# TAXREP 39/15 (ICAEW REPRESENTATION 110/15)

## REVIEW OF EMPLOYEE BENEFITS AND EXPENSES – DRAFT LEGISLATION

ICAEW welcomes the opportunity to comment on the consultation on draft legislation *Review of employee benefits and expenses – draft legislation* published by HMRC on 8 July 2015.

This response of 2 September 2015 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

On 30 July and 14 August we attended meetings with HMRC jointly with other professional bodies in which we were able to put forward some key comments and concerns and discuss aspects of the draft legislation.

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.



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# MAJOR POINTS

## Key point summary

**1.** We suggest that the implementation date for payrolling employee benefits-in-kind (BiK) should be delayed until 6 April 2017.

**2.** We believe the draft legislation is too prescriptive. It is unlikely to represent what employers do who currently payroll voluntarily with permission from HMRC, which appears to work satisfactorily for all concerned.

**3.** The proposed rules will cause problems for existing payrolling systems (employers will not have time to comply with the new rules by rewriting their systems and procedures before 6 April 2016) and the rules are unlikely to encourage employers who are not already doing so voluntarily to payroll their BiK.

## General comments

*Payrolling BiK*

**4.** The project to give statutory backing to payrolling BiK started out as a simplification measure. We fear that the draft regulations are too prescriptive to qualify as simplification, especially since most employers currently payrolling BiK will have to redesign their software and systems to comply to the letter of the statutory requirements.

**5.** In today's digital age, it is essential that employers'/payroll agents' BiK payrolling and HMRC's processing software is fit for purpose from the day that employers start payrolling. The number and extent of our comments below on the regulations and matters that we feel need to be explained in guidance make us concerned that, by the time HMRC has considered what changes are needed to the draft regulations to ensure that the rules are right first time, and laid amended regulations, perhaps after further consultation (we hope), it will be impossible if the start date is 6 April 2016 for HMRC to draft and provide definitive software specifications to its own information technology (IT) people let alone third party software houses early enough to design, test and install satisfactory software and train users.

**6.** HMRC needs to prescribe FPS data fields and should also prescribe the BiK detail to be shown on end of year forms P60 (to replace P11D information) so employees know what taxable and NICable BiK they have been provided with.

**7.** Two and a half years after RTI became business as usual, there are continuing misunderstandings by employers and errors in liabilities and payment entries on HMRC's employer PAYE accounts, employee code numbers, communications to employers, and P800s, and the anticipated compliance cost savings are not being made. The necessary changes to IT to enable BiK to be payrolled satisfactorily need more time and planning.

**8.** We therefore strongly recommend that the implementation date for payrolling BiK under these regulations should be put back to 6 April 2017 at the earliest and the informal arrangements for employers currently payrolling with permission from HMRC should be continued until the same date.

**9.** We should appreciate clarification of the rationale for such detailed prescription of employers' obligations, which does not match what most, if not all, of the current 3,000 payrolling employers do. We question whether it would not make more sense to legitimise current practices, by explicitly permitting HMRC to continue to agree to payrolling methods in individual cases (the work has already been done, in essence), but also to publish a model methodology for future payrolling of benefits, perhaps from 2020, towards which employers should be encouraged to move. The software houses and in-house IT departments can then consult with HMRC at a sensible pace about how to make the idealised system work, while not

disturbing current practices and Exchequer cash flows, and not exposing employers to unnecessary compliance burdens and penalties.

*Benchmark scale rates*

**10.** We consider that employer record-keeping requirements should be light touch. The normal employer does not pay expenses to employees if they think that the employee has not undertaken qualifying business travel. We also suggest that there should be benchmark accommodation rates.

**11.** We also recommend that to help HMRC manage workloads, the requirement on employers to re-register bespoke scale rate agreements should be a rolling programme based on the fifth anniversary of when the agreements started, rather than every employer having to meet the proposed deadline of 5 April 2016.

