

**Working Families' Tax Credit and Disabled Person's  
Tax Credit: The views, attitudes and experiences of  
employers**

By Rosemary Athayde, Robert Blackburn, Mark Hart and John  
Kitching



**Inland Revenue Research Report 3**

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**Published by the Inland Revenue 2003**

**ISBN 1-904983-01-4**

## **ACKNOWLEDGEMENTS**

The authors would like to thank the following for their help in the various stages of research and analyses on which this report is based. We are grateful to staff at the Inland Revenue for their feedback at each stage of the project and their comments on earlier drafts of the report, and especially to Mike Bielby and Andrea Collier, for their advice and encouragement throughout the project. Finally, we would like to thank the business owner-managers for giving up their valuable time to relate their experiences, without which this research would not have been possible.

Rosemary Athayde  
Professor Robert Blackburn  
Professor Mark Hart  
Dr John Kitching  
Small Business Research Centre  
Kingston University, Kingston Hill  
Surrey UK  
KT2 7LB  
Tel: 020 8547 7247  
Fax: 020 8547 7140  
[www:Kingston.ac.uk/sbrc](http://www:Kingston.ac.uk/sbrc)

The views expressed in this report are the authors' own and do not necessarily reflect those of the Inland Revenue or any other government department.

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## **Executive Summary**

### Chapter One: Introduction and Background to the Report

- This report presents the results of a qualitative study of employers' experiences of managing the introduction and early operation of tax credits. The research was commissioned by the Inland Revenue. The focus of the study is the Working Families' Tax Credit (WFTC) and the Disabled Person's Tax Credit (DPTC). The research is part of a programme of evaluation to assess the effect of the tax credits on employers and recipients. This qualitative research study, which took place from January 2001 to April 2002, provides an important grounding for a large-scale survey of employers.
- Recent welfare reforms have been hailed as "the biggest shake-up of the tax and benefit system since Beveridge". The principles behind the reforms are to eliminate child poverty in Britain and to make work pay. Tax credits are key components of these reforms.
- Since April 2000, employers who operate a Pay As You Earn (PAYE) system are responsible for paying tax credits through the payroll: a process known as Payment Via Employer (PVE). Employers make tax credit payments, in accordance with Inland Revenue instructions, along with regular wage and salary payments.
- Tax credits and PVE are relatively new and little rigorous empirical research is available. A study on employers' experiences of Family Credit, a forerunner of WFTC, provides some background.<sup>1</sup> The study found that employers were familiar with the principle behind Family Credit though it had little impact on businesses. Employers' involvement and responsibilities under Family Credit were significantly less than those required for PVE in WFTC and DPTC.

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<sup>1</sup> Callender, Court, Thompson and Patch (1994) 'Employers and Family Credit' Department of Social Security Research Report No. 32

- This study seeks to investigate employers' responses to tax credits and the practical experiences of administering them. Some of the main aims are to:
  - Report on employers' awareness of information and advice provided by Inland Revenue, e.g. employer packs, video and the helpline.
  - Report on employers' experiences of incorporating the payment of tax credits into their pay-rolling process.
  - Report employers' experiences of PVE in situations such as when an employee joins/leaves the workforce or over holiday or leave periods.
  - Report on employers' experiences of PVE with regard to funding issues including (a) any additional costs incurred and (b) obtaining advances from Inland Revenue.
  - Report any intended and actual changes in employment practices relating to the introduction of the tax credits.
  - Compare experiences of PVE in small firms with those in large firms.
  - Report examples of good practice in relation to PVE
- The findings seek to provide an in-depth analysis of employers' experiences of, and attitudes towards, the tax credits. A qualitative approach to the evaluation allowed employers to influence the issues for discussion. As this is a qualitative piece of research statistical generalisations to the wider population of businesses should not be made.
- Face-to-face, audio-taped interviews were carried out with 50 employers, (plus some book-keepers and payroll managers). These were selected to explore the range of employer experiences of tax credits. Employers were purposefully sampled by region, size of firm, type of payroll (external, in-house manual/computerised), and receipt or non-receipt of additional funding.
- There was a particular emphasis on small firms employing less than 50 employees, since it is assumed that they are likely to experience the highest compliance costs when meeting legislative obligations.
- Employers were selected through the tax credit administrative database. Participating firms were drawn from four regions: North East; South East; London; and the Midlands. Businesses were drawn from a range of sectors including; catering; manufacturing; protective and personal services; distribution; and business services.

## Chapter Two: Attitudes Towards and Understanding of the Tax Credits

- The study revealed that employers have complex and sometimes apparently contradictory attitudes towards tax credits. They may hold one view as a citizen but an entirely different view as an employer. Experiences with tax credits were also found to shape employers' perceptions.
- Employers were often unaware of the underlying philosophy behind tax credits as being rewards for work. Instead many viewed tax credits as another type of welfare benefit. Related to this, was a lack of awareness about which government department now has responsibility for tax credits.

- Some employers reported beneficial effects of tax credits on their businesses. Among the perceived benefits were the reduction of stigma normally associated with 'benefits'; additional income to attract better qualified staff; a beneficial impact on morale; and helping in the retention of staff through higher incomes. It may be that where employers have a better understanding of the policy changes involved they are more likely to express positive views about tax credits.
- Employers also experienced some drawbacks to tax credits. For some, PVE was perceived as a cost saving exercise by government. Concerns were expressed about an increasing amount of state led bureaucracy generally. Specific complaints were voiced about the cost of administering PVE in time, money and labour. Those using manual payroll systems tended to find PVE more time-consuming than employers using payroll software.

### Chapter Three: Introducing PVE to the Business

- The best remembered initial government source of information about tax credits was the Inland Revenue video. Overall it was judged to be a good source of information about tax credits, although some employers would have liked it to contain more information on the rationale for PVE.
- Initially, some employers mentioned feeling daunted at the prospect of introducing PVE into their payroll. In practice, most employers in this study found this a straightforward process. However, experiences varied according to the type of payroll system in use.
- Some employers prefer to delegate the payroll and hence PVE to external agents such as accountants and payroll bureaux, deriving peace of mind from giving responsibility to these 'professionals'.
- The majority of businesses we spoke to had internal computerised payroll systems. Employers in these businesses found the introduction of PVE a relatively straightforward process as the provision for this was programmed into payroll software. Both small and large firms use this kind of software and employers found the instructions clear and useful. Indeed, many employers attributed the smooth integration of PVE to the use of tax credit 'ready' payroll software.
- For employers using manual payroll systems the introduction of PVE was sometimes less smooth. Employers used manual systems either out of habit or choice; a lack of knowledge about computers; changeable working hours; or because the business was cash based. These were mainly small firms. The time taken to set up PVE was the biggest issue for these employers. Once up and running employers and payroll managers found PVE more manageable.

### Chapter Four: Day-to-day Management of PVE

- Employers used a variety of sources of advice and information in the day-to-day management of PVE. Inland Revenue sources of on-going advice provided useful services but were not widely used by employers. The telephone helpline was described as friendly and approachable; and seminars and courses run by local tax



offices were highly rated; and, for those few who had used it, the website was described as providing comprehensive and easily accessible information. The annual employer's pack was used as a reference manual but many found this a time-consuming way of finding specific information.

- The use of non-governmental sources of advice by employers was common. Accountants and payroll software suppliers were the most popular sources of advice. The study found that these intermediaries were often acknowledged by employers as key to the successful introduction and operation of tax credits. Payroll associations and professional and trade associations were also useful sources of information.
- Accountants provide a range of services to businesses often because of a lack of in-house expertise. Proprietary software suppliers provide annual upgrades as well as documentary instructions about new tax legislation.
- Overall, employers reported that PVE is a simple system and easy to maintain on a daily basis. Most found that PVE integrated smoothly into their existing PAYE systems. Many also found the instructions provided by the Inland Revenue to be clear and easy to follow.
- Employers using manual payroll systems, who found the day-to-day management of PVE a simple process, though sometimes time-consuming, put this down to confidence in their own level of education and training. Some employers, however, were less confident about their ability to understand and manage PVE within a manual system, and some were concerned about the length of time needed for record keeping.
- Typically, those using payroll software perceived that the introduction went well because software was pre-programmed to accommodate PVE. There were a number of cases, however, where bugs were discovered in the software. These sometimes occurred through misunderstandings by software developers about aspects of PVE. This was more common in bespoke software rather than off-the-shelf purchases.
- Some employers clearly understood their obligation to pay tax credits during holiday, sickness and maternity leave. Some employers also took into account the preferences of staff when deciding how to pay tax credits during holidays. Many employers, however, were unaware of these responsibilities. A small number felt that tax credits were undeserved during holidays, sickness or maternity leave and claimed to refuse to pay them.
- Transition periods, which occur every six months, were a source of complaint for a number of employers. This process, whereby payments cease while a re-assessment takes place, has caused problems with cashflow for some. The frequency of transitions is perceived to exacerbate this problem. The amount of time spent answering queries during re-assessments was also an issue for larger firms.

## Chapter Five: Additional Funding

- Employers can apply to the Inland Revenue for additional funding where their PAYE tax and National Insurance Contributions (NICs) payments are insufficient to cover the amount paid out in tax credits.
- For some employers, applying for additional funding posed no problems though they sometimes found the paperwork involved a nuisance. For others, though, the process was a source of quite major problems leading to difficulties with cashflow management.
- In some cases, unexplained delays in assessing and receiving funding meant employers were owed money. Other employers were wrongly advised by their accountants and in some cases failed to apply for additional funding, to which they were entitled. In other cases delays occurred because it was not clear who had responsibility, the accountant or the employer, to apply for additional funding.
- A potentially more serious source of problems is the unavoidable variable and unpredictable working patterns common in some sectors. Variable working patterns make it difficult for employers to estimate how much they will need in additional funding because monthly payments of PAYE and NICs vary as hours fluctuate.

## Chapter Six: Employment Issues and Relations in the Workplace

- Some employers felt the additional income provided by the tax credits had enabled them to retain staff who might otherwise have left because of low wages. Employers also described the positive effects that tax credits have had on the morale of staff in low-paid jobs.
- In a few cases, employers were able to take on more experienced part-time staff who may not have been attracted to these vacancies in the absence of tax credits. Employer's felt they had been able to attract better educated trainees to low-paid posts because income was boosted by the tax credits.
- The effect of tax credits on working hours was quite complex. In businesses with low but regular hours, such as some childcare related businesses, the qualifying criterion of 16 hours is viewed in a positive light. However, in businesses where variable working hours are common, employers have found that, because of tax credits, staff are now unwilling to work flexibly and prefer stable hours so that their tax credit entitlement remains constant.
- Some employers anticipate that the extra income from the tax credits will help to attract better qualified staff in future. However, in businesses with variable and unpredictable working patterns, employers want to avoid recruiting potential tax credit recipients in future because of problems of forecasting additional funding and because of the inflexibility of current recipients towards their working hours.
- Employers also reported the effect of tax credits on salaries and wages sometimes created tensions in the workplace. There were perceptions that recipients receive

more money in their pay packets than colleagues doing similar work and that pay differentials between management and staff are eroded by tax credits.

### Chapter Seven: Conclusions

- Employers' attitudes towards tax credits are often complex. As citizens, they may have a positive attitude towards the principles behind the tax credits, but as employers they may feel differently. Employers can also be influenced by their experiences with tax credits. Factors that can shape an employer's perceptions of PVE, for better or for worse, include:
  - The type of payroll system used in the business (manual or computerised)
  - The process of additional funding
  - The impact of the tax credits on working hours and recruitment
  - The role of intermediaries in helping them manage the tax credit system (accountants, payroll bureaux, payroll software suppliers)

When these factors have had either a positive or neutral impact then the introduction and day-to-day management of PVE went smoothly, and employers were therefore more likely to accept their role in the tax credit system and their responsibility for PVE. However where any of these factors have had an adverse impact, resulting in problems, employers were more likely to express negative views about PVE and the tax credit system as a whole.

## **Chapter One: Introduction and Background to the Report**

### **1.1 Introduction**

In December 2000 the Small Business Research Centre at Kingston University was commissioned by the Inland Revenue to carry out a qualitative study of employers' experiences of tax credits. The tax credits include Working Families' Tax Credit (WFTC) and Disabled Person's Tax Credit (DPTC). The aims of these tax credits are part of the Government's twin strategies of making work pay and reducing child poverty.

This study is part of a programme of evaluation of the tax credits. This qualitative research is the first stage of a wider research programme leading to a large-scale quantitative survey of employers. The overall aims of this research are to provide evidence about the kinds of experiences, both positive and negative, employers' encounter in relation to tax credits.

This chapter provides the context for this research. Section 1.2 is an overview of the policy background to the evaluation, followed by a review of some of the key findings from previous literature. Section 1.4 gives an outline of the aims and objectives of the study. An overview of the methodology and sample profile are presented in the final section of the chapter.

### **1.2 Policy background to the study**

The welfare reforms, of which the tax credits are an important component, have been hailed as the "biggest shake-up of the tax and benefits system since Beveridge."<sup>2</sup> Tax credits can be viewed in the wider context of the government's welfare-to-work strategy. WFTC and DPTC constitute one element of a series of measures designed to demonstrate that work pays and to support families with children. Other measures have included the National Minimum Wage; the Children's Tax Credit; the 10p starting rate of income tax; and reforms to National Insurance designed to reduce tax and National Insurance for the low paid; as well as increases in the universal Child Benefit.

The current reform of the tax and benefits systems has been guided by the report, in 1998 by Martin Taylor's task force, on the 'Modernisation of Britain's Tax and Benefit Systems'<sup>3</sup>. The report recommended a shift in focus of policy strategy towards poverty away, from out-of-work benefits, in favour of in-work financial rewards.

Labour's welfare-to-work strategy included substituting tax credits for some of the welfare benefits; making individual payments more generous; and providing extra

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<sup>2</sup> HM Treasury News Release, 140/99

<sup>3</sup> See Taylor (1998) M. The Modernisation of Britain's Tax and Benefit Systems no 2 – Work Incentives.

help for childcare costs. Previously, Family Credit had replaced Family Income Supplement in 1988 and was targeted at low-paid workers with children, and paid direct to claimants who worked at least 24 hours. In April 1992 the number of working hours needed to qualify for Family Credit was reduced to 16 hours. The Disability Working Allowance was also introduced during 1992 and was payable to people in work who have a disability.

October 1999 saw the introduction of WFTC, which replaced Family Credit, and DPTC, which replaced the Disability Working Allowance. This shift in emphasis was also mirrored within government by a switch in the responsibility for policy from the Department of Social Security to the Inland Revenue, with the aim of streamlining the tax and benefit systems. These tax credits are paid directly to recipients by the Inland Revenue. Another major change was the introduction of payment via the employer (PVE), which took effect from April 2000. PVE is a practical reinforcement of the message that ‘work pays’.

