These notes refer to the Welfare Reform and Pensions Act 1999 (c.30) which received Royal Assent on 11 November 1999

WELFARE REFORM AND PENSIONS ACT 1999

EXPLANATORY NOTES

COMMENTARY

Commentary

Part III

Paragraph 9 of Schedule 9 amends section 162 of the Social Security Administration Act 1992. This ensures that the proportion of contribution revenue allocated to the National Health Service remains broadly unchanged when the starting point for employee contributions is increased to the primary threshold.

Sections 75 and 76: Earnings of workers supplied by service companies etc.

Background

Section 75 provides for a new power to counter the risk of avoidance of National Insurance contributions where an individual (the worker) provides personal services through an intermediary. It is intended that the provisions in this Act will be matched by tax legislation that will, in specified circumstances, require the intermediary to operate Pay As You Earn (PAYE) on the payments made to, or in respect of, the worker. The Chancellor of the Exchequer announced in his Budget that these measures would take effect from 6 April 2000. Consequently, the regulations to be made under Section 75 will come into force from that date. Equivalent provisions for Northern Ireland are contained in Section 76.

Section 75 concerns the situation where the worker is engaged by a business (the client) through a third party (such as a service company). In the absence of such a third party, the relationship between a client and a worker would determine the employment status for the purposes of both tax and National Insurance. Liability would then be assessed according to whether the person was employed or self-employed. However, where a worker is engaged through one or more third parties, it is possible to escape any direct contractual relationship between client and worker. This provides scope for the avoidance of tax and National Insurance contributions (NICs).

The powers in section 75 are intended to deal with the situation where the relationship between a client and a worker would be one of employer and employee, but for the intermediary. They provide for a specified amount of the payments made in respect of the worker to be treated as earnings paid to an employee – and therefore liable for NICs. Regulations under the section will ensure that specified amounts will be regarded as paid to the worker for the purposes of primary Class 1 NICs and the intermediary will be liable for the corresponding secondary Class 1 NICs. The regulations will identify how the amount to be treated as earnings paid to the worker will be calculated.

In order to minimise the administrative burden, the Chancellor announced that certain details of the new rules would only be finalised after discussion with representative bodies. An outline of the proposed new rules was circulated to those who had expressed

an interest in this measure and there have been a number of discussions with business representatives on the original proposals.

In the light of this consultation, the Paymaster General announced various changes to the proposal on 23 September 1999. The main changes were:

to make the intermediary rather than the client responsible for operating the new rules and deducting and accounting for NICs where required;

to ensure that the conventional test used to distinguish between employment and self-employment for individuals not using intermediaries would also apply in cases covered by the new legislation; and

to allow a deduction for certain expenses in determining the amount of money which is to be treated as earnings subject to Class 1 contributions in cases where the new rules apply.

These new proposals are reflected in the section.

Section 75 will enable NICs regulations to take effect at the same time as the proposed new tax rules without the need for retrospection. It sets out the general powers on the face of the Act and allows for the technical detail to be contained in regulations. This approach is consistent with current social security legislation.

For example, section 4(6) of the Social Security Contributions and Benefits Act 1992 enables regulations to be made for the purpose of treating as earnings certain forms of employee shares (conditional and convertible shares) and the Social Security (Contributions) Regulations 1979 (S.I. 1979/591) ("the Contributions Regulations") provide all the consequential technical detail. Regulation 18 of the Contributions Regulations provides the basis on which the amount of earnings comprised in a payment of conditional or convertible shares is to be ascertained and regulation 19 provides when such shares are to be disregarded from earnings. This section takes the same approach, which also has the advantage that it provides the flexibility to enable changes to be made more easily should the parallel tax provisions or business practice change in the future.

Commentary

Subsection (1) sets out the circumstances in which the regulation-making power is to operate. Regulations will set out which arrangements involving a worker hired through an intermediary will be caught by the provision.

The normal range of tests to decide a worker's status, which have developed through the courts and the principles of common law, will be used to determine whether the relationship between the client and the worker should be subject to the new rules.

Subsection (1) also enables regulations to specify (i) what payments and benefits are to be treated as earnings paid to the worker in respect of employed earner's employment for the purposes of the Contributions and Benefits Act, and (ii) the extent to which they are to be so treated.

It is intended that regulations will provide that, in addition to payments that are earnings by virtue of section 3 of the Contributions and Benefits Act, payments treated as earnings by virtue of section 4 of that Act (for instance, conditional and convertible shares) will be treated as earnings under this provision.

It is intended that the regulations will prescribe how to calculate the amount to be treated as earnings. This follows the existing practice whereby regulations made under section 3(2) of the Contributions and Benefits Act provide for the calculation of the amount of earnings comprised in specified payments (see regulation 18 of the Contributions Regulations); and regulations made under section 3(3) of that Act specify what payments that are to be exempt from that calculation (see regulation 19 of the Contributions Regulations).