## COMMENTS ON THE REGULATIONS

### The Income Tax (Pay As You Earn) (Amendment No *) Regulations 2016

**Removing the requirement for form P9D following abolition of £8,500 threshold**

**12.** We have no comments on these Regulations.

### The Income Tax (Pay As you Earn) (Amendment No *) Regulations 2016

**Payrolling of employer-provided benefits-in-kind (BiK) and removing requirement to report such BiK on form P11D**

*General comments*

**13.** The project to give statutory backing to payrolling BiK started out as a simplification measure. We fear that the draft regulations are too prescriptive to qualify as simplification, especially since most employers currently payrolling BiK will have to redesign their software and systems to comply to the letter with the statutory requirements.

**14.** We welcome the fact that most of the rules for payrolling seem reasonably practical, although the prescriptive approach adopted to the calculation of the notional addition to pay in each pay period will not match the ways in which employers currently apply PAYE, which broadly achieves the result intended without being so prescriptive. The re-writing and testing of systems required in order to follow HMRC's prescriptions, for which no detailed IT specification yet exists, will probably mean that no employer currently payrolling informally will be able to register for payrolling by April 2016 and comply with the Regulations going forward. They will therefore be in some difficulty, as they will not wish to switch out of payrolling to reporting on P11D for a year or two until their human resources (HR) and payroll software has been rewritten to comply with HMRC's requirements. We would therefore recommend that implementation of these prescriptive regulations be deferred until 6 April 2017 at the earliest and that the current informal payrolling arrangements be maintained for a further year or two.

**15.** Delaying implementation even for a year would also enable HMRC to design comprehensive and final software specifications for themselves and third party software houses in sufficient time before payrolling of BiK goes live, so that the software works reliably. It must not only be designed and built, but also tested and probably amended before being installed by employers, payroll agents/bureaux and HMRC. Operators will need to be trained. The PAYE real time information (RTI) project, 2½ years after transitioning to 'business as usual', is still not providing the compliance cost savings that were envisaged, and we would recommend caution.

**16.** Allowing 'formal' and 'informal' payrolling of benefits for a transitional year or two would also facilitate the incorporation of the new software in software developers' development cycles (including HMRC's).

**17.** We look forward to reviewing the guidance, which we understand will be available in September. However, in the light of the number of concerns that we and others have about the draft regulations, we recommend that draft guidance is not exposed for comment before responses to this consultation have been properly considered and incorporated where appropriate into the draft regulations – no one will want to waste time considering multiple drafts of guidance based on deficient or incomplete draft legislation.

**18.** We comment below on the regulations and have set out some other suggestions about matters that we feel might usefully be considered when drafting the final regulations and guidance. Alongside this we should welcome clarification of the full payment submission data fields that will need to be completed under RTI.

**19.** We understand that there will be no information in the end of year form P60 to enable the employee to satisfy himself that tax and Class 1 NIC have been correctly calculated for the year (without having to refer to 12 monthly or possibly 52 weekly individual payslips), complete his SA return, or check end of year reconciliation P800, and obviate the need for the employer providing the employee with a separate breakdown on the lines of form P11D. Many large employers provide a total reward statement, detailing the value of pay and benefits, but not necessarily for the tax year and not necessarily with a link to the amounts that have been taxed via PAYE or P11D. This statement could be re-purposed and redesigned, but this will also take time. HMRC has long required the employer to supply a copy of the P11D information to employees so they can complete their tax returns correctly. Since payrolling BiK will dispense with the P11D, there needs to be a replacement. We understand that HMRC does not wish to be prescriptive as to the method, but there must be some duty on employers to break down the taxable values of BiK so that the employee (or his agent) can check that the values are correct and can include them as necessary in the SA return.

**20.** We are also concerned that without a full specification HMRC will not be able to determine from the data submitted by employers the validity of the calculations without needing to request more data from employers' agents and payroll bureaux.

