

## ***COMPLIANCE COST REVIEW***

Regulatory Impact Assessment considering the Mandatory Electronic Payment for Large Employers provisions

### **1. Introduction**

#### **1.1 Background**

In line with Government commitments to reduce the compliance burdens that are placed on businesses, HM Revenue & Customs (HMRC) assesses the likely change in compliance costs whenever a policy is introduced or changed. The results of that analysis are published in a final Regulatory Impact Assessment (RIA) when the associated legislation is laid before Parliament.

This document summarises the outcome of a post-implementation review of the final RIA that was published in September 2003 for the above-mentioned measure by HMRC. The measure was implemented with effect from April 2004. A copy of the published final RIA is attached.

This review re-assesses the compliance cost analysis published in the original RIA and addresses two main questions:

- whether the estimates of compliance costs used in the RIA were correct, with hindsight; and
- whether the processes used to estimate compliance costs were appropriate and reasonable, given the circumstances at the time.

HMRC intend to use this review to improve the Impact Assessment process, and also to assist in future policy development and evaluation work in general. As such, the emphasis is on identifying learning points for future assessment of compliance costs. The review does not revisit the original policy decision.

### **2. The published RIA**

#### **2.1 Description of the policy change**

The proposal was to require electronic payment of PAYE from employers with 250 or more employees. The aim was to ensure prompt and secure payment from approximately 10,000 large employers. At the same time, Inland Revenue introduced a later due date for electronic payments made by all employers. The aim was to provide a cash-flow advantage to employers to replace the lost cash-

flow advantage from cheque payment. It was also hoped that this would encourage smaller employers to adopt electronic payment voluntarily.

The RIA also suggested that some large employers might upgrade their internal procedures to be sure of avoiding the new surcharges for late payment, and that there might be costs for employers in discussing reasonable excuse claims with Inland Revenue staff.

## **2.2 Anticipated compliance costs or savings**

### **Savings to Employers**

The RIA stated that the costs of making an electronic payment compared with a cheque payment would depend on the employer's banking arrangements and how they implemented electronic payment. Research from BACS quoted in the RIA suggested that each direct payment costs at least £1 less than a cheque, and the saving may be higher depending on the functionality of the software.

The RIA predicted a cash-flow benefit of around £5m for employers as a result of the later due date.

### **Costs to Employers**

The RIA suggested that there would be a small transitional cost for large employers that currently paid by cheque, representing the cost of changing their internal procedures and arranging for their bank to make electronic payments.

## **3. Conduct of the review**

Each compliance cost review is conducted individually, and the review process is adapted to suit the particular circumstances applying in each case. The emphasis is on making sure that the review itself - and any burden of consultation - is sufficient to meet the objectives of the review, but proportionate to the likely benefits.

In this case, the review was led by an HMRC project team supported by consultants. The staff in the review team were completely independent of those involved with the original policy change.

An essential element of the review was consultation with those actually affected, and consultants were commissioned to carry out a small number of targeted in-depth interviews with some of those affected and their trade bodies. The research was not intended to deliver any degree of statistical robustness (to do so would have been costly and impractical) but instead to provide indicative findings. Reflecting the limited impact of the measure, a small number of businesses and trade bodies were interviewed. Coupled with the consultants'

own knowledge and expertise, this has allowed the research to identify the major issues and any associated learning points.

The external research was complemented by an internal review of HMRC paperwork and electronic files.

#### 4. Were the original estimates of compliance costs accurate?

This section addresses two main aspects – the nature of the change in compliance costs (i.e. what did people have to do differently) and the monetary impact of that change (what did it cost or save them).

<b>Question</b>	<b>Comments</b>
<p><i>Were the specific types of cost and benefit identified in the RIA (e.g. reading legislation, filling in forms, updating IT systems, saving time etc.) incurred?</i></p>	<p>The RIA did not go into detail on the specific one-off compliance costs for large employers (e.g. updating systems, retraining staff, and advisers' fees in ascertaining the effect of the changes.)</p> <p>Respondents noted that when the electronic payment was first implemented there was a small amount of training time, but that this time was recovered in later months as the procedure was found to be quicker than the old process.</p> <p>No additional professional advice was required in this matter as it was a very straightforward procedure. Any queries were dealt with in communication with HMRC.</p> <p>No additional upgrades of hardware or software were required after implementation. Software already in use within the business dealt with the payment without any difficulty.</p> <p>On the cash-flow benefit from holding the tax for an additional three days, some employers did find that the additional three days led to a saving either on overdraft charges or greater interest received. The larger employers were most affected by this. Money held on deposit was placed on slightly longer terms, which some respondents highlighted as an advantage, but this was considered to make an insignificant difference in reference to the employers' overall</p>