### 1.3 Employers’ Responsibilities in PVE

From April 2000, employers who operate a PAYE system have become responsible for paying tax credits, to eligible employees, through pay packets, known as Payment Via Employer (PVE). Employers’ main responsibilities are to make tax credit payments, in accordance with Inland Revenue instructions, along with regular wage and salary payments. To recoup money paid out in tax credits, employers deduct this sum from the total monthly bill for PAYE tax; National Insurance contributions (NICs); and student loans. Employers have a number of responsibilities with PVE:

- To calculate the tax credits for the pay period from a daily rate and add to net pay.
- Enter the tax credit amount on the employee’s payslip and record total tax credits paid in a tax year.
- To provide information about wages and hours worked to Inland Revenue and employees at the end of each six month payment period where the employee reapplies for tax credits.
- To pay tax credits during holiday, sickness and maternity leave.
- To issue a Certificate of Payments to Inland Revenue and the employee, if the latter quits work before the end of their tax credit award.
- Apply for additional funding in advance when the sum paid out in tax credits exceeds that due in monthly/quarterly Inland Revenue returns.
- Record details of tax credit transactions on all relevant Inland Revenue forms (e.g. P32; P35; P14 and P60).

### 1.4 Key findings of Previous Literature

A key study to inform this research is a large-scale study on Employers’ attitudes towards Family Credit, which was the fore-runner to WFTC.<sup>4</sup> The main difference between Family Credit and WFTC is that the former was paid via the Department of Social Security direct to claimants whereas WFTC is usually paid via the employer

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<sup>4</sup> Callender, Court, Thompson and Patch (1994) ‘Employers and Family Credit’ Department of Social Security Research Report No. 32

(PVE). The Callender *et al* (1994) study combined postal surveys with face-to-face interviews. Findings focused on employers' understanding and experiences of Family Credit and any impacts on their employment practices. The study found that employers generally understood the aims of Family Credit but lacked any detailed knowledge about eligibility and other details. Recipients were more likely to be women working part-time in manual or low-skilled jobs.

Employers' perceptions were often influenced by previous experience with Family Credit recipients. A main concern of employers was the amount of time spent processing forms for Family Credit. They were unlikely to use Family Credit as part of any wage-setting strategy, or to actively promote it to staff or in recruitment practices. Employers felt that wages and hours were dictated by the needs of the business and the market and that Family Credit was irrelevant in setting these. Overall, the research found that there was little scope for either employers or employees to manipulate hours to fit Family Credit criteria.

Employers had relatively little administrative responsibility for Family Credit. This is in contrast to WFTC and DPTC where payment via employer (PVE) comprises an important component of employers' responsibility for tax credits. There is little rigorous research to date on PVE though there are some sources, which may provide a context for employers' experiences of PVE.

The Better Regulation Task Force, for instance, has reviewed the impact of regulation on business and identified a number of challenges.<sup>5</sup> There is a potential that PVE may be perceived as an additional administrative burden, particularly in small firms. Recent legislation, which includes the Working Time Directive and the National Minimum Wage, has also sometimes been perceived in this light. The main challenges identified by the Task Force are:

1. Regulations put small firms at a disadvantage against larger competitors because of fixed costs of compliance.
2. Information about regulations is difficult to obtain.
3. Bunching of regulations (e.g. April 2000) increases administrative burden.
4. Higher level of expertise needed in small firms to manage regulations.

The report goes on to make a number of recommendations that are designed to help small firms comply with increasing regulations. These include:

1. Tailored information, guidance and training.
2. Simplified procedures.
3. Compensation for businesses to administer tax credits.
4. Incentives for small business to go on-line.

Another source of information about the potential impact of PVE comes from the Citizen's Advice Bureau (CAB) report<sup>6</sup>. It should be stressed that this report focuses on tax credit recipients rather than employers and needs to be interpreted in the context of CAB constituent activities. Findings of this report are thus partial and are

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<sup>5</sup> Helping Small Firms cope with Regulation. April 2000

<sup>6</sup> 'CAB clients' experiences of Working Families Tax Credit' Evidence Report NACAB, 02/2001

concerned with negative experiences of recipients at the cost of positive ones. The report concluded that PVE provides businesses with a number of particular challenges.

1. Cashflow problems due to delays with additional funding.
2. Payment of tax credits during sick leave.
3. Correct procedures for Certificate of Payments.
4. Impact of tax credits on working hours.

### 1.5 Aims of the study

The aims of the research are to provide an analysis of the information, advice and help received by employers from the Inland Revenue with regard to WFTC and DPTC, and employers practical experiences of implementing and managing PVE through the payroll. The analysis seeks to report positive and negative impacts, and where possible to distinguish between short-term and long-term issues, and also to identify good-practice solutions where these occur. The specific research objectives are to:

1. Compare experiences of PVE in small firms with those in large firms.
2. Report examples of good practice in relation to PVE.
3. Report on employers' awareness of information and advice provided by Inland Revenue, e.g. employer packs, video and the helpline.
4. Report employers' views as to the clarity and usefulness of any information they received.
5. Report on experiences of applying for and using additional funding.
6. Report employers' experiences of obtaining information and help through the Employers' Helpline
7. Report on employers' experiences of incorporating the payment of tax credits into their pay-rolling process.
8. Report employers' experiences of PVE in situations such as when an employee joins/leaves the workforce or over holiday or leave periods.
9. Report on employers' experiences of PVE with regard to funding issues including (a) any additional costs incurred and (b) obtaining advances from Inland Revenue.
10. Report any intended and actual changes in employment practices relating to the introduction of the tax credits.
11. Report on employers' provision of information and advice about tax credits to staff.
12. Provide preliminary evidence to help inform a large-scale quantitative survey of employers.

### 1.6 Methodology<sup>7</sup>

This report is based on qualitative research. A qualitative approach allowed respondents to influence the issues for discussion and enabled respondents to discuss their experiences, motives, and attitudes in their own words. The sample of employers was designed purposefully to cover a broad range of experiences of the tax credits. Firms were selected according to size and region to ensure the views and experiences

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<sup>7</sup> See Appendix A and B for further details on methodology and interview schedule.

of employers operating in regions around the country in small and large firms, in a variety of sectors, were recorded. An interview schedule, covering the relevant areas, was designed in close consultation with the Inland Revenue. As this is a qualitative piece of research statistical generalisations to the wider population of businesses cannot be made. Instead, findings seek to provide an in-depth analysis of employers' experiences of, and attitudes towards, the tax credits.

The first stage of the research was a pilot study carried out in the London area, with six employers, during March/April 2001. One third of the employers, who received a letter, opted out of the study at this stage. Six pilot interviews went ahead and the interview schedule was tested and found to be a satisfactory qualitative research instrument. During the main stage of the research one third of employers, contacted by letter, also opted out of the study.

After the pilot study, the main-stage fieldwork was carried out from June to September 2001. Face-to-face interviews, lasting from one hour to an hour and a half, were audio tape-recorded. Respondents were mainly owner-managers in small firms along with some bookkeepers, and payroll managers in large firms. In some cases external accountants were also consulted.

## 1.7 Sample Profile

Overall, 50, mainly small, businesses were included in the study, with a variety of characteristics.<sup>8</sup> Most employed less than 50 people apart from a sub-sample of seven larger businesses that employed more than this. The sample was stratified to allow comparisons among different types of businesses and to ensure that the potential breadth of experiences of implementing the tax credits was covered. Therefore, the sample took account of the following business characteristics:

- Location
- Sector
- Use of additional funding/non-use
- Payroll systems

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<sup>8</sup> Details of the types of firms can be found in Appendix A.



## Chapter Two: Employers' Attitudes Towards and Understanding of Tax Credits

### 2.1 Introduction

The introduction of the tax credits represents a major change in the way in which financial support is provided for working families with children and people in work with a disability. The changes are designed to demonstrate that work pays and as such employers' role in paying tax credits through PVE is central. This chapter seeks to analyse employers' understanding of and attitudes towards tax credits. How aware are employers of these changes and what is their understanding of the aims of the tax credits? What are employers' reactions to PVE and the tax credits?

The first section of the chapter reveals the often complex and sometimes contradictory attitudes employers hold towards tax credits; these issues are explored through two case studies. Section 2.3 assesses employers' levels of understanding about the shift towards welfare-to-work policies. The perceived benefits of the tax credits on aspects of business management, identified by employers, are discussed in the following section. The final section reviews the perceived drawbacks of the tax credits.

### 2.2 Attitudes towards the tax credits

Employers' attitudes towards tax credits generally focus on two levels: first, on the general *principle* of tax credits, and second on how it affects them as *employers*. A respondent may have very negative attitudes towards the concept of the tax credit system itself but, *as an employer*, may be very supportive of an individual employee, who is in receipt of tax credits. Alternatively, another employer may be positive about the idea of tax credits *in principle* but is unhappy with a particular employee who receives tax credits. Given that owner-managers are citizens as well as employers, it could be argued that these views are not logically inconsistent.

Personal experience with either administering PVE and/or employing a tax credit recipient may also influence an employer's opinion of the tax credit system in the long run. So, for instance, those who feel they have had bad experiences, whether because of the quality of work by a tax credit recipient or because of problems with additional funding, may say that they would prefer not to employ people eligible for tax credits in future. Alternatively, employers who have had positive experiences, in connection with tax credits, remain positive to employing tax credit recipients in future.

Two cases illustrate some of these different attitudes towards the tax credits and the reasons for them. In the first case, (Box 2.1) an employer who had initially been pleased with the way the tax credit system enabled her to take on a member of staff, became disillusioned when the employee left suddenly. The employee in this case was only able to accept her position because of the additional income she received through tax credits.

In this case, from her perspective as a citizen, the employer's view of the tax credit system, did not change and remained positive. From her perspective as an employer, however, her attitude towards tax credits changed from positive to a negative. This change arose through her experiences of employing a tax credit recipient. The

personal circumstances of the recipient, who was a lone parent, led to a conflict between her roles as a mother and as an employee. Eventually the employee left due to the incompatibility of combining the two roles.

Currently, tax credits are targeted at people with children and people with a disability. Such people may face particular circumstances with which the demands of their work need to be compatible. This case highlights the need for employers as well as prospective employees to make realistic assessments about the compatibility between demands at work and personal circumstances, and this may be particularly so for some people who claim tax credits.

Box 2.1 Occupational Health Auditors, 5 employees, 1 TCR.

This business carries out occupational health audits in various sectors such as mining and construction. It is a relatively new business, (four years old), employing mainly sub-contracting medical professionals (about 12 on their books), with a core staff, mainly administrative, of five. The tax credit recipient provided both secretarial and administrative skills as well as childminding for the sub-contractors. At first the employer was very satisfied with the quality of work and the tax credit arrangements, which she perceived as giving her employee a better deal:

*“Well, she was very good, she had to do all sorts here really. And at first I was very pleased with her. She was able to afford a car and everything. I think the tax credit is a really good idea. I think it helps people earn a decent living and they deserve it.”*

A lot of thought went into the flexible arrangement of the employee’s working hours and the employer was sympathetic about time off when her child was sick. In return the employee was expected to fit in with the often unsociable working hours of the business:

*“..we are very flexible. I have been looking back through the diary and you know whenever the child’s ill she doesn’t have to work, and if she needs to do something else, she doesn’t need to work and so on... We have to work all hours in this job. The fact is that we have to work unsociable hours and we have lots of people who come in and need to drop their children off occasionally out of hours so that’s what she does, she does a bit of everything really, childminding, admin and secretarial as well.”*

Business demands means that the busiest period is during the summer months. Therefore the employee was required to work on average 20 hours per week with 11.25 hours per week during term time and 40 hours per week during the holidays. Eventually the hours demanded by work and the needs of her school age child during the holidays conflicted.

In fact the problem for this employer, the loss of a valued employee, was not caused by the tax credits. However, the kinds of people who are eligible for tax credits, in this case a lone parent, may face particular circumstances, which may have an impact on their availability to work. During the summer holidays this recipient experienced a conflict between her role as an employee and her role as a mother, which led her to give up her job. Consequently, the employer has been put off employing anyone on tax credits in future:

*“It’s made me think twice. I don’t think I would go to the bother of setting all this up again really for someone else. Then they could just up and leave once it’s all set up. I really don’t think I would take anyone else on who was claiming. But I can see why the government has done it I really can, and I think it is a good thing. I just don’t think we would get involved again”.*

Though, at a conceptual level, this employer maintains a positive view of the tax credits, her experience has led her to perceive them in a negative light as an employer.

Other employers' attitudes towards tax credit recipients have been influenced by their management approach and in particular their approach to employment relations. A number of employers in small firms appeared to take for granted that they were, to some extent, responsible for the welfare of employees. This sets the background for the next case where the employer's approach to employment relations could be described as 'paternalistic' (Box 2.2).

In this case the employer expressed strong negative views about the whole concept of paying tax credits to people with families. His view is that the additional income is undeserved and biased towards people with children. At a conceptual level, therefore, this employer exhibits negative attitudes towards the tax credits. However, in practice his behaviour towards the (only) tax credit recipient has been very supportive.

Box 2.2 Drinks Wholesaler, 10 staff, 1 TCR

This business sells drinks wholesale to a range of customers in the south east of England. There are 10 employees, with one woman who does secretarial and administrative work, and nine men, who are employed mainly as drivers, one of whom receives a tax credit. At the start of the interview this employer was quite emphatic about his opposition to the introduction to the tax credits. His opposition was not expressed in the context of the impact on his business but rather it was directed at what he perceived to be the philosophy behind the tax credits:

*“I’m against it to be quite honest, Because the way I look at it is if people want to have children they should have money to support those children and if they haven’t got money to support those children then they shouldn’t have them. And I don’t feel that the actual British person should be victimised all the time for those people who have children that they can’t support.”*

Nevertheless, in his personal dealings with the tax credit recipient this respondent claimed he was scrupulously fair, even going so far as to advise his employee to contact the Inland Revenue on reaching the end of a 26 week period, and continuing to pay the tax credit:

*“And what I said to the actual employee at the time was when it was coming near the end of the 6 month period, I said to him have you got a letter from the Inland Revenue about your tax credit, “No”, I said why don’t you phone them up to make sure you are not going to miss out. So he did, but for a couple of weeks he didn’t get the letter. But I did, I knew it was a kosher claim so I paid him the money.”*

Despite this employer’s disapproval of the system of tax credits, at an individual level, he was still prepared to safeguard his employee’s entitlement to tax credits. This employer’s approach to employment relations, which could be described as paternalistic, affected how he dealt with the tax credit process:

*“Because I look after my staff. Even though a lot I don’t agree with, it’s something that once its been implemented, whether I like it or not, I make sure that they get everything that they are entitled to. As I say, even if I don’t like it, they have got children as well. I mean you can’t take a grievance out on the children can you?”*

As in the previous case, this employer’s attitude towards the system of tax credits, as a citizen, which was negative, remained unchanged. As an employer, he took a pragmatic view, which led him to support the employee in receipt of tax credits.