**21.** We should also welcome confirmation that individuals' digital accounts and agent online self serve will display 'remuneration' in sufficient detail to enable payrolled BiK to be ascertained and that the correct NIC treatment has been applied. This will be particularly important for employees with multiple employers, any one or more of which payrolls BiKs.

**22.** We understand that the approach planned for the coalface will involve employers who opt to payroll BiKs using a tool that provides a list of those employees who are to be included, and that the tool will simply result in the BiK being removed from the relevant employees' PAYE codes. Given the block nature of the option, with the ability to remove specific employees and report their benefits on a P11D, we are surprised at the approach adopted in the draft regulations, which requires specific nomination of each employee involved. Given that those employees not having their BiKs payrolled are likely to be the exceptions, we would have expected a blanket election to payroll with the ability to nominate the exceptions, which, we suggest, would be less onerous.

**23.** We note that it planned to allow payrolling of cars from April 2016 but no mention or reference has been made in respect of car averaging or what may happen in trades such as car dealerships where cars change on a very frequent basis. We should welcome clarification of what is proposed here.

*Comments on specific regulations*

**24.** Reg 61C(3)(a) *Authorised employer* says that if an authorised employer tells HMRC that a specified BiK is no longer being provided to specified employees then the employer will cease to be an authorised employer. We question whether this across-the-board disqualification is intended where the employer continues to payroll BiK provided to other employees or indeed other BiKs to the same employee. Perhaps (a) should to be changed to read: 'no specified benefits are being provided to any specified employees, or'.

**25.** Reg 61C(2)(b)(i) allows employers to register as an authorised employer if they provide employees with a specified benefit for the first time during the year. We should welcome clarification of whether this refers to BiK provided for the first time to employees, and/or to a previously provided BiK which first becomes a specified benefit, ie a BiK which is first payrolled, during the year.

**26.** If employers are to be allowed to switch to payrolling mid-year, as the wording suggests, we would welcome clarification of how HMRC is to ascertain the correct amount of any BiK to include in the PAYE code for the part of the year where PAYE does not apply. Since the election is to result in PAYE codes being amended to remove the nominated BiKs, we would expect the election to apply only for complete tax years, in order to avoid unnecessary and widespread errors.

**27.** If the general rule is that employers should register before the start of the tax year (and at the consultation meeting HMRC recommended that employers should register before the January coding run), then we recommend that this is highlighted prominently in HMRC's guidance. This loose deadline of early January adds to our expectation that employers will not register for payrolling from April 2016. As already noted, employers will struggle to make their systems compliant by April 2016, so January 2016 is likely to be impossible to achieve.

**28.** Reg 61D *Deduction and repayments of tax: general rule.* This point assumes that Reg 61C(2)(b)(i) includes previously provided BiK which start to be payrolled mid-year (see the ante preceding paragraph). Reg 61D in Step 1 refers to 'the first main relevant payment … in a tax year' (our emphasis). In order to cover employers who register as authorised employers during the tax year under Reg 61C(2)(b)(i) and so have already made at least one main relevant payment to one or more employees in which it is now too late to payroll the BiK, we suggest that an additional Regulation '*Modification of the general rule: specified benefits first provided after the first tax month of the year*' is needed.

**29.** Regulation 61E(2) *Method of calculating the cash equivalent of the benefit of a car or van* refers to the making good payments that the employee is required to make in the tax year, and this follows what is provided for in the primary legislation in sections 144(1) and 158(1) ITEPA 2003. Regulation 61L *Modification of the general rule: making good* tells employers what to do if the employee has not made good before the final payday of the year. Payroll processing deadlines are likely to render these regulations impossible to meet as the employer to be certain would have to have received the making good payment before the cut-off date for collating data for the final payroll of the year, which could be in the first or second week of March.

