

# **PARTIAL REGULATORY IMPACT ASSESSMENT (RIA)**

## **Mandatory Electronic Payment for Large Employers**

### **Purpose and intended effect**

1. Regulations will be made to require electronic payment from employers with 250 or more employees with effect from April 2004. The purpose of this measure is to ensure prompt and secure payment from the largest employers.
2. At the same time the Inland Revenue will introduce a later due date for electronic payments made by all employers. This will compensate for the loss of the cash flow advantage offered by cheque payment. It will also encourage smaller employers to adopt electronic payment voluntarily.

### **Risks**

3. Cheque payment is less secure than electronic payment and the funds take longer to pass to the recipient. The majority of cheque payments made to the Inland Revenue are sent through the post to their Accounts Offices. This means that the transfer of funds, represented by those payments, is also vulnerable to postal delays.
4. Most large employers pay promptly but approximately one third still pay by cheque. There is no interest charge for late payments made by employers during the year<sup>1</sup>. A minority of employers take advantage of this and regularly make their monthly payments a few days late. And a few employers exploit the cheque payment rules<sup>2</sup> by paying with cheques drawn on overseas bank accounts which take longer to clear.
5. This measure will ensure secure and prompt payment by the 10,000 (approx.) largest employers. The payments made by this category of employers represent around two thirds of the total PAYE and NIC yield. It will remove the unfair competitive advantage currently enjoyed by the minority of large employers that pay late or exploit the cheque payment rules. It will also build on the Carter measures<sup>3</sup>, promote the use of modern electronic communications methods throughout the employer's businesses and improve the efficiency of the administration of the tax system.

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<sup>1</sup> Interest is charged on PAYE and NICs paid after 19 April following the end of the tax year to which the payment relates.

<sup>2</sup> In law a cheque payment is treated as made when the cheque is received. Value passes to the recipient when the cheque clears through his bank, at least two days later.

<sup>3</sup> Patrick Carter undertook a Review of Payroll Services in 2001 for the Chancellor. His principle finding was that an electronic strategy was the best way for employers to deal with their payroll obligations and that the Inland Revenue should encourage employers to make greater use of technology in their businesses generally. The Chancellor announced a package of measures in Budget 2002, based on Patrick Carter's recommendations. These include mandatory electronic filing for large employers from 2004/05.

## Options

### *Option 1 –Do nothing*

6. Doing nothing would permit some large employers to continue to use an outmoded and less secure payment method. And it would mean that the minority of large employers that deliberately pay late or exploit the cheque payment rules would continue to have a competitive advantage over compliant employers and at the expense of the Exchequer.

### *Option 2 – introduce an in year interest charge for employer payments*

7. This option would encourage prompt payment but would not do anything to move employers from cheque payment to the more secure electronic payment methods. And it wouldn't prevent exploitation of the cheque payment rules. An effective interest regime would need more detailed information from employers about the amounts due for each month, perhaps involving monthly returns. That would involve fairly wide ranging changes to the PAYE system which would be high risk and burdensome at a time when employers are gearing up for mandatory electronic filing.

### *Option 3 – require electronic payment from all employers*

8. The Government is committed to encouraging all employers to make greater use of new technology in operating payroll and running their businesses. However, it recognises that there are cultural and financial barriers to be overcome and that the adoption of electronic strategies will be more gradual for smaller employers. There are economies of scale in operating payroll and it is proportionally more expensive for small and medium sized employers than for large employers. The particular needs of these employers need to be borne in mind in evaluating options.

### *Option 4 – require electronic payment from employers with 250 or more employees.*

9. This option would require electronic payment from the same category of employers that will be required, under the Carter provisions, to send their returns electronically from 2004/5. It would ensure that a large proportion of PAYE and NICs funds were transferred securely and promptly to the Exchequer and it would affect less than 1% of employers. Approximately two thirds of the total yield of PAYE and NICs is received from the 10000 largest employers. Restricting the requirement to pay electronically to large employers therefore strikes a balance between ensuring the prompt and secure flow of funds to the Exchequer and imposing additional regulatory requirements on the majority of employers.

