



Prime Minister ①

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PRIME MINISTER

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MPs' EXPENSES PAYMENTS AND TAX

A difficult problem has arisen affecting the sensitive issue of the tax treatment of MPs' expenses. This note, which has been agreed with the Lord Privy Seal and the Chief Whip, describes how the problem has arisen and the solution we propose.

Background

2. As you know, Members for constituencies outside Inner London are entitled to receive from the Fees Office an "additional cost allowance" (ACA), worth at present about £6,000, to cover the extra living costs they incur because they have two places of work - the constituency and Westminster. In law, in common with other expenses payments made to higher-paid employees and office-holders (MPs are office-holders), sums received by way of ACA are deemed to be taxable emoluments, but a tax deduction is given for those expenses incurred "wholly, exclusively and necessarily" in the performance of the job - in this case, parliamentary duties. Under the same test, any excess of expenses incurred over the reimbursements may qualify for a tax deduction.

3. Until recently, few problems had arisen. Where a Member's expenses claim for tax purposes has not exceeded the amount of ACA he received from the Fees Office, the Revenue have in general been content to accept that the expenses qualified for a deduction under the "wholly, exclusively and necessarily" rule. In many cases, they have not required a breakdown of the expenditure in question or asked exactly how the money was being spent. But as some Members' claims have risen above the ACA payment and claims for additional tax relief have been made against a salary, Inland Revenue inspectors have naturally requested a breakdown more often and have sometimes subsequently queried or disallowed claims.



4. It has come to light that claims have been made for meals eaten away from home. Although some were quite modest, others were very large. The Revenue consulted their lawyers on whether such claims were admissible and were advised that, while in law Members were entitled to a deduction for the cost of meals taken while travelling on parliamentary business (eg between Westminster and the constituency or to some third location) no deduction was available for meals taken either in the constituency or at Westminster.

5. With the agreement of Geoffrey Howe, the Revenue therefore promulgated a statement of the law as they were advised it stood in Notes on Income Tax for Members of Parliament, a copy of which was supplied to each Member immediately after the General Election last June. The idea was to apply the law strictly to all MPs for current years (from April 1982) with a fairly generous transitional arrangement for Members who had open claims for earlier years.

6. The result has been to create a storm of protest in the House. Some Members, whose total claims may not be above the ACA, have found their expenditure on meals has been disallowed, even though they have followed the same practice for a decade or more and their claims have been accepted in the past by the Revenue. So far the Whips on both sides of the House have held this protest in check - but only because Members assume that some solution to the problem can be found.

7. There is little doubt that as the law stands the Revenue are right and that this sort of expenditure on meals cannot be tax deductible, whatever may have happened in the past. The Revenue cannot be told to ignore the problem. It would clearly be indefensible for MPs to be given tax relief by what would in effect be an extra-statutory concession. Nor can the problem be dismissed on de minimis grounds, since some of the claims are high and the Revenue would be failing in their duty if they admitted them without enquiry.

8. The crux of the problem - given the wide range of MPs' expenses - is that there can be no end to the disputes that will arise, even if we found a way of dealing with the specific question of meals. I have examined carefully the scope for establishing clear guidelines or a code, and concluded that it is impossible.



9. Members of Parliament are unusual in having two different regular places of work which may necessarily involve them in expenditure, particularly on keeping a second home, which should be tax deductible. But what expenditure? It is impossible to make objective judgements about what should qualify and what not.

10. Where, as is usually the case, a Member has an additional home, what limit should be placed on the cost of items such as the bed and the desk? Can the desk be antique? Does he need a lamp and curtains; how many chairs should he be allowed; and what can be legitimately claimed for cleaning and upkeep of the house and garden?

11. Questions of this sort are unanswerable and it is impossible to give unambiguous guidance on them either to Inspectors or MPs. If we do not take action, Members and the Revenue will become embroiled in endless skirmishing over claims which could bring both into disrepute. If details of what was being allowed and disallowed became public knowledge, the House would be brought into ridicule.

The proposed solution

12. In the business world, it is for the employer in the first instance to determine what expenses are appropriate and reimbursable for an executive who works away from home from time to time. The Revenue will tax the employee on those reimbursements but will allow a matching deduction, when the expenses are "necessarily" etc incurred, in line with the law. Although, in most cases, the amount reimbursed by the employer is adequate, an employee who actually spends more may claim a tax deduction for the excess.