Subsection (2) defines the meaning of an "intermediary" for the purposes of the provision. It is intended that regulations should provide for the intermediary to be either the company that employs the worker or a partnership in which he is a partner.

Subsection (3) then provides specific, but non-exhaustive, illustrations of what the regulations made under the section may provide.

Subsection (3)(a) enables regulations to specify that a worker is to be treated as employed in employed earner's employment for the purposes of the Contributions and Benefits Act in respect of his "attributable earnings".

"*Attributable earnings*" are a specified amount of the "relevant payments and benefits" made or provided in connection with the services the worker performs for the client. They will be a minimum amount, which must be treated as salary paid to the worker by the intermediary within the tax year and subject to Class 1 NICs.

Subsection (3)(b) enables the intermediary (whether or not he fulfils the prescribed conditions about residence and presence in Great Britain) to be treated as *the* secondary contributor in respect of the worker's attributable earnings.

Subsection (3)(c)(i) enables regulations to specify what deductions are to be made in calculating the amounts on the payments that are treated as earnings paid to the worker in respect of the *services* provided to the client. Regulations would allow for the deduction of certain allowable expenses currently exempt for the purposes of other parts of the Act.

An example of this is found in regulation 18(4)(b) of the Contributions Regulations, where identifiable payments towards expenses incurred by an employee in carrying out his employment are exempted from NICs.

Subsection (3)(c)(ii) enables regulations to specify how the amount of earnings that the worker is to be treated as having been paid is to be calculated or estimated. It will be for the intermediary to *calculate* the earnings caught by the provision and what deductions can be made.

Subsection (3) (d) enables *regulations* to set out how the worker's "attributable earnings" may be aggregated with any other earnings he has, in order to calculate the full year's NICs liability correctly.

Subsection (3)(e) provides for regulations to determine the date by which contributions payable under *the* provision have to be paid and accounted for.

Subsection (3)(f) enables regulations to specify how relevant payments and benefits are to be apportioned. It is intended to specify in regulations how an aggregate payment in respect of two or more workers is to be apportioned (including apportionment in cases where one or more of that number would be regarded as in employed earner's employment with the client other than by virtue of the regulations). In circumstances where, at the time of payment, it is not possible for the intermediary to identify the amount attributable to each worker/ individual, it is proposed that the regulations will provide for apportionment on a just and reasonable basis, and for contributions to be calculated on the "apportioned" earnings.

This is consistent with the approach found in regulation 18 of the Contributions Regulations. Regulation 18 already includes an apportionment calculation following section 48 of the Social Security Act 1998 (which amended section 3 of the Contributions and Benefits Act by inserting a new subsection (2A)). Paragraph (21) and (24) of regulation 18 of the Contributions Regulations, which were made under the power in the new subsection (2A), specify the basis of apportionment in respect of payments to two or more employed earners in the form of a contribution to an unapproved retirement benefit scheme and a non-cash voucher (paragraphs (21) and (24) respectively).

Subsection (3)(g) will enable the worker's employment with an intermediary or otherwise to be disregarded *for* NIC purposes.

Subsection (3)(h) enables regulations to be made to ensure that a relevant payment or benefit is not subject to a double National Insurance liability. This may be necessary in cases where an amount to be treated as earnings by virtue of the new rules would otherwise be liable to NICs under other provisions.

Subsection (3)(i) enables regulations to specify the extent to which two or more connected persons should be treated as a single person for the purposes of the regulations.

This is necessary, for example, to deal with cases where a worker is engaged to work for the client via a connected party (such as an associate company), within the meaning of section 839 of the Income and Corporation Taxes Act 1988, and no contract exists between the intermediary and the associate for the worker's services. It is intended that regulations will determine whether the client and the associate are to be treated as single persons and consequently, whether the new rules should apply to them. Regulations may specify persons of any other specified description as being single persons for the purposes of the provision.

Subsection (3)(j) will *ensure* that the new rules are still applicable where the contract is not made by the client but someone "connected" to him.

Subsection (3)(k) allows for *regulations* to modify or exclude the application of the new rules.

Subsection (4) enables the regulations to set out what expenses may be deducted by the intermediary when calculating a worker's attributable earnings. The Government has proposed that 5 per cent of the intermediary's receipts from relevant engagements should be deducted, to cover general expenses. In addition, any employer's pension contributions to an approved scheme in respect of the worker and any secondary Class 1 contributions paid by the employer will be deductible.

Subsection (5) enables regulations to specify that terms and conditions of a contract or arrangement may be disregarded for the purposes of applying the new rules. It is intended to use regulations to ensure that the substance of the relationship will determine whether the worker should be treated as being in employed earner's employment for the purposes of the Contributions and Benefits Act.

