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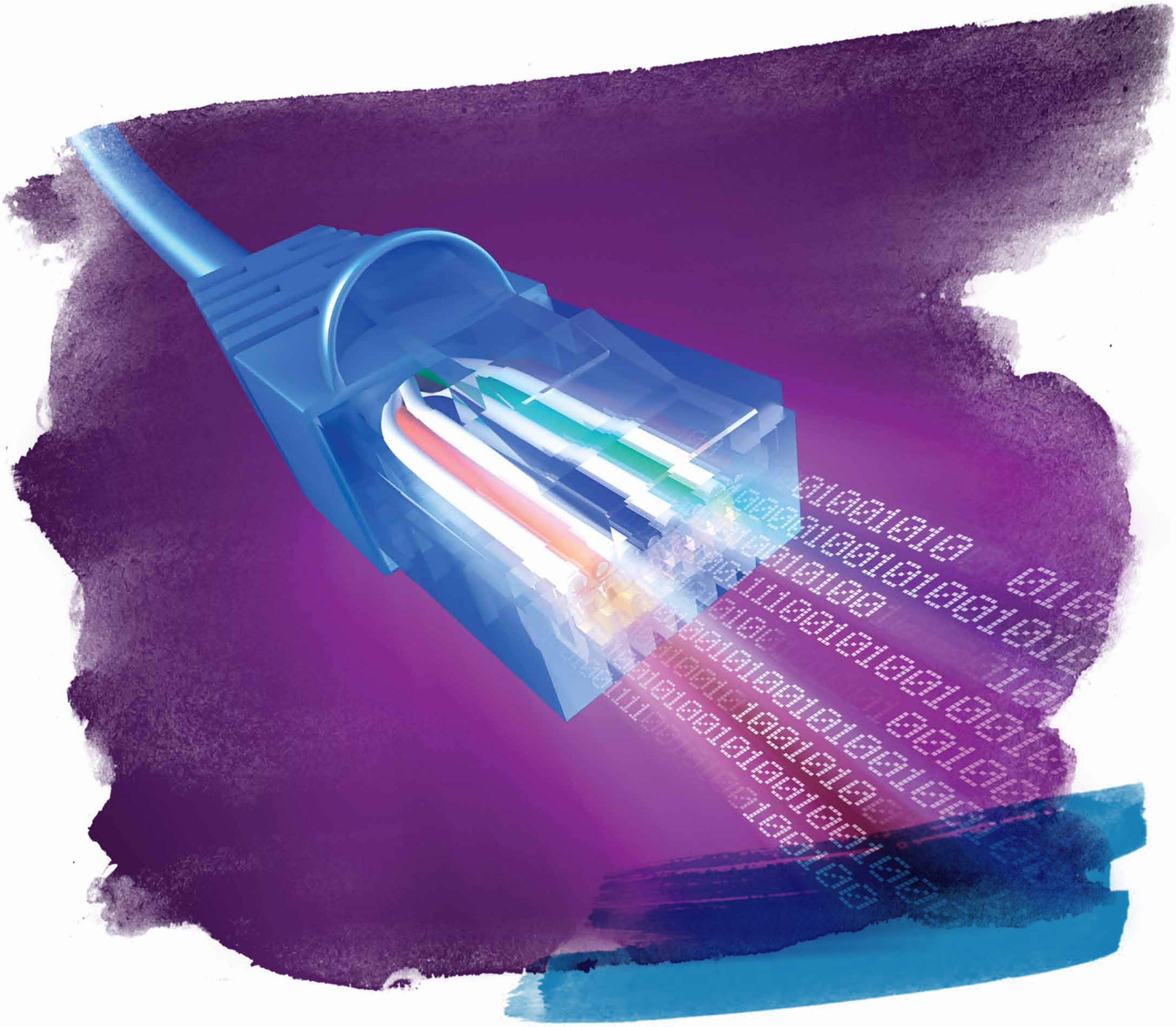
KEY GUIDE

PAYE and Real Time Information



Why the change?

