

## Summary: Intervention & Options

<b>Department /Agency:</b> <b>HMT/HMRC</b>	<b>Title:</b> <b>Impact Assessment of Options for the NICs exemption for holiday pay schemes</b>	
<b>Stage:</b> Final proposal	<b>Version:</b>	<b>Date:</b> 5 October 2007
<b>Related Publications:</b>		

### Available to view or download at:

<http://www.hmrc.gov.uk>

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### What is the problem under consideration? Why is government intervention necessary?

- An exemption has existed since at least the 1960s so that where employers in the construction industry pay into a third-party pooled holiday pay scheme, from which employees receive their holiday pay, there is no liability to deduct employer and employee NICs on that payment.
- We have become increasingly aware over the last year that this exemption is now being used by large employers of workers outside the construction industry, putting at risk significant amounts of revenue. Currently we believe that this use is costing the Exchequer around £100-150 million per annum.

### What are the policy objectives and the intended effects?

The exemption was intended for the construction industry (it pre-dates the leave entitlement provisions of the Working Time Regulations) to address issues of high mobility and ensure that employers did not face problems with accounting for NICs in making payments of holiday pay. The exemption was not limited to construction in legislation. The introduction of the Working Time Regulations and the increasing mobility of labour generally makes retention of an exemption increasingly difficult to justify in the face of increasing Exchequer cost.

### What policy options have been considered? Please justify any preferred option.

1. Do nothing - this is not viable because of the Exchequer risk;
2. Limit the exemption indefinitely to the construction sector - this is not viable as construction is no longer the only industry to employ people on a short-term basis and the Working Time Regulations ensure that holiday entitlement is preserved even for short time periods;
3. Remove the exemption for all sectors with immediate effect - this gives long-standing Construction industry schemes no time to adapt;
4. Remove the exemption, but give 5 years transitional relief for construction - the implemented option.

**When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?** A Compliance Cost Review will be undertaken once the policy has been implemented, probably between one and three years after implementation.

### **Ministerial Sign-off** For final proposal/implementation stage Impact Assessments:

***I have read the Impact Assessment and am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impacts of the policy, and (b) the benefits justify the costs.***

**Signed by the responsible Minister:** Jane Kennedy

**Date:** 5 October 2007

## Summary: Analysis & Evidence

Policy Option: 1

Description: Do nothing

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' We estimate that the additional NICs at risk if we do not act to prevent the further use of the exemption outside the Construction industry will be £1.2 billion pa by 2012/13.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£		<b>Total Cost (PV)</b> £
Other <b>key non-monetised costs</b> by 'main affected groups'			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' We estimate that the additional NICs at risk if we do not act to prevent the further use of the exemption outside the Construction industry will be £1.2 billion pa by 2012/13. No effect on admin burdens or wider compliance costs.
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£		<b>Total Benefit (PV)</b> £
Other <b>key non-monetised benefits</b> by 'main affected groups'			

Key Assumptions/Sensitivities/Risks

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £
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What is the geographic coverage of the policy/option?			UK		
On what date will the policy be implemented?			21 days from PBR		
Which organisation(s) will enforce the policy?			HMRC		
What is the total annual cost of enforcement for these organisations?			£		
Does enforcement comply with Hampton principles?			Yes		
Will implementation go beyond minimum EU requirements?			No		
What is the value of the proposed offsetting measure per year?			£		
What is the value of changes in greenhouse gas emissions?			£		
Will the proposal have a significant impact on competition?			No		
Annual cost (£-£) per organisation (excluding one-off)		Micro	Small	Medium	Large
Are any of these organisations exempt?		No	No	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)		
Increase of	£	Decrease of	£	<b>Net Impact</b>	£ nil

