



Low Incomes  
Tax Reform  
Group  
A voice for the unrepresented

**Simplifying the PAYE Settlement Agreement (PSA) process  
HM Revenue & Customs (HMRC) consultation document  
Response from the Low Incomes Tax Reform Group (LITRG)**

**1 Executive summary**

- 1.1 We welcome the opportunity to comment on HMRC proposals to simplify the PSA process. We do so as tax specialists with particular interest and expertise in the tax and related welfare problems of the smallest of employers and the lowest paid of employees.
- 1.2 We have previously contributed to the Office of Tax Simplification (OTS) review of employee benefits and expenses and responded to HMRC's consultation on an exemption for trivial benefits as well as its draft legislation and guidance on the same matter.<sup>1</sup>
- 1.3 We support the overall aim of the new system to save time and money for employers and HMRC alike, however we have a number of reservations regarding the effects of the proposed changes. In some ways the proposals are likely to increase employer burdens, for example from a timing perspective, given the move of the tax payment deadline from 19 October to 19 July – which is also the Class 1A National Insurance payment deadline.
- 1.4 The proposals will also arguably push even more onus towards employers, as they will have to decide for themselves what benefits can be included within a PSA. It is essential that employers will

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<sup>1</sup> The relevant submissions can be found on the LITRG website:

<http://www.litrg.org.uk/latest-news/submissions/140909-employee-benefits-and-expenses-%E2%80%93-four-consultation-documents>

<http://www.litrg.org.uk/latest-news/submissions/150202-draft-finance-bill-2015-%E2%80%93-employee-expenses-and-benefits>

<http://www.litrg.org.uk/latest-news/submissions/150901-draft-legislation-review-employee-benefits-and-expenses>

<http://www.litrg.org.uk/latest-news/submissions/160125-draft-finance-bill-2016-%E2%80%93-exemption-income-tax-trivial-benefits>

<http://www.litrg.org.uk/latest-news/submissions/160322-tax-exemption-trivial-benefits-kind-%E2%80%93-draft-guidance>

still be able to contact HMRC for assurance (or reassurance) that they are dealing with the PSA correctly.

- 1.5 With regards to moving to digital, there should be an alternative paper process where it is not reasonably practicable for the employer to file online. While we note that employers that are currently exempt from completing digital RTI returns would not be required to complete the digital PSA return, as it stands, from April 2017 the RTI exemption will only apply to those with religious objections to using the internet or disabled or elderly people who employ care workers in their home. This will leave many other employers facing a daunting (if not impossible) task. We therefore suggest that HMRC widen the RTI exemptions – especially if they are going to be drawn on in the rollout of other employer digital systems.
- 1.6 Finally, we are concerned that the removal of ‘minor’ as a category of items that can be covered by a PSA in order to simplify things for employers, will be at the cost of employees – who as a result may face a tax/National Insurance contribution (NIC) charge that previously would not have arisen. For the lowest paid, the receipt of an ‘official’ benefit in kind (BIK) may also have a knock on effect on their tax credits. This is unlikely to go down well with either employees or indeed employers – who will probably want their employees to enjoy what has been given to them without the worry of how it will affect their finances. It is therefore crucial that HMRC fully explore the potential impact of the proposed change before making it.

## **2 Who we are**

- 2.1 The LITRG is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HMRC and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT’s primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

## **3 General comments**

- 3.1 We support the overall aim of the new system to save time and money for employers and HMRC alike. However, we have a number of reservations regarding the effects the proposed administrative

‘simplifications’ might have on small and micro employers, for example care and support employers.<sup>2</sup>

- 3.2 As a representative body for low paid workers we are also concerned that while removing the ‘minor’ category of items that can be covered by a PSA may provide employers with greater clarity about what can and cannot be included in a PSA, it could also leave more employees facing a BIK tax charge on items that neither they nor their employers view as BIKs.
- 3.3 We feel we can make the best contribution by concentrating on the questions around these two issues, meaning that we have not answered all of the questions posed in the consultation document.

