

NATIONAL INSURANCE CONTRIBUTIONS AND STATUTORY PAYMENTS ACT 2004

EXPLANATORY NOTES

BACKGROUND TO THE ACT

Liability for National Insurance contributions

Recovery of primary National Insurance contributions from employees following payments of security-based earnings.

11. Instead of paying by cash an employer may choose to reward an employee by, for instance, giving them “securities” or granting them options to acquire securities (“securities-based earnings”). Broadly speaking, the term “securities” covers shares, company loan stock, Government gilts and a number of specialised financial instruments. It does not cover cash, cheques, leases, insurance or options. Section 420 of ITEPA 2003 (as substituted by Schedule 22 to the Finance Act 2003), which is reproduced at Annex A, defines the term for the purposes of Chapters 1 to 5 of Part 7 of that Act.

Current position

12. Securities-based earnings paid by an employer are earnings for National Insurance purposes and are therefore subject to Class 1 contributions. The employer is liable for secondary Class 1 contributions and the employee is liable for primary Class 1 contributions. The employer is liable to account for and pay those primary contributions to the Inland Revenue and may recover them through deductions from the employee's "cash" earnings. There are no "cash" earnings for the employer to deduct the employee's primary contributions liability on the securities based earnings from. Therefore they initially have to make the payment of primary contributions to the Inland Revenue on behalf of the employee. Up to 2002/3 there was rarely any primary contribution liability to pay. This was because earnings above the Upper Earnings Limit (UEL) £30,420 were not liable to primary contributions. Most employees who receive security-based remuneration earned above the UEL and the employer did not have to pay primary contributions on their behalf. From 2003/4 onwards there is a 1% primary Class 1 contribution charge above the UEL. The current limits on recovery from the employee may result in the employer being left unable to recover the primary contributions from his employee when the employer has paid them on the employee's behalf.

Effect of the measure

13. [Section 1](#) (Great Britain) and section 2 (Northern Ireland) and supporting secondary legislation, will extend the ability of the employer to recover contributions in two ways:
 - the employer, with the written consent of the employee, will be able to retain, or require the employee to sell, an amount of securities equal to their contribution liability; and

These notes refer to the National Insurance Contributions and Statutory Payments Act 2004 (c.3) which received Royal Assent on 13 May 2004

- the employer, with the written consent of the employee, will be able to retain, or require the employee to sell, an amount of securities equal to their National Insurance contribution liability in the year that the employee ceased working for the employer and the following year.

Agreements and joint elections - employment-related securities

14. [Section 3](#) (Great Britain) and section 4 (Northern Ireland) amend Schedule 1 to the Social Security Contributions and Benefits Act 1992 (CBA 1992) and Schedule 1 to the Social Security Contributions and Benefits (Northern Ireland) Act 1992 (CB(NI)A 1992) to widen the scope of joint National Insurance contributions elections and agreements.

Current position

15. Currently, employers can ask their employees to fund the employer's contribution liability arising when an employee exercises an employment-related option to acquire securities, either through a "joint National Insurance contributions election" or a "joint National Insurance contributions agreement". Using a National Insurance contributions election legally transfers the secondary liability to the employee. It thus removes the need for the employer to provide for the unpredictable secondary liability for contributions in their accounts, when the amount of the employer's contribution liability is contingent on the gain from options on exercise. Under a National Insurance contributions agreement, the liability remains that of the employer and must, therefore, be reflected in the company's accounts. The employee simply reimburses the cost of the liability to the employer.

Effect of the measure

16. Employers who award restricted and convertible securities also face a similar problem in respect of accounting for the unpredictable "post-acquisition" secondary contribution liability on these awards. The term "post-acquisition" relates to a chargeable event following the employee taking ownership of restricted or convertible securities. Typically, a charge to income tax and National Insurance contributions will occur when a restriction applying to the security is lifted or the security is converted into another more valuable form of security. For example, where an employee is awarded shares without any voting or dividend rights for the first two years following the award, the restriction will reduce the value of the shares. When the restriction is lifted at the end of the two year period the shares will increase in value with the benefit of the voting and benefit rights returned. The changes at sections 3 and 4 will allow an employer to ask the employee to fund the employer's (secondary) National Insurance contributions liability on post-acquisition earnings derived from restricted and convertible securities.

Administration of National Insurance contributions and Statutory Sick

Pay and Statutory Maternity Pay

Aligning the periods of notice required for distraint action in England and Wales and application for summary warrant in Scotland to recover contribution debt and aligning distraint procedures in Northern Ireland with those which apply in England and Wales

17. The measures at sections 5 and 6 apply to the 3% of contributions which are currently not collected with tax and to which separate processes apply. The purpose of the changes is to allow the Inland Revenue to align the collection and administration of the contributions, so far as is practicable, with the collection of tax in order to allow the Department to deal with a person's tax and National Insurance affairs in one transaction. The contributions in questions are mainly Class 2 contributions paid on a monthly

or quarterly basis by the self-employed. However, misalignments with tax provisions also arise in relation to Class 1A contributions (paid by employers on certain benefits received by their employees) and some Class 4 contributions.