These two cases demonstrate the complexity of employers’ attitudes towards tax credits, and tax credit recipients. They highlight the different and sometimes contradictory perspectives from which one employer may perceive them.

### 2.3 Employers' understanding of the tax credits

Most employers interviewed were largely unaware of the underlying philosophy behind the tax credits and the overall concept of the tax credits being rewards for working, instead of welfare benefits. Respondents tended to regard tax credits as a new way of administering an old benefit rather than a new policy. Those that were aware of this change in emphasis were more inclined to make positive comments about the tax credits and the implications for their businesses. This employer acknowledges the differences between previous welfare systems and the current welfare-to-work system:

“It’s a positive thing. It can help people leave the totally unemployed and having to look after a child. A lot of them haven’t got any professional skills and are on the lower end of the pay scale and the job market. In the past they were better off staying at home, while at least this way they are given x amount to make it up to a sensible wage. So it’s an incentive to make people more active.” (Prepared vegetable supplier, 30 employees, 1TCR)

There was a common tendency among employers, however, to perceive tax credits as ‘welfare benefits’ rather than as a new initiative to provide incentives for working. During interviews tax credits were frequently referred to as ‘benefits’ by employers as the following quotation illustrates:

“It’s a way for the government to pay a particular type of benefit through the employer rather than through their own system.” (Property managers, 5 staff, 2 TCRs)

Some employers felt uncomfortable about their role in what they perceived to be the ‘welfare system’. For these employers the additional information they received about tax credit recipients and the need to sometimes talk with them about, something perceived as personal, was unwelcome. This employer explains her discomfort:

“I feel embarrassed, I mean it’s not my business. I don’t want to know really, I’d rather the DHSS paid it. It’s nothing to do with me or with the business. We’d rather not get involved in that side of things. It’s not up to us.” (Greengrocer, 5 staff, 1 TCR).

Other employers interpreted the rationale behind PVE as a cost saving exercise on the part of the government. These employers perceived that cost savings were being made at the expense of businesses like theirs who have taken over some of the administration previously carried out within government departments. This employer sums up this view:

“It’s cutting out the paperwork for the government by making me responsible for giving out benefits instead of them.” (Residential care, 17 staff, 5 TCRs).

The perception that WFTC and DPTC are ‘benefits’ rather than additional financial rewards for working, is widely held among employers, and is reinforced by the low level of awareness shown about which government department is now responsible for administering them. Few respondents correctly identified the Inland Revenue as the department responsible, while the most common response was the ‘DSS’ or ‘DHSS’.

Some employers felt they needed more information about why *they* were involved and how the tax credits were calculated. Although there were many complaints about receiving too much literature there is clearly promotional work of some kind that needs to be done to educate employers about the philosophy behind the tax credits and their role in it. It is possible that more education of this kind would better prepare employers to take on the responsibilities of PVE.

## 2.4 Perceived benefits of the tax credits for businesses

A number of employers commented on the beneficial impacts of the tax credits on their businesses. Some employers perceived that tax credits had reduced the stigma normally associated with ‘benefits’. Others felt that the additional income provided by the tax credits would be an aid to future recruitment. Some claimed that the motivation and morale of employees was positively affected by the extra money they received in tax credits, and some had been able to retain staff because of the extra income. For a few employers the elimination or reduction of the monthly PAYE tax bill to the Inland Revenue helped cashflow management. Many of these employers appeared to have a clearer appreciation of the shift in emphasis from ‘welfare benefits’ to in-work incentives than those employers who expressed more negative views of the tax credits.

### 2.4.1 Reduction of stigma

The research revealed that, for a minority of employers, the tax credits do not have the same stigma attached to them as previous welfare benefits. This is an important finding although it was confined to a few employers. Part of the rationale for in-work incentives is to encourage more people to apply for them than have applied for benefits in the past; thus increasing the pool of available workers for businesses. Previous research on Family Credit found that eligible employees in protective and personal services were most likely to apply. In this study some employers operating in protective services, usually childcare businesses, were more likely to cite positive impacts of the tax credits. Here, one employer talks about the stigma attached to previous benefits and contrasts this with tax credits:

“Its been fairly fool proof and simple, yes and I think that tax credits doesn’t have the same sort of stigma that family credit had because family credit was still a benefit, whereas tax credits is almost an incentive. Family tax credit has got different connotation. With family credit, especially if you had it in benefit book it was like your income support benefit book, it was just another benefit. You didn’t feel as though you were earning it.” (After school club, 8 staff , 2 TCRs)

Perhaps, these employers have greater familiarity with previous welfare systems and as such are better able to discern the differences in emphasis embodied by the tax credits, than other employers who are less familiar.

#### 2.4.2 Improve recruitment prospects

Altogether, owners of three childcare-related businesses commented that tax credits would provide an additional financial incentive for prospective employees to work and so help employers in their recruitment. There was also a perception that the additional money provided through the tax credits would attract better qualified people to apply. As the treasurer of this after school club explains:

I mean it will make a practical difference in future, I can offer these people more money... In future we can say to people okay this is the wages but on top of that you will get the tax credit. So, the better qualified people will be more likely now to accept ” (After school club, 8 staff, 2 TCRs)

Although no employers reported any direct benefits, in other sectors, from the provision of tax credits, these were anticipated by some. The overall impression given was that it was too soon after the introduction of the tax credits to have had any real impact yet on recruitment. Some respondents were unclear whether it would be ‘ethical’ to use tax credits as an incentive to attract more experienced staff. A partner in an engineering firm describes her confusion about this point:

“...we could attract a much better educated sort of person...I’m not sure where our responsibility lies you know, if you were allowed to interview people and say well because of your circumstances you would be able to claim this...I’m not quite sure where the legislation is.” (Engineering firm, 12 staff, 1 TCR)

#### 2.4.3 Enhance employee morale

Some employers perceived there to be beneficial effects for employees of extra income for employees. Some employers added that they thought the additional income was well deserved. These comments were often made by owners of small firms where a close working relationship exists between employer and staff. One employer in a small firm also felt that the way in which tax credits are paid through the employer gives an added value to the employee’s work:

“It probably makes people feel that there is more value in working. I have one woman in particular, who struggled to come to work for me because there was no benefit there. She wanted to work, because she had been a long time on social so now it encourages her to work, she gets a bit more. It gives the impression that the job is more valuable, because the money is coming from me and not the government.” (Animal Feed Supplier, 5 staff, 2 TCRs)



The beneficial effects of tax credits on staff morale were also mentioned by employers in larger firms, particularly in sectors characterised by low wages. This partner in a temping agency welcomes the tax credits which she perceives will improve the circumstances of the temps employed.

“As long as we can claim it back, it’s no problem. A happier employee is a benefit to us so we welcome any of that sort of help to the employee in what necessarily for us is a low income, a low wage sector... part-time workers can be on the bottom rung of the ladder wage wise so anything that can help them improve their circumstances then we welcome it.” (Temping agency, 58 Temps, 23 TCRs)

#### 2.4.4 Retention of staff

Some employers, particularly those involved in childcare claimed to be quite proactive in advertising the tax credits to existing employees. This was in the hope, some said, that it would help retain staff. Some employers in other sectors anticipated that this would also be the case for some of their lower paid employees. One employer had already experienced this positive effect of the tax credit on a member of staff who otherwise, would have left her job. The additional income from the tax credit enabled this employee to continue working. As the employer explains:

“There is always a place for a few part-time staff. I had one young woman who wasn’t earning very much. And then the tax credit, she heard about it and said can I have this? I said of course if it means you can keep working.” (Clothing manufacturer, 15 staff, 3 TCRs)

#### 2.4.5 Elimination of monthly tax bill

A few employers regarded the reduction or elimination of a monthly tax bill through additional funding as an advantage for their business. This was referred to obliquely by a few employers but only two actually articulated this effect directly.

“If anything, I think it’s easier...So like, for them to take it off at source, actually helps us. It’s just done. I’ll find it a lot easier. It’s the best thing that could have happened for us, you know, because I won’t have to deal with the Inland Revenue at all. So it’s taken a lot of [the] burden off of us by doing it for us... It’s paid into the bank with [employee’s] off-takes taken off. Great! To me that’s less hassle... It’s one less bother for us being a small company...” (Electronic repair, 4 staff, 1TCR)

## 2.5 Perceived drawbacks of the tax credits for businesses

When asked to put the introduction of PVE into the context of the overall running of the business most employers said that it was in fact a minor issue. The employers who were less likely to say this were those who had experienced specific problems with PVE. Typically these centred around the extra time needed to administer PVE and problems with additional funding.

Some of the negative comments made by employers about the tax credits tended to focus on the principle of, what was perceived as, doing the ‘government’s work for them’. Specific complaints were voiced about the cost of PVE to their business. Cost in time was the most common negative comment, particularly for employers using manual payroll systems, followed by financial costs. Financial costs were incurred in two main ways. Firstly through problems with additional funding. The second, and less costly, was through (slightly) larger fees from accountants.

### 2.5.1 The principle of PVE and the accumulation of bureaucracy

Several employers mentioned that they felt that small businesses were having to comply with more and more legislation. Often, tax credits (and the PVE aspect in particular) were viewed by these employers as part of this regulatory burden. There was a perception that there has been an accumulation of bureaucracy from the collection of national statistics to employment rights including the National Minimum Wage and pensions. This attitude was often related to complaints that employers were being asked to take over what they perceive as government responsibilities. Here, one employer sums up this view:

“But come next year we are going to have to look at the pensions the company pension schemes for employees and see how that is going to affect the running of the business. That’s something else, as these things are passed onto the employer by the government it’s something that I imagine every employer is going to have to sit down and say well how much is it going to cost me? If we are running these schemes that were originally government run by civil servants now they are pushing it on to the employer to do in-house. We already have a lot of forms to fill in about what we do, and as more things are passed on to us these things will accumulate.” (Prepared vegetable supplier, 30 staff, 1TCR)

### 2.5.2 Time consuming: Manual and Computerised Payroll Systems

There were two groups of employers for whom the extra time needed to process PVE was a source of complaint. The first group comprises some of the employers that used manual payroll systems. The second group comprises owners of residential homes.

Employers whose businesses used a manual payroll system sometimes found PVE more time consuming than those using computerised payroll software. For others

using manual systems, handling the paperwork themselves was a form of reassurance that things were being done correctly. However, it is clear that some employers found managing PVE within their existing manual payroll processes an onerous task. One employer found the process of applying for additional funding and the transitional periods the most time-consuming aspects:

It's not time consuming, once the forms have been done at the beginning of the six months it's not time consuming. It's at the end of the six months when the forms have to be filled in again, and the tax, the funding has to be claimed, that's when it's time consuming for me...because of the paperwork that comes with it, and the bank account system, and the paying of money. It was all very complicated although it ran very smoothly" (Public House, 5 staff, 1 TCR, manual system)

Another employer, with a manual payroll system, also complained about the additional work caused by PVE:

"It is quite a big task. Just the time, time consuming and irritable. It's bad enough doing the tax and NI working and whatever, and then you have got to start adding that little bit more at the end." (Convenience store, 7 staff, 3 TCRs, manual system)

The owners of residential care homes that were interviewed placed PVE in the wider context of regulatory legislation. Owners of these businesses commented on the extent of the legislation with which they had to comply. Health and safety legislation is a high priority for instance. These respondents sometimes resented the time spent on PVE and the additional paperwork it involves. This employer explains how the accumulation of his daily paperwork has increased in recent years:

"We are very busy, at one time it took 2 hours a day to do the paperwork, now it takes 6 hours a day. And that time could go on caring. From my point of view it's (PVE) a very devious way of the government to put this burden on employers, to save them time and money. And cost us time and money instead. We were very surprised. We are tax collectors. I would prefer not to pay tax credits. In my experience it is draining our resources from the business, from caring." (Residential care, 12 staff, 3 TCRs)

Another owner of a nursing home makes a similar complaint about the increased workload caused by PVE. This comment was also made in the broader context of increased regulation generally:

"It's just paperwork, paperwork, paperwork, we have such a lot already, I mean we could really have done without anymore. We run a very tight ship as it is. I can't afford not to comply with all the health and safety and what have you. That's fair enough, we are being paid to look after these people, but really I shouldn't have to be paying out

benefits to my workers as well. That's not my role. That's not what this business is about. It's about caring for people." (Nursing Home, 20 staff, 6 TCRs)

### 2.5.3 Financial costs

Payments of tax credits by employers is funded either from PAYE tax/NICs (and student loan repayments where applicable). Where the total sum of these payments is insufficient to cover the cost of tax credit payments then employers are eligible for additional funding to meet this shortfall. Employers need only provide an *estimate* of the shortfall, as opposed to an accurate forecast, when applying to the Inland Revenue for additional funding.

A consequence of using PAYE/NICs in this way is that employers lose the use of these funds in their daily cashflow management. Interestingly, this loss was not mentioned by respondents as a disadvantage of the tax credit system. Respondents were more concerned about the unexpected costs they had incurred through PVE.

Unexpected financial costs were reported mainly in businesses that had applied, or were eligible for additional funding. A common cause for businesses to lose out financially was through misunderstandings about the mechanics of the process of additional funding. Misunderstandings also caused delays in receiving additional funding and in some cases employers, who appeared to be eligible, had not applied. The other main problem with additional funding faced by some employers was the difficulty of estimating the amounts needed in additional funding where working hours were unpredictable. There were also reports of genuine delays in receiving additional funding from Inland Revenue.

This employer has experienced delays in receiving funding, because, as a result of confusions between himself and his accountant, the correct forms were not submitted to the Inland Revenue in time:

"I'm not really happy at all with the system. I am paying out over £1,000 a month. And the money is just not there. I have to pay an overdraft on that. Additional costs with money going in and going out. I can't keep up with it. All I know is it's costing me money every month." (Residential care, 12 staff, 3 TCRs)

Other employers also experienced difficulties that arose over misunderstandings about the additional funding form. In some cases accountants were responsible for errors and mistakes during applications for funding.