13. In the case of Members, the House has determined that the ACA should be payable, up to a maximum (about £6,000 per annum currently). But Members are being reimbursed for working, and probably living, in two different places, and this is what is virtually unique. After consulting the Lord Privy Seal and the Chief Whip, I have concluded that the best way to resolve the problem is to legislate to take the ACA paid by the Fees Office out of tax altogether with



effect from 1984/85. In that way, MPs will be in an analogous position to that of most businessmen whose reimbursed expenses are taken out of tax because they qualify for a matching deduction. But I would propose that Members spending more than the ACA on living away from home would no longer be able to claim a tax deduction for the excess. In this respect, MPs would be relatively worse off than businessmen since businessmen are not held to a maximum in the amount they can claim for tax purposes.

14. I believe this arrangement would dispose of the problem once and for all and would have the support of most MPs on all sides of the House, except some of those who currently claim a tax deduction on more than the ACA (and certain others who would object in principle to anything that might be represented as an improvement in MPs' remuneration). There are perhaps 50 MPs who would be substantial "losers" under this proposal, in general those who maintain expensive London homes.

15. There would be little or no loss of existing tax revenue, because no tax has yet been paid on the expenses for meals. If we were to enforce the letter of the existing law, the total yield of disallowing all current meals' claims might be up to some £½m in a full year. In practice, we would not receive that amount. The large number of Members who are in the habit of claiming up to the ACA ceiling, and currently put a fairly high proportion of this down to meals, would continue to claim the maximum but would take care to incur a different kind of expenditure which, perhaps after a further dispute with the Revenue, might be deemed to be tax-deductible. So we would not realise the theoretical gain, and the disputes would go on. The proposed solution would, by contrast, take the Revenue out of this very awkward area entirely and would release the resources currently tied up in this work for more productive use elsewhere.

16. The TSRB has recommended - and we have publicly accepted - that Members should account more fully to the Fees Office for expenditure against the ACA. Such a change would be helpful in demonstrating that MPs would still be required to report their expenditure to the Fees Office, in much the same way as the businessman claims from his employer.



17. I believe that we can justify such an arrangement to meet special circumstances. The key point is that an MP's job is probably unique in this country in requiring him to meet the costs of maintaining two homes at or near two places of work. But there is no denying that it would need the most careful presentation.

18. One side effect of a solution on the lines proposed would be that Ministers would no longer suffer relative to other Members from the ruling that, as the law now stands, claims for the cost of a constituency home must normally be restricted to two-sevenths of the total costs - you may remember that this was a point raised particularly by Norman Tebbit shortly after the Election last year.

Next Steps

19. In sum, I believe we should legislate in this year's Finance Bill:

- to take MPs' ACA out of tax altogether from 1984-85, but
- to deny MPs the right to claim any tax relief for expenditure over and above the ACA on living away from home in the constituency or in London.

In order to distance this measure from the Budget itself, I propose to introduce it as a New Clause at Committee Stage.

20. John Biffen and John Wakeham endorse this recommendation.

21. An extra-statutory concession would allow MPs to elect for the new regime for open years up to 1983-84. The Inland Revenue will be issuing to Members at the end of the current tax year a new edition of their Notes for Members which could spell out the details of the proposed change and the concession covering past years.

22. Needless to say, I should be happy to discuss this with you further.

23. Copies of this minute go to John Biffen and John Wakeham.

N.L.

16 February 1984

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CONDICION





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CONFIDENTIAL

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17 February 1984

Dear Robin

MPs' EXPENSES PAYMENTS AND TAX

... As agreed during your telephone conversation this morning with Sir Peter Middleton, I enclose a copy of the draft clause prepared by Parliamentary Counsel taking MPs' additional cost allowance out of tax.

Yours sincerely
John Williams
J WILLIAMS

Accommodation allowances and expenditure of MPs.

- .-(1) An allowance -
- (a) which is paid to a Member of the Commons House of Parliament in respect of any period after 31st March 1984, and
 - (b) for which provision is made by Resolution of that House, and
 - (c) which is expressed to be in respect of additional expenses necessarily incurred by the Member in staying overnight away from his only or main residence for the purpose of performing his parliamentary duties, either in the London area, as defined in such a Resolution, or in his constituency,
- shall not be regarded as income for any income tax purpose.

- (2) For the year 1984-85 and subsequent years of assessment, -
- (a) no deduction shall be made under section 189 of the Taxes Act (relief for necessary expenses) in respect of expenditure incurred by a Member of the Commons House of Parliament in, or in connection with, the provision or use of residential ^{or} overnight accommodation to enable him to perform his duties as such a Member in or about the Palace of Westminster or his constituency; and
 - (b) no allowance shall be made under Chapter I of Part III of the Finance Act 1971 (capital allowances) in respect of any expenditure so incurred.