few cases for these businesses to cease trading. Despite this, the Government does not believe that this

option will affect labour supply, as many Employment Businesses do not currently operate these schemes.

On the available evidence, HMRC does not expect there to be any significant impacts, either in terms of one-off transitional costs, administrative burdens or other compliance costs to businesses. The related costs depend on precisely how Employment Businesses and umbrella companies respond to the amended Regulations. There will be some one-off costs for business, as they may have to re-structure their employment contracts. Current travel and subsistence schemes are administered through the scheme user's payroll. Both the salary sacrifice which the worker enters into to reduce his gross pay, and the expenses that are paid in addition to net pay for travel to a temporary workplace, are processed as payroll adjustments. The change in the Regulations would mean that these adjustments would no longer be required. The full amount of NMW pay would simply be processed as gross pay for tax and NICs, as would be the case if the worker did not participate in a travel and subsistence scheme.

### Benefits

The Labour Force Survey (LFS) estimates 1.3million temporary workers during 2009 and the Government estimates that this will rise to 1.4million in October 2010. Further analysis of the LFS data indicates that about 350,000 (25%) of temporary workers are paid at or near the National Minimum Wage. The Government then estimates that of this number, 90,000 will be paid using a travel and subsistence scheme.

Amending the NMW Regulations helps to protect the contributory benefit position of those 90,000 workers, particularly in relation to basic and additional State Pension and stops others being potentially prejudiced. It preserves simplicity in the NMW rules and ensures that the NMW operates effectively as a wage floor.

This option creates a level playing field, and results in a fairer marketplace where Employment Businesses are subject to the same levels of taxation. This is because a well functioning market, free from the distortionary impact of these schemes, underpins greater and fairer competition between firms which promotes better resource allocation. However, it is difficult to quantify the value of these benefits.

This option potentially reduces the risk of reputational damage to end user clients, as there will be less scope for Employment Businesses to prejudice workers' contributory benefit, and artificially distort the labour market.

### Revenue Effects

This option also increases the amount of income subject to tax and NICs. In practical terms this would mean that a worker working 40 hours per week at the adult NMW rate would need to be paid any travel and subsistence expenses *in addition* to the £232 NMW pay.

The Government estimates that on average, a temporary worker earning the National Minimum Wage works 27 hours per week. It is assumed that approximately 33% of their pay is sacrificed to the travel and subsistence scheme. This, along with workers reduced entitlement to working tax credits, results in an expected Exchequer yield of £20m in 2010-11 and £90m for 2011 onwards. This is based on a proposed implementation date of 1 January 2011 and that all businesses will comply with the change of Regulations.

It is standard practice for all tax measures that revenue effects or changes in tax yield are not incorporated into the main cost/benefit analysis. This is primarily due to the fact that they are pure transfers and, as they are generally much larger than the other costs and benefits, tend to distort the cost/benefit ratio. This could give a misleading picture of the balance between the costs and benefits of the measure. As a consequence, any quantified revenue effects are shown on the summary sheet within the 'Key Assumptions/Sensitivities/Risks' box, which is outside the main appraisal of the costs and benefits.

## 7. Impact Tests

A main source of evidence for the specific impact tests is the 2008 report by the Department for Business Innovation and Skills (BIS) on the scope of 'agency' working<sup>1</sup>. The study concluded that the best estimate for the number of agency workers in the UK was between 1.1 and 1.5 million with a mid-point of 1.3 million. This estimate was compiled using the LFS alongside 2006 and 2007 data from the BIS Survey of Recruitment Agencies (SORA) and the Recruitment and Employment Confederation's (REC) 'census'.

To consider the specific impact on workers at or near the NMW, four quarters of the LFS from October 2008 to September 2009 have been used. These benefit from larger sample sizes than single quarters. It is important to note once the LFS sample is filtered for agency workers earning at or near the NMW, the remaining sample size becomes small which limits the information that can be found for some impact tests. Focusing on those agency workers who were aged 18 or over at the preceding 31 August, who earned a wage lower than £8.55 per hour (the rate at which 33% salary sacrifice reduces basic pay to the NMW) further reduces the sample. The impact tests using LFS 08/09 data are therefore based on a total of 508 respondents.

