EXPLANATORY MEMORANDUM TO

THE INCOME TAX (PAY AS YOU EARN) (AMENDMENT NO. 3) REGULATIONS 2026

2026 No. 1082

1. Introduction

1.1 This Explanatory Memorandum has been prepared by His Majesty's Revenue and Customs (HMRC) and is laid before the House of Commons by Command of His Majesty.

2. Declaration

2.1 The Rt Hon James Murray, Financial Secretary to the Treasury and Paymaster General confirms that this Explanatory Memorandum meets the required standard.

2.2 Gareth Cooper, Deputy Director for the Income Tax Policy Directorate, at HMRC confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Demi Abeynayake at HMRC can be contacted by email at the following address with any queries regarding the instrument: policyemploymentbenefitsexpenses@hmrc.gov.uk

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument amends the Income Tax (Pay As You Earn) Regulations 2003 (the PAYE Regulations) so that employers may voluntarily register to report non-mandated benefits in kind using payroll software. It allows employers to report the taxable benefit of employment-related loans and employer-provided living accommodation voluntarily using payroll software from the 2027-28 tax year. It also sets out how employers must calculate the cash equivalent or relevant amount of those benefits for payrolling purposes, including where information needed for the calculation is not known when the calculation is made.

4.2 The instrument also reopens the voluntary payrolling registration service, which had previously been closed to new applications, by removing the restriction that would otherwise prevent employers from applying to become authorised employers for the 2027-28 tax year and later years. Transitional provision ensures that the amendments do not permit an in-year application for voluntary payrolling for a tax year before 2027-28.

Where does the legislation extend to, and apply?

4.3 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the United Kingdom.

4.4 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the United Kingdom.

5. Policy Context

What is being done and why?

5.1 Benefits in kind are non-cash benefits or facilities provided to employees by reason of their employment. Unless an exemption applies, the value of a benefit in kind forms part of the employee's taxable employment income.

5.2 Under the existing voluntary payrolling framework in Chapter 3A of Part 3 of the PAYE Regulations, an employer may apply to HMRC to become an "authorised employer" and account for Income Tax on specified benefits through Pay As You Earn during the tax year. Employment-related loans and living accommodation are not currently included within the definition of specified benefits.

5.3 As part of the government's wider reforms to mandate the reporting and payment of tax on benefits in kind through payroll, registrations for the voluntary payrolling service were closed in order to make technical changes to the service ahead of the introduction of mandatory payrolling. The move to mandatory payrolling is being implemented in two phases to support employers and software providers in adapting to the new requirements. As a result, a voluntary payrolling service remains necessary for benefits that are not mandated in the first phase, benefits that will be brought into scope in a later phase, and benefits that are excluded from the scope of mandatory payrolling.

5.4 This instrument brings employment-related loans and living accommodation into that framework for the 2027-28 tax year and subsequent tax years. Employers that choose to payroll either benefit will calculate its cash equivalent, or relevant amount where the optional remuneration arrangement rules apply, using the existing valuation rules in the Income Tax (Earnings and Pensions) Act 2003 (ITEPA).

5.5 The value of a loan or living accommodation benefit can depend on information that is not available when the employer first needs to calculate the amount to payroll. The instrument therefore allows an authorised employer to make reasonable assumptions about missing information, provided those assumptions are based on a contract or agreement with the employee. Existing in-year adjustment rules will then apply where the value of the benefit changes or the original calculation is no longer accurate.

5.6 This change gives employers the option to collect and report Income Tax and National Insurance Contributions (NICs) on these benefits through payroll during the year rather than reporting them after the end of the tax year. It supports the wider move towards reporting and collecting tax and NICs on benefits in kind through payroll while retaining voluntary treatment for loans and living accommodation.

What was the previous policy, how is this different?

5.7 The instrument removes the restriction on applications to become an authorised employer for the 2027-28 tax year and later years. This will allow HMRC to reopen the voluntary payrolling registration service, enabling employers to apply to payroll non-mandated benefits as part of the first phase.

5.8 Previously, employers could not use the statutory voluntary payrolling framework for employment-related loans or living accommodation. Where those benefits were taxable, they were reported after the end of the tax year using form P11D, and the related Income Tax was normally collected from the employee separately, including through an adjustment to the employee's PAYE code.

5.9 From the 2027-28 tax year, an employer may instead apply to payroll these benefits voluntarily. The underlying ITEPA rules for determining whether a taxable benefit arises and for calculating its final value are not changed by this instrument. The instrument changes the benefits that may be brought within the voluntary payrolling framework and provides rules that enable the value to be calculated for payroll purposes.