**30.** HMRC's manuals EIM25253 *Car benefit calculation Step 8, payments for private use 2014/15 onwards - exceptional circumstances* and EIM22845 *Van benefit from 2014/15: payments for private use of van* allow the making good to be delayed until 6 July if there are exceptional circumstances. We should welcome confirmation that this policy will continue to apply to authorised employers who provide company cars and vans for which employees have to make good so they can treat the law as having been complied with in year provided making good will occur by the cut-off date for collating data for processing in the June payroll in the subsequent tax year. This will obviate the complications that would arise from a previous year's BiK being payrolled in a subsequent year. See also point below on Reg 61M.

**31.** Reg 61F(2) *Method of calculating the cash equivalent of the benefit of fuel* refers to the making good payments that the employee is required to make in the tax year, and this follows what is provided for in the primary legislation in section 151(2) ITEPA 2003. Regulation 61M *Modification of the general rule: failure to make good fuel benefit* tells employers what to do if the employee has not made good within 30 days of the end of the tax year. Many employers use charge cards for fuel as they provide management information on fuel usage, but the combination of paperwork delays from employees and card merchants – which can in some cases be as much as 90 days after the year end – and the time needed to collate the data and payroll processing deadlines are likely to render these regulations impossible to comply with. The employer, to be certain, would have to have calculated and received the making good payment before the cut-off date for collating data for processing in the first payroll of the following year ('tax year 2'), and some large employers who payroll BiKs currently have a cut-off date for payroll in the second week of the month.

**32.** HMRC's manual EIM25660 *Car fuel benefit: belated making good* grants leeway where mileage records and repayments in the final month or so of the year take a little time to process – the terms of the legislation are taken as being met provided final settlement is made 'without unreasonable delay'. We should welcome confirmation that this policy will continue to apply for authorised employers who provide car fuel for which employees have to make good. They can then treat the law as having been complied with in-year (ie, process payroll on the basis that the employee has made good) provided making good will occur by the cut-off date for collating data for processing in the June payroll of tax year 2. This will simplify compliance and obviate the complications that would arise from a previous year's BiK being payrolled in a subsequent year. See also point below on Reg 61M.

**33.** Reg 61H(2) *Modification of the general rule: continuing benefit where employment has ceased* We question whether in Step 1 the reference to sections 150, 161 and 203 of ITEPA is correct; we would have thought that the amount of the benefit to be payrolled should be calculated by reference to Regulations 61E, 61F and 61G, otherwise amounts made good by the employee will not be taken into account.

**34.** Reg 61H in sub (1) contains a superfluous 'but' after 'employee' and in (2) at Step 6 a 'final' that does not make sense. We also do not understand how this regulation is supposed to work, even reading the regulation as it was presumably meant to be written. The intention is presumably to capture all the tax on post-termination BiK in the final salary or wage slip, but where an employment is terminated there are normally no next or subsequent 'main relevant payments' as defined. We also doubt that any PAYE ought to be deductible in respect of post-termination benefits. Even if the employer pays for an annual gym subscription or PMI policy while the employee is still in post, the ITEPA tax charge arises on the provision of the benefit, which accrues from day to day, not on the payment of the bill. Any proportion that relates to a period when the employee has ceased to be employed is not a P11D benefit. This point was settled when the termination payment rules were last re-cast by s58 FA 1998. The current drafting (assuming corrected wording to achieve the intention) would collect tax that is not due through the PAYE system, assuming employers managed to create a 'subsequent' final payment as envisaged by the draft legislation.

**35.** Reg 61J *Modification of the general rule: in-year adjustments: other* at sub (2) Step 4 should refer to Step 3 not Step 2.