## **Benefits**

### *Doing nothing*

10. Doing nothing would benefit the minority of large employers that pay late or exploit the cheque payment rules at the expense of the Exchequer. These employers would also continue to enjoy an unfair advantage over compliant employers.

### *In year interest charge for employer payments*

11. An in year interest charge would benefit the Exchequer but it would involve changes to the information required in returns from employers, and the number and regularity of employers returns. Such changes would be high risk and burdensome at a time when both employers and the Inland Revenue are gearing up for mandatory electronic filing.

### *Mandatory electronic payment for all employers*

12. Introducing mandatory electronic payment for all employers would benefit the Exchequer as it would ensure that all employer payments were received securely and promptly. However, it would involve the imposition of a further statutory requirement on all employers and the Government has decided that this should not be imposed on small and medium sized employers.

### *Mandatory electronic payment for large employers*

13. Requiring electronic payment from large employers will ensure that the majority of PAYE and NICs funds are received securely and promptly whilst not imposing costs upon smaller employers. It will also benefit large employers that are already paying electronically and on time by removing the unfair competitive advantage non-compliant employers currently enjoy.

## **Policy Costs**

14. Employers that currently pay on time by cheque should, on switching to electronic payment, be broadly in the same cash flow position. The later due date for electronic payments will mean that the value of an electronic payment, made on time, will leave their bank account at approximately the same time as a timely cheque payment would have cleared under the old arrangements.

15. Employers that currently pay electronically will, potentially, gain a couple of days' interest on the funds as a result of the new later due date for electronic payments.

## **Implementation costs**

16. There will be a small transitional cost for large employers that currently pay by cheque representing the cost of changing their internal procedures and arranging for their bank to make electronic payments.

17. The costs of making an electronic payment compared with a cheque payment will depend on the individual employer's banking arrangements but the costs are expected to be broadly equivalent. Some employers may find electronic payment cheaper overall as many payroll software products include functionality for initiating electronic payments.

18. Some large employers may upgrade internal procedures to be sure of avoiding surcharges after the initial warnings. There may be costs for compliant and non-compliant employers in discussing reasonable excuse claims with Inland Revenue staff.

19. The Inland Revenue's receivables management systems will need to be upgraded to handle the surcharge element of securing compliance.

## **Securing Compliance**

20. The value of an electronic payment passes to the recipient on the same day that it is received. The regulations will include provision for a surcharge which will be applied, after a number of warnings, where the value of a payment is received by the Exchequer after the relevant due date. (Cheque payments that are made early so that value passes to the Exchequer by the due date for cheque payments will be disregarded for the purposes of calculating the surcharge, despite the employer's failure to comply with the requirement to pay electronically.)

21. The surcharge has been modelled, in part, on the VAT default surcharge. The regulations will provide for employers to receive two warnings before they start to incur surcharge. The surcharge will be calculated at the end of the year and based on the total amount due for the year. There will be a progressive scale of surcharge rates for each payment made in default. The primary legislation provides that the maximum surcharge rate for a default payment will be 0.83% of the total amount due for the year. This is equivalent to 10% of the employer's average monthly payment. The maximum rate will only be reached where the employer has failed to make prompt payment for twelve months. An employer's position on the scale of surcharge rates will not automatically start from scratch each year, but will incorporate a backward look at the previous year. Full details of the surcharge rates will be set out in the draft regulations to be published in June.

## **Impact on Small Business**

22. The requirement to pay electronically will only apply to large employers. (Large employer will be defined in terms of having 250 or more employees.)

Small and medium sized employers will be unaffected, but the later due date for electronic payments will encourage them to adopt electronic payment methods voluntarily.

### **Consultation**

23. The Inland Revenue plan to publish draft regulations in June 2003. A 12 week period of consultation will follow and the final regulations will be made in autumn 2003. This impact assessment will be updated then. Comments, including information about the costs and benefits involved in these measures, will be welcomed and will be used to inform the updating of the assessment.

### **Competition Assessment**

24. There is no expectation of a significant detrimental effect on competition (in banking markets) by requiring electronic payment in place of cheque. Rather the measure is competition enhancing between large employers, because it encourages all large employers to pay on the same monthly date and removes the gain from non-compliance.

### **Contact Point**

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