Forecasting additional funding requirements was a particular problem in businesses characterised by variable and unpredictable working patterns. The owner of this domestic and commercial cleaning company explains her situation:

"I can't see any easy way round it because you've got to be able to estimate what your Pay-As-You-Earn is going to be for the next few

months. That fluctuates here, because people don't always earn the same amount of money every month." (Cleaning company, 80 staff, 4 TCRs)

Employers facing these circumstances often reported being out-of-pocket for at least one month until new funding arrangements were put in place. As a result cashflow management became more difficult to control.

Finally, some employers mentioned that they had incurred slightly larger bills from their accountants as a result of the extra work spent on PVE.

## 2.6 Conclusions

Employers have mixed attitudes and varying levels of understanding of the tax credits. Views as citizens, mixed with direct experience as employers and sometimes perceptions based on low awareness levels combine to create a variety of attitudes amongst these employers. As citizens, employers may disagree or agree with the concept of welfare-to-work policies. As employers, however, they may feel differently. Attitudes may be influenced by either good or bad experiences with tax credit recipients and also by their approach to managing employees. Some employers, particularly in small firms, may take a personal interest in employees, while some may not and prefer to distance themselves from staff. All these factors combine to produce the complex views and opinions expressed by employers in this study.

Some employers, who were more familiar as employers with previous benefit systems and understood the shift in emphasis towards welfare-to-work policies, expressed positive views of the tax credits and cited benefits for aspects of business management. These perceived benefits included a reduction in stigma associated with benefits; an aid to recruitment; staff retention and enhanced employee morale.

It is also clear however that many employers take a cynical view of tax credits and see them as resource and money saving tactics by government. There are some employers who obviously have genuine complaints about the impact PVE has had on their businesses. These complaints were sometimes made, by employers, in the context of what they perceive to be the increasing burden of regulation and its associated costs in time and resources.

## **Chapter Three: Introducing PVE to the Business**

### **3.1 Introduction**

This chapter analyses employers' experiences of introducing Payment Via Employer (PVE) to their businesses. Employers were asked to describe any changes they had made to their payroll systems to accommodate PVE and whether these changes had been easy or difficult to make.

The Inland Revenue sought to raise awareness and provide information and advice on the introduction of tax credits through a variety of media. To find out more about how employers dealt with the introduction of PVE, they were asked about any sources of information, help and advice they may have used.

Employers' experiences of PVE differed according to how they processed their payroll. Where the payroll was externally managed, the introduction of PVE was handled by the external organisation, most commonly an accountancy firm or a payroll bureau. Internal payroll systems comprised two types: computerised and manual systems. Businesses with computerised payrolls comprised the largest group.

Following this broad finding, this chapter is divided into four sections. Section 3.2 analyses the information and advice received and used by respondents when PVE was first introduced. The next section focuses on businesses where the payroll is externally managed. The final two sections are about internal computerised and internal manual payroll systems respectively.

### **3.2 Sources of Initial Information and Advice**

Prior to and during the introduction of PVE the Inland Revenue ran a media campaign including press, radio and television advertisements and articles in the Employers' Bulletin. Some employers also received a video about PVE. A consultation process with employers across the country also took place.

Although some employers mentioned hearing about the tax credits for the first time through press or television publicity, the time lapse between the date of these early campaigns and that of the study meant that these suffered from loss of recall.

Many employers were aware that changes would take place from the media campaigns, although they were not always sure of the detail. This accounts' clerk explains how he became aware of tax credits from a variety of sources:

“...it probably would have been in the various media, probably in the papers, in the tax bulletins we get and .../... other publications from the tax people. So, it's probably straight from the Revenue, from the press, and from the tax experts who send us the bulletins and inform us what's going on. It's all a combined thing really.” (Accountants, 6 staff, 2 TCRs)

Although specific recall of each source of initial information was limited, the best remembered was the video. This was thought to provide a good overall introduction to the tax credits. One employer explained how she found the video useful for answering the queries that first occurred to her:

“We thought the video was very useful...it answered all the questions that, you know, immediately cropped up in my mind. It dealt with all those and was a good introduction.” (After-school club, 8 staff, 2 TCRs)

Some felt that the video could have served an additional purpose, or have provided more detailed content. This bookkeeper, who preferred to use a manual payroll system, worked for a travel agent and tour operator, employing 21 staff. As she explains, she would have preferred a tutorial type format:

“It wasn’t what I was expecting. It was just an overview and it left me none the wiser about what I was expected to do. I thought well, what am I supposed to fill in, and how do I work out what I am supposed to pay everyone? How do I calculate the end of month, all that sort of thing. I expected a lesson on the tax credits.” (Travel Agents and tour operator, 21 staff, 3 TCRs)

The owner of a greengrocers, who also used a manual payroll system, likewise found the video inadequate for her needs. This owner manager explained that though she watched the video around six times, when she came to go through the paperwork she still did not fully understand what was required. These respondents, operating manual payroll systems, would have benefited from a more detailed and tutorial type video, perhaps with examples and exercises for the viewer to complete.

One final point made about the video was that more information could have been provided about the background to the policy and the rationale for PVE. Given the low levels of awareness among employers about the policy changes and emphasis involved, the video may provide an opportunity to educate employers about this.

### 3.3 External Payroll Systems

Employers that relied on their accountants to process their payroll also delegated responsibility for payment of tax credits. These included both micro employers (i.e. five or less employees) and small firms (i.e. up to 35 employees). These businesses operated in a range of sectors including public houses; shops; an events organiser; a clothes manufacturer; and a wholesale prepared fruit and vegetable supplier.

These employers made tax credit payments to staff as directed by these external agents. Many employers were unaware of any changes that may have been made to payroll systems to accommodate tax credit legislation. Payroll was often delegated to external agents because of a lack of knowledge in-house or no time to do the work. There is also a perception that delegating this task to professionals ensures peace of mind because it will be done accurately and correct procedures followed. Employers commented that it was worth paying extra for this peace of mind, as this employer explains:

“Well, I don’t make myself familiar with every detail. As I say, when it comes to wages and anything on the accountancy side, we try to give it to them. That’s what they’re being paid for. This [PVE] has added to their costs and they’re charging us. At least it's done professionally and I don’t have to worry about it.” (Fruit and Vegetable Supplier, 30 Staff, 1TCR)

In other businesses only minimal changes had to be made to integrate PVE into existing systems. One business, a residential home that uses a payroll bureau, amended the format of their worksheets to include details of the tax credits recipients. These worksheets are then passed on to a payroll bureau for processing. The bookkeeper describes how their system works and what they did to accommodate PVE:

“We start with employees recording their hours onto timesheets on a daily basis which cuts off at 31<sup>st</sup> each month. I add them all up manually. And I collect all the information about starters and leavers, induction forms and P45s and P46s. And hand it all to the bureau... We just added a couple of lines onto our front sheet, the starters and leavers sheets. We just add names to that sheet with the amount of tax credit due.” (Nursing Home, 20 staff, 6 TCRs)

Overall, those employers externalising their payroll appeared less knowledgeable about the details of PVE. This was often bundled together with other payroll matters and unsurprisingly, therefore, employers were not interested in the detail of PVE and how it had affected the payroll process. In some cases, however, the additional time undertaken by external payroll agencies to incorporate PVE did lead to a rise in the fees for this service.

#### 3.4 Computerised Payroll Systems

The majority of businesses in the sample had internal computerised payroll systems. Businesses tended to use off-the-shelf software, although some of the larger firms (employing over 100 people) used customised software.

As with firms that externalised their payroll, businesses with computerised payroll covered a range of sectors. These included two firms of accountants; a paper products manufacturer; a helicopter operator; a convenience store; a travel agent; and a cleaning contractor. Some firms, for instance residential homes and a temping agency, used sector specific software payroll. Most employers with computerised payrolls found the introduction of PVE straightforward and were not able to report any particular effects on the running of their businesses.

All the off-the-shelf payroll software is supplied with annual updates to incorporate any tax changes. Although some employers may have been worried initially at the prospect of having to manage PVE most were reassured on finding that the provision for tax credits was written into the software. One employer explains:



“I panicked. I thought what am I going to do with this? Luckily I went into payroll on the computer and it was all there for me, which was quite good. The package is updated every year and last year’s update had the tax credits in it. If I was doing it manually I would need a lot more help. We have an accountant and an auditor who do our books at the end of the year. The accountant spent quite a lot of time going through it with me.” (Family Centre and counselling Service, 7 staff, 1TCR)

One employer, who had written his own payroll software, resorted to buying off-the-shelf payroll software because he thought he would need it to manage tax credits. He describes how, when he realised how easy the changes needed would be to make, he was able to amend his own software:

“I wrote my own payroll package in [proprietary spreadsheet package]. Then I cheated and I bought [proprietary payroll software]... I bought it for tax credits. And then when I realised what it was and how easy it is, it was quite straightforward to amend my own payroll. Now I use [proprietary payroll software] to print payslips.” (Software consultant and Public House, 9 staff, 2 TCRs).

It was more common for large firms to use customised payroll software. One was a health club group based in London employing 3,500 staff with 96 tax credit recipients. Many of the staff are women who work part-time in the beauty salons and crèches of the 62 health clubs. The payroll manager trained four members of staff in the use of the payroll software. Training is updated as changes to the software are made to accommodate new legislation. The payroll manager describes the software and how she goes about training staff:

“The software has a base file. In the base file we have a tax credit screen with a start and stop date; the daily rates; the total amount; and obviously a reference number...We didn’t have any problems setting it up...I actually trained the staff myself. When they [the software developers] release new facilities on the software they always send you guidance notes on how to use them.” (Health Club Group, 3,500 staff, 96 TCRs)

Although most employers using computerised payroll software found the incorporation of the tax credits to be easy, there were exceptions. These occurred in cases where the software had errors. To rectify problems employers used a telephone helpline provided by the software suppliers or contacted the software developers direct. This employer recalls the initial problem with the software and describes how the software company responded:

“...we just got an update at the year end from [proprietary payroll software] and it did an automatic update. You get a new disc, it was input on a year end update. I do recall there were problems with it. The [proprietary payroll software company] didn't get it quite right and it fouled up some but they put it right. That was in the early stages, that

was right at the start. They had to put a patch in I remember.” (Timber Products, 90 staff, 3 TCRs)

### 3.5 Manual payroll systems

A few firms who participated in the study used manual payroll systems. Some of these employers found setting up PVE a challenge while others found it quite straightforward. However, most said that they found it relatively easy to manage PVE after they had gone through the process once and learnt the various procedures involved. Thus, for some employers the introduction of PVE posed no problems even though those using manual systems are often regarded as more likely to be affected by PVE.

Some employers felt that a manual system suited the changeable working patterns of staff or because payments were made in cash. One business, an after-school club (a charity) ran a manual system because of the changeable nature of the hours staff work. Hours changed monthly and fit around inset days and holidays. The treasurer of the club describes how she used the information provided by the Inland Revenue when setting up PVE and found the process quite straightforward:

“It’s all manual because our workers ... there is never more than four or five weeks when the wages are the same... I found the process [of setting up PVE] quite straightforward. I just read the information [from the IR about the tax credits] through and copied it and found it very clear. (After-school club, 8 staff, 2 TCRs)

Others found the process more difficult. In the following example, a partner in a greengrocers has been responsible for book-keeping for five years. Although she is confident about keeping the accounts, she found the task of setting up PVE a daunting and time-consuming one. The business uses payroll stationery supplied by the Inland Revenue. However, the bookkeeper found the application of the forms difficult. As a result, she believes that she would have benefited from training to learn how to use the revised forms and doing the calculations:

“I use the Inland Revenue forms, the ones they sent me. If I had someone to show me it would have been fine. We had to put in everything differently on the forms...It was very hard and I got into such a muddle at first. I really thought I’d never be able to understand it [the tax credits]. It took us so long to work it all out it really did.” (Greengrocers, 5 staff, 1 TCR)

The largest firm with a manual payroll system was a cleaning service for commercial premises and private homes (employing 80 staff). Staff are employed part-time to cover shift work. The payroll is done in-house every four weeks. Most are paid by BACS; although a few employees were paid cash by request. One employer plans to move to a computerised system but at the moment has a bookkeeper to do the payroll and does the tax credits component herself. Here she describes her reasons for using a manual system and her experiences of setting up PVE:

“I’m a manual person really and I like paper. I like to see what’s on there. I don’t trust a computer. I do the Pay As You Earn and the tax credit side. Setting up the tax credit side ... it was really just spending more time just working it all out. It’s finding time to read all these books and to understand it all, what you have to do and then fill in the forms. .” (Cleaning Company, 80 staff, 8 TCRs)

It was during the process of actually setting up PVE that this employer first realised the effect it would have on her business. Customers are invoiced and the business actually handles little cash. As such, this employer was concerned initially about finding the money to pay the tax credits. As she explains it was at this stage that she began to think about additional funding:

“Initially I had no idea this was going to be thousands of pounds...It quite threw me when I came to the first lot of forms. When I worked out those first amounts I was quite amazed at how much this was going to be. It was going to have an immediate effect on the cashflow...It took me most of one Sunday to read all the information, get my act together, get the form filled in and then try to estimate how much I would need in future funding.” (Cleaning Company, 80 staff, 8 TCRs)

A further complication arose for staff who had moved from receiving weekly Family Credit payments to PVE monthly payments. Some wanted to continue to receive these payments on a weekly basis rather than as part of their monthly pay. This complicated payroll calculations and, therefore, required extra management time. However, as requests for advance payments have become less common, the problem had receded. The main impact for this respondent has been the amount of time spent calculating the amounts needed for additional funding.

### 3.6 Conclusions

Most employers familiarised themselves with details of tax credits only when they actually had to deal with them. Respondents were aware of tax credits, to varying degrees, before they became involved, through a combination of sources (including the Inland Revenue and various media).

The Inland Revenue video about tax credits was the best remembered vehicle of initial information and advice. Many respondents were satisfied with the overall introduction it provided. However, some employers and bookkeepers, who use manual payroll systems, would have benefited from a more tutorial style format. Other respondents thought the video needed to include more detail about the philosophy behind the tax credits and in particular the rationale for PVE.

Initial perceptions of what the introduction of PVE would entail caused some concern for employers. However, in practice these concerns tended to be assuaged. The study revealed a variety of experiences of introducing PVE. These tended to vary according to the type of payroll system used by the enterprise. Payroll systems included in-house computerised and manual systems as well as externally managed payrolls.

Accountants, payroll bureaux and software suppliers played an important intermediary role and influenced employers' understanding, implementation and perceptions of PVE. Many employers derived peace of mind from entrusting the introduction and management of PVE to accountants and payroll bureaux. Likewise, the use of payroll software often positively influenced the integration of PVE into existing payroll systems.

Only when the software was faulty (a rare occasion in this sample) did employers complain about PVE. Although literature about tax credits is available to software developers it appears that not all suppliers are paying sufficient attention to the details of PVE. Though the software problems described by employers were short-term ones new updates may well be accompanied by more software faults.