Before the introduction of Real Time Information (RTI), PAYE remained largely unchanged from its inception in 1944. Even with the introduction of online reporting in 2004/05, the same forms continued to be submitted to the same timetable. However, the vast majority of employers and pension providers started reporting in real time during 2013/14, and this means that the UK's 40 million taxpayers now have their earnings data sent to HM Revenue & Customs (HMRC) on or before their payment date - rather than at the end of the tax year.

Receiving earnings data in real time allows HMRC to adjust tax codes in-year to make PAYE work more effectively. This should mean that fewer individuals are caught up in post-year-end adjustments. HMRC is also able to provide the Department for Work and Pensions (DWP) with actual earnings and personal data to be used in validating and adjusting Universal Credit claims.

Universal Credit is the new overarching state benefit that is currently being introduced to replace tax credits and several other welfare benefits. RTI data is also passed to the Child Maintenance Service to be used for the calculation of child maintenance.

The basics

RTI must be filed electronically, so it is not possible for you to produce payroll manually. The choice is therefore between using payroll software and using the services of a payroll provider. An option if you have no more than nine employees is to use HMRC's Basic PAYE Tools package. Although not a full payroll package, this works out PAYE deductions and reports the relevant information to HMRC.

Focus point

RTI must be filed electronically, so it is no longer possible for you to produce payroll manually.

HMRC gives you a PAYE code for each of your employees so that each time an employee is paid the right amount of tax can be deducted. Payroll software makes this process very easy. The PAYE code is designed to deduct the correct amount of tax from the employee's pay so that many employees do not need to complete a tax return. The tax code takes account of an employee's personal allowance, allowable expenses and taxable benefits, and can also be used to collect tax on income where tax has not been deducted at source and tax owing from previous tax years.

Payroll information

Payroll software automates much of the payroll process for you, especially where employees are paid a fixed salary each week or month. However, RTI also requires you to provide the number of normal hours that an employee works each week. This is for Universal Credit purposes, and is a matter of selecting the most appropriate one of four bandings:

- Up to 15.99 hours.
- 16 to 29.99 hours.
- 30 hours or more.
- Other (this should only be used where an employee does not have a regular work pattern or the payment relates to a pensioner).

If using payroll software, it should just be a case of initially setting the employee record, and then updating this if an employee's work pattern changes.

With RTI, you must report payments to employees even when they are earning below the national insurance (NI) lower earnings threshold. Payments to temporary, irregular and casual staff must also be reported. With such employees it may be necessary to set the irregular payment pattern indicator so that HMRC doesn't assume that they've left your employment just because they haven't worked for a while.

If you pay all your employees below the NI lower earnings threshold then you are not required to run a PAYE scheme, and therefore no RTI reporting is necessary. But in this situation you should be very careful – if just one employee has, say, two jobs, then they may need to be taxed at the basic rate, meaning that PAYE deductions are required. It will then be necessary for you to run a PAYE scheme and report details for all employees under RTI. So it is essential to establish the correct tax status of each employee.

What has not changed?

Although the introduction of RTI has meant considerable change when it comes to the filing requirements, the underlying basics of PAYE remain the same. This means that there is no change to the type of employee payments which are subject to PAYE. These include:

- Wages, salaries, overtime, bonuses and commissions.
- Holiday pay.
- Certain expenses allowances paid in cash.
- Statutory sick pay and statutory maternity, paternity or adoption pay.
- Certain lump sum payments.

Focus point

The irregular payment indicator is used where an employee is unlikely to be paid for three months or more.

There is also no change to the time that employee payments are treated as being received. The basic rule is that you should operate PAYE when an employee becomes entitled to receive a payment, even if this is earlier than the actual payment date. However, for directors the position is a bit more complicated as there are two situations where a payment is treated as being made earlier than under the basic rule. This is where a payment is credited in your company's books or where the payment is fixed or agreed prior to the date of entitlement or payment.

Sending information to HMRC and making payments

The basic principle with RTI is that payroll information must be sent to HMRC on or before the date that your employees are paid, be it weekly, monthly or for any other time period. This is known as a Full Payment Submission (FPS). Of course with payroll software the FPS process is simply an extra step after you have run the normal payroll.

