

**EXPLANATORY MEMORANDUM TO
THE SOCIAL SECURITY (CONTRIBUTIONS) (AMENDMENT No.3)
REGULATIONS 2008**

2008 No. 636

- 1.** This Explanatory Memorandum has been prepared by HM Revenue and Customs and is laid before Parliament by Command of Her Majesty. This memorandum contains information for the Select Committee on Statutory Instruments.

- 2. Description**
 - 2.1 These Regulations amend the Social Security (Contributions) Regulations 2001 (SI 2001/1004).

 - 2.2 Paragraphs 15, 16 and 17, of Schedule 4 of the Regulations are amended to enable HM Revenue & Customs (HMRC) to specify, certify, charge interest on and enforce a single amount of employer current year debt which includes an unspecified sum of earnings-related contributions without having to separately identify those contributions.

 - 2.3 There remains a requirement for HMRC to specify a single amount of employer debt having regard to an employer's previous payments. But, in arriving at the specified single amount, HMRC will only need to have regard to the total of an employer's monthly payments as opposed to the earnings-related contributions element.

 - 2.4 The amended paragraphs are only relevant to the extent that an employer has not paid their monthly earnings-related contributions on time.

 - 2.5 Paragraphs 22 and 31 of Schedule 4 of the Regulations are amended to reflect that the penalty regime which now applies to incorrect returns in respect of National Insurance contributions (NICs) is now Schedule 24 to the Finance Act 2007 ("Schedule 24"). Schedule 24 introduced a single new penalty regime for incorrect documents (mainly returns) for income tax, corporation tax, pay as you earn (PAYE) and value added tax. It also provided for penalties where a taxpayer fails to report an under-assessment by HMRC where a taxpayer has failed to submit a return. Schedule 24 repeals the existing penalty regimes for these taxes, including section 98A(4) of the Taxes Management Act 1970.

 - 2.6 The effect of these Regulations is that the provisions of Schedule 24 apply to Class 1 and Class 1A NIC exactly as they do for PAYE and for Class 4 NIC exactly as they do for income tax.

 - 2.7 By Order under section 97 of Finance Act 2007, the provisions of Schedule 24 are being brought into force so that, for all the taxes specified, the new penalty regime will apply for:
 - return periods commencing on or after 1 April 2008 where;

- the due date for filing the return is on or after 1 April 2009.

It also provides that the existing penalty regimes for each tax will be preserved for prior periods.

2.8 A minor drafting amendment to regulation 67 of S.I. 2001/1004 which introduces Schedule 4 has also been made.

3. Matters of Special Interest to the Select Committee on Statutory Instruments

3.1 The amendments to Paragraphs 15, 16 and 17 of Schedule 4 are related to amendments being made to the Income Tax (Pay As You Earn) Regulations 2003-SI 2003/2682 by the Income Tax (Pay As You Earn) (Amendment) Regulations 2008. Additionally, amendments are being made to the Income Tax (Construction Industry Scheme) Regulations 2005-SI 2005/2045 by the Income Tax (Construction Industry Scheme) (Amendment) Regulations 2008. These Instruments ensure that a single amount of employer debt might comprise Income Tax, National Insurance contributions and Construction Industry Scheme deductions.

3.2 The Department for Innovation, Universities and Skills will in due course make mirroring changes to the Education(Student Loans)(Repayments) Regulations 2000 which provide for employers to account to HMRC for deductions made in respect repayments of student loans.

4. Legislative Background

4.1. The provisions contained in Schedule 4 of the Social Security (Contributions) Regulations 2001 are made under paragraphs 6 and 7 of Schedule 1 to the Social Security Contributions and Benefits Act 1992 and paragraphs 6 and 7 of Schedule 1 to the Social Security Contributions and Benefits (Northern Ireland) Act 1992 and are derived from the Income Tax Acts and the Income Tax (Pay As You Earn) Regulations 2003.

4.2 Paragraphs 15, 16 and 17 in Schedule 4, which broadly mirror PAYE Regulations, are applicable where an employer fails to pay earnings-related contributions, due monthly, on time. The existing paragraphs enable HMRC to specify, certify, charge interest on and enforce an amount of current-year earnings-related contributions having regard to previous payments of such contributions.

4.3 The existing Paragraph 16 also enables proceedings to be brought for recovery of earnings-related contributions and tax without the need to distinguish between the constituent sums.