Key: Annual costs and benefits: Constant Prices (Net) Present Value

## Summary: Analysis & Evidence

Policy Option: 2

Description: Limit the exemption indefinitely to the construction sector

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' We estimate that the NICs yield effects are about £200m per annum.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£		<b>Total Cost (PV)</b> £
Other <b>key non-monetised costs</b> by 'main affected groups'			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' We estimate that the NICs yield effects are about £200m per annum.  There is no estimate in the HMRC 'standard cost model' of the current admin burden of the exemption, but we estimate that limiting it represents an annual saving to business of £100,000.
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 100,000		<b>Total Benefit (PV)</b> £
Other <b>key non-monetised benefits</b> by 'main affected groups'			

### Key Assumptions/Sensitivities/Risks

This is not viable as the construction industry is no longer the only industry to employ people on a short-term basis and the Working Time Regulations ensures that holiday entitlement is preserved even where individuals are employed for very short periods of time.

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	21 days from PBR			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	£			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	No			
What is the value of the proposed offsetting measure per year?	£			
What is the value of changes in greenhouse gas emissions?	£			
Will the proposal have a significant impact on competition?	No			
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)		
Increase of	£	Decrease of	£	<b>Net Impact</b>	£ Nil

Key: Annual costs and benefits: Constant Prices (Net) Present Value

## Summary: Analysis & Evidence

**Policy Option: 3**

**Description: Remove the exemption for all sectors with immediate effect**

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' We estimate that the NICs yield effects are about £350m per annum.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£		<b>Total Cost (PV)</b> £
Other <b>key non-monetised costs</b> by 'main affected groups'			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' We estimate that the NICs yield effects are about £350m per annum.  There is no estimate in the HMRC 'standard cost model' of the current admin burden of the exemption, but we estimate that removing it represents an annual saving to business of £200,000.
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 200,000		<b>Total Benefit (PV)</b> £
Other <b>key non-monetised benefits</b> by 'main affected groups'			

### Key Assumptions/Sensitivities/Risks

Does not allow for transitional relief in the Construction industry. (see discussion in 'Evidence Base' below).

Price Base Year 0	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £
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What is the geographic coverage of the policy/option?	UK			
On what date will the policy be implemented?	21 days from PBR			
Which organisation(s) will enforce the policy?	HMRC			
What is the total annual cost of enforcement for these organisations?	£			
Does enforcement comply with Hampton principles?	Yes			
Will implementation go beyond minimum EU requirements?	No			
What is the value of the proposed offsetting measure per year?	£			
What is the value of changes in greenhouse gas emissions?	£			
Will the proposal have a significant impact on competition?	No			
Annual cost (£-£) per organisation (excluding one-off)	Micro	Small	Medium	Large
Are any of these organisations exempt?	No	No	N/A	N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)			(Increase - Decrease)		
Increase of	£	Decrease of	£	<b>Net Impact</b>	£ nil

Key: Annual costs and benefits: Constant Prices (Net) Present Value

## Summary: Analysis & Evidence

**Policy Option: 4**

**Description: Remove the exemption, but give 5 years transitional relief for construction - the option being implemented.**

<b>COSTS</b>	<b>ANNUAL COSTS</b>		Description and scale of <b>key monetised costs</b> by 'main affected groups' We estimate that the NICs yield effects are £200m per annum, rising to £350m per annum after the transitional period.
	<b>One-off</b> (Transition)	<b>Yrs</b>	
	£		
	<b>Average Annual Cost</b> (excluding one-off)		
	£		<b>Total Cost (PV)</b> £
Other <b>key non-monetised costs</b> by 'main affected groups'			

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>		Description and scale of <b>key monetised benefits</b> by 'main affected groups' We estimate that the NICs yield effects are £200m p.a., rising to £350m p.a. after the transitional period.  There is no estimate in the HMRC 'standard cost model' of the current admin burden of the exemption, but we estimate that removing it represents an annual saving to business of £200,000 after the transition.
	<b>One-off</b>	<b>Yrs</b>	
	£		
	<b>Average Annual Benefit</b> (excluding one-off)		
	£ 200,000		<b>Total Benefit (PV)</b> £
Other <b>key non-monetised benefits</b> by 'main affected groups'			

