

## ***COMPLIANCE COST REVIEW***

### **PAYMENTS BY EMPLOYERS TOWARDS THE INCIDENTAL COSTS OF HOMEWORKING**

#### **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. Where a consultation document is published during the analysis period, it is accompanied by a partial RIA.

This document summarises the outcome of a post-implementation review of the final RIA that was published in March 2003 for the above-mentioned measure by the Inland Revenue. The measure was implemented with effect from April 2003. 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 RIA 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**

This measure aimed to support the Government's policy of helping employers promote the benefits of flexible working. The measure also aligned the tax treatment of employer-paid homeworking expenses with the National Insurance Contributions (NICs) treatment.

Prior to the change, when an employer paid an employee for additional household costs incurred as a result of working from home, the employee was taxed on this payment.

After the change, employers were able to pay employees for such costs without this payment being taxed. Such payments could already be made without the employer having to pay NICs.

The amount employers are allowed to pay without question under the new scheme is £2 per week (£104 per year). There is no need for the employer to notify HMRC that such payments are being made.

If an employer pays more than that amount, the exemption is still available if the employer provides HMRC with supporting evidence that the payment is wholly in respect of additional household expenses incurred by the employee as a result of carrying out work duties at home.

Prior to the change, employers could obtain dispensations from their local tax offices but only in relation to employees who, because of the nature of their duties, had to work from home, rather than for employees who chose to work from home, perhaps on a flexible basis. The new scheme therefore applied to a different type of homeworking employee.

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

The RIA believed that the new scheme would lower compliance costs for employers and employees. This was because employees and employers who wished to work from home would no longer need to keep records of, or return details of, reimbursed homeworking expenses.

The RIA estimated that these recurring compliance cost savings would be modest at first, i.e. below £3m, but that they would increase over time as the population of people working from home rises.

The RIA did not consider the change in compliance costs relating to employees whose homeworking costs exceed £2 per week.

The RIA did not provide information on the number of firms or employees likely to benefit from the new scheme, nor how those numbers would change in future.

The RIA believed that there would be minor one-off compliance costs associated with understanding the nature of the new scheme, but these would be negligible.

### **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 - are 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.

Evidence relating to the accuracy of the compliance analysis in the RIA, to its appropriateness and reasonableness in the circumstances, and to how improvements might be made in the future, were obtained from a small group of interviewees, selected to ensure a diverse range of opinion. The selection process took the following factors into consideration; (i) range of industries covered; (ii) size of organisations both in turnover and employee numbers; and (iii) mix between trade bodies, representative organisations and actual businesses.

This evidence was complemented by an independent internal examination and review of HMRC's paperwork and electronic files, and a detailed interview of those responsible for this policy area and for producing the original RIA. This considered, amongst other issues, HMRC's decision-making processes and analysis of compliance costs.

### **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>
Were the specific types of cost and benefit identified in the RIA actually incurred? (e.g. reading legislation, filling in forms, updating IT systems,	<i>Yes, on the whole. Under the new measure employers are not required by HMRC to keep records of their employees' expenditure. Some</i>

<p>saving time etc.)</p>	<p><i>employers may have chosen to retain their own in-house record keeping requirements, for their own internal purposes. Business take-up of the new allowance is not monitored and it is unclear how many employers are aware of it, and hence to what extent the one-off implementation costs relating to familiarisation have been incurred. Some evidence indicates that some employers may be unaware of the allowance.</i></p>
<p>Were costs/savings incurred at the expected time?</p>	<p><i>Yes, to the extent that the allowance was taken up.</i></p>
<p>Were costs/savings incurred by the expected people?</p>	<p><i>Yes, to the extent that the allowance was taken up.</i></p>
<p>Were any other costs/savings, not identified in the RIA, incurred ?</p>	<p><i>The measure does not require firms with an existing dispensation to renegotiate that dispensation. We are aware of one instance where the introduction of the new allowance triggered a firm to reopen an existing dispensation. This firm chose to instruct agents for this purpose, at some cost. We believe that this reaction was not widespread. It may have been exceptional.</i></p> <p><i>The RIA did not explicitly consider the following costs, although their size is unlikely to be major:</i></p> <ul style="list-style-type: none"> <li><i>• costs to business of working out whether it would be worth making use of the new allowance, i.e. identifying and surveying homeworkers and their level of incidental costs.</i></li> <li><i>• costs to business of establishing and operating systems to enable employees to apply for homeworking payments.</i></li> </ul>
<p>If the type of costs/savings varied from the original estimates, why was</p>	<p><i>Variance related to the following issues:</i></p>

that?	<ul style="list-style-type: none"> <li>• <i>employers' motivation to consider whether to make use of the new allowance, and the practical implications of actually making use of it.</i></li> <li>• <i>awareness of the new allowance.</i></li> </ul>
Could such variances have been foreseen at the time?	<i>The RIA could possibly have provided more analysis of the likely uptake of the new allowance.</i>
What is the assessment now of the total value of costs and savings?	<i>One-off familiarisation costs seem to have been negligible in aggregate, as identified by the RIA, partly because awareness and take-up of the allowance appears to be low. The size of one-off costs to business of establishing systems to apply the new allowance is unclear, although these would appear to be low. Ongoing compliance cost savings seem to have been modest and below £3m per year, as suggested by the RIA. There is little indication at this stage that take-up will rise significantly in future.</i>
If different from the original RIA, what has caused the discrepancies?	<i>Discrepancies relate largely to lower growth in take-up than implied by the RIA.</i>
With hindsight, were the compliance cost estimates accurate?	<i>Overall the RIA was broadly accurate in its assessment of compliance costs. The total anticipated cost savings were modest and less than £3m per year, as suggested by the RIA.</i>