## **Chapter Four: Day to Day Management of PVE**

### **4.1 Introduction**

A main aim of WFTC and DPTC is to demonstrate more clearly the financial returns for working and so make working a more attractive option for people with families and those with disabilities. From the employers' perspective this may increase the pool of available labour. The payment of tax credits via the employer (PVE) seeks to reinforce the link between work and financial rewards by making the in-work support paid within wages.

This chapter, provides an analysis of employers' experiences of the day to day management of PVE. Employers were asked about their experiences and about how they coped with aspects of PVE and, if they faced any problems, how they had addressed them and where they went to for advice and information.

Discussions with employers focused on:

- how well PVE fitted into the PAYE process.
- experiences of paying tax credits so far.
- views about the administrative forms, provided by the Inland Revenue, such as start notifications.
- dealing with leavers, new recruits and transitional periods.
- employers' obligations to pay tax credits during holiday, sickness and maternity leave and how easily these have been to administer.

Details of the sources of advice and information, used by employers in the day-to-day management of tax credits, are given in the following section. Section 4.3 looks at employers' assessments of how well PVE fits into their existing payroll systems. The next section focuses on employers' awareness and experiences of managing tax credits during holiday, sickness and maternity leave. Section 4.5 assesses employers' views of the instructions they receive from Inland Revenue to start paying tax credits and how they have coped with tax credit leavers. The impact of transition periods on businesses is reviewed in the following section. The final section comprises the conclusions.

### **4.2 On-going Sources of Advice and Information**

Employers were asked to describe and comment on sources of advice and information about the day-to-day management of PVE, including use of the Employers Tax Credit Helpline, which is provided by the Inland Revenue.

The Inland Revenue provides employers with a range of sources of information and advice about tax legislation. Employers were asked to describe and comment on sources of advice and information about the day-to-day management of PVE, including use of the Employers Tax Credit Helpline, which is provided by the Inland Revenue.

The Inland Revenue also offers a range of on-going sources of information and advice about tax legislation. The annual employers' pack, for instance, with details of all tax legislation is now supplemented with details about PVE and a separate booklet about the tax credits. Local Inland Revenue Tax offices run various seminars for employers, the self-employed, and for book-keepers and payroll managers. Finally, details of tax legislation including PVE can also be viewed and downloaded from the Inland Revenue website. Employers were also invited to comment on any alternative sources of advice, that they used, such as accountants and software suppliers.

#### 4.2.1 Use of Annual Employers' Pack

Some employers recalled first coming across the tax credits through reading about them in the annual employers' pack. This was viewed as a useful source of information, though used on a need to know basis.

In businesses where the payroll is managed in-house, the employers' pack is kept and used as a manual, as this payroll manager explains:

“Well, it's there in the cupboard when I need it. It's all very clearly laid out and straightforward. I don't read it all through, I just refer to it when I need it. I've got to know most of it by now so I don't need to look at it so often. But if someone is leaving or starting then I'll just have a look and check what I am supposed to do.” (Engineering firm, 12 staff, 1 TCR)

In businesses where the payroll was managed by a bureau or by accountants, employers often passed any information about tax legislation, including the employers' pack, to these external agents. In these cases, employers were unable to provide comments on the Employers Pack.

#### 4.2.2 Inland Revenue Seminars

Inland Revenue seminars, held at local tax offices, were perceived as very helpful by those respondents who had attended. They were attended by bookkeepers and payroll managers in large firms and some owner managers of small firms. Small employers, who used a manual payroll system, found the instruction they received particularly useful. They also commented that meeting other people in similar situations to themselves was a great help. This owner manager of a convenience store describes what took place at the seminar for the self-employed, which he attended:

“They had all the forms there: the P11s, the worksheets, and the tax returns and so on and so forth. It was all there. They took you through it all, step at a time. It was hard work but doing it there with everyone else made you realise all small employers like me have to do this. We just have to get on with it, better do it right and everyone else is in the same boat, I mean.” (Convenience store, 5 staff, 2 TCRs, manual payroll)

In this way the seminars also succeeded in overcoming the feelings of isolation, particularly felt by owner managers of very small firms. Feeling isolated can

exacerbate anxiety over PVE for some. This attendance at Inland Revenue seminars proved especially beneficial for employers using manual payroll systems.

Payroll managers in larger firms also found the seminars very useful. This payroll manager describes how she enjoyed the informal atmosphere of the seminar and felt that it was pitched at the right level for her:

“The seminar was on tax credits. It was just a very relaxed one. It was just very straightforward. Just basics, which is what I like, nothing fancy. And I came away quite happy. I think it was a good general chat with two or three people.” (Military accessories manufacturer, 115 staff, 3 TCRs).

Generally, therefore the feedback on the seminars was positive from all those that attended.

#### 4.2.3 Employers’ Tax Credit Helpline

The Employers’ Tax Credit Helpline provides a reactive service for those employers looking for guidance and help with tax credits. Some of those who used the Helpline had specific queries while others used it to confirm that their own understanding of parts of the process were correct. The most common queries concerned additional funding, payment during sickness leave and holidays and filling out tax returns. Overall, the telephone helpline was viewed as offering a good service with advisers often described as “friendly” and “approachable”. This employer had used the helpline on several occasions and explains how she was satisfied with the overall service she received:

“I’m really impressed with the way the people on the Helpline at the Inland Revenue deal with things, they are really very good. Because the Helpline is so easy to use and friendly. So I feel that I’m getting one hundred percent from them because when you are dealing with peoples wages, you don’t want to be making mistakes, you can’t go back and correct them.” (Property Managers, 6 staff, 2 TCRs)

Others found the helpline useful for clarifying and confirming that they had correctly interpreted instructions. This payroll manager contacted the helpline to clarify the final payment of a tax credit recipient who was due to leave the company:

“You know I just wanted to clarify that. I was fairly sure that I just paid her for the one day. And they were very good they didn’t make you feel stupid or anything. They were just really nice and friendly and just confirmed what I was going to do anyway. But I felt reassured you know. (Temping Agency, 58 staff, 23 TCRs)

Concerns were expressed by some about getting through to the helpline and being kept waiting, and some scepticism about the quality of advice given. An accounts clerk in an accountancy firm sought advice about completing a P35 form. He explains how he received advice from the helpline that contradicted that given by his local tax office:

“Now, what you’re meant to do on the P35 form is summarise how much tax credit you’ve paid out and how much funding you’ve received. There wasn’t, as far as I could see, any good guidance as to what should go on the P35 form. So I had to phone up the Helpline and they weren’t necessarily sure... I had different, conflicting, information from the tax office when I spoke to them. And I just settled on the answer I thought made the most sense and then used that.” (Accountants, 6 staff, 2 TCRs)

Finally, there were some employers, from both large and small firms, who were unaware of the existence of the helpline, or were unclear that there was a specific helpline about the tax credits.

#### 4.2.4 Inland Revenue Website

Only a few people had used the Inland Revenue website. Users stated that the material was easily accessible and the website was a comprehensive source of information. Speed of access to information compared with retrieving booklets that have been filed away was perceived as a big advantage:

“...we used the Employer’s Helpline on the website. I can download information, can print information off the website, most of the books now are on the website, we probably did have one [Employers Pack] at the time it got filed away. But I looked on the website and I did notice on the year end that there was quite a lot of help if you needed it.” (Engineering firm, 12 staff, 1TCR)

Overall, although the website was not used extensively those who had used it were impressed with the navigation and material accessed.

#### 4.2.5 Non-government Sources of Information and Advice

Instead of using Inland Revenue materials and sources of advice, many employers relied on trusted intermediaries, including accountants and payroll software suppliers, or professional and trade associations.

For some employers the main source of advice about tax matters is determined by how their payroll is managed. Where the payroll is externally managed the external organisation, usually accountants or payroll bureaux, is a source of information and advice about tax legislation. In businesses where the payroll is internal and computerised, payroll software suppliers provide information about changes in regulations. Proprietary software suppliers also provide telephone helplines for any queries or problems with the software.

A further important source of information about tax credits, mentioned by payroll managers, are magazines distributed by payroll membership associations. Similarly, employers operating in the engineering sector described how they had received information about tax credits via their trade associations.



#### 4.2.6 Use of Accountants and Payroll Bureaux

In businesses where the payroll was externally managed, employers turned first to their accountant or payroll bureau for advice about implementing tax credits. For many employers the task of managing PVE was delegated to external payroll managers. In this way the need to understand tax credits was circumvented by farming out “the problem”. Employers that used in-house payroll systems also sought advice about financial matters including tax legislation, from external sources, chiefly accountants.

Firms use accountants for a range of services and research elsewhere shows that they are the most common external source of advice. Many smaller employers use accountants to do the entire accounts, payroll, and VAT returns. This externalisation is usually because of a lack of in-house expertise or time. In other cases these financial tasks are divided between the accountant and the business, depending on the level of financial knowledge (or time available) in-house.

Employers often viewed accountants as the financial professionals and therefore the “experts” on financial and related matters. When set against this background, it was no surprise that accountants were trusted sources of advice and used heavily in the implementation of PVE. The trust placed in accountants, to deal with new regulations, by small business clients, is illustrated by this employer:

“This one [i.e. PVE] is wages related and it’s not done in-house. I didn’t sit there to check all the information that came in. I suppose there was sufficient at the time and I just said well this has come up now, we have this person, and it’s down to you. So the accountant is worrying about that rather than us. The accountants are the experts. That’s what I pay them for. They’re the professionals.” (Prepared vegetable wholesalers, 30 staff, 1 TCR)

Another employer, who was initially concerned about managing the tax credits herself, was reassured by her accountants who offered to ‘sort it out’ on her behalf. The employer explained:

“If you don’t get it right, it can cause horrendous problems. I prefer the easier route. I knew that [an employee] was going to be getting this through her pay and I had a chat to my accountants. Basically, they said as soon as you get the paperwork, just send it to us and we’ll sort it out.” (Children’s activity franchise, 8 staff, 2 TCRs)

However, not all accountants were able to provide the necessary information or assurances to their small business clients. In one case, a small employer was surprised to find that her accountants knew less about the tax credits than she did. In this letting agency, the payroll is done in-house while the end of year accounts are compiled by a firm of accountants. When the owner-manager asked for information about the tax credits, however, they were unable to help, as she explains:

“They were a bit taken aback when I phoned. I could hear them asking around the office ‘does anyone know anything about tax credits?’ But they didn’t know what they were. It was quite early on but I wanted to find out for [her administrator] in case she could claim, and what it would mean for me for the business. But they didn’t know...They’ve been back to me since but I already had the information from the tax people by then.” (Property Managers, 6 staff, 2 TCRs)

Other respondents also discovered, to their cost, that their accountants lacked vital information about aspects of PVE, particularly additional funding (see Chapter Five).

#### 4.2.7 Payroll software suppliers

A further important source of advice on tax credits for owner-managers was payroll software suppliers. Businesses with computerised payroll systems used two different types of software providers. The first provides off-the-shelf proprietary software packages used by both small and large firms. These packages are produced by leading software firms who have a strong brand image and market penetration. They devote resources to producing packages which are user friendly and focused on the small business market. The second, less common group, involved the developers of customised payroll software for large firms.

Both types of software suppliers were cited, by employers, as sources of information and advice, about PVE. These respondents also often found the daily management of PVE was simplified by the use of payroll software.

Respondents described how off-the-shelf payroll software is updated annually and new tax regulations are incorporated into the upgrades. These were usually accompanied by documentation explaining amendments to the software and the reasons for the changes. One payroll manager’s views of the information received from software suppliers sums up the feelings expressed by those using these kinds of packages:

“I believe it was from a mailing from [proprietary software supplier] saying that the legislation was coming in. They send emails once a month with all the new things on and what the legislation is going to be. I find it very good, very self explanatory and it is very easy to follow. As well as the email mailings you get a ... I don’t know whether its quarterly or two monthly, they send you a book with all the new changes.” (Engineering firm, 12 staff, 1 TCR)

The use of payroll software packages appeared to have a positive influence on perceptions of the ease or difficulty of daily management of tax credits and on PVE in particular. Here a partner in a firm of quantity surveyors describes how the payroll software he uses has helped with the day-to-day management of PVE:

“The computer does it all for me. I don’t have to do anything once it’s been set up. It’s just at the beginning and at the end I have to put in the new figures.” (Quantity Surveyors, 9 staff, 1 TCR, computerised)

This kind of positive perception about the advantages of payroll software was quite typical among respondents.

In some of the larger firms, with over 100 employees, payroll software was customised by software developers. This payroll manager was aware early on that the business would be affected by PVE because of the large proportion of part-time staff. She was confident that the service provided by the software developers would adequately meet their needs:

“I don’t think we were too worried. I think when we heard we knew we would have a large amount [of tax credit recipients] obviously because of having quite a lot of part-time employees. But we had confidence that our payroll software provider would give us the tools within their software to deal with the tax credits. (Health and Fitness Group, 3,500 staff, 96 TCRs).

These bespoke software suppliers, however, were not always viewed as a reliable source of advice. One payroll manager felt let down by her software suppliers because it was only after attending a seminar that she realised that they did not have sufficient knowledge about the tax credit process to make the necessary adjustments to the software programme. Here, the payroll manager, who had encountered a problem with the seven-day payment cycle, describes how she identified that it was a software problem:

“The programme was not set up to calculate on a seven-day basis, it’s five days, you know a normal week. And the software people hadn’t cottoned on to this. It took me a long time to figure out that it was the computer that was wrong and not me. Then I called them in and told them and they sorted it but they didn’t know – they said they hadn’t been informed about it.” (Military accessories manufacturer, 115staff, 3 TCRs).

For a few employers then errors in software programmes meant that the integration of PVE was not so smooth. However, software problems like these were rare and, for most people, using software simplified the PVE process and cut down on the time taken to carry out day-to-day management.

#### 4.3 Integration of PVE with PAYE Process

Overall, employers reported that PVE is a simple system and easy to maintain on a daily basis. Most employers found that PVE integrated smoothly into their existing PAYE systems. Many also found the instructions provided by the Inland Revenue to be clear and easy to follow.

