

Non-cash benefits during Statutory Maternity Leave and Statutory Adoption Leave Tax and NICs consequences

This guidance has been prepared in response to requests from employers following the publication by HM Revenue and Customs [HMRC] of earlier guidance on “*Statutory maternity leave – salary sacrifice and non-cash benefits*”. This was published in May 2008 and can be found at <http://www.hmrc.gov.uk/employers/sml-salary-sacrifice.pdf>

Background

Employers often provide contractual non-cash benefits to employees. Following legislation in 2008 they must provide those benefits not just during Ordinary Maternity / Adoption Leave but also during Additional Maternity / Adoption Leave.

Non-cash benefits are described in the guidance above as follows:

The term “contractual non-cash benefits” used in this document refers to all the terms and conditions of employment other than those relating to remuneration. Remuneration means sums payable to an employee by way of wages or salary.

The variety of non-cash benefits can be considerable. Their treatment for tax and National Insurance Contributions [NICs] purposes varies – they can be subject to tax under PAYE or under the P11D (Expenses and Benefits) procedure; they can be subject to NICs under Class 1, Class 1A or Class 1B. Indeed some can be exempt from tax or NICs, in whole or in part.

Non-cash benefits include:

- a) company cars, mobile phones, living accommodation or other assets provided to the employee for non-business use, without ownership being transferred to the employee;
- b) medical / dental / critical illness / travel / car insurance provided under company insurance policies; employer-provided health checks;
- c) non-cash vouchers, such as childcare vouchers which can only be used by the employee for qualifying childcare and are not transferable.

Issues

Employers required to provide non-cash benefits as above have identified two issues needing additional guidance:

1. The tax and NICs consequences and recording and reporting obligations when non-cash benefits chargeable to Class 1 NICs are provided but the employee has no cash earnings.
2. Whether tax refunds can be made to employees who are receiving non-cash benefits but no cash earnings.

1. Tax and NICs consequences of non-cash benefits

1.1 *The normal situation when there are cash earnings*

When employees receive cash wages and salaries and non-cash benefits the tax and NICs obligations are as follows:

- Tax is deducted from cash earnings through the PAYE system.
- The taxable element of non-cash benefits is reported to HMRC by the employer on form P11D or P9D after the end of the tax year. Any tax due is collected either through the Self Assessment system or the PAYE system.
- Primary Class 1 NICs (the employee's) are deducted from cash earnings.
- Secondary Class 1 NICs (the employer's) are due from the employer in respect of the employee's cash earnings.
- Class 1A NICs are due on many non-cash benefits. These are reported by the employer in July after the end of the tax year using form P11D or P9D and form P11D(b). The employer pays Class 1A NICs. The employee is not liable for Class 1A NICs.

Some non-cash benefits, however, are subject to Class 1 NICs. In such cases the value of the benefit must be added to any other earnings paid in the same earnings period as the benefit was provided, and both primary and secondary Class 1 NICs should be calculated and paid to HMRC. The employer can deduct primary Class 1 NICs from the employee's earnings. Vouchers are a common example. The tax rules require vouchers to be reported by the employer on form P11D or P9D after the end of the tax year. The NICs rules require that:

- primary and secondary Class 1 NICs are accounted for in the pay period when the vouchers are provided,
- NICs are paid to HMRC,
- the NICs and the earnings, which include the vouchers, are recorded in-year on P11 (or equivalent) and reported at the end of the year on P14.

1.2 *The rare situation when there are non-cash benefits chargeable to Class 1 NICs but no cash earnings for the same earnings period*

This situation can arise when employees on Statutory Maternity Leave [SML] or Statutory Adoption Leave [SAL] are provided with non-cash benefits which are chargeable to Class 1 NICs, but are not entitled (or no longer entitled) to contractual maternity / adoption pay, or Statutory Maternity Pay / Statutory Adoption Pay, or indeed any other cash earnings from that employment for that same earnings period. This is most likely to happen in the later stages of SML or SAL.

In this situation any primary Class 1 NICs due on the non-cash benefits cannot be deducted, as normal, from cash wages or salary. However, the NICs must still be paid to HMRC by the employer, and the benefits along with the NICs must be recorded in-year on P11 or equivalent, and reported at the end of the year on P14.

There are three things to note:

i. Rarity

The circumstances in which the employer is required to account for primary Class 1 NICs on non-cash benefits will be rare:

(a) Most non-cash benefits are liable to Class 1A NICs, not Class 1. (Note - Class 1A, which is due from the employer, only arises if the employee is earning at a rate of £8,500 or more per year. Employees on SML or SAL may well earn less than this.)

(b) Class 1 NICs is only due if the employee's total earnings, including benefits, from that employment in that earnings period exceed the Primary Threshold (£110 per week for 2009/10). For example, an employee receiving vouchers of £100 per week would only be charged Class 1 NICs if other earnings exceeded £10.