Subsection (7) ensures that the reference in subsection (1)(a) above to a worker being under an obligation to perform services is carried through.

Subsection (8) provides that any regulations made under the provision by the Treasury will require the concurrence of the Secretary of State for Social Security. This reflects the interaction between contributions and contributory benefits. The latter are the responsibility of the Secretary of State.

The regulations implementing this measure will come into force on 6 April 2000 and will parallel the tax clauses due to be introduced in the Finance Bill 2000. However, in order to ensure the simplest possible systems for business to operate, it is necessary to keep the tax and NIC rules in line with each other.

Subsection (9) therefore gives a power to enable this section to be adapted by order if the parallel tax provisions change.

There are a number of precedents for a use of this type of power. One example of the modification of primary legislation by order is found in section 10 of the Contributions and Benefits Act. Section 10 provides for a Class 1A contribution to be paid annually by an employer in respect of the provision of a car or fuel to an employee. The Class 1A charge applies where, for any tax year, an income tax benefit is chargeable under Schedule E by virtue of sections 157 and 158 Income and Corporation Taxes Act 1988 (ICTA) in respect of the provision of the car and/or fuel. Section 10 includes a modification power at subsection (7) to enable the Secretary of State to make regulations modifying section 10 where it is necessary or expedient to do so in consequence of any alteration to section 157 and 158 ICTA.

The annual Finance Bill means that changes to the tax legislation could occur annually, subject to Parliamentary approval. There is no equivalent annual legislation available to make changes to primary legislation covering National Insurance contributions. So, without this subsection, it would be difficult to amend the Contributions and Benefits Act to mirror the changes to the Finance Act.

Sections 77 and 78: National Insurance Class 1B contributions

Section 77 ties the National Insurance Class 1B rate to the rate of 'secondary' (employer) Class 1 contributions, thus preventing the Class 1B rate from being raised independently by regulations. Both rates are currently set at 12.2%.

It amends section 10A of the Contributions and Benefits Act which deals with Class 1B contributions, replacing subsection (6) (which provides that the percentage rate is to be 12.2%, but enables it to be altered under section 143A of the Administration Act) with a provision to tie it to the rate of the secondary contribution, as specified in section 9(2) of the Contributions and Benefits Act.

Background

Measures introduced in the Social Security Act 1998 provide that, from 6 April 1999, employers can settle the National Insurance liability on a Pay As You Earn Settlement Agreement (PSA) for tax purposes. This introduced a new class of National Insurance contributions known as Class 1B.

The percentage rate of Class 1B NICs was initially set at the same level as the rate of secondary (employer) contributions, but was capable of being varied independently of the secondary Class 1 rate.

This section ties the rate of Class 1B directly to the rate of secondary (employer) contributions, thus taking away the ability for it to be varied independently of that rate.

Section 78 makes corresponding provision for Northern Ireland.

Schedule 13 Parts VI and VII: Repeals : National Insurance contributions

Parts VI and VII contain repeals which are consequential on sections 73, 74, 77 and 78. The repeal of paragraphs 8(2) and (3) of Schedule 1 to the Contributions and Benefits Act updates the legislation by removing reference to the payment of National Insurance contributions by adhesive stamps, to reflect the current methods of payment available.

Background

Before April 1993, flat rate National Insurance contributions payable by the self-employed (Class 2) or paid on a voluntary basis (Class 3) could be made by affixing a stamp of appropriate value to a contribution card in respect of each contribution week. Since then, it has been possible to:

> make a payment of the amount of contributions specified in a written notice issued within 14 days of the end of the quarter in question; or
>
> pay by direct debit.

Adhesive stamps ceased to be sold by the Post Office soon afterwards, and could not therefore be used as a method of paying National Insurance contributions. The references in paragraph 8(2) and (3) of Schedule 1 are therefore redundant.

Parts VI and VII of Schedule 13 also include repeals consequential on section 81 and Schedule 11.

Chapter III: Other Welfare Provisions

Section 79: measures to reduce under-occupation by housing benefit claimants

This section will allow tenants living in the social rented sector (typically, property owned or managed by a local authority or a housing association), who are in receipt of Housing Benefit (HB), to keep part of any benefit saving generated by moving to cheaper and smaller accommodation.

The scheme to be made under this section will encourage tenants who are "under-occupying" accommodation in the public or social rented sector (that is, living in accommodation that is considered large in relation to their number and needs) to move to smaller and cheaper accommodation. On completion of the move, HB claimants will be rewarded with a lump-sum payment equivalent to half the difference between their old and new weekly rent, multiplied by 156. Since HB usually meets 100% of rental costs in the social rented sector, this is roughly half of the benefit savings expected over three years. It is intended that the lump sum will be disregarded as capital in the calculation of entitlement to income-related benefits, such as Income Support or the Working Families Tax Credit.