Many employers commented that they found PVE to be much easier to administer than Statutory Sick Pay and Statutory Maternity Pay. This employer compares the calculation of the tax credits with that of Statutory Sick Pay and comments on the clarity of the instructions on the start notification:

“It fits in fine. In fact I think it is a lot simpler than sickness pay. I mean that is a nightmare to work out. Getting the Doctors’ certificates and the days right and everything. That is much more difficult to work out than tax credits. Tax credits are simple, straightforward, you just do exactly what is says on the form [start notification]. That’s all.”  
(Manufacturing firm, 26 employees, 3 TCRs)

Another employer, who uses a software payroll system, describes how much easier she finds implementing the tax credits in her business than Statutory Maternity Pay. Being provided with a breakdown of the daily rate was perceived by this employer to be particularly useful:

“It’s (PVE) much, much better. I have statutory maternity benefit on there, and I have made a mess of it. It was pretty clear, they did as well give a break down of the daily credit. It was clear to work through.”  
(Community Centre and Counselling Service, 7 staff, 1 TCR)

#### 4.3.1 Manual Payroll Systems

Those employers using manual systems were more likely to encounter problems in the daily management of PVE and to find the process more time consuming than employers using computerised payroll systems.

Not all those using manual systems have encountered problems however. For some the confidence to manage PVE within a manual payroll system derives from their level of education. An owner manager of a convenience store claimed he found doing the calculations easy because he had always been good at math’s and had done well in the subject at school. This employer had also attended a four-day course on tax legislation for the self-employed, which included a session on tax credits, and so felt he was well prepared. He describes his careful approach to PVE:

“I have always been good at maths...The first few weeks, I really had to think now what I am doing here, but then it just came naturally and I could work it out...It’s easy really. There’s nothing to it. You have got your centre figure and all you do is just fill in the column... [pointing to stationery supplied by the Inland Revenue]. I still always double check though, I always check my sums. It does take longer but I suppose it’s not that bad really.”(Convenience store, 5 staff, 2 TCRs, manual system)

Another employer also cites her level of education as the reason she finds PVE easy to manage in her manual payroll system. This employer also does not perceive the paperwork as onerous even though it did take some time to complete. She describes how she found the video useful:

“We got the video and we thought it was very useful. I find the paperwork very straightforward, but I have to admit that I do have a degree and am used to dealing with paperwork. I find it all

straightforward. ...it's a little bit of extra paperwork but I don't find it too difficult." (After-school club, 8 staff, 2 TCRs)

In another business, the bookkeeper prefers to use a manual system, though her employer would like her to use a computer and has offered to send her on a course. The business, a travel agent and tour operator, employs 21 staff. According to the bookkeeper the proprietor is concerned about the time taken to administer PVE:

"It's quite straightforward but it's something else to think about every month. And it takes time, it's a simple sum, but I have to check it for each of the girls to make sure I haven't got them mixed up, you know the amounts. They're different for each girl. So, it all takes longer, and the boss doesn't like it." (Travel Agents and tour operator, 21 staff, 3 TCRs, manual system)

Other employers using manual systems were also concerned about the time needed to manage tax credits. Some also mentioned feeling confused about aspects of PVE or not understanding how to carry out some of the calculations. In these cases employers turned to family members or the Inland Revenue Employers' Tax Credit Helpline for advice.

Overall, level of education combined with training have helped some employers to cope better with managing PVE within a manual payroll system.

#### 4.4 Awareness of Employer Responsibilities for Tax Credits

In most cases, employers are responsible for continuing to pay tax credits during holiday, sickness and maternity leave. Although some employers felt that they were aware of their responsibilities for paying tax credits on these occasions and were able to correctly relate procedures, misunderstandings were quite common. Some employers were genuinely unaware that they were obliged to pay tax credits on top of holiday or sickness pay while a few felt that this was undeserved and claimed that they refused to pay.

##### 4.4.1 Payment of tax credits during maternity leave

None of the employers had any experience of a recipient on maternity leave though a recipient in a large firm was due to go on maternity leave shortly. The employer, in this case, did not know the procedure with regards tax credits and intended to seek help from the Employers' Tax Credit Helpline. In the meantime, he intended to wait and see whether their software will add or deduct the tax credit once they input the relevant information about maternity leave. This employer is not overly concerned as he is confident that he will eventually find the necessary information:

"We'll be very interested to see what our computer does. We'll input the information to say she's starting maternity leave and it might actually have it built into it that it stops paying the Family Credit [WFTC] or carry on paying it. We don't know. It'll be interesting to see what happens...If it's not set up for maternity leave I'll just phone the Helpline." (Helicopter Operator, 800 staff, 1 TCR).

#### 4.4.2 Payment of tax credits during holidays

Some employers were willing to come to an agreement with staff about how tax credits were paid during holidays and took into account the preferences of employees. Employers have a number of options about how tax credits are paid during holiday periods. Tax credits can be paid:

- in advance of holidays
- into bank accounts during holidays.
- on return from holidays.

In one case, an employee asked for the tax credit to be paid weekly over the holiday period rather than in advance to help her manage her domestic budget. This the employer did, though it complicated the payroll calculations. In the end the employee received three separate payments of which two were paid into her bank account while she was away. The employer explains how they managed this:

“Well the two weeks tax credit that she would’ve received she didn’t want. She got this massive payslip with the two weeks pay in advance for her holiday and for the last week she was at work, and three weeks tax credit...She said I don’t want that. And I said well we can pay those two weeks tax credit for you when you are on holiday...So today someone will go round to the bank and pay the second week in for her.” (Children’s activity franchise, 8 staff, 2 TCRs)

Another employer paid staff tax credits by BACS transfer directly into the bank account while the employee was away. This employer would pay for work done in any four week period up to the employee going on holiday, but not in advance, to avoid the risk of people quitting and keeping the money advanced, as this had happened previously.

Other employers were less accommodating, some even going so far as to refuse to pay tax credits during holiday periods. This employer feels that staff do not deserve tax credits on top of holiday or sickness pay and claims that he refuses to pay them:

“Well, it’s very nice for them to have a holiday. But I have to pay it. Now they want tax credit as well. On top of holiday pay. I don’t think so. Nobody pays me all this money. This is coming out of my pocket. I still haven’t had the money back from the Inland Revenue. So I say you’re not having tax credit with holiday pay and sickness pay unless you work. I can’t afford it.” (Residential care, 12 staff, 3 TCRs).

There were other cases of employers who felt that tax credits during holidays or sickness were undeserved, even though they were aware that the money came out of PAYE and NICs. Objections were based partly on the principle and partly the impact on cashflow.

Some employers had no experience of a tax credit recipient being on holiday and did not know what was expected. This employer explains how she would have found it difficult if faced with a recipient on holiday:

“It would have been difficult, I’m sure, if they had gone on holiday ... I don’t know how to calculate it. Really, say she had gone on a month’s holiday and then came back the following month in the period of tax credits. Would I have stopped the payment? Restarted it?”  
(Community Centre and Counselling Service, 7 staff, 1 TCR)

#### 4.4.3 Payment of tax credits during sick leave

Few employers had any direct experience of a tax credit recipient on sickness leave and understanding of their obligations was mixed. Some assumed rightly that the tax credit entitlement would continue while many assumed wrongly that it would not. A few employers mentioned that an employee had reported in sick on the odd day. In the following example the employer explains what happened:

“Yes, I think just the odd day that’s all. We just carried on paying [the tax credits]. I assumed that was what we were supposed to do.”  
(Bookshop, 6 staff, 1 TCR).

In another case the employer was unclear what to do when a tax credit recipient was on long-term sick leave. In the end he rang up the Employers’ Tax Credit Helpline to ask for advice and was surprised when told to continue paying the tax credit:

“I’ve had someone who’s been on the sick while receiving them. I rang up and said what’s the situation regarding this person and they said pay the sick money and the tax credit, and I thought that’s very nice for not doing anything, seeing she had depression and a sick note from the doctor for four or five weeks.” (Sportswear manufacturer, 8 staff, 2 TCRs).

As with the payment of tax credits during holidays, a small number of employers made a moral judgement that tax credits should not be paid during sick leave. This employer uses his own experience of self-employment as a justification for not paying staff for either holidays or sickness:

“I have always worked for my living. I have always been self-employed and nobody ever paid me for being on holiday. Nobody ever paid me when I was off sick – so I wasn’t sick. Simple as that. Why should they get all this money when I have all the responsibility. I’m not paying tax credits, holiday pay, or sickness pay. They get paid when they work the same as me. That’s fair isn’t it?” (Animal Feed Supplier, 6 staff, 2 TCRs)

As fewer employers have had experience of a recipient on sick leave than on holiday there is more confusion and doubt over the correct procedure to follow. Furthermore,

some employers pointed out that they cannot be expected to remember all the details of the legislation and that they are often too busy to look things up.

#### 4.5 Beginning and End of Award

There are several administrative elements to PVE that employers are required to carry out, including setting up procedures for eligible employees and dealing with recipients who leave. In most cases tax credit recipients were existing employees rather than new recruits. Respondents, therefore, had more experience of setting up PVE procedures for existing employees.

Start notifications, issued by the Inland Revenue, stipulate the start and end dates for employers' payments to tax credit recipients; the total amount payable; and a daily rate based on a seven-day cycle. Overall, most respondents thought start notifications were very clear. A few employers remarked that they were an example of how government information has improved in recent years:

“Well, it’s all laid out very straightforward. It’s easy to follow, and in simple language. It’s a great improvement on government forms in the past. They were terrible things that no one could understand. So I’ll say that for them they are a great improvement.” (Nursing Home, 40 staff, 6 TCRs)

There were some criticisms that there was too much information given in the start notifications and that five pages was too long. As well as the start notification there are copies of the Certificate of Payments, which is issued when an employee leaves before the end of the tax credit payment period. This led to confusion in one business when a Certificate of Payments was returned to the Inland Revenue by mistake at the end of a six-month period.

The MD of the company had taken over temporary responsibility for payroll while the payroll manager was absent. The MD was unaware that each six-month award needed a separate start notice so they continued paying tax credits beyond the end date. During the next six months the recipient was paid both by the Inland Revenue and by the business. The payments made by the business were unauthorised and they were unable to recover the money from the employee who had been overpaid. The mistake continued costing the business money they were unable to recover:

“I was away for a week sick and my MD had inadvertently sent back some of the copies which informed the Inland Revenue that we were no longer paying this employee and we were... In an ideal world anyone who hasn’t worked for 4 weeks will have their P45 issued and then the tax credits will be stopped. But in this particular case my MD had sent off the forms and not told anyone. So this lady was getting double credits, and we were unable to claim any of that money back. (Temping agency, 58 Temps, 23 TCRs)

One employer claimed that she only received a start notification the day before the first payment was due (Electronic repair, 4 employees, 1 TCR). Other employers



were given more notice but still felt unprepared as this proprietor of a public house explains:

“It came as a shock all right. I would have liked more to time to study it all. But there was no time because we had to start paying straight away. I just did it and hoped it was right.” (Public House, 8 staff, 1 TCR)

So while many employers found the instructions straightforward there were those who encountered difficulties because of either misunderstandings or what they perceived to be a lack of time to prepare.

Employers are required to issue copies of a Certificate of Payments when a recipient leaves before the final date given on the start notification. This entitles the individual to receive tax credits from another employer or, if unemployed, from the Inland Revenue. Two copies go to the employee, who sends one to the Inland Revenue and one is retained by the employer.

Not many employers had experience of this. However, some of those that did, remembered it as a straightforward process. One employer, in a nursing home, first sought advice from a payroll bureau. He remembers completing the Certificate of Payments and how, because it was the first time he had done it, this was a learning process:

“I spoke to the [payroll] bureau. [Looks for documentation]. There’s a box to tick here, employment ceased. And send it off. I think it was quite straightforward. It’s like anything the first time you do it it’s quite confusing. It’s another complication at the end of each payroll to make sure that you are keeping your tax credit records straight.” (Nursing Home, 40 staff, 6 TCRs)

For others processing a tax credit recipient who left was complicated by software. A payroll manager, in a large firm, encountered errors in the (customised) software programme, which did not recognise a date to stop payments if it occurred other than at the end of a month. When an employee left part way through a month the software calculated the tax credit for the whole month:

“If they were leaving part way through the month, the software would calculate the payment for the whole month. We didn’t notice until after it had happened that the person got the whole tax credit. It would be better if it could recognise a leaving date. It doesn’t actually produce a report to say what’s been paid out so we have written our own report which then allows us to check whether someone is leaving” (Health and Fitness Group, 3,500 staff, 96 TCRs).

There were a small group of employers who were unable to say whether they had correctly completed and distributed Certificates of Payment. Some of this vagueness may be due to attempts to recall past events.

## 4.6 Transition Periods

Currently, transition periods occur every six months. At the end of a six-month payment period recipients must re-apply if they wish to continue to receive tax credits. This process, and in particular its frequency, is a cause of complaint for many employers who perceive it as unnecessary additional bureaucracy.

The frequency of transition periods is perceived to exacerbate problems. A number of employees requested that reassessments be made annually rather than bi-annually. Halting of PVE led some staff to appeal for help from some employers who subsequently found this disconcerting and their own involvement in personal issues inappropriate. Some employers wondered why there were transition periods at all; why not merely continue payments?

Complaints can be divided into two main types. The first concerns the impact on businesses, for instance cashflow problems, resulting from the starting and stopping of payments. The second category comprises complaints from larger businesses about requests for information about wages and hours from the Inland Revenue and of requests from staff for copies of payslips.

Employers' misunderstandings about transition periods were found to have effects on business cashflow. Some employers had calculated additional funding amounts without taking into account transition periods during which no tax credits are paid. These employers were unaware that their responsibilities for paying tax credits ends while re-assessments are made. As a result they claimed too much money from the Inland Revenue. These extra amounts subsequently had to be repaid thus reducing the amount of cash available to the businesses.

One owner of a residential home experienced problems forecasting amounts for additional funding. For this employer, changes in the amount paid out in tax credits also made managing cashflow more difficult:

“I had a bill at the end of the last year for £900. I had done my calculations, as to how much money I would need from the Government, based on the number of staff I had and what their tax credits were. What I failed to take account of was that every six months it stops. So [for] all those weeks I was claiming money that I wasn't paying out.” (Elderly Residential Care, 17 staff, 5 TCRs)

A further issue raised by employers about transition periods relates to the time spent answering queries when providing information for re-assessments. These derive from both staff and the Inland Revenue concerning wages and hours worked. Some respondents, particularly in large firms, expressed concern that this aspect of tax credit administration would greatly increase in the future as tax credits become more popular and widespread in the workforce. It was a particular worry for this payroll manager in a large company that employed many women who worked part-time and were likely to be eligible for tax credits:

“Each time the tax credit is due to finish, before they issue another one, they write to us or the employee passes the form to us. That's fairly

complicated, because they want to know what their deductions were; are they likely to have their hours changed; are they likely to change shifts? Considering we probably get something like 15 forms a month to complete it probably takes someone a good half a day to a day. I think it's likely to become more difficult because the number is going to increase." (Health and Fitness Group, 3,500 staff, 96 TCRs).