6. Legislative and Legal Context

How has the law changed?

6.1 The instrument is made by the Commissioners for HMRC under section 684(1) and (2) of ITEPA.

6.2 Regulation 3 amends regulation 61A of the PAYE Regulations. It expands the definitions of "relevant amount" and "specified benefit" to include living accommodation within sections 97 and 103A of ITEPA and loans within sections 173 and 175A of ITEPA.

6.3 Regulation 4 omits regulation 61C(9A) of the PAYE Regulations, removing the existing restriction on applications to become an authorised employer from the 2027-28 tax year onwards. The amendment ensures that employers may continue to apply for authorisation to payroll benefits and expenses where voluntary payrolling is available under the PAYE Regulations.

6.4 Regulation 6 inserts new regulations 61GA and 61GB into the PAYE Regulations. These require the cash equivalent or relevant amount of living accommodation and loans to be calculated under the relevant ITEPA provisions and allow reasonable assumptions to be made in those calculations, based on a contract or agreement with the employee, where necessary information is not known on the calculation date.

6.5 Regulations 5 and 7 to 9 make consequential amendments to the general deduction rule and the rules dealing with cessation of employment and in-year changes.

6.6 Regulation 10 provides that the amendments apply, for the purposes of in-year applications under regulation 61C(4) and (5) of the PAYE Regulations, for the 2027-28 tax year and subsequent tax years.

Why was this approach taken to change the law?

6.7 Amending Chapter 3A of Part 3 of the PAYE Regulations is the appropriate way to add loans and living accommodation to the existing statutory voluntary payrolling framework and to prescribe how their value is calculated for PAYE purposes.

7. Consultation

Summary of consultation outcome and methodology

7.1 No consultation was undertaken. The government announced the introduction of mandatory real-time reporting of benefits in kind in January 2024 and has carried out stakeholder engagement to explain the change.

8. Applicable Guidance

8.1 HMRC guidance on payrolling benefits in kind, employment-related loans and employer-provided living accommodation will be updated to explain the voluntary

option and the calculation rules before employers begin operating the changes for the 2027-28 tax year. This guidance can be reviewed on the gov.uk website.[1]

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A Tax Information and Impact Note covering this instrument was published on 23 July 2026 alongside draft primary legislation for reform of the reporting of, and payment of tax on, benefits in kind. It will be updated to reflect changes to the impacts arising from this instrument. It is available on the GOV.UK website.[2]

Impact on businesses, charities and voluntary bodies

9.2 The measure is expected to have a negligible impact on businesses, charities and voluntary bodies. Employers may choose to payroll non-mandated benefits in kind or continue using the existing P11D and P11D(b) process. Based on historically low take-up of voluntary payrolling, most employers are expected to retain the current process.

9.3 Employers choosing to voluntarily payroll non-mandated benefits in kind may incur one-off costs from familiarisation, registration, system and process changes, and staff training, alongside ongoing costs from more frequent recording and reporting. These costs may be offset by reduced agent costs and savings from removing some end-of-year reporting obligations. Overall, the measure should simplify administration for participating employers by allowing them to avoid operating separate real-time and annual reporting processes.

9.4 Although these changes impact small and micro businesses, their obligations will be unchanged unless they choose to voluntarily payroll benefits in kind.

9.5 There is no, or no significant, impact on the public sector for this legislation. There are no new obligations being imposed on public bodies.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring the instrument is through normal compliance activity and regular communications with representative bodies.

10.2 The instrument does not include a statutory review clause because in accordance with the requirements of the Small Business, Enterprise and Employment Act 2015, it is made in relation to the imposition of a tax, duty, levy or other charge.

[1] See the Mandatory Payrolling of benefits in kind and expenses – interim guidance and legislation document at: https://www.gov.uk/guidance/draft-guidance-and-legislation-to-aid-preparation-for-reporting-benefits-in-kind-in-real-time

[2] See the Tax Impact Information Note for Mandatory reporting of benefits in kind in Real Time Information (RTI) from April 2027, published on 13 July 2026 at: https://www.gov.uk/government/publications/changes-to-reporting-of-benefits-in-kind-from-april-2027/mandatory-reporting-of-benefits-in-kind-in-real-time-information-rti-from-april-2027

10.3

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None.

12. European Convention on Human Rights

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

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").