Regulations under *subsections (1)* and *(3)* would define exactly how the sum paid to claimants should be calculated, and in what circumstances a dwelling would be regarded as "under-occupied" (for example, a 3-bedroom house could be regarded as exceeding the requirements of a couple).

Subsection (4) gives power to make deductions from the lump-sum payment for any arrears of rent owed by the tenant, or for any overpayment of HB which is recoverable from the claimant.

Other debts to the local authority or to the DSS (e.g. the Social Fund) are not to be deducted; deductions are to be strictly limited to the two items mentioned.

Subsection (5) provides a right of appeal against decisions made under the scheme.

The details of the appeal – for example, the appeal body, the determinations that may be appealed against and the appeals procedure – will be set out in regulations.

The section would allow the under-occupation scheme to be applied nationwide, though *subsection (7)* makes clear that no local authority would be obliged to take part in the scheme. However, the intention is to pilot the scheme in three local authorities; therefore *subsection (6)* allows the power to be used for a limited time and in certain areas only, and for any necessary transitional arrangements to be made. Section 83(8) would allow different provision in different areas.

Subsection (9) provides that the under-occupation scheme payments should be administered under the rules and powers for Housing Benefit (which are set out in the Administration Act)—but allows for exceptions to be specified.

Among the HB rules is the procedure for the DSS to reimburse local authorities for the money they pay in benefits. Normally this happens through a subsidy system; the subsidy rules mean that an authority may not always receive the full amount it pays out. However, *subsection (8)* provides the power to prescribe a different claims and payments mechanism. The intention is that, under the scheme, authorities should be reimbursed *in full* for the lump-sum payments they make.

Section 80: Supply of information for child support purposes

This provision allows the Inland Revenue, on a discretionary basis, to supply tax information it holds in respect of self-employed non-resident parents to the Child Support Agency (CSA). This is intended to enable the CSA to build up a financial

picture of non-resident parents whose earnings either are not known or need to be verified.

The CSA is required by law to assess maintenance liability when a valid application is received. To make this assessment, it needs details of the non-resident parent's earnings. This information is sometimes difficult to obtain directly from the non-resident parent, who may deliberately withhold information with a view to delaying a demand for maintenance or may simply be unable to locate the relevant documentation. Whilst this is less significant for employed earners, where the CSA can approach the employer direct, non-resident parents who are self-employed, and who refuse to supply details of their profits, are extremely difficult to assess.

The Agency therefore needs to be in a position to build up a financial picture of a non-resident parent who does not provide details of his income, using as wide as possible a range of alternative sources of information. Tax information held by the Inland Revenue may offer the only alternative source of such information for the self-employed. However, the intention is that this will be a last resort measure, where the CSA has asked the non-resident parent for information, and issued a reminder, but there is still inadequate detail to make an assessment.

Access to tax information relating to self-employed non-resident parents is necessary to ensure that more non-resident parents pay the maintenance they owe. Given the Revenue's confidentiality provisions, the CSA can only gain access to this information if there is a specific statutory gateway. This provision provides this gateway and allows direct access, at the Revenue's discretion, to any tax information about self-employed non-resident parents held by the Inland Revenue.

Schedule 2 to the Child Support Act 1991 already allows the Secretary of State to request the Inland Revenue to provide information for the purposes of tracing non-resident parents. This information is restricted to the current address of the non-resident parent and his current employer. The CSA has access, via the Contributions Agency, to earnings information recorded on end-of-year tax returns that employers currently submit to the Inland Revenue. There is currently no provision, however, for other tax information to be used in assessing child support liability.

Commentary

The section inserts a *new paragraph 1A* into Schedule 2 to the Child Support Act 1991.

Sub-paragraph (1) limits the power to obtaining tax information about *self-employed* non-resident parents, not all non-resident parents. It allows access to information for any tax year in which the non-resident parent was or is self-employed.

Sub-paragraph (2) exempts the Revenue from its confidentiality rules when providing this particular information.

Sub-paragraph (3) ensures that the paragraph only applies to disclosures made to the CSA by, or under the authority of, the Commissioners of the Inland Revenue.

Sub-paragraph (4) prevents, as a general rule, any tax information disclosed to the CSA under this power from being disclosed further.

For example, this overrides the power in section 3 of the Social Security Act 1998, which allows child support information to be used for the purposes of administering social security benefits. The exception in *sub-paragraph (4)(b)* allows the information to be used in civil and criminal court cases brought under the Child Support Act. For example, if a non-resident parent is served with a liability order, it may be possible to use information covered by this provision to satisfy the court that there is income to meet the liability.