**36.** Reg 61K *Modification of the general rule: insufficient income* seems to us a recipe for confusion. For employees in receipt over several pay periods of statutory payments (in particular SMP, SAP and even more so ShPP) there will have to be multiple recalculations and carry forwards. For employees with irregular pay periods, the prescribed calculations may be impossible, and for those with irregular earnings (eg, low basic salary plus periodic fluctuating commissions), there will be a need for recalculations in every pay period. This may also apply to motor trade employees whose BiK may depend on the actual cars they use privately. All of

these cases are, we believe, better dealt with by means of a PAYE coding adjustment, which automatically smooths the tax-free pay to date (assuming cumulative rather than W1/M1 codes) and we would suggest that anyone in receipt of SMP, SAP or ShPP be automatically excluded from the prescriptive payrolling provisions of Reg 61K.

**37.** Reg 61M *Modification of the general rule: failure to make good fuel benefit.* We would suggest that, where an employee is obliged to make good, payrolling will only be practical if the rule in draft Reg 61M(1) for fuel reimbursement is (a) extended to 90 days and (b) extended to other BiK. We can see no risk to revenue if this extension is permitted – on the contrary, HMRC is much more likely to receive accurate returns and payments.

*Other points*

**38.** We suggest that consideration be given to the following which may need to be covered in the regulations or in guidance:

(a) that payrolling of BiK covers BiK provided to members of the employee's family or household as well as directly to the employee;

(b) that where payroll frequencies change or a supplementary payroll run is made, employers may need to recalculate the amounts of the BiK to be included in subsequent main relevant payments (in some cases the payroll software may not do this automatically);

(c) how employers notify HMRC where payrolling is suspended as in Regs 61C(4) or 61H (could this be done via the full payment submission?);

(d) how the 50% limit works; in practice: if the rule is all or nothing and the answer was 'nothing', then the full carry forward may also result in the following month being 'nothing', and so on indefinitely. Also 61K(1) refers to 'the benefit' but what happens if there are a number of benefits and tax on some would breach the 50% tax rule but tax on others would not – should the regulation use the plural?

(e) what happens if an amount that should have been made good is not, so that it has to be carried over to the following year and then the employee leaves;

(f) how incoming and outgoing expatriate workers are affected and in particular how employees on modified schemes are impacted (they are after all currently taxed on their BiK on an estimated basis that seems to work);

(g) individuals with more than one contract of employment or two payroll records with BiK on both;

(h) for benefits that are provided late in the tax year before the switch to payrolling, eg a car for a new starter or newly promoted employee, HMRC will not receive a P46(car) for the last quarter of the tax year until May in the following year, so the tax on that BiK will have to be reported on form P11D and the tax liability included on P800 issued after the year end, and the PAYE code could be wrong;

(i) employer obligation to complete form P46(Car) or its replacement (we understand none for cars that are payrolled but a replacement in 2017);

(j) that employees whose BiK are payrolled and who have unpaid sick leave or go on maternity leave should be removed from payrolling using the exclusion tool and a P11D completed instead owing to the earnings being insufficient to payroll BiK, and, where applicable, using the 'made good' box on the P11D for that part year;

(k) how employers will inform the employee that they are payrolling BiK, and notify the amounts of each BiK and the amounts of tax deducted for the year;

(l) how the 3,000 employers who are currently payrolling with permission from HMRC but not in accordance with the draft regulations should continue in the transition whilst software houses are redesigning software;

(m) the Scottish rate of income tax, which may become due after one or more of the recalculations has been carried out; and

(n) we should welcome worked examples in HMRC's guidance of how Regs 61L and 61M would operate in practice, particularly as Reg 61L looks like it is taxing the same benefit twice, in year 1 and year 2.

**39.** We also recommend that HMRC use the drafting of guidance on payrolling and the new expenses exemption as an opportunity to highlight the following common errors on forms P11D completed in draft by employers and picked up by practitioner members prior to submission. Removing the need for employers to complete forms P11D may mean that such errors do not come to light until HMRC undertakes a PAYE inspection, maybe several years later if at all (small businesses are fee sensitive so often do not seek professional advice if they think they understand what is required):

(a) failure to apply Class 1 NIC on the assumption that all non-cash remuneration is Class 1A;

(b) not appreciating the difference in NIC treatment depending on in whose name a contract is made, for example home telephone bills paid for by the employer;

(c) payments by employers for employees' home internet connection where they choose to work at home and there is some business use; and

(d) home to work travel payments where the relevant conditions are not met.