Other employers complained generally about the time taken to change tax credit details in their payroll systems every time payments stopped and then started again. There was evident frustration from some employers about what they perceived to be unnecessary breaks in tax credit payments.

#### 4.7 Conclusions

Overall, employers used a range of sources of advice and information about the day-to-day management of PVE and some media were considered more relevant and useful than others. Accountants and payroll software suppliers were some of the more common sources of advice. Inland Revenue sources of advice such as the website, the Helpline and seminars were highly rated though under-used.

Many employers reported that PVE has integrated well with existing payroll systems. Comments were made that PVE was easier to manage than either Statutory Sick Pay or Statutory Maternity Pay. Experiences varied according to the type of payroll system in use and whether this was computerised or manual.

Typically, those using computerised payroll systems perceived that PVE had integrated smoothly because payroll software was pre-programmed to process tax credits. Occasionally, problems arose when software errors occurred. It is clear that some software suppliers are either still unaware of all the details of PVE procedures or else misunderstand what is required. This is likely to be a perennial problem as some future software upgrades may also contain errors.

Some employers prefer to use manual payroll systems in their business and it was here where PVE caused most problems and challenges. Those who coped best with managing PVE put their success down to confidence in their level of education and training. Some felt they had a facility for maths or paperwork. Attendance at Inland Revenue seminars on tax legislation for the self-employed also boosted confidence in some. There were employers who were less confident in their ability to understand and manage PVE while others were concerned about the length of time needed for record keeping.

Although many employers were aware of the correct procedures, a lack of knowledge and misunderstandings about aspects of their responsibilities for paying tax credits during holiday, sickness and maternity leave were fairly widespread.

Misunderstandings also exist in some cases about start notifications and how to deal with leavers. Finally, confusion over transition periods and the accompanying

bureaucracy involved when processing tax credits were a major source of complaint by employers.

## **Chapter Five: Additional Funding**

### **5.1 Introduction**

In order to pay the tax credits employers are able to offset this amount against their monthly PAYE, NICs and student loan repayments to the Inland Revenue. Where the PAYE tax, NICs deductions and student loan deductions are sufficient to cover tax credits payments to staff, employers will not be out of pocket. However, where the monthly payments to the Inland Revenue are less than the tax credits amount, employers may experience a shortfall. In these cases, employers are eligible to apply for additional funding. Additional funding is paid in advance into a nominated employer account so that funds are available to make tax credit payments without causing a cashflow problem.

Payment Via Employer (PVE) is a relatively new mechanism and the additional funding aspect of it is designed to make PVE run smoothly. It was therefore important to assess employers' understanding and experience of additional funding. Employers were asked to discuss:

- where they thought the money came from to pay the tax credits.
- to discuss any experiences of additional funding.
- to dwell on the processes they went through.
- if they had experienced any problems, whether and how these had been overcome.

Shortly after receiving a start notification for the first time, employers are sent two copies of the additional funding application form (TC11). Applications are made for six months at a time and paid in instalments via Automated Credit Transfer. Employers provide details of the business and the recipient; the first and last date funding is needed; the total tax credit to be paid; an estimation of the total amount from PAYE tax and NICs; and the resulting shortfall, which is the amount claimed in additional funding.

This chapter is divided into four sections. Section 5.2 reports on employers' experiences of using additional funding. A review of the role played by accountants in the additional funding process comprises the next section. Section 5.4 examines some of the difficulties encountered in forecasting additional funding requirements.

### **5.2 Experiences of Additional Funding**

All respondents (including those not receiving funding) clearly understood that the money to pay tax credits comes from taxes. None felt that they were personally paying for the tax credits. When talking about where the money came from respondents mentioned, 'my taxes'; 'taxes'; 'PAYE tax and NICs'; and the 'government'.

However, there were quite a few employers who felt that additional funding had cost the business money. Problems were most likely to occur through delays in funding. Misunderstandings among owner managers, bookkeepers and accountants about eligibility criteria and process of applying for additional funding also caused delays.

For some employers applying for additional funding was a fairly straightforward process, though they may have had minor complaints about the paperwork involved in claiming every six months. An owner of a public house describes how the process worked well for her. This employer sought help from the Inland Revenue about how much funding to apply for and was impressed by the accuracy of the forecast:

“I rang them. They said there was a form, it was a T11 or T something, I believe that you fill in, and just send off. So I filled in the form and sent it off telling ... you have to tell them how much your NI is for the month, NI and tax, they then work out what your shortfall will be and pay you. And they got it all basically right. By the time I came to the end of my financial year, all I had was £7 to pay. So, they actually worked it very well, because it's all guess work. We don't know, what your figures [will be] particularly in our trade. You don't know how much tax and NI you are going to pay.” (Public House, 8 staff, 1 TCR)

For other employers the process of additional funding is an area that has caused some of the most serious problems with PVE. In one case delays in receiving funding have cost one employer £2,000 (Box 5.1). This employer felt that claiming additional funding would have been easier initially if the claim form had been included along with the start notification. She was also only informed that she had to pay tax credits one day before the payments were due to start. This short notice, combined with what she perceives to be a lack of information about additional funding, cost the business money. The employer suffered delays in having her application for additional funding processed. This issue had still not been resolved at the time of the interview, and the employer calculates that she is owed £2,000 by the Inland Revenue for payments already made and that she owes between £4-500 for tax payments not yet made.

*Box 5.1 Electronic sale and repair.*

This business is involved in the sale, installation and repair of TVs, videos and digital satellites. The business employs two partners (husband and wife), one full-time member of staff and one part-time administrator who is also the tax credit recipient. The problems began when the employer was given only one day's notice to start paying tax credits. Problems were compounded by delays in additional funding. The partner feels that applying for funding would have been easier if she had received the appropriate forms sooner:

*"But, you see, to me, if they'd put the funding and everything in one envelope and given you everything - the whole kit-and-caboodle - to me, that would have been far easier. We've actually had a phone call this morning because we are now owed £2000. That's what we've paid. And we have been ringing them up, we've sent all the paperwork in which was done end of December, beginning of January, like over the holidays we got it all filled in, and we are still waiting now [June]."*

Delays occurred because the Inland Revenue had no record of the additional funding form that the employer remembers sending to them. She has since completed and sent off another form but with the same result:

*"We heard nothing back the first time and when we rang them up - it was about 6 weeks after, because we didn't know how long it was supposed to take - we actually rang them up and they said "oh we've got nothing. We will send you out another form". Which [they] did. [We] immediately did that one, sent it back, left it another 5 or 6 weeks, and then I think when we actually rang, when she said they didn't have one, we just started laughing and said "no, taking the mick you know"...."*

They have not paid recent PAYE tax and NICs owed for the full-time member of staff. The Inland Revenue contacted her about this and she again complained about the delay receiving additional funding for the tax credit:

*"I mean, they actually rang us up this morning and said "were you behind in paying the income tax for him?" And I said "well, you're behind paying us for family funding thing, which is like nearly two grand. We probably owe you about £400/ £500 at the most".*

She hoped to get the funding issue resolved because potentially the tax credits will cancel out PAYE tax and NICs payments, which would be a benefit to the business.

*And he said "alright, come in on Thursday and we'll get this sorted out once and for all". So I'm actually going in on Thursday with the intention of not leaving until it's sorted. In the end it could make life easier for us. It could cancel out the monthly tax bill. Anything that makes doing the paperwork easier is a godsend."*

Potentially this employer feels that the new system of tax credits might make things easier for her (assuming payments owed to her are settled and additional funding is received in time in future). Her perception is that the benefit would be not in having to make any payments to the Inland Revenue at all. Tax credits exceed the amount she

pays in PAYE tax and NICs so potentially she need not have to make payments in future.

#### 5.4 Role of Accountants in Additional Funding

In some cases, where firms use an accountant, problems have arisen either, as a result of having another person in the chain of correspondence with the Inland Revenue about funding, or from the accountants' own lack of knowledge about how additional funding actually works. Some of the employers' interviewed reported being out of pocket because of failure to act by their accountants. In other cases, working on advice from their accountant, employers may be eligible for additional funding but have not applied.

Some accountants are either not taking sufficient notice of procedural instructions or are unaware of the provision of advanced funding altogether. In one case the accountant wrongly advised his client, that a claim for additional funding could only be made once the end of year returns are made:

“Well my accountant has told me I need to send off the P35 (end of year tax return). And then I can claim back the £2,900 that they owe me in tax credits. I didn't know how it all worked out until the accountant said, Oh by the way, the tax owes you £2,900.” (Animal Feed Supplier, 6 staff, 2 TCRs)

One of the main issues seems to be that lines of responsibility for the tax credits, and in particular additional funding, are often blurred between the accountant and the employer. In this case, the employer explains that delays in receiving funding occurred because his accountant did not give him the assistance he wanted. This appears to have been caused, at least in part, by a lack of clarity about who has responsibility for applying for additional funding. Though, on the one hand, the employer complains about what he perceives as the lack of help and poor service from his accountant, on the other hand, he is concerned about what the accountant charges for his time. Here, the employer explains what happened:

“They are paying us through direct debit, but there is a lot of paperwork, and the accountant won't come and help me sign the papers. We pay a month's wages to people, £1,000 a month and two months tax credits. We pay that and interest on the overdraft ... We've already paid last months wages and now they are due again next week and the money still hasn't come. The problem is we didn't send the paperwork in time. So they don't pay. I signed it and sent it to the accountant, but he's late. So, I'm out of pocket. And he charges £60 an hour.” (Residential care, 12 staff, 3 TCRs)

In the next example, lack of clarity about lines of responsibility between the accountant and the employer also resulted in delays (Box 5.2). The employer initially handed over responsibility for the tax credits to her accountant. This worked fine for the first six months until after the transition period when instructions for the next tax credit period were sent directly to her. On this occasion, the employer confused the additional funding application form with the Certificates of Payment and so did not



apply for additional funding. She also believed she was misled because on the previous occasion her accountant had applied for funding on her behalf and she assumed that he would do so again.

*Box 5.2 Public House.*

This business is a public house in the North East with 3 full-time staff (including the owner). There is one part-time employee who works for 16 hours per week and is also the tax credit recipient. This employer explains that she immediately sent the start notification to her accountant to deal with. He applied for additional funding and for the first six months things went smoothly. However, during the second payment period she realised that she had not received any additional funding.

*“The first time I got funding, the accountant saw to it all for us. But the second time I didn’t realise you’ve got like three forms and one of them is to sign and send back. Then I looked at my bank statement and I thought her money’s not going in so I told the accountant and he said have you not got the form?”*

When trying to sort things out with her accountant it appears that she confused the Certificate of Payments with the additional funding form (T11):

*“I tried to read them but I couldn’t understand them. I was mystified, so I sent them to the accountant and said I can’t understand this. He said it’s a reply to a tax credit and should have been sent in as soon as you got it. I don’t know, all I understood it had a certificate on it to keep in a safe place and it must be signed if ever she [tax credit recipient] leaves employment and that’s all it had on it. It says keep this form safe.”*

Whether this employer had received an additional funding form (T11) or not is not clear. In any case, if she did receive a T11 form she obviously did not realise what it was. As a result, funding was not paid and the employer, though out of pocket, was unaware of this for the whole six months:

*“I’ve been paying the tax credit and I’ve never been getting it back so I explained to the accountant and he’s sent the forms off. He’s done everything for us and normally they’ve sent everything to him. But they sent them to me and I didn’t know what to do with them, so he’s sorted it out and says I should get the money shortly.”*

This employer, though not particularly comfortable dealing with the tax credits has decided to take more responsibility for the wages in future rather than leaving everything for her accountant to do:

*“Bookwork is not my greatest thing. I hate it but I’m gradually now getting into it you know. I’ve started doing my weekly sheet now every week. I sat with the accountant and went through it and now I do it myself.”*

## 5.5 Forecasting Additional Funding Requirements

Making estimations about future working hours was a particular problem for businesses that operate variable working hours. A high variation in working hours

was caused by combinations of part-time, temporary and casual labour. Variable and/or unpredictable demand for labour stemmed from an unstable business environment. In one of the care homes, the owner manager spent a lot of time adjusting the amounts of advanced funding he would need to fit in with staff changes (Box 5.3). Even so, he still ended up having to pay money back because his original estimations proved inaccurate due to changing circumstances.

**Box 5.3**      *Residential Care Home for the Elderly.*

This business is a residential care home for the elderly and employs 16 part-time members of staff plus the owner and his son. There are currently five tax credit recipients though the number fluctuates frequently. The business uses a software payroll system specifically designed for nursing homes. The main impact of PVE on the business has been the difficulties of forecasting additional funding requirements based on unpredictable working patterns. To date estimates have had to be updated at least six times because the amount people receive in tax credits may go up or down thus affecting the amount needed in funding:

*“Having to work out what we thought our expenditures were going to be, what we thought the amount of tax credits was going to be and I’ve had to update that quite a few times really. Several times, in fact, about six or seven times now. People change around so much and the tax credits themselves have changed. So I have to fill in the forms all over again and send it off and then there is a shortfall of a few weeks till that kicks in. So it is a bit awkward...I can’t fix exactly what the payments are going to be, how much I’ve got coming in and going out.”*

Having to project funding needs six months in advance is particularly difficult. This employer would prefer to work on a monthly funding basis as the tax credit payment periods are different for each recipient and when one ends it affects funding needs:

*“Every time somebody’s tax credits go up or down I have then got to project it for everybody over the next six months. So one way it could be easier than it is if they ask us to project it over the next month. I wouldn’t mind if I had to send a form in every month as long as I knew it was correct. It is the fact that I am having to project it so far ahead the figures become meaningless when it is for 6 months into the future. Once you have got it working for somebody it is not the case that it divides up into the 26 weeks, is it variable from week to week the tax credit element.”*

Like others, this employer felt that money lost in this way translated into reduced services for the residents:

*“Whatever is left over gets spent on the residents here, trips out, getting entertainers in that sort of thing. When you are looking at a £900 bill [overpaid additional funding] that all stops for a month until things get sorted out. So it would have affected them [the residents] more than anything else. It would have been different if I was ... a business and I could have increased my overheads, and decreased my profits somewhere, or charged them more over a certain period of time, but I am constrained by what I can charge. That means that services, basically have to be cut in order to make up any extra cash.”*

Two large cleaning companies also experienced problems calculating additional funding requirements because of variable working hours and a high turnover of staff. There is a perception by one of these employers that the situation will worsen as more people apply for tax credits. As he explained:

“It’s just a problem trying to figure out what you need. It’s a guesstimate, pick a figure, because you can guarantee it’s going to change...If we get more of them [tax credit recipients] then it’s going to be a nightmare.” (Cleaning Company, 200 staff, 7 TCRs at time of interview, though fluctuates)

Another employer in a similar business described how tax credit payments regularly exceed PAYE collected. She suggested that PAYE might be around £600-700 per month while tax credit payments might be £2,500. This employer was late applying for additional funding and she estimates she was owed £3,000 by the Inland Revenue before she received any additional funding. She also resents the time needed to fill in the application forms and working out how much is required. It is difficult to estimate how much funding is needed because staff leave and others start so both PAYE and tax credits vary constantly. She periodically re-applies for funding. As she explains:

“I can’t see any easy way round it because you’ve got to be able to estimate what your Pay-As-You-Earn is going to be for the next few months. This fluctuates here, because people don’t always earn the same amount of money every month because one month you’ll have more work than another month.” (Cleaning Company, 80 staff, 4 TCRs)

When asked how the advanced funding process could be improved this employer emphasised more detailed help from the Employers’ Tax Credit Helpline. In fact, what this employer wants is actual advice on what to claim and how to best make a claim to minimise the negative impacts on her business, instead of advice and information:

“If there was somebody on the other end [of the telephone] who could actually work it out as well who, I wouldn’t actually mind somebody ringing me to say that you are overpaid by about £30 a week, do you mind sending another? ...Or they said look you are not claiming enough I think we need to review it. It would be nice to know that there was somebody actually checking it. So that would be good if there was a reviewer.” (Cleaning Company, 80 staff, 4 TCRs)

## 5.6 Conclusions

This chapter has presented evidence on one of the more problematic areas of PVE, applying for additional funding. The provision of more advice and consultancy, when making applications for advanced funding, would probably have helped many of the respondents who experienced problems with this. Accountants are amongst the most popular sources of advice and external services for small firms. It is clear that many employers are, on the one hand, relying on their accountants to alert them to any

difficulties in relation to tax credits, while on the other hand they are also wary of increasing their accountancy bills.