Other bodies have conducted surveys aimed specifically at the agency, temporary or migrant-intensive sectors. The LFS however remains the preferred source of data because of its National Statistic status and, even after extensive filtering, still produces larger sample sizes than other surveys we have seen. Details of other data sources are, however, provided where relevant below because they may benefit from specifically targeting low-paid agency workers.

It must be noted all sources only act as a proxy for the population of interest – workers in travel and subsistence schemes paid at or near the NMW. The impact tests refer to the pool of employees who would be affected if they were taking place in such schemes at the assumed level of salary sacrifice.

### Gender Equality

The 2008 BIS report concluded that the proportion of all agency workers who are female is lower than the proportion of all employees who are female. The estimates of the proportion of agency workers who were female varied by source but the two with the largest sample sizes, SORA and LFS, indicated it was around 43 - 44% (the other, the REC census, suggested 58%).

More recent evidence from the LFS between October 2008 and September 2009 indicates females now account for 50% of agency workers. However those earning at or near the NMW are slightly more likely to be male.

	% male	% female
All agency workers	50	50
At or near the NMW	53	47
All employees	51	49

Source: LFS. Sample size for smallest group: 508

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<sup>1</sup> 'Agency working in the UK: A review of the evidence', Employment Relations research series No. 93  
<http://www.berr.gov.uk/files/file48720.pdf>

## Race Equality

### *Ethnicity*

The REC and LFS were also the main sources used for examining the proportion of agency workers who were from ethnic minorities. These results were better matched than for some of the other statistics, with both implying that agency workers are around twice as likely to be from an ethnic minority compared to all employees.

The 2008/09 LFS data indicates ethnic minorities are still more likely to be in agency work than employees as a whole.

### *Migrant workers<sup>2</sup>*

Data from the LFS between October 2008 and September 2009 indicates that around 8% of all employees are non-UK nationals, roughly equally split between those from the European Economic Area (EEA) and other countries. The LFS suggests that non-UK nationals are more heavily represented in agency work, at around 23%.

Amongst those at or near the NMW, the concentration of migrant employees is greater still than for all agency workers – in the LFS figures around 29% are estimated to be foreign nationals. The main cause of this difference is a higher proportion of EEA nationals amongst the lower paid group.

	% UK nationality	% EEA	% Non-EEA
All agency workers	76	13	10
At or near the NMW	71	18	11
All employees	92	4	4

Source: LFS. Sample size for smallest group: 508.

Some other sources of evidence on agency work have indicated higher proportions of migrant workers in some sectors. The Equalities and Human Rights Commission (EHRC) in their report on the Inquiry into recruitment and employment in the meat and poultry processing sector stated that 70% of the agency workers in this particular sector are migrants.

However, for migrant workers as a whole, the LFS is still regarded as the best source of information on nationality within a population. In the case of agency workers near the NMW, the sample size is still substantial compared to many surveys and sources of anecdotal evidence and covers all sectors rather than a subset. For these reasons, the LFS figures are used for the impact tests with the caveat that, since travel and subsistence scheme participants are not observable, then the sample used is a proxy. If migrant workers were systematically more likely than native employees to take part in salary sacrifice schemes then the proportion of migrants affected would likely be larger, and vice versa.

In summary, ethnic minorities and migrants are more likely to be engaged in temporary agency work and be paid at or near the NMW compared to both the whole population of agency workers and all employees. One of the policy objectives is to prevent exploitation of workers. Ethnic minorities and migrant workers are likely to be amongst the most vulnerable and accordingly more susceptible to exploitation. For example, English may not be the first language of many migrant workers. The report of the EHRC, as referred to above, stated that more than one-third of migrant workers interviewed did not understand the documentation that their Employment Business had given them but felt under pressure to sign up to it. The Government's decision to amend the NMW Regulations will ensure that temporary workers paid at or near the NMW, which include a high proportion of ethnic minorities and migrants, will not be subject to exploitation.

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<sup>2</sup> Migrant workers are here defined as being of non-UK nationality.

## Age

The BIS report provided data on the age distribution of all agency workers from REC and the LFS in 2007. The REC figures implied a similar distribution to all employees whereas the LFS implied agency workers were disproportionately young. With the much larger sample size the LFS figures were given greater weighting leading to the conclusion that more agency workers were aged under 35 compared with all those who are employees.