## 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.

Question	Comments
Who worked on the original RIA?	<i>Members of the policy team, HMRC Better Regulation Unit and HMRC</i>

	<i>analysis team.</i>
Was an adequate audit trail maintained?	Yes.
Was Cabinet Office and/or internal HMRC guidance on RIAs followed correctly?	Yes.
How much effort was devoted to compliance cost estimation, and was that effort proportionate in the context of the policy measure?	<i>The amount of effort devoted was not disproportionate to the scale of compliance costs involved. .</i>
Were the right people (both internal and external) consulted, and were their views reflected appropriately?	<i>Consultation was somewhat limited, for legitimate wider compliance reasons. The views of consultees were reflected.</i>
Did those who were consulted when the RIA was written express views on the reasonableness of the process?	<i>Those consulted at the time did not express views about the reasonableness of the RIA process.</i>
Have those who have been consulted now as part of this compliance cost review expressed views on the reasonableness of the process?	<i>Those consulted as part of this exercise believed that the consultation process with business should have been more expansive. With this RIA, HMRC chose to adopt a limited consultation exercise for legitimate wider compliance reasons.</i>
Were compliance costs estimated for all options mentioned in the RIA?	<i>No, only for the lead option which emerged from the consultation process.</i>
Were compliance costs estimated separately for key groups (such as small businesses, large businesses, self-employed)?	<i>No breakdown was provided amongst different sizes or types of business, nor were per business costs published.</i>
Was an appropriate analytical approach used, with economists or other analysts consulted appropriately?	<i>Yes, Departmental analysts and economists were involved. Given the circumstances of this RIA, their approach to this RIA was not inappropriate.</i>
Was there sufficient time to produce a robust assessment of compliance costs?	<i>A limited consultation exercise and tight timeframe reduced the scope for robust assessment, but this was necessary for legitimate wider compliance reasons.</i>

<p>Were any assumptions reasonable, given the circumstances at the time?</p>	<p><i>It was reasonable for the RIA to assume that employees with costs under £2 would no longer need to keep records of their expenditure, although some businesses seem to have retained this as an internal requirement for their own purposes. In the time available assumptions about take-up were not unreasonable.</i></p>
<p>Were any estimates of compliance costs caveated appropriately?</p>	<p><i>Partly. Presentationally the RIA probably should have given the impression that costs and savings were somewhat uncertain. Phrases used such as 'will lower compliance costs', 'will be negligible' and 'will increase' perhaps gave too strong an impression of certainty.</i></p>
<p>Were any risks correctly identified, addressed and explained?</p>	<p><i>The RIA did not identify key risks.</i></p>
<p>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)?</p>	<p><i>No disagreements were identified in relation to the compliance cost analysis.</i></p>
<p>Would HMRC do anything differently if the exercise were repeated, and hence could the RIA process have been improved?</p>	<p><i>The somewhat limited consultation exercise was proportionate in the circumstances of this measure, and would probably be repeated in similar circumstances. The overall assessment of compliance costs was broadly accurate. Although with hindsight some of the analysis could have been developed further in places, this was basically a small measure and the overall level of effort was proportionate. Presentationally, the RIA might have given less of an impression of certainty.</i></p>

## **6. Learning points arising from the review**

### **6.1 Learning points for future work in this policy area**

- The incentives facing business to adopt the new allowance should be considered, including the in-house business costs of establishing and operating new schemes to administer the allowance.
- The population of employers and employees affected should be considered, including any growth trends in homeworking and any changes in awareness and take-up levels.

### **6.2 Learning points for the RIA and compliance cost process in general**

- The need to complete an RIA when the costs and benefits are small should be considered carefully.
- Where schemes or allowances are voluntary, analysis should consider the circumstances and conditions driving business take-up.
- RIAs should make greater use of caveats in the presentation of analysis where the consultation period is short and/or where few have been consulted.
- Analysis should consider carefully whether business will, for their own internal purposes, retain or introduce an administrative requirement, e.g. record keeping, when HMRC regulations do not require this explicitly.
- The derivation of cost figures should be explained, and per business costs should be provided where possible.
- Key risks should be identified where possible, including their likelihood of arising and their impact on costs and benefits.

## **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 homework specifically:

Bill Streeter HMRC 100 Parliament Street London SW1A 2BQ

Telephone: 020-7147-2486

E-mail: [bill.streeter@hmrc.gsi.gov.uk](mailto:bill.streeter@hmrc.gsi.gov.uk)

For issues relating to the compliance cost review programme generally:

Richard Bowyer HMRC 100 Parliament Street London SW1A 2BQ

Telephone: 020-7147-0062

Email: [richard.bowyer@hmrc.gsi.gov.uk](mailto:richard.bowyer@hmrc.gsi.gov.uk)

If you have a query about your own affairs in this tax area, please contact the HMRC helpline number on 08457 143 143.

## **THE PUBLISHED REGULATORY IMPACT ASSESSMENT**

[Payments by Employers towards the initial costs of Homeworking \(PDF 87K\)](#)