

**EXPLANATORY MEMORANDUM TO**  
**THE INCOME TAX (PAY AS YOU EARN) (AMENDMENT) REGULATIONS 2018**  
**2018 No. 267**

**1. Introduction**

1.1 This explanatory memorandum has been prepared by Her Majesty's 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 amends the Income Tax (Pay As You Earn) Regulations 2003 (S.I. 2003/2682) (the "PAYE Regulations") which make provision for the assessment, charge, collection and recovery of income tax under the PAYE system. The changes have effect from 6th April 2018.

*Scottish rates of income tax*

2.2 Regulations 2 to 6 make consequential amendments to the PAYE Regulations following the rate resolutions made by the Scottish Parliament on 20 February 2018 under section 80C of the Scotland Act 1998. The resolutions set new bands and rates of income tax for the tax year 2018-19 for Scottish taxpayers, in particular setting a new "starter" rate which is lower than the Scottish basic rate ("SBR") and an "intermediate" rate which is between the SBR and the Scottish higher rate.

*PAYE Settlement agreements*

2.3 Regulations 7 to 16 amend Part 6 of the PAYE Regulations which deal with PAYE settlement agreements ("PSAs"). The amendments extend the duration of PSAs by removing the need for annual renewal. Instead, a PSA will continue to have effect for each subsequent tax year until varied or cancelled, either by the employer, or HMRC. Further changes will allow PSA applications to be processed electronically without the need for agreement with an officer of HMRC, if and when digital processes are introduced.

2.4 The changes have effect in relation to PSAs for the 2018/19 tax year and subsequent tax years.

*State Pension Lump Sums*

2.5 Regulations 17 to 19 amend the provisions in Chapter 2A in Part 7 of the PAYE Regulations which deal with the deduction of tax by the Department for Work and Pensions (DWP) upon paying social security pension lump sums. In the case of Scottish taxpayers, with the agreement of the Scottish Government, these amendments allow DWP to deduct tax from lump sums at rates which apply in the rest of the United Kingdom. Any tax overpaid or underpaid as a result of this treatment will be dealt with by HMRC when they reconcile the individual's tax position after the end of the relevant tax year.

### *Apprenticeship Levy*

- 2.6 Regulations 21 to 23 correct minor, non-reportable errors that relate to the PAYE Regulations Part 7A Apprenticeship Levy as highlighted by the Select Committee on Statutory Instruments in a memorandum issued to HMRC on 25 April 2017.

## **3. Matters of special interest to Parliament**

### *Matters of special interest to the Select Committee on Statutory Instruments*

- 3.1 None.

### *Other matters of interest to the House of Commons*

- 3.2 As this instrument is subject to negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

## **4. Legislative Context**

### *Scottish Rate of Income Tax*

- 4.1 The Scotland Act 2016 provides the Scottish Parliament with the power to set all income tax rates and bands (except the personal allowance, which remains reserved) that will apply to Scottish taxpayers' non-savings, non-dividend income.
- 4.2 Consequential changes to the PAYE Regulations are required to implement new rates of Scottish Income Tax which will come into force for the tax year 2018/19.

### *PAYE Settlement agreements*

- 4.3 Section 6 of the Finance (No.2) Act 2017 amended sections 703 and 704 in Chapter 5 of Part 11, Income Tax (Earnings and Pensions Act) 2003 (ITEPA), removing the need for PSAs to be agreed with an officer of HMRC.
- 4.4 Further changes are required to Part 6 of the PAYE Regulations to implement the new process for entering into a PSA.
- 4.5 Part 6 relates to the making, the form and effect of PSAs.

### *The Apprenticeship Levy*

- 4.6 None, Changes are to correct minor, non-substantial errors.

## **5. Extent and Territorial Application**

- 5.1 The extent of this instrument is the United Kingdom.
- 5.2 The territorial application of this instrument is 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**

### *What is being done and why*

#### *PAYE Settlement agreements*

- 7.1 PSAs are arrangements under which employers can, in a single payment, settle their employees' income tax liabilities for certain benefits and expenses. The government aims to reduce the administrative burden on employers of operating PSAs in their current form.
- 7.2 The amendments to the PAYE Regulations will simplify the PSA process. They make provision for a PSA to be an 'enduring' agreement. This agreement will continue to remain in place for subsequent tax years unless varied or withdrawn by the employer or cancelled by HMRC. This simplification removes the need for an ongoing annual agreement for employers who have a PSA in place for the 2017/18 tax year or who enter into a new PSA with 2018/19 being the first year to which the agreement relates.