	activities.
<i>Were costs/savings incurred at the expected time?</i>	<p>The RIA indicated that there were potentially significant savings in relation to moving the payment date to the 22<sup>nd</sup> of each month. The majority of respondents did not take advantage of the extra time available. Those who did were generally the very large employers who found the benefit to be significant. Those who benefited did so at the anticipated time.</p> <p>Only minor costs were experienced at the time of implementation.</p>
<i>Were costs/savings incurred by the expected people?</i>	Costs and savings were incurred by large employers as anticipated in the RIA.
<i>Were any other costs/savings, not identified in the RIA, incurred?</i>	No.
<i>If the type of costs/savings varied from the original estimates, why was that?</i>	It was perhaps surprising that all the respondents did not take advantage of the later payment date, however this was stated as being because the associated saving was negligible compared to the overall activities of the employers.
<i>Could such variances have been foreseen at the time?</i>	No.
<i>What is the assessment now of the total value of costs and savings?</i>	There have been no additional costs incurred other than time costs on the initial set up, which was quickly recovered in later months. The electronic process is generally considered to be quicker (and therefore cheaper) however the anticipated savings relating to later payment dates has in many cases not been experienced as the later payment date is not (yet) being used.
<i>If different from the original RIA, what has caused the discrepancies?</i>	The RIA may have overstated the likely take up of the later payment date. This would not necessarily have been predictable.
<i>With hindsight, were the compliance cost estimates accurate?</i>	There was very little cost involved. The initial time spent when first switching to the electronic payment was quickly recovered in later months. We feel that the view that there would be little impact was accurate.

**5. Was the process used to estimate compliance costs reasonable?**

Irrespective of whether the analysis turned out to be correct, the review has considered whether the original analysis was completed in a reasonable way.

<b>Question</b>	<b>Comments</b>
<i>Who worked on the original RIA?</i>	Members of the Policy Team, the Better Regulation Unit and the department's analysts worked on the RIA.
<i>Was an adequate audit trail maintained?</i>	A full audit trail does not appear to have been maintained. However, systems have improved since this RIA was done and the learning points have been addressed to a large extent.
<i>Was Cabinet Office and/or internal HMRC guidance on RIAs followed correctly?</i>	Yes – no problems have been identified.
<i>How much effort was devoted to compliance cost estimation, and was that effort proportionate in the context of the policy measure?</i>	The effort devoted to compliance costs was proportionate, and focused on what was believed to be the largest impact, the cash-flow benefit.
<i>Were the right people (both internal and external) consulted, and were their views reflected appropriately?</i>	Yes. A partial impact assessment was published in April 2003 and draft regulations were published for a 12 week consultation. Comments received were dealt with in the final regulations. As a result of the consultation, quarterly payments were excluded from the requirement to pay electronically.
<i>Did those who were consulted when the RIA was written express views on the reasonableness of the process?</i>	No problems have been identified in this respect.
<i>Have those who have been consulted now as part of this compliance cost review expressed views on the reasonableness of the process?</i>	No comments were made.
<i>Were compliance costs estimated for all options mentioned in the RIA?</i>	Options were presented in the RIA, but only evaluated in broad qualitative terms. Compliance costs and savings were only considered for the chosen option.
<i>Were compliance costs estimated separately for key groups (such as small businesses, large businesses,</i>	The measure affected large employers in general and there is no reason to believe that more discreet groups should have been

<i>self-employed)?</i>	considered
<i>Was an appropriate analytical approach used, with economists or other analysts consulted appropriately?</i>	Yes. Advice from Knowledge, Analysis and Intelligence Division was sought on the likely cash-flow impact.
<i>Was there sufficient time to produce a robust assessment of compliance costs?</i>	Time was not a problem.
<i>Were any assumptions reasonable, given the circumstances at the time?</i>	Respondents generally agreed that the assumptions made were reasonable. There is evidence that a proportion of large businesses had already implemented electronic payment before the change became compulsory. This reflects the willingness to change and the relatively low cost.
<i>Were any estimates of compliance costs caveated appropriately?</i>	The RIA included caveats such as “may increase” and “may make” in referring to potential savings/costs. Respondents generally considered these caveats to be appropriate in the circumstances.
<i>Were any risks correctly identified, addressed and explained?</i>	No risks for the policy proposal were identified in the RIA, however this appears to have been appropriate based on the views of the respondents. In retrospect the measure was very low impact as predicted.
<i>Were any disagreements identified and reflected appropriately (e.g. if the figures were disputed by businesses, or if more than one set of figures was available)?</i>	Not applicable.
<i>Would HMRC do anything differently if the exercise was repeated, and hence could the RIA process have been improved?</i>	No evidence has been identified to suggest that a change in process is required.

## 6. Learning points arising from the review

- Impact assessments need to consider that a business will not always change established business practices just because of a tax change. In

this case the likelihood of change appears to depend on the significance of the saving to the individual business.

## **7. The way forward**

Comments are invited on any aspect of this report or the wider compliance cost review programme.

The learning points are being fed into the policy development process directly if particular to one RIA or policy area. More generic recommendations are being collated across the review programme overall, and will be used to create an action plan for HMRC to take forward to improve the RIA process and development.

## **8. Contact points for further information**

For issues relating to mandatory electronic payment specifically:

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For issues relating to the compliance cost review programme generally:

Richard Bowyer  
3E/14, 100 Parliament Street  
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If you have a query about your own affairs in this tax area, please contact the HMRC helpline number on 08457 143 143.

**ANNEX : THE PUBLISHED REGULATORY IMPACT ASSESSMENT**

<http://www.hmrc.gov.uk/ria/large-employers.pdf>