4.4 Section 97 of Finance Act 2007 introduced Schedule 24, which provides for penalties to be charged on taxpayers who make errors in documents they send to HM Revenue and Customs (HMRC). In addition it provided for

penalties to be imposed where taxpayers fail to take reasonable steps to report errors in assessments made by HMRC where a taxpayer had failed to submit a return.

4.5 This creates a single penalty framework for inaccurate documents and under-assessments, for a number of different taxes, where there were previously different ones. The penalty is determined by the amount of tax understated, the nature of the behaviour giving rise to the understatement and the extent of disclosure by the taxpayer. Appeal rights are also set out as well as repeals of the current penalty provisions.

4.6 The taxes covered by the Schedule are income tax, capital gains tax, corporation tax, value added tax, pay as you earn, deductions under the construction industry scheme and (by means of these Regulations) national insurance contributions.

4.7 There will be no penalty where a taxpayer makes a mistake; penalties of 30% of tax lost for failures to take reasonable care; 70% of tax lost for deliberate action, and 100% of tax lost for deliberate and concealed action.

4.8 Penalties can be substantially reduced to recognise taxpayer disclosure, more so if this is unprompted. “Disclosure” is defined in the law as telling HMRC of the error, helping correct it and giving access for HMRC to check. The Schedule introduces a new concept of suspended penalties. It also deals with how penalties will apply in a number of particular circumstances – including groups of companies, overstated losses and failures by agents.

4.7 The legislation was introduced to provide a period at least 20 months between Royal Assent, and the first penalty being chargeable under the new regime. This was to ensure that people know the consequences of an inaccuracy in a return (in terms of penalties) before the commencement of that return period. It allows for the first penalties to apply across the taxes at broadly the same time, enabling a programme of work to be undertaken to prepare HMRC staff, taxpayers and agents for the new penalty regime. This includes the publication of detailed technical guidance, communication and training.

5. Extent

5.1 This Instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

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

7. Policy Background

7.1 HMRC has concluded that requiring employers to provide an itemised payslip with their monthly remittances of earnings-related contributions and tax (which may also include Construction Industry Scheme deductions and payments of student loan repayments), is an unnecessary burden. Sums remitted during the current tax year are only reconciled to the constituent components of contributions, tax, etc at the end of the year on receipt of employers' annual returns. In terms of current year monthly remittances, the focus needs simply to be on the total sum due.

7.2 These amendments ensure that where a single amount is returned on a payslip (without a breakdown of the constituent parts) HMRC will be able to specify, certify and enforce a single total amount of current year debt. The need for this change was raised in HMRC's January 2008 consultation document: *Modernising Powers, Deterrents and Safeguards: Payments, Repayments and Debt*. This is available on the HMRC website.

7.3 The HMRC Review of Powers, Deterrents and Safeguards began in 2005, following the merger of the Inland Revenue and HM Customs and Excise, to provide a framework of law and practice for HMRC that supports the Government's objectives of a tax system that is fair and better adapted to the needs of customers. The penalties measures in Finance Act 2007 were one of the first legislative outputs of the Review.

7.4 The underlying theme of the review is to support those who seek to comply while coming down hard on those seeking an unfair advantage by not complying. The behaviourally based penalty regime supports this approach. Aligning penalties across taxes enables clearer deterrent messages and facilitates cross-tax compliance checks.

7.5 Draft legislation was published with a consultation document: *Modernising Powers, Deterrents and Safeguards: Penalties for Incorrect Returns* on 19 December 2006. The consultation ran until 13 March 2007 and a Summary of Responses was published in March 2007. Both documents are available on the HMRC website.

8. Impact

8.1. An Impact Assessment has not been prepared as no additional impact arises from these Regulations.

8.2 A Regulatory Impact Assessment entitled HMRC and the Taxpayer: *Modernising Powers, Deterrents and Safeguards: Penalties for Incorrect Returns: Finance Bill 2007* was signed on 19 March 2007 and is available on the HMRC website.

9. Contact

9.1 Robin Wythes at HM Revenue and Customs, Tel: 0207 147 2511 or e-mail: robin.wythes@hmrc.gsi.gov.uk can answer questions regarding changes to Paragraphs 15, 16 and 17 of Schedule 4,

9.2 Rachel Button at HM Revenue and Customs, Tel: 0207 147 2341 or e-mail: rachel.p.button@hmrc.gsi.gov.uk can answer any queries regarding changes to Paragraphs 22 and 31 of Schedule 4.