(c) Approved childcare vouchers are exempt from tax and NICs up to £55 per week or £243 per month. So, an employee receiving just childcare vouchers would only be charged Class 1 NICs if the vouchers were greater than £165 per week (childcare vouchers exempt up to £55 per week; plus Primary Threshold £110 per week).

ii. Recovery

The employer cannot immediately recover the cost of the primary Class 1 NICs by deducting it from any cash earnings of the employee for the same earnings period. However -

(a) If the employee receives cash earnings later in the same tax year, the employer can recover unrecovered primary NICs by deduction from the later cash earnings.¹ There is a limit to what can be recovered this way.² The additional deduction to recover the cost of the primary NICs for the earlier period cannot exceed the amount of primary NICs due on the later earnings for the same tax year. In effect the total primary NICs deductions in respect of those later earnings must not be more than double the amount of primary NICs that would normally be payable on those earnings in the absence of any recovery.

(b) If the employee receives no further cash earnings later in the same tax year upon which Class 1 NICs are due (or if those cash earnings are insufficient), then the employer is unable to recover the full cost of the primary NICs for the earlier period. In this case the employer is not permitted to recover any unrecovered primary NICs from the employee's cash earnings in any future year.

Please note:

In some exceptional circumstances (for example, when there is an under-deduction of Class 1 by reason of an error made by the employer in good faith³) the employer can deduct unrecovered primary Class 1 NICs from later earnings in the following tax year. However, this does not apply to unrecovered NICs described at (b)

¹ Social Security (Contributions) Regulations 2001 Schedule 4 paragraph 7(6) and 7(8)

² Social Security (Contributions) Regulations 2001 Schedule 4 paragraph 5

³ Social Security (Contributions) Regulations 2001 Schedule 4 paragraph 7(3)

above, which do not arise from any error made by the employer, but from the absence or insufficiency of cash earnings in the same earnings period.

iii. Pecuniary liability

The payment of primary Class 1 NICs by the employer in these circumstances does not amount to the meeting of a pecuniary liability of the employee, nor does it amount to the provision of a benefit. So the fact that the primary NICs have been paid by the employer but not deducted from cash earnings of the employee does not create a fresh charge to tax or NICs for the employee, either as earnings or as a benefit. (However, when the employer pays the primary NICs on the non-cash benefits they must still record the benefits and the NICs on P11 (or equivalent) and report them at the end of the year on P14.)

2. Can tax refunds be made to employees who are receiving non-cash benefits but no cash earnings?

2.1 Employees who are on a cumulative tax code may be entitled to refunds of income tax when they are on SML or SAL, and receiving non-cash benefits but no cash pay. This is most likely to happen in the later stages of SML or SAL.

2.2 There are specific provisions for this sort of “unpaid leave” scenario.⁴ An employer must repay any income tax due to an employee who is on a cumulative tax code and is on “unpaid leave” – if the employee, or authorised representative, has requested it. In effect the employer must operate PAYE on the normal pay day as if a payment of nil had been made, therefore generating a tax repayment.

2.3 There are two things to note:

- i. This rule applies whether or not the employee with no cash pay is in receipt of non-cash benefits.
- ii. The employee is not entitled to the repayment if absent due to involvement in a pay dispute.⁵

Potential misunderstandings

In addition to the two topics covered above, HMRC has become aware of the following misunderstandings:

Misunderstanding 1: an employee on SML or SAL is not actually working for the employer and is, therefore, not liable to tax or NICs on any non-cash benefits from that employer while doing no work.

Comment: employees on SML or SAL are still liable to tax and NICs under the normal rules on any earnings from their employers. It is not relevant that the employees are not attending work and performing duties. They continue to be employees therefore any earnings and benefits are liable to tax and NICs under

⁴ Regulation 63 Income Tax (Pay As You Earn) Regulations 2003

⁵ Regulation 63(1)(c) and 64 Income Tax (Pay As You Earn) Regulations 2003

the normal rules. For example, Statutory Maternity Pay remains chargeable to tax and NICs even though the woman is not working.

Misunderstanding 2: when an employee receives approved childcare vouchers the chargeable value of that benefit to the employee is the sum of the tax and NICs they saved through the tax and NICs exemption.

Comment: childcare vouchers provided for an employee by an employer are non-cash benefits subject to tax and NICs under the normal rules. The tax and Class 1 NICs charges on childcare vouchers are based on the value of the childcare that can be obtained by using the vouchers. However, the first £55 per week or £243 per month of approved childcare vouchers plus any associated administration costs are exempt from income tax and NICs if the relevant conditions are met. The rules for charge and exemption do not change during maternity or adoption leave. They are the same whether or not salary sacrifice arrangements are in place.