EXPLANATORY MEMORANDUM TO

THE INCOME TAX (PAY AS YOU EARN) (AMENDMENT No. 4) REGULATIONS 2014

2014 No. 2689

1. This explanatory memorandum has been prepared by HM Revenue and Customs (HMRC) and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 Most debts due to HMRC can be recovered by making deductions from the Pay As You Earn (PAYE) income of the debtor. This process is known as "coding out" because the person's tax code is adjusted to allow this recovery. These Regulations amend the main PAYE Regulations to insert a graduated scale, by reference to the person's income, for the amount of debt which can be coded out.

2.2 The PAYE Regulations are also amended to provide a statutory safeguard that no more than 50% of income can be deducted from payments.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 None.

4. Legislative Context

4.1 Sections 684(3A) and (3B) of the Income Tax (Earnings and Pensions) Act 2003 make provision for recovery of "relevant" debts by making deductions from PAYE income. A "relevant" debt is a sum owed to HMRC under or by virtue of an enactment or under a contract settlement, and can be recovered from PAYE income at HMRC's discretion and without the debtor's consent. Tax credit debts are excluded from the definition of relevant debts, but can be recovered from PAYE income with the claimant's agreement (see section 29(5) of the Tax Credits Act 2002).

4.2 These Regulations amend the main PAYE Regulations (S.I. 2003/2682) by inserting new regulation 14D. This provides a graduated scale for the total amount of debt which can be coded out, by reference to the debtor's income. They should be read in conjunction with The Income Tax (Earnings and Pensions) Act 2003 (Section 684(3A)) Order 2014, which raises the limit on the amount of relevant debt that can be coded out from £3,000 to £17,000.

4.3 Debt in this context means both relevant debt and tax credit debt. These Regulations insert new regulation 14C into the main PAYE Regulations to make specific provision for the coding out of tax credit debt. New regulation 14C makes it clear that those with tax credit debt can object to coding out.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

- ***What is being done and why***

7.1 The amount of debt due to HMRC that can be coded out is being increased. This will permit more debts to be collected in this relatively simple, cheap and less intrusive way. It also minimises the compliance burden on the taxpayer.

7.2 Currently there is a limit of £3,000 on amounts which can be coded out, regardless of the income of the person. The total amount of relevant debt and tax credit debt that can be coded out is being increased from £3,000 to £17,000. A graduated scale will apply so that the amount to be coded out from any particular debtor will depend on their PAYE income. This change will increase the maximum amount that can be recovered through coding out from those with higher incomes. There is no change to the amount that can be coded out for those with incomes of up to £30,000, which will remain at £3,000.

7.3 There is no change to HMRC's powers to code out PAYE underpayments or SA balancing payments. There is no statutory upper limit for coding out such amounts, and HMRC will continue to code them out up to the current administrative limit of £3,000, unless the taxpayer objects. HMRC will count such deductions towards the graduated statutory limit so that in no circumstances will more than £17,000 be coded out.

7.4 Currently for certain tax codes (K codes) there is a statutory rule that deductions cannot exceed 50% of income. The rule is applied administratively to all tax codes by HMRC but is now being put on a statutory basis through regulations 3 and 5-7.

- Consolidation

7.5 There are currently no plans to consolidate the instrument that is being amended.

8. Consultation outcome

8.1 A consultation on this was issued in July 2013[1] with a response document being published in February 2014[2].

8.2 A total of 23 responses were received. In general, the responses supported the proposals' intentions, recognising that coding out as a mechanism for debt collection is convenient for both taxpayers and HMRC. The new statutory 50% limit was welcomed.

8.3 The draft Regulations were published for technical consultation on 25 July 2014 and one response was received.

9. Guidance

9.1 Draft guidance is available on the HMRC website, and this will be updated in due course.

9.2 Taxpayers are notified of their tax code in advance of any deductions being made. All those affected by this change will already have been notified of the debt due by HMRC. They will also be notified by letter of the amounts that will be deducted and will have the opportunity to contact HMRC and challenge the amounts before any deductions are made.

10. Impact

10.1 The impact on business, charities or voluntary bodies is negligible. Although employers will not have any additional burden in collecting more debt, they and civil society groups may receive more enquiries from debtors about the new limits.

10.2 A table of impacts was published as part of the consultation. A Tax Information and Impact Note (TIIN) was published on 25 July 2014 and is attached to this memorandum. It will be published alongside the Explanatory Memorandum on www.legislation.gov.uk.

11. Regulating small business

11.1 The legislation will apply to small businesses that employ individuals who owe HMRC tax debts. But the legislation places no additional burden on such businesses as they will already be subject to the provisions of the PAYE Regulations. However, it may be that a proportion of the employees and pensioners likely to be affected by this measure query their tax codes, and the employer or pension provider may have to spend more time addressing these questions or directing the payee to HMRC's website or helplines.

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[1] How to improve HMRC's collection of debt: coding out.

[2] How to improve HMRC's collection of debt: coding out: Summary of Responses.

11.2 A publicity programme is in place for this work aimed at ensuring taxpayers, employers and their advisers are aware of the extended use to be made of collecting tax debts via PAYE coding out. Full information will be available on HMRC's website, and additional detail and contact numbers for queries will be included on the P2 coding notices to be issued before the start of the 2015/16 tax year.

12. Monitoring & review

12.1 HMRC will monitor the use of the increased coding out limit through information captured within its operational and administration systems.

13. Contact

12.1 **John Tully** at HM Revenue & Customs (Tel: 03000 586687 or email: john.tully@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.