Integrating the operation of income tax and National Insurance contributions

Working Group 2:
Meeting 4: 28 February 2012

Attending

Norman Green  BCS/Logica
Chris Hind  BCC
Steve Wade  ICAEW/CBI
John Black  Midland HR/CIPP
Helen Harvey  Nannytax
Peter Arrowsmith  ICAEW

Elizabeth Morgan  HMT
Jayesh Patel  HMT
Simon Manclark  HMRC (Chair)
Mellannie Merrifield  HMRC
Sam Tennakoon  HMRC
Margaret McCollgan  HMRC
Simon Carr  HMRC
David McDowell  HMRC

Introduction

HMRC explained that the purpose of this meeting was to discuss options considered by Working Group 1 (WG1) on the structure of NICs and the interdependencies between the options for base and structure.

Points raised in the discussion

HMRC explained that WG1 had been considering mis-alignments in the earnings base between tax and NICs. In particular they had been considering the differences in the treatment of benefits and expenses.

Benefits-in-kind (BIKs) are not subject to Class 1 NICs and WG1 had looked options to equalise the tax and NICs treatment. They suggested that in each pay period the employer would only need to estimate the value of the benefit and include it in the payroll in that period, finally reconciling in the last pay period in the year. Although this would be a strain on the payroll for the final period. It was noted the PAYE regulations would need to change to allow for this reconciliation.

The Group concurred with the views of WG1 in that it would be difficult to payroll all benefits in kind (BIKs), in particular items like private medical treatment and beneficial loans (unless the rules around loans changed). But
for the remainder payroll software can do a lot of the payrolling work. The Group also held the view that a Class 1 NICs charge on BIKs should mirror tax in the way it is assessed and collected.

HMRC then asked the Group about payrolling expenses. The Group held the view that the current process, whereby all expenses are recorded on form P11D (in the absence of a dispensation or PSA), and the employee claims back business expenses from HMRC should change. And that after the business element of the expense had been established, the profit element should simply be put through the payroll, removing the need to report to HMRC. The point was also made that it was doubtful that an employee would necessarily know that they could make a claim, unless their employer advised them to.

The Group all agreed that generally there should be simpler, clearer rules and processes for BIKs and expenses. There was general confusion around what is taxable/NIC-able and what should and shouldn’t get reported.

With regard to interdependencies, one member of the Group noted that a NICs code would not necessarily be required where expenses were aligned and NICs were moved to the tax model. Instead the tax code could be used.

The meeting was then concluded and HMRC/HMT expresses their thanks to the Group for participating in this consultation exercise.

Views were sought on the overall benefits of reform. Points made in the discussion included:

As this was the last WG2 meeting before the Budget HMRC asked the group for their views on whether there was a case for reform and if so what the ‘prize’ may be.

The Group felt that on balance there was a case for reform, but that solutions were not always that obvious, and that the objectives (fairness, transparency, etc.) may not always be achieved. Summarising, the Group also made the following comments.

Some changes may make things simpler and less complicated, whereas others may not. As with most changes, there will be winners and losers. The Group thought that the fairer outcomes could be achieved through a NICs operation that was annual, cumulative and aggregated across employments (ACA), but that ACA might not make things that much simpler for employers or employees. Introducing a second code for NICs for example may lead to some confusion, but having a NICs code is probably unavoidable with ACA.

Some felt that ACA would need to have a reasonable lead-in time in order for employers and employees to familiarise themselves with any changes to come, as some would find themselves accounting for NI for the first time.
With regard to employer NICs and what has been proposed to date, one Group member stated that a payroll charge would be fairer if it was based on the size of the employer as opposed to employee NICs as it is currently. It was also recognised that there would also be winners and losers with a payroll charge.

Benefit rules would have to change if the calculation and collection of NI was to change.

Generally, the Group also felt that if whatever was proposed didn’t make things simpler then we shouldn’t pursue that particular change.

One Group member said HMRC/HMT should conduct a longer term review of NICs simplification and the main objective should be to make tax and NICs simpler and easier to understand for both employers and employees. And what’s been suggested so far may not always do that, but we should continue to work towards that goal.

The Group also indentified the Lower Earnings Limit (LEL) as being an issue. Some questioned why an individual should be entitled to certain benefits, but could in theory have paid no employee NICs, as would be the case if they were paid between the LEL and the Primary Threshold (PT).

The meeting was then concluded and HMRC/HMT expressed their thanks to the Group for participating in this consultation exercise.