Key Assumptions/Sensitivities/Risks

Price Base Year	Time Period Years	<b>Net Benefit Range (NPV)</b> £	<b>NET BENEFIT (NPV Best estimate)</b> £
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What is the geographic coverage of the policy/option?	UK
On what date will the policy be implemented?	21 days from PBR
Which organisation(s) will enforce the policy?	HMRC
What is the total annual cost of enforcement for these organisations?	£
Does enforcement comply with Hampton principles?	Yes
Will implementation go beyond minimum EU requirements?	No
What is the value of the proposed offsetting measure per year?	£
What is the value of changes in greenhouse gas emissions?	£
Will the proposal have a significant impact on competition?	No
Annual cost (£-£) per organisation (excluding one-off)	Micro      Small      Medium      Large
Are any of these organisations exempt?	No      No      N/A      N/A

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)
Increase of £	Decrease of £	<b>Net Impact</b> £ nil

Key: Annual costs and benefits: Constant Prices (Net) Present Value

## Evidence Base (for summary sheets)

[Use this space (with a recommended maximum of 30 pages) to set out the evidence, analysis and detailed narrative from which you have generated your policy options or proposal. Ensure that the information is organised in such a way as to explain clearly the summary information on the preceding pages of this form.]

This Impact Assessment considers 4 options:

1. Do nothing;
2. Limit the exemption indefinitely to the construction sector;
3. Remove the exemption for all sectors with immediate effect;
4. Remove the exemption, but give 5 years transitional relief for construction - the option being implemented.

### Revenue effects

The table below sets out the estimated Exchequer Revenue effect from removing the exemption in the non-Construction sectors.

<b>REVENUE EFFECT Cost (-) / Yield (+) (£M):</b>						
	<b>2007/08</b>	<b>2008/09</b>	<b>2009/10</b>	<b>2010/11</b>	<b>2011/12</b>	<b>2012/13</b>
Yield	+100	+200	+200	+200	+200	+200
Revenue protected	+100	+250	+450	+700	+950	+1200

In addition, the estimated Exchequer Revenue effect from the Construction sector is £150million per annum.

### Admin burdens effects

We estimate that removing the exemption represents an annual saving to business of £200,000. This is based on the following assumptions:

- Approximately 300,000 employees affected in the non-construction sectors.
- Approximately 400,000 employees affected in the Construction sector.
- Admin time-saving of 1 minute per affected employee per annum.
- Wage rate of relevant administrative staff is £18 per hour.

There is no estimate in the HMRC 'Standard Cost Model' of the current admin burden of the NICs exemption for holiday pay schemes and as a result, this estimate is subject to wide margins of error. Where possible, the assumptions have been benchmarked against similar processes in the Standard Cost Model.

### Transitional Relief

The lead option involves 5 years transitional relief for the Construction industry. This is intended to:

- Allow a new wage-setting mechanism to establish itself. Such a relief is much more important for long-standing construction schemes (where the current wage-bargaining system has bedded down) than for more recent schemes.
- Take into account the time taken for a full development cycle (average 5 years) in the construction industry - ie takes into account land-banks held by developers, land which they have already bought at pre-announcement prices.

### Economic impact

The effect of removing the current NICs concession would be to reverse the effects of the current system. In the long run it is likely, in large part, to be passed through to reduce the value of economic rent received by land-owners selling for development.

### Distributional effect

The majority of employees working in the construction industry are likely to be basic rate taxpayers. We do not have the Departmental information necessary to lay out the distributional effect of removing the exemption on employees by income decile. The economic impact suggests that this distributional effect might only be short-term, as the effect should in the long-term be passed through the development chain.

In steady state, we assume that the removal of the exemption in the construction industry will largely fall on development land prices. Given this, the result of removing the exemption is likely to be progressive across the population.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	No	No
Small Firms Impact Test	No	No
Legal Aid	No	No
Sustainable Development	No	No
Carbon Assessment	No	No
Other Environment	No	No
Health Impact Assessment	No	No
Race Equality	No	No
Disability Equality	No	No
Gender Equality	No	No
Human Rights	No	No
Rural Proofing	No	No