Recovery of unpaid contributions by distraint in England and Wales

Current position

18. Distraint involves taking possession of a debtor's goods and, if the debtor fails to pay the sum owed in the time allowed, removing them and putting them up for sale by public auction.
19. Where National Insurance contributions are collected with tax, paragraph 6 of Schedule 1 to the CBA 1992 provides for them to be paid, accounted for and recovered in a similar manner to tax. Thus, where both National Insurance contributions and tax are unpaid, the debt can be recovered in a single distraint action governed by tax legislation.
20. However, where, for example, a self-employed person has failed to pay both Class 2 contributions and tax, distraint on the contributions debt is governed by section 121A of the Social Security Administration Act 1992 (SSAA 1992) in England and Wales whereas distraint on the tax debt is governed by section 61 of the Taxes Management Act 1970 (TMA 1970).
21. The provisions of section 121A of the SSAA 1992 require a debtor to be given a 30 day period of notice of distraint action whereas, under tax legislation, there is no such requirement. This requirement pre-dates the transfer of responsibility for contribution matters from the then Department of Social Security to the Inland Revenue. The 30 day period was originally intended to reflect the period allowed for making an appeal against an adverse decision. However, the standard debt collection procedures in the Inland Revenue provide for a series of stages where the debt can be challenged and, if necessary, appealed against before the issue of a notice of distraint.
22. Although there is no statutory requirement in tax legislation to provide notice of distraint, in line with accepted good practice and the Government's proposals for effective enforcement of debt recovery, the Inland Revenue's guidance specifies that debtors should be given a 7 day period of notice of distraint action.

Effect of the measure

23. [Section 5\(1\)](#) provides for the period of notice of distraint action in respect of National Insurance contributions to be aligned with that which is given in respect of tax debts. This will enable both tax and contribution debts to be recovered in a single action and as a result debtors will not face separate actions for recovery and the attendant duplication of costs.
24. However, the Government has no intention of disturbing the current provisions at section 117A of the SSAA 1992 whereby, in cases where a person has appealed a decision on liability for contributions, no action to recover the debt is taken until the appeal has been decided.

Recovery of unpaid contributions by summary warrant in Scotland

Current position

25. From 30 December 2002, the Debt Arrangement and Attachment (Scotland) Act 2002 (DAA(S)A 2002) replaced the diligence of poinding and warrant sales (the Scottish equivalent of distraint) with a new diligence of attachment.

26. Section 121B of the SSAA 1992 provides, following the granting of a summary warrant by the sheriff, for recovery of unpaid National Insurance contributions, which are not collected with tax, by:
- an attachment;
 - an earnings arrestment; or
 - an arrestment and action of furthcoming or sale.
27. In a similar vein to section 121A of the SSAA 1992 in relation to England and Wales, in Scotland section 121B of that Act requires that a 30 day period of notice must have elapsed before a summary warrant can be sought from the sheriff. The recovery of tax debt in Scotland is governed by section 63 of the TMA 1970 which stipulates a minimum period of 14 days which must have elapsed before a summary warrant may be sought. As a result, a similar misalignment to that described in relation to England and Wales at paragraphs 21 and 22 also occurs in Scotland.
28. The DAA(S)A 2002 does not impose a statutory period of notice to attachment. However, amongst the safeguards introduced by that Act is a requirement to provide the debtor with a “debt advice and information package”. This takes the form of a booklet “Dealing with Debt: finding your feet” which is published by the Scottish Executive. The booklet stipulates that the debtor has 14 days to pay following a “charge for payment”. In the absence of a charge to pay in summary warrant cases, the creditor is required to provide the debtor with a debt advice and information pack.

Effect of the measure

29. [Section 5\(2\)](#) provides for the period of notice specified at section 121B to be reduced to 14 days – this is in keeping with the spirit of the DAA(S)A 2002 and will, as in England and Wales, enable both tax and contribution debts to be recovered in a single action.

Recovery of unpaid contributions by distraint in Northern Ireland

Current position

30. The Inland Revenue does not have the same rights to use distraint to recover unpaid contributions in Northern Ireland as it does in England and Wales.
31. Section 115A(1) of the Social Security Administration (Northern Ireland) Act 1992 (SSA(NI)A 1992) provides that the Judgments Enforcement (Northern Ireland) Order 1981 applies:
- where a person is served with a certificate under section 112(1) of that Act; and
 - he neglects or refuses to pay contributions, interest or penalty to which the certificate relates within 30 days.

The amount unpaid is then enforceable as a money judgment by the Enforcement of Judgments Office on an application to it by the Inland Revenue.

Effect of the measure

32. [Section 6\(1\)](#) provides for authorised officers of the Inland Revenue to take distraint action in their own right in Northern Ireland and for the powers they can call upon to levy distraint to be consistent with those which apply in England and Wales.