It is particularly important that the file arrives on or before the payment date if your employees are paid by BACS, since there will be a four-digit ID set on their FPS record and a matching ID on the BACS file. HMRC use the matching ID on the BACS file to verify that the bank payment has also gone through the payroll. There is no cross-referencing required for any other payment method.

If your business has a fluctuating, weekly paid, workforce (for example, where you are involved in the catering or entertainment sectors employing casual staff) you may find the RTI reporting requirements particularly onerous. HMRC has therefore introduced a seven-day grace period before you have to report pay, but only for certain staff, such as casual employees and piece workers. Until 5 April 2016, there is a relaxation of the reporting requirements if your business has nine or fewer employees. If you process and pay your employees weekly but only run the payroll monthly, then you do not need to submit a FPS until the end of the tax month instead of on or before each weekly payment. However, this relaxation of the reporting rules does not apply if you are a new business that started after 5 April 2014.

RTI has not changed the dates that PAYE has to be paid to HMRC, but HMRC can now calculate the payment due each month or quarter from the FPS files that you have sent in the preceding month or quarter. If there is any reduction to the amount you owe to HMRC for a particular month (for example, due to statutory payment compensation) then you need to submit an Employer Payment Summary (EPS). This has to arrive on or before the 19th of the month after the month just ended i.e. an EPS for May 2014 (the tax month to 5 June) must be received by 19 June. The EPS can also be used to indicate that no employees will be paid for up to six months or to inform HMRC that as a sub-contractor you have had tax deducted from an invoice, as this can be used to offset your PAYE liability.

Focus point

The relaxation of the reporting requirements for businesses with fewer than 50 employees is only temporary, so by 2014/15 you will either have to make the transition to weekly reporting or, alternatively, switch to paying your employees monthly.

The due date for PAYE paid electronically is the 22nd following the tax month. For example, the payment for May 2014 will be due on 22 June, and this will consist of the FPSs for May adjusted for any corrections or EPS submitted by 19 June.

If your total PAYE payment is estimated to be, on average, less than £1,500 per month, then you can choose to make quarterly rather than monthly payments. But this does not affect the requirement to file an FPS on or before the date that your employees are paid.

Penalties are charged for late payment of PAYE, and inaccurate FPSs could also attract a penalty. From 6 October 2014, you will be charged penalties on a monthly basis if your FPSs are late.

Annual information

With RTI there is no requirement for you to send any year-end forms to HMRC. It is simply a matter of marking the last FPS or EPS for the tax year as the final submission, and then answering the end of year declarations and questions.

This will close the PAYE scheme down for the year and ensure that a 'failure to file penalty' is not incurred. For 2014/15, information will normally be submitted by 5 April 2015, although it will be possible for you to submit a FPS or EPS up to 19 April

2015. After that, only an Earlier Year Update can be submitted.

Employees who are still employed by you at the end of the tax year must be given a P60 summarising their total pay and deductions for the year. For 2014/15, employees must be provided with P60s by 31 May 2015. P60s will normally be produced by the payroll software, and can be in either paper or electronic format.

Starters and leavers

When a new employee starts to work for you, they should be set up on the payroll using the information from their P45, and it is also necessary for you to record their date of birth, gender, full address and the date they started work. Similar information will have to be obtained for an employee who does not have a P45. A new starter declaration showing the employee's employment status is included in the FPS, and you will have to obtain this information from the employee if they do not have a P45.

HMRC's system automatically verifies the NI number when starting details are submitted for a new employee. If the NI number is wrong then you will be told to stop using it until the correct number can be established. It is also possible for you to check an employee's NI number in advance of using it on your payroll, and this is done by submitting an NI number verification request using payroll software. HMRC will check that the number is in the right format and that it belongs to the individual concerned, so it is a useful tool if you are involved in a sector where identity fraud is prevalent. Where HMRC finds that a NI number is incorrect or not being used by the right person, it will advise you electronically.

Focus point

You can include a payroll ID to make identifying an employee easier. If you have casual employees who work for you more than once during the tax year, ensure that your software uses a different payroll ID to alert HMRC that this is a new period of employment.