## 4 Questions

### 4.1 ***Do you agree that removing the requirement to agree the items in a PSA will provide simplification for employers? Please give your reasons.***

- 4.1.1 For some employers confident in what they are doing, removing the requirement to agree the items in a PSA upfront will be beneficial. However, we cannot agree that this will provide simplification for *all* employers. Some new or ‘accidental employers’ for example, will be nervous of ‘self-assessing’ whether items are eligible for inclusion in a PSA return by referring to the legislative rules and guidance alone.
- 4.1.2 For this new system to work for them, HMRC will need to build significantly on the PSA information currently available within GOV.UK<sup>3</sup> – ensuring they provide plenty of examples of what can and cannot be included. While we accept it may be difficult or impossible to provide comprehensive lists of items that may or may not be included in PSAs, we think it would be helpful to provide a list of items that could never be included in a PSA – as long as that carried a clear note that the list was not supposed to imply that all other items *could* be included.
- 4.1.3 In reality, we think it is crucial that they can also receive specific guidance from HMRC, whether by telephone or webchat, as we go on to explain.

### 4.2 ***ii) Are there reasons why the formal agreement element of a PSA should be retained? If so, what changes should the government consider to an agreement based system so that it is easier to administer***

- 4.2.1 So that employers can feel a sense of certainty and support under the new regime, we think that, for those that want it, it is vital to retain a means of dialogue around what can be included in a PSA. This may not constitute a formal agreement as such, but would nevertheless be helpful to employers to prevent situations where they ‘take a view’ and get things wrong by including a benefit on a PSA, or on the contrary are unduly cautious and leave a benefit out when in fact it would be allowed.

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<sup>2</sup> i.e. those that have taken on a personal assistant (carer) to help them live independently and thus become responsible for complying with administrative requirements associated with being an employer

<sup>3</sup> <https://www.gov.uk/payee-settlement-agreements/overview>

4.2.2 An alternative could be to retain a formal approval system for items to include in a PSA when it is first used i.e. for new employers or those using it for the first time. Then if most PSAs stay the same year on year this would reduce the contact with HMRC but still give certainty. Perhaps if there is then any change to PSA items there could be a process to approve the variation if employer wanted to do so.

**4.3 *iii) Do you agree that having a digital PSA return would be simpler for employers to administer rather than the current PSA1 paper return? Please provide your reasons.***

4.3.1 Whilst we recognise that a shift to digital channels can save some employers time and money, a significant number will be without digital access and/or capabilities. This is only one of the reasons that, in general, we do not agree with the mandation of online systems. (Another, of course if that if the system is good enough, then people will naturally migrate to it – this approach has proved successful in relation to the self-assessment tax return where ever-increasing numbers now choose to file online.)

4.3.2 We note the intention is to exempt certain categories of employers from the requirement to file digital PSA returns, based on those who are currently exempted from completing digital RTI returns. This sounds sensible. However in reality, on HMRC's current thinking,<sup>4</sup> this will only apply to practicing members of religious societies or orders whose beliefs are incompatible with the use of electronic methods of communication and certain people who employ someone providing care or support services at or from their home – two very narrow groups of people.

4.3.3 In our view, HMRC really need to create a permanent 'general' exemption for those who have significant difficulty in using an online channel or who are unable to use an online channel – particularly if the RTI exemptions are going to be drawn on in the rollout of additional employer digital services (please note that such an exemption exists for contractors in the Construction Industry Scheme).<sup>5</sup>

4.3.4 If HMRC needed further persuading, we would urge them to consider the case of *LH Bishop Electrical Co Ltd & Others v HMRC Commissioners* [2013] UKFTT 522 (TC) in which three appellants, supported by the LITRG, won their appeal against an HMRC requirement that they file their VAT returns online. The judge held that the HMRC regulations, which required mandatory filing of VAT returns online, were in breach of those appellants' human rights and were unlawful under the EU law as there were no exemptions for older people, those with disabilities or those who lived in parts of the country which were not well served for internet access.

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<sup>4</sup> The exemption that currently applies to people such as those with a disability which prevents them from using computers, those who cannot access an internet connection, including 'dial up', and those who are elderly and are unable to use an online channel, is set to be disbanded from April 2017.

