

Paying expenses – what can you ignore for tax purposes?

Employees often incur expenses when doing their job. For example, an employee may be required to attend a meeting with a client or supplier and may incur travel expenses and possibly subsistence expenses in doing so. The employee will often incur the expense in the first instance and reclaim the amount from their employer, in accordance with the employer's expenses policy.

Where an employer meets or reimburses expenses incurred by an employee, what are the tax implications and what, if anything, needs to be reported to HMRC?

Exemption not dispensation

It is no longer necessary to consider whether a dispensation is in force – an exemption for qualifying paid and reimbursed expenses replaced the dispensation regime from 6 April 2016 onwards. This makes life easier – if the item would be deductible if the employee incurred the expense him or herself, the exemption applies and the payment or reimbursement of the expenses can simply be ignored for tax purposes – there is no need to tell HMRC about it and no tax to pay.

The general rule governing whether an expense is deductible applies and to qualify the employee must be obliged to incur the expense and it must be incurred wholly, exclusively and necessarily in the performance of their duties. Separate tests apply for travel expenses – with deductions for travel in the performance of the duties and necessary attendance, subject to the exclusion for home to work travel ('ordinary commuting') and more generous rules for short-term postings of less than 24 months. Specific deductions are allowed for fees and subscriptions (paid to qualifying bodies on HMRC's List 3), and also for employee liabilities and indemnities and associated insurance.

In practice, this means that if an employee is required to travel to meet with a customer in another part of the country and in doing so incurs bus, train and taxi fees, which he or she reclaims from the employer, the employer and employee can ignore the reimbursement for tax purposes and do not need to tell HMRC.

Scale rates

To simplify matters, the employer may pay scale rate expenses rather than reimburse the actual costs incurred by the employee. As long as the employer pays expenses at the statutory rate, there is no tax to pay and the expenses do not need to be reported to HMRC. Where an employee is covered by a Working Rule Agreement under which specific rates are set for particular occupations, the rates set out in the agreement can be paid tax-free. The employer can also agree bespoke rates with HMRC, which can be paid tax-free.

Mileage allowance

Many employees use their own cars for work and claim a mileage allowance from their employer. As long as the amount paid does not exceed the tax-free amount under the Approved Mileage Allowance Payments Scheme, the mileage payments are tax-free and do not need to be reported to HMRC. The tax-free rates are 45p per mile for the first 10,000 business miles and 25p per mile thereafter for cars and vans, and 24p per mile for motorcycles.

Beware salary sacrifice

As with most exemptions, the exemption for paid and reimbursed expenses does not apply where the expenses are met under a salary sacrifice arrangement.

Mixed payments

Where the amount paid by the employer covers both deductible and non-deductible expenses, it is necessary to split the payment and report the non-deductible (non-qualifying) element to HMRC.