EXPLANATORY MEMORANDUM TO

THE INCOME TAX (PAY AS YOU EARN) (AMENDMENT NO. 3) REGULATIONS 2014

2014 No. 2396

1. This explanatory memorandum has been prepared by HM Revenue and Customs (HMRC) and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument makes amendments to the Income Tax (Pay As You Earn) Regulations (S.I. 2003/2682) (the 2003 Regulations) in relation to penalties for employers who are reporting information regarding payments (including tax deducted at source) on or before the making of a payment and who fail to deliver a return by the relevant filing date. This instrument is consequential upon The Finance Act 2009, Schedule 55 (Penalties for failure to make returns) (Appointed Days and Consequential Provision) Order 2014 (S.I. 2014/2395 (C. 105)) ("the Appointed Day Order") which appoints the days from which employers will be liable to in-year filing penalties.

3. Matters of special interest to the Select Committee on Statutory Instruments

None.

4. Legislative Context

4.1 The 2003 Regulations govern the operation of the Pay As You Earn (PAYE) system under which Income Tax is deducted at source from an employee's pay. Certain other deductions are also made under the PAYE system.

4.2 Under the 2003 Regulations, as amended from 6 April 2012, employers are required to deliver a return to HMRC in respect of every payment made to an employee on or before the payment is made.

4.3 This instrument amends the 2003 Regulations by specifying the quantum of the penalties for Real Time Information (RTI) employers who fail to file a return by the relevant filing date. The quantum of the penalty relates to the number of employees at the date of the failure. This instrument also disapplies the unpenalised default provision contained in paragraph 6C(4) of Schedule 55 to the Finance Act 2009 (c. 10) in two specific circumstances. The first is a transitional arrangement and applies only for the period 6 March to 5 April 2015 and only where the employer employs no more than 49 employees on 6 October 2014. The second is where an employer is one which

operates an annual pay as you earn scheme (that is it pays all its employees only once a year).

4.4 This instrument is made under paragraph 6C of Schedule 55 Finance Act 2009 and it is the first use of the powers therein.

5. Territorial Extent and Application

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

- ***What is being done and why***

7.1 The Finance Act 2009 introduced penalties where returns are delivered to HMRC after the relevant filing date. These penalties have already been applied to various taxes, and by the Appointed Day Order those penalties are applied to employers who file their returns after the relevant filing date.

7.2 In April 2012 HMRC began to pilot the delivery of information to HMRC for PAYE in real time with volunteer employers and software developers. Once reporting PAYE in real time, employers are required to report information about payments to employees (including the tax deducted) on or before making the payment to the employee. In April 2013 the requirement to report in real time was introduced for all employers. However, HMRC recognised that employers needed time to adapt to the requirement to report more frequently. As a consequence HMRC delayed the introduction of late filing penalties to ensure employers had more time to adjust to the new system.

7.3 Most employers have now been reporting PAYE information in real time for over a year and most report on time. Therefore, to encourage the remaining employers to make a return on or before the relevant filing date, the Appointed Day Order applies the penalties in Schedule 55 to the Finance Act 2009 to a failure to make a return of real time information on time.

7.4 However, HMRC experience in introducing real-time PAYE reporting has shown that, where possible, introducing changes in stages is preferable as it allows HMRC to update systems and enhance guidance and customer support as needed.

7.5 Therefore, the Appointed Day Order applies the penalties to Real Time Information employers (those who have at least 50 employees on 6 October 2014) from 6 October 2014. It applies these penalties to small Real Time

Information employers (those who at 6 October 2014 have no more than 49 employees), and those who become an employer after 5 October 2014, from 6 March 2015.

7.6 Applying these penalties to small Real Time Information employers from a later date gives these employers longer to adapt. In addition, a proportion of small employers were previously using a reporting easement and have only started reporting on or before from April 2014. It is apparent that many employers with 9 or fewer employees are still not using the late reporting code on their submissions and this additional time will enable HMRC to raise awareness without those employers incurring a penalty.

7.7 Applying these penalties to small Real Time Information employers from 6 March 2015 means that if an employer fails to file the final return for the tax year 2014/15 (which will include all the relevant information for the tax year) that employer will be liable to a penalty similar to the 'end of year' penalty previously charged for a failure to submit the end of year P35 and the P14 forms by 19th May following the year in question.

7.8 This instrument sets the amount of the late filing penalty which is calculated by reference to the number of employees employed by the Real Time Information employer in the tax month the failure occurred. It is a non-escalating penalty.

7.9 New Real Time Information employers will not be liable to a penalty in respect of the first return if that return is made within 30 days of the date on which the employer was required to submit a return.

7.10 A Real Time Information employer is not liable to a penalty in respect of the first failure to make a return on or before the relevant filing date in any tax year.

7.11 However, that provision does not apply to Real Time Information employers who operate an annual PAYE scheme (which applies where all employees are paid annually, within the same tax month and is only required by HMRC to pay annually) and for small Real Time Information employers during the period 6 March 2015 to 5 April 2015 only.

- ***Consolidation***

There are currently no plans to consolidate the instrument that is being amended.

8. Consultation outcome

8.1 HMRC has consulted widely on the impact of employers reporting PAYE in real time. Analysis of the evidence indicates that the majority of employers are able to file 'on or before' and that they believe they will experience, over time, a reduction in their administrative costs when the

changes to end-of-year processes are taken into account.

8.2 Consultation on this instrument which sets out the in-year penalty provisions took place during the period 29 November 2013 to 24 January 2014.

8.3 Following customer feedback to the consultation, HMRC announced in February 2014 that late filing penalties would not be introduced until October 2014 http://www.mynewsdesk.com/uk/hm-revenue-customs-hmrc/pressreleases/hmrc-unveils-new-timetable-for-rti-penalties-960361. HMRC have now further extended that introduction date for small employers.

9. Guidance

9.1 Employers will be advised by an electronic Generic Notification Service message of the date from which the penalties will apply to them.

9.2 Guidance has been published on HMRC's website for employers using RTI and this will be updated to reflect the staged introduction of in year late filing penalties.

10. Impact

10.1 As businesses, charities and voluntary bodies are employers they will be liable to penalties if they fail to deliver a return regarding employees by the relevant filing date.

10.2 A Tax Information and Impact Note covering this instrument was published on 20th March 2013 alongside Budget 2013 documentation and is available on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm. It remains an accurate summary of the impacts that apply to it.

11. Regulating small business

11.1 The legislation applies to small business.

12. Monitoring & review

12.1 HMRC will monitor the operation and administration of this change through continued communication with employers and external stakeholder groups. Successful implementation of this measure will result in a reduction in the number of employers filing their returns after the relevant filing date.

13. Contact

Ady Garrett at HMRC tel. 03000 586936 or email: ady.garrett@hmrc.gsi.gov.uk can answer any queries regarding the instrument.