#### *Scottish Rate of Income Tax*

- 7.3 The Scotland Act 2016 provides the Scottish Parliament with power to set the rates and band thresholds that will apply to all non-savings non-dividend income tax paid by Scottish taxpayers. The Scottish Parliament set the rates and band thresholds (excluding the personal allowance) for tax year 2018/19 on the 20 February 2018 .
- 7.4 This instrument makes changes to the PAYE Regulations, providing for the new Scottish rates and band thresholds.
- 7.5 Where the DWP pays a social security pension lump sum, they are currently required to deduct tax either at the marginal rate notified by the recipient of the lump sum or at the basic rate, if no rate is notified. From 6 April 2018 the DWP will continue to deduct tax from all lump sums at the UK basic or higher rate. All recipients of a lump sum (including Scottish taxpayers) will be invited to nominate either the UK basic rate or the UK higher rate, or state that they will not be liable to tax. HMRC will calculate whether the correct tax has been paid at the end of the tax year as part of the reconciliation it undertakes, ensuring that individuals pay the correct amount of tax and will demand any tax due or repay any overpayment, as appropriate.
- 7.6 The payment of lump sums only applies to those who reached state pension age before 6 April 2016. Given the small and finite numbers affected, after consultation between DWP, HMRC and Scottish Government it was not considered cost effective to the taxpayer to make changes to IT systems which would allow for state pension lump sums to be taxed by DWP at the Scottish marginal rate.

#### *The Apprenticeship Levy*

- 7.7 The opportunity is being taken to correct 3 minor drafting errors as highlighted by the Select Committee on Statutory Instruments, which relate to the Apprenticeship Levy contained in Part 7A of the PAYE regulations. These amendments have no substantial effect.

#### *Consolidation*

- 7.8 There are currently no plans to consolidate the PAYE Regulations.

## **8. Consultation Outcome**

### *PAYE settlement agreements*

- 8.1 To be completed post-consultation.

### *Scottish Rate of Income Tax*

- 8.2 No consultation has been carried out on the provisions of this instrument.

### *The Apprenticeship Levy*

- 8.3 The draft regulations for the Apprenticeship Levy were consulted on from 14 December 2016 to 3 February 2017. As a result, published guidance was updated and minor amendments made to Part 7A of the PAYE regulations which came into effect from 6 April 2017

## **9. Guidance**

- 9.1 Extensive guidance concerning the operation of PAYE has been published on both the HMRC and Gov.uk websites, viewable by both employers and individuals. This will be updated to reflect these changes.
- 9.2 Apprenticeship Levy guidance is provided on GOV.UK.

## **10. Impact**

### *PAYE Settlement agreements*

- 10.1 The amendments will offer employers the opportunity to reduce their administrative burdens when entering into PSAs. There is no impact on charities or voluntary bodies.
- 10.2 There is no impact on the public sector. The simplified process will give rise to operational savings for HMRC of £235 - £285k.

### *Scottish Rate of Income Tax*

- 10.3 This change impacts on all employers employing Scottish taxpayers as their payroll systems will need to be able to deal with Scottish bands and rates regardless of where the employer is based.
- 10.4 An Impact Assessment covering this instrument was published on 28 May 2015 alongside the draft clauses and explanatory notes for the Scotland Bill and is available on the Parliament website at <http://www.parliament.uk/documents/impact-assessments/IA15-004.pdf>. It remains an accurate summary of the impacts that apply to this instrument.

### *The Apprenticeship Levy*

- 10.5 The [Tax Information and Impact Note](#) for the Apprenticeship Levy was published on 4 February 2016 alongside the draft clauses and explanatory notes for the Finance Bill 2016 and is available on the website at <https://www.gov.uk/government/publications/apprenticeship-levy>. It remains an accurate summary of the impacts that apply to this instrument.

## **11. Regulating small business**

### *PAYE Settlement agreements, Scottish Rate of Income Tax*

- 11.1 The legislation applies to activities that are undertaken by all employers.
- 11.2 No specific action is required to minimise regulatory burdens on small businesses. As regards PSAs, although the amendments made by the instrument apply to all businesses, they serve to reduce administrative burdens such that specific action in relation to small businesses was not required.

### *The Apprenticeship Levy*

- 11.3 There is no impact to small business, as the regulations are simply correcting 3 minor drafting errors, which have no substantial effect.

## **12. Monitoring & review**

- 12.1 The effectiveness of the processes set out in PAYE legislation will be subject to internal review by HMRC at regular intervals.
- 12.2 HMRC monitors the operation and administration of the Apprenticeship Levy through continued communication with employers and external stakeholder groups.

## **13. Contact**

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