<sup>5</sup> Per the The Income Tax (Construction Industry Scheme) (Amendment) Regulations, SI 2016/348) from April 2016 a contractor must file monthly returns online unless the contractor's religious beliefs preclude the use of electronic communications; or *HMRC has agreed that it would be impractical (based on, for example, age or ill health).*

**4.4 *iv) A digital return would reduce error rates. Are there other changes the government should consider to reduce these further?***

4.4.1 If HMRC have been seeing arithmetical errors in paper PSA returns to date (which they hope will be solved through digitalisation), then we would suggest that those that remain on a paper process will require better guidance on completing the form and calculating the amount of tax/NIC payable, with step-by-step instructions and worked examples, etc. – in order to avoid making the same errors.

4.4.2 Also, the consultation document notes at 3.5 that one of the common errors is using the incorrect tax rate: we cannot see that this is going to be solved by digitalisation, so perhaps HMRC could clarify this.

**4.5 *v) Would aligning the PSA payment date with the Class 1A NICs payment deadline cause any employers particular hardship? Please provide your reasons.***

4.5.1 We do think that aligning the PSA calculation and payment dates with the P11D/P11D(B) deadlines is a simplification, however we trust that there will be appropriate communications well in advance about the changes to ensure that all employers, particularly those on limited budgets, or who are already overwhelmed with compliance matters at that time of year, are aware of them and can try and adapt, as required.

4.5.2 With regards to the shortened payment date, and in case of innocent oversights in meeting it, we would expect to see a ‘soft landing’ approach to penalties for late payment for at least the first year and also a sympathetic approach to short term time to pay arrangements if requested.<sup>6</sup>

**4.6 *vi) Do you agree that this approach would be proportionate?***

4.6.1 We support the proposal to provide employers with a warning rather than a penalty if they have included an item in a PSA in good faith, which HMRC determine should not have been included. In such instances, we trust that we will not see any automatic computer generated penalties which the taxpayer needs to appeal against in order that they may be cancelled.

**4.7 *vii) Do you have any other comments about the proposed new PSA process?***

4.7.1 We are unsure as to when these proposed changes would take effect. We assume that they are intended to come into effect for April 2017. However we would suggest that employers have had a lot of changes to deal with recently, for example, auto-enrolment and changes to the benefits and expenses regime, the cumulative effect of which is essentially administrative ‘overload’, so suggest that April 2018 may be a more appropriate date.

4.7.2 This would also ensure enough time to publicise properly – it is getting very late in the day in terms of getting clear information out to employers about a change that will come in in six months’ time.

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<sup>6</sup> Otherwise, employers could find themselves paying penalties – for example 5% of the unpaid Class 1B NIC due if the payment is more than 30 days late (FA2009, Sch56, Para3) which would be an unfortunate consequence of the simplification.

**4.8 *viii) In light of the new trivial BiKs exemption, would the removal of ‘minor’ pose any problems for employers? Please provide reasons for your answer and examples of BiKs which this would cause difficulty for.***

4.8.1 The word ‘minor’ is open to interpretation and therefore rubs slightly with the stated aim of making the PSA process clear and easy for employers to administer. In this regard then, we acknowledge removing the category ‘minor’ would seem to be a solution to this.

4.8.2 However the new trivial BiKs exemption does not completely fill the gap that is then left by removal of ‘minor’ – remembering that per HMRC’s Statement of Practice 5/96,<sup>7</sup> minor does not necessarily just mean low monetary value (as stated in the consultation document) but should be given its natural meaning (per the Oxford English dictionary: ‘lesser in importance, seriousness, or significance’).

4.8.3 Under the new rules, a trivial benefit will qualify for the exemption if it meets four conditions:

1. the cost of providing the benefit does not exceed £50 (or the average cost per employee if a benefit is provided to a group of employees and it is impracticable to work out the exact cost per person)
2. the benefit is not cash or a cash voucher
3. the employee is not entitled to the benefit as part of any contractual obligation (including under salary sacrifice arrangements)
4. the benefit is not provided in recognition of particular services performed by the employee as part of their employment duties (or in anticipation of such services).