When an employee leaves, their date of leaving is included on the FPS. You must provide the employee with a P45, although this will normally be produced by the payroll software. The P45 summarises an employee's tax status so that this data can be passed on to a new employer. It is not necessary for you to send P45s to HMRC.

P11D completion

P11D completion is not part of RTI, although most payroll software will include P11D completion together with electronic submission to HMRC. An alternative is for you to use HMRC's online expenses and benefits service, which can deal with up to 250 employees.

A P11D or P9D must be completed for each employee who you have provided with expenses or benefits during the tax year, and for 2014/15 these must be submitted to HMRC by 6 July 2015. A P11D is used where an employee earns £8,500 or more a year (and for almost all directors regardless of earnings), while a P9D is used where earnings are below the £8,500 threshold.

Form P11D(b) is used to declare the overall amount of class 1A NICs due on expenses and benefits for the tax year, and this will normally be submitted electronically. The submission deadline for 2014/15 is 6 July 2015, and the class 1A NIC payment deadline is 22 July 2014 if your payment is made electronically.

In-house or outsourced

Should you run your own payroll software, or should the payroll function be outsourced? This really depends on your business circumstances, but there are several points to consider.

- Very good single PAYE scheme payroll software is available for not much more than £50 a year, making it reasonably easy for you to do the work in-house if your payroll is straightforward.
- Outsourcing enables you to focus on the core aspect of your business, and means there is no need to employ someone full-time for a task where there may be several periods each month when little work is necessary.
- Outsourcing provides access to payroll expertise, and the provider should be up to date with the latest legislation and HMRC requirements. This avoids investment in ongoing staff training and new software.
- In-house payroll means that staff are always on-site and available to deal with problems as they arise, but there must be cover for when employees are on holiday or off sick. This could be a particular problem if yours is a smaller business where payroll is dealt with by just one person.
- Outsourcing does not necessarily mean losing control of the payroll process. Payroll data should be made available for approval to you before it is submitted to HMRC, and reports will be provided following submission.
- Outsourcing can range from a bureau service (where you retain data entry and maybe some other payroll areas in house) to a fully managed service (where every aspect of the payroll is undertaken by the payroll provider), or even be a part managed service (where you retain access to the payroll data).

Focus point

RTI makes it very easy for the Pensions Regulator to access information about a business's payroll in order to establish whether the automatic enrolment requirements are being complied with.

Automatic enrolment

The automatic enrolment of employees into workplace pension schemes has already taken place for larger employers, and medium sized businesses with between 50 and 249 employees will join by 1 April 2015. For the very smallest employers with fewer than 30 employees, automatic enrolment will be between 1 January 2016 and 1 April 2017, but new employers will have an even later start date.

Automatic enrolment will mean classifying your employees into three categories depending on earnings and age:

- **Eligible jobholders** are those employees aged between 22 and the state pension age who earn more than the income tax personal allowance.
- **Non-eligible jobholders** are generally those employees aged between 16 and 75 who earn more than the NI lower earnings threshold but who are not eligible jobholders.
- **Entitled workers** are those employees aged between 16 and 75 earning below the NI lower earnings threshold.

You will have to automatically enrol eligible jobholders, while non-eligible jobholders will be able to opt in if they so wish. An entitled worker will simply have the right to require you to arrange membership of a pension scheme for them, and there is no need for you to make any pension contributions on their behalf.

Payroll software should be able to automatically classify employees, although it will still be necessary for you to record whether they have opted in or out of automatic enrolment. The software should also be able to establish an employee's automatic enrolment date, although again it will be necessary for you to record whether or not a waiting period is being applied. You can impose a waiting period of up to three months so for example, there is no need to enrol very short-time employees, such as seasonal staff employed over Christmas. Payroll software should also pick up the three-yearly review date for employees who have opted out of automatic enrolment.

How we can help

If we are not already managing your payroll, then we are more than happy to take over any aspect of this that you may be struggling with given the RTI requirements. And of course we can offer advice and guidance if you are running payroll in-house. Even for smaller businesses, automatic enrolment will be here soon, and this is another area where we can offer our expertise.

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