More recent evidence from the LFS corroborates this finding. Limiting the sample to those earning at or near the NMW strengthens the conclusion further – i.e. agency workers under 35 are more likely to be paid at or near the NMW than their elder counterparts.

	% 18-24	% 25-34	% 35-44	% 45-54	% 55-64
All agency workers	30.5	26.9	16.9	15.5	10.1
At or near the NMW	34.5	28.2	14.7	15.3	7.3
All employees	16.0	22.7	25.6	22.7	13.0

Source: LFS. Sample size for smallest group: 508

## Disability equality

Both the REC census and the LFS figures in the 2008 BIS study implied there were fewer people with disabilities in agency work compared with employees as a whole (7% and 11% respectively compared with 13% of all employees).

More recent LFS evidence confirms this conclusion still holds true, including for agency workers at or near the NMW. Given the sample sizes, there is no evidence that disabled employees are more likely to be affected by the proposal in this impact assessment.

	% with disability	% not disabled
All agency workers	11	89
At or near the NMW	11	89
All employees	12	88

Source: LFS. Sample size for smallest group: 508. Includes current and work-limiting disability

## Human Rights

The Government considers that the proposal in option 2 to amend the NMW Regulations is compatible with EU law and the Human Rights Act.

## Competition Assessment

Employment Businesses and umbrella companies using travel and subsistence schemes for NMW workers are likely to find their competitiveness against Employment Businesses using other business models is reduced. Depending on the proportion of their profit margin that is made up of the tax relief they were accessing through these arrangements, some may find that their business model is no longer viable. This may reduce the number of businesses providing lower income temporary workers. However, those larger Employment Businesses operating these schemes are likely to be better placed to be able to adjust their business model to reflect the legislative change.

The Government does not consider this to be an anti-competitive effect of this proposal. Employment Businesses and umbrella companies that are using salary sacrifice to reduce their costs and potentially reduce pay below the minimum wage use their business structure to obtain

an unfair advantage over Employment Businesses and umbrella companies who are unwilling to do the same.

The proposed solution that travel and subsistence expenses would not count as pay for NMW purposes ensures that all Employment Businesses providing temporary workers are competing equally.

### Small firms

Data from the SORA and the REC 'census' indicates that there are approximately 16,000 agencies across the UK and these employ a combined workforce of approximately 225,000 people. Of the 16,000 recruitment sites, 54% are thought to be single-site agency establishments with one branch/office. The rest are workplaces belonging to a larger organisation. Around 57% of sites employ between one and five people with another 21 per cent employing between six and ten people.

There is no evidence to suggest that small businesses are more or less likely than average to participate in travel and subsistence schemes. Although there has been some feedback that engaging low-paid workers under an overarching employment contract is not financially viable where only small numbers of workers are concerned, because of the costs associated with implementation and maintaining processes.

As the estimation of costs and benefits showed, following the change, employment businesses that participate in travel and subsistence schemes are likely to be required to pay higher NICs. However, employment businesses that do not participate will benefit from increased competitiveness. Small businesses would therefore face costs or benefits depending on their degree of salary sacrifice arrangement rather than on their size.

### Rural proofing

The LFS provides an estimate of whether respondents live in urban or rural areas. The variable does not refer to the location where the individual works (or to where the employment business is located) but provides the most appropriate proxy to assess the effect on rural areas.

The table below shows the resident location of all agency workers, those earning at or near the NMW and all employees as a comparator. Both agency workers as a whole and the subset earning around the NMW are estimated to be slightly less likely to live in rural locations than employees as a whole. Therefore, although work locations are not visible, it seems unlikely on the basis of the available evidence that the proposal will affect rural areas disproportionately.

	% live in urban location	% live in rural location
All agency workers	86	14
At or near the NMW	87	13
All employees	79	21

Source: LFS using variable 'URIND'. Sample size for smallest group: 508.

### Other Specific Impact Tests

The Government has considered the remaining impact tests and does not think that the options will impact on legal aid, sustainable development, carbon assessment, other environment or health.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No

### HM Treasury contacts

This document can be found in full on our website at:  
[hm-treasury.gov.uk](http://hm-treasury.gov.uk)

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