4.8.4 With this in mind, it is worth now looking at the list given in HMRC’s PSA manual<sup>8</sup> of what may constitute a minor item:

- incentive awards
- reimbursement of late night taxi fares outside s248 ITEPA 2003
- personal incidental expenses in excess of the statutory daily limit
- present for an employee in hospital
- staff entertainment, for example a ticket for Wimbledon
- use of a pool car where the conditions for tax exemption are not satisfied
- subscriptions to gyms, sports clubs etc.
- telephone bills

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<sup>7</sup> <https://www.gov.uk/government/publications/statement-of-practice-5-1996>

<sup>8</sup> <https://www.gov.uk/hmrc-internal-manuals/payee-settlement-agreements/psa1060>

- gift vouchers and small gifts.

4.8.5 HMRC will see that not all these ‘minor’ benefits will be covered by the trivial benefits exemption – for example, an incentive award will not satisfy the requirement that it is not provided in recognition of particular services performed by the employee.

4.8.6 Furthermore, even for those that are currently covered, if the £50 limit is not kept up-to-date,<sup>9</sup> the trivial benefits exemption will become less useful. This could see employers wanting to revert to PSAs to stop their kind gesture backfiring and penalising their employee who may end up with an unexpected tax bill as a result.

4.8.7 As such, we think having flexibility over items that can be included in a PSA will be more valuable to employers than the small simplification suggested. In any case, we think that with clear, easy to understand, user-friendly information and guidance on ‘minor’, employers would be able to correctly identify the appropriate items pretty comfortably.

**4.9 *ix) Are there items which you include in your current PSA which are ‘minor’ and which are not either ‘irregular’ or ‘impracticable’ as well?***

4.9.1 We are not an employer and do not have a current PSA, however from our research we cannot agree that most ‘minor’ PSA items also tend to fall into the irregular or impracticable categories, particularly given the proposed refinement of the ‘irregular’ condition to exclude items that are received on a regular pattern (every day, week, month, other month, or quarter) and those that are contractual.

4.9.2 For example, looking at the list given in the paragraph above – which HMRC will be aware, is not an exhaustive list – depending on the circumstances in which the benefits were paid/provided, there would appear to be potential ‘regularity’ difficulties with nearly all of them.

4.9.3 With no way for an employer to assume the responsibility for a ‘minor’ benefit through a PSA, the likely outcome is that employees will foot the bill, leaving them shocked and confused. (Please note that while employers could put a ‘grossed up’ payment through the payroll to reimburse the employee for the cost that they have suffered, as suggested in the consultation document, this will likely be beyond the comprehension/capability of most employers we are concerned with.)

4.9.4 This seems particularly unfair and even discriminatory, to those receiving a ‘minor’ benefit who would have to pay the tax themselves whereas someone receiving a more expensive benefit would pay no tax on it.

4.9.5 Receiving a benefit which is reported by the employer through ordinary P11D channels, could also then have a knock on effect on the employee’s state benefits. This may not be a significant issue for universal credit (UC) as generally benefits are ignored when calculating income, however HMRC will be aware that UC roll-out is still very slow, meaning that tax credits will be around for some time yet. The BIK rules for tax credits are complex – depending on the nature of the benefit, they could be

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<sup>9</sup> The legislation allows for the limit to be updated in the future however the government have not committed to regular reviews.

counted as income for tax credits.<sup>10</sup> This could see many more low paid employees not only having to undertake a cumbersome analysis of their P11D's in order to complete their tax credits applications correctly but potentially also receiving a lower level of financial support via tax credits as a consequence.

- 4.9.6 In summary we would like to say, that while it is one thing not to widen the scope of PSAs in line with the OTS's recommendations, it is another altogether to make them less generous. The proposal to remove the ability to include 'minor' items in a PSA is likely to frustrate employers, not to mention hit the pocket of their employees – and therefore requires further consideration.

LITRG

14 October 2016

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<sup>10</sup> We explain the rules fully here: <http://revenuebenefits.org.uk/tax-credits/guidance/how-do-tax-credits-work/what-is-income/employment-income/>