Powers to combine recovery of contributions with tax

Current position

33. National Insurance matters are outside the scope of Finance Acts. Para 6 of Schedule 1 to the CBA 1992 provides for the provisions of the Income Tax Acts or PAYE regulations to have effect in respect of administration of various contributions. This provision obviates the need to amend primary legislation relating to National Insurance contributions to reflect changes to tax legislation made through the Finance Act.
34. There is no equivalent provision in relation to contributions which are not collected with tax (in particular Class 1A and Class 2). As a result, misalignment with the tax system can arise until such time as space is found in the Government's legislative programme for change to the relevant contributions legislation.

Effect of the measure

35. [Section 5\(4\)](#) (Great Britain) and section 6(3) (Northern Ireland) provide a power for the Inland Revenue to make regulations to apply the provisions of tax legislation to the recovery of unpaid National Insurance contributions which are not collected with tax.

Aligning the powers of Inland Revenue officers to gather information for tax and contributions purposes

Current position

36. Inland Revenue powers to obtain information in relation to contributions are governed by section 110ZA of the SSAA 1992. Section 110ZA was inserted by the ToFA 1999 and was derived from the provisions of section 110 as they previously applied to the then Department of Social Security in relation to contributions. The officers' powers in relation to tax are governed by section 20 of the TMA 1970.
37. The powers in relation to contributions are significantly different to those which apply in relation to tax and include the ability to:
 - enter premises without a warrant;
 - question anybody found on the premises; and
 - compel the provision of information and documents without first issuing a notice subject to third party scrutiny. (Requests for information for tax purposes under section 20 of the TMA 1970 are normally subject to third party scrutiny).

Effect of the measure

38. [Section 7](#) (Great Britain) and section 8 (Northern Ireland) provide for the provisions of section 20, 20B and 20BB of the TMA 1970 to apply to National Insurance contributions.
39. Section 20 of the TMA 1970 allows the Inland Revenue to obtain information about a person's tax affairs. It applies to other aspects of the Inland Revenue's business, for example, Tax Credits.
40. The application of section 20 to National Insurance contributions will allow the Inland Revenue to ask any contributor (including secondary contributors) to provide documents and information about their liability for National Insurance contributions. The Inland Revenue can also ask third parties to provide documents that they have which are relevant to the contributions liability of another.
41. Information and documents are provided in response to formal notices. The consent of a Tax Appeal Commissioner is needed before such a notice can be issued.

Aligning the powers of Inland Revenue officers to inspect records for SSP and SMP purposes

Current position

42. Inland Revenue officers' powers in relation to SSP and SMP are governed by section 110ZA of the SSAA 1992 in Great Britain and section 104ZA of the SSA(NI)A 1992 in Northern Ireland. The officers' powers in relation to tax are governed by regulation 55 of the Income Tax (Employments) Regulations 1993 ([S.I. 1993 No. 744](#))¹
43. The powers in relation to SSP and SMP are significantly different to those which apply in relation to tax and include the ability to:
- enter premises without a warrant;
 - question anybody found on the premises; and
 - compel the provision of information and documents (without first subjecting that request to third party scrutiny).

Effect of the measure

44. [Section 9](#) (Great Britain) and section 10 (Northern Ireland) replace the provisions of section 110ZA of the SSAA 1992 and section 104ZA of the SSA(NI)A 1992 in relation to SSP and SMP with regulation making powers to allow for regulations equivalent to the tax regulations to be made for SSP and SMP purposes.

Aligning the compliance regime for SSP and SMP with that which applies to tax and the other statutory payments

Current position

45. Employers' failures to meet their obligations under the SSP and SMP schemes are currently dealt with by a series of minor criminal offences under section 113 of the SSAA 1992 which are punishable by a fine not exceeding level 3 on the standard scale – currently £1,000. Equivalent failures in relation to tax, statutory paternity pay and statutory adoption pay are dealt with by civil penalties up to a maximum of £3,000.
46. As a result an employer's failure in relation to SSP and SMP can result in him receiving a criminal record whereas an identical failure in relation to another statutory payment does not.

Effect of the measure

47. [Section 9](#) (Great Britain) and section 10 (Northern Ireland) provide that, as is the case with statutory paternity pay and statutory adoption pay, employers' failures to meet their obligations under the SSP and SMP schemes are subject to civil penalties which reflect those applicable under the TMA 1970.

¹ As amended by: regulation 6 of the Income Tax (Employments) (Amendment No 2) Regulations 1995 ([SI 1995 No. 447](#)); regulation 19 of the Income Tax (Employments) (Amendment) Regulations 1998 ([SI 1998 No. 2484](#)) and regulations 7 and 21 of the Income Tax (Electronic Communications) (Miscellaneous Amendments) Regulations 2001 ([SI 2001 No. 1081](#)).