## The Income Tax (Approved Expenses) Regulations 2016

### Benchmark scale rates for employee meals under the new qualifying business expenses exemption

**40.** In the light of the requirement at new Reg 11 that the benchmark scale rates are to cover meals purchased by the employee, we should welcome clarification of the extent to which employers will be expected to retain records of exactly what meals employees have purchased. We trust that such requirements will be implemented with a light touch given that the average employer will not give money to an employee even at the benchmark scale rate if they do not believe that that employee has undertaken qualifying business travel.

**41.** We do not understand why employers with existing bespoke rate agreements made in the last five years have to re-register those rates before 6 April 2016 rather than before the fifth anniversary of entering into such agreements. HMRC does not have the manpower to police all of these bespoke agreements and is likely in practice to do nothing with the registrations except note them. Re-registration as presently envisaged seems likely to create a peak of work for all concerned with no discernible purpose or desirable outcome. It would seem to make more sense to programme a rolling review so that existing agreements renewed in the past five years are brought into the new regime on the expiry of five years from the last renewal.

**42.** The benchmark rates chosen have been unchanged for many years. We would suggest that they be reviewed and uprated. While a £5 allowance will just about buy a single sandwich and a drink in most parts of the UK, the costs for larger meals during full-day absences are well beyond the allowances proposed. Employers may, of course, choose to reimburse actual amounts (assuming no salary sacrifice), but this does seem at odds with our understanding of the policy intent, ie to minimise the number of times an employer needs to resort to actual instead of standard benchmark amounts.

**43.** We would also question the absence of a benchmark rate for accommodation. The civil service is able to set suitable rates for its own staff in and outside London, and the FCO can set rates for overseas locations, so it seems anomalous that HMRC does not publish a benchmark rate for UK accommodation. We would suggest that the HMRC staff rates be

added to the benchmark provisions for employers to use as a fair and acceptable reflection of costs likely to be incurred and as a way to reduce compliance costs for large and small employers and the HMRC compliance staff who police them.

**44.** As well as the above, we suggest that consideration be given to covering the following in the regulations and/or in guidance as appropriate:

(a) recognition in the scale rates for where a hotel bill includes breakfast and/or an evening meal;

(b) that where employers have reimbursed £5 or £10 they can pay an additional £10 if travel continued after 8pm;

(c) non-reimbursed expenses can still be subject to a tax relief claim by the employee;

(d) checking and record keeping requirements for employers;

(e) that, if our suggestion above is not taken up, employers with existing bespoke scale rates must re-request them before 5 April 2016 to get the rest of the five years of such rates being acceptable or a new five year exemption;

(f) the mechanism to do the re-application, and whether there will be a bulk process for agents and if so how it will work;

(g) that no action by employers is needed unless they are using bespoke rates (so not for benchmark scale rates or working rule agreements, but if employers use industry wide rates that are not statutory, that they must be included in a dispensation which should be applied for well before 5 April 2016 so they are agreed by HMRC and therefore can be re-applied for before 6 April 2016); and

(h) what happens where employers do not re-register their existing agreed rates (do the rates paid become a round sum allowance so subject to tax and NIC, triggering the need for large numbers of P87 claims?).

## The Income Tax (Pay As You Earn) (Amendment No *) Regulations 2016

### Removing the need for employers to report expenses paid to employees on form P11D

**45.** We have no comments on these Regs subject to those in the previous paragraph about matters that we feel might usefully be included in regulations and/or guidance.

APPENDIX 1

## ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.

2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.

3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.

4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.

5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.

6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.

7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.

8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.

9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.

10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see via http://www.icaew.com/en/about-icaew/what-we-do/technical-releases/tax).