This means that employers are, therefore, unlikely to encourage their accountants to pro-actively seek to do more work on their behalf. This has resulted in confusion, in some businesses, about who bears responsibility for managing the tax credits, and in particular for applying for additional funding. The role played by accountants is clearly a contributing factor in the kinds of problems with advanced funding reported by some employers.

The other major source of quite serious problems with additional funding stems from the unpredictable and variable working hours common in some businesses. The variable working patterns of often part-time jobs make it difficult for employers to estimate how much they need in additional funding. This is because monthly payments of PAYE tax and NICs vary as accumulated hours go up and down.

## **Chapter Six: Employment Issues and Relations in the Workplace**

### **6.1 Introduction**

This Chapter examines some of the effects of the tax credits on employment recruitment, retention, working hours and relations in the enterprise. One of the wider aims of the tax credits is to encourage more people, particularly parents with children and people with disabilities, to take up paid employment, by making work pay. The payment of tax credits through the employer was designed to help forge a link in people's minds between work and financial incentives. Consequently, one of the aims of this study was to gather information about any impacts tax credits might be having on recruitment as well as any other wider effects on employment issues.

The interviews allowed employers to discuss the effects of tax credits on related employment issues including the allocation of working hours; managing employees; and staff motivation and morale. Where any of these issues were reported to have been affected by tax credits, employers were invited to reflect on the nature of the impact and whether they considered the effects would be short-term or long-term and positive and/or negative. Employers were also encouraged to share solutions to any problems they had encountered and how they were adapting to any changes generally.

Section 6.2 looks at the impact of tax credits on staff motivation and the retention of staff. The impact of tax credits on the allocation of working hours is reviewed in section three. Section 6.4 examines any effects on current and future recruitment practices. The final section comprises an analysis of employment relations in the workplace.

### **6.2 Motivation and Retention of Staff**

Some respondents felt that the additional income provided through tax credits had helped some of their staff stay in work who might otherwise have been forced to leave and apply for benefits instead. A clothing manufacturer explained that, though he preferred to employ full-time staff, he has the capacity for some (efficient and hard-working) part-time staff. Tax credits have enabled him to retain a valued part-time employee who otherwise would have left because of the low wages she was receiving prior to the introduction of tax credits:

“My main aim is to employ full time staff. But there is always a place for a few part-time staff. And now if I get someone good, I had one young woman, but she wasn't earning very much. And then the tax credit, she heard about it and said can I have this? I said of course, if it means you can keep working. So she did. Some people can come to work and do only 6 hours work in 8 hours. But she comes to work and does 10 hours in only 5 so it is well worth it. She is very, very good.”  
(Clothing manufacturer, 15 staff, 3 TCRs)

Generally, this was one of the main positive impacts of the tax credits. It was more common that tax credits were an incentive to retain existing staff rather than act as an encouragement to new recruits. As reported by one employer, the provision of the tax

credits also has the potential to help fathers in low-paid jobs, both by boosting their income and improving their morale. This employer expressed approval that his sole employee now receives a tax credit, which he feels is deserved:

“Yes, it just takes the pressure off doesn’t it. He has more money in his pocket and at the end of the day he is going to make a bit more out of his wage. I think he is probably happier coming in every week, you know, he’s more contented with his lot. It makes it worth his while.”  
(Toolshop, 1 staff, 1 TCR)

In contrast to these positive stories one employer blames the provision of the tax credits for losing a member of staff. The employee concerned told her employer that she was leaving her job because her husband was claiming tax credits. The employer explains how the couple had worked out that the tax credit could replace the wife’s earnings thus enabling her to stop working and stay at home to look after their children:

“I did lose a member of staff because she was entitled to Working Families Tax Credit. Her partner applied for it. She was pregnant so she was leaving anyway. She left us about 2 months earlier than she would have done. She left us high and dry. And she said “we’ve been given this and I can stop working”... ‘he is entitled to get it, so I’m going to pack my job in because what he’s going to get Working Families Tax Credit is virtually what I’m earning from you’.(Children’s activity franchise, 8 staff, 2 TCRs)

There was only one incident of this kind reported by respondents but it shows the potential for tax credits to act as a disincentive to work. On the other hand, it could be argued that the provision of tax credits gives more choice to couples as it enables one partner to remain at home and look after young children instead of having to go out to work for financial reasons.

### 6.3 Working Hours

The allocation of working hours is another issue where the intervention of the tax credits was perceived by employers to have both negative and positive consequences for their businesses. To be eligible to receive tax credits employees must be working at least 16 hours, though the hours may be made up by different part-time jobs and need not all be with the same employer.

On the negative side, employers have found that employees demands for a strict adherence to a 16 hour working week to ensure, what they perceive as their entitlement to a certain level of tax credits, has led to inflexibility in the number of hours worked. This effect was particularly evident in businesses that relied on part-time staff. This employer describes his experience of this inflexibility and what he perceives as the ‘extra hassle’ involved if he wanted to change a tax credit recipient’s hours:

“The only fiddly thing for me is to make sure that they only do so many hours. If I wanted somebody to work extra, it’s very strict on

how much they are allowed to earn. So it means that if someone is sick or something I can't really draw on anyone else. So it's a bit inflexible because it is very strict, there is too much hassle to change them. It's best to just leave it and say that's your job and just leave it." (Tack Shop and Animal Feed Supplier, 5 staff, 2 TCRs)

One owner of a cleaning company that provides a service to commercial premises and private homes, has experienced problems with staff who refuse to work more or less than 16 hours. They want to work at least 16 hours to qualify for tax credits but not more because of a perception that they would experience a reduction in tax credit payments.

There is also a perception by employers that staff would rather work the minimum number of hours to qualify for tax credits than earn more in wages through working longer hours. As this employer explains:

"The other irritating thing is I've got people who are working 16 hours and sticking to 16 hours and there's no earthly reason why they couldn't do 24 or 30 hours. But they can't because then they would be worse off. So there's no encouragement to get them off the 16 hours because they are getting all this other money for not working the additional hours." (Cleaning Company, 80 staff, 4 TCRs)

Respondents in residential homes have found, increasingly, that their staff specifically request to work only 16 hours so that they qualify for, what they perceive to be, the maximum entitlement of tax credits. This owner of a residential care home explains how he is unable to fill a vacancy at present:

"People ring up and ask how many hours are available and tell us that they need to work 16 hours, no more and no less. That has become a big constraint. Everyone is obsessed with the 16 hours, it makes them eligible for tax credits. I haven't got it, so at the minute I have empty place, a staff place and that is being filled by other members of staff simply because I don't have this magic 16 hours to offer. It is the nature of the care work – that's women who are predominantly at home with family. So I imagine everyone coming in now will be on tax credits and want a certain number hours a week in order to have their benefits." (Residential Home, 17 staff, 5 TCRs)

Some businesses have found that it is a bonus being able to offer staff 16 hours and thereby secure their entitlement to additional income through tax credits. Here, positions are predominantly part-time and filled by women. This employer explains the impact of the tax credits on existing staff:

"Well, we only want them to work 16 hours so it's a real bonus being able to offer the tax credits on top of what we normally pay anyway." (After School Club, 8 employees, 2 TCRs)

Overall, the analysis has shown that the effect of the tax credits on working hours can be quite complex. The effect seems to depend on the nature and requirements of the business and the needs of employees and on their understanding of tax credits. Some businesses want part-time staff who can work more when needed. This causes problems for recipients who do not want to have their tax credit amount cut and who do not want to work more than 16 hours per week. This then causes difficulties for employers who need staff to be flexible.

## 6.4 Recruitment

The study revealed both negative and positive consequences on recruitment for different types of businesses. Employers thought they would be able to recruit better qualified core staff in the future by being able to offer higher wages through the addition of the tax credits. This was particularly so for childcare related businesses that attract women returners. Tax credits also had a positive impact in the recruitment of new trainees. On the negative side, some employers were deterred from recruiting tax credit recipients.

### 6.4.1 Impact of the tax credits on new recruits and training

Few of the employers had taken on new recruits who were eligible for tax credits. In one business, that did take on a new member of staff, the employer was able to guarantee stable working hours to ensure a fixed level of income from the tax credits, and thus reassure the employee:

“She was quite new to us – and she wanted to know her hours would be stable, because we had swapped her days around. So she wanted me to guarantee that she would be working x number of hours or so many days a week. I said, “ that’s not a problem, that’s what we’ve agreed and that’s what we’ll do... She wanted to be sure she had the same amount of money coming in” (Children’s Activity Franchise, 8 staff, 2 TCRs)

Other employers were able to provide training for new recruits with the aid of tax credits. In the past the low wages paid to trainees was perceived to adversely affect the quality of candidates applying for training posts. One employer took on two single mothers through a restart programme. One of them, who has received office training, has turned out to be satisfactory and has been kept on by the business:

“When I took them on they were on a restart sort of programme. They were both single mothers that is one of the criteria for this scheme. They both claimed the tax credit when they started. One of them left. The other one ... we took her on office training and we took her on a trial and after the initial trial we decided that she was quite reasonable worker and she is quite good – she is still with us and she does the job we ask her to do.” (Fruit and Vegetable Supplier, 30 staff, 2 TCRs)

Another employer found that the additional cash provided through the tax credits was an incentive for training a new member of staff recruited through New Deal, who would otherwise have been on a very low income and may not have been able to



afford to work. The employer believes that in future recruitment for these training positions, will be made easier by being able to offer tax credits:

“We actually took her on through a package called New Deal. She wouldn’t have been able to survive on that package without the tax credits. She wouldn’t be working here now if it wasn’t for the tax credit. Someone who has turned out to be a good trainee for us but it wouldn’t have happened without the tax credit. She wouldn’t have been able to afford to work here she has got three kiddies, a house to run she couldn’t have done it on what we can afford to pay a trainee.” (Debt Collection Agency, 14 employees, 1 TCR)

In short, the study found that tax credits had some positive training effects in these businesses.

#### 6.4.2 Positive impacts of tax credits on future recruitment

The positive effects of the tax credits in the form of enabling recruitment were less tangible than the effects of retention. However, a number of employers were able to articulate potential effects in the form of opening up opportunities to a wider range of possible recruits.

One employer felt that the wages for part-time workers is not sufficient for many families. Therefore the extra income provided by the tax credits will provide a top-up which she feels should help future recruitment by attracting better qualified staff. Although she has no experience of this yet she explains why she is anticipating a future benefit:

“I think it will make a big difference, because especially for women returners. Our after school club is only open 16 hours a week. If you are a single parent it is not enough to get you off benefits really. So that top up of the family credit [WTFEC] it does make a difference, it gives a full wage for that introductory period when people tend to move on to full time employment. It does help us, it’s useful because we can only offer part-time work and it’s not enough for families to live on. In future, we can say to people okay this is the wages, but on top you will get the tax credit. So, the better qualified will be more likely now to accept.” (After School Club, 8 staff, 2 TCRs)

Respondents in childcare related businesses anticipated that the tax credits will have an impact on the recruitment of their core staff. Respondents in a range of other businesses anticipated an impact on peripheral staff. A number of businesses, from a variety of sectors, attributed better recruitment prospects to the ability to offer better wages to future administrative and secretarial staff.

This respondent, a payroll manager from a manufacturing firm in the Midlands, thinks that tax credits have the potential to make a difference to future recruitment. But like a number of other respondents she is uncertain about the firm’s legal status in advertising the tax credits and discussing them during recruitment interviews. Here, this payroll manager sums up this dilemma:

“Yes I think [the tax credits] would definitely make a difference. We could attract a much better educated sort of person. As long as people are aware of it. I don’t quite know where our responsibility lies, if you are allowed to interview people and say well, because of your circumstances you would be able to claim this [tax credits]. I mean are we supposed to push that or is it up to them to claim? I’m not quite sure where the legislation is. Neither is the recruitment manager, he does all the interviews. I don’t know, I will have to look into that.” (Manufacturing firm, 9 staff, 1TCR)

#### 6.4.3 Negative impact of the tax credits on future recruitment practices

A few business owners felt that the introduction of tax credits will affect their recruitment policy negatively. These views were based on previous experience with tax credits. Their negative experiences so far have led them to want to avoid recruiting potential future tax credit recipients. Some of the problems they have incurred relate to the extra paperwork involved, delays with additional funding but most seriously the perceived inflexibility in working hours.

One employer stated that he has had problems recruiting staff prepared to work for less than 16 hours because they want to receive tax credits on top of their wages. An owner manager of a convenience store would rather not get involved with tax credits in future because of the impact of additional funding on his cashflow, the added paperwork and the lack of inflexibility in working hours by staff. He has recently taken on two members of staff but employed them both deliberately for less than the qualifying 16 hours. As he explains, his previous experience with tax credit recipients has led him to this conclusion:

“I only employ part-timers, and it makes me think twice about getting involved in tax credits. Then there is the extra work. I came to the conclusion a while ago. I took two girls on but I said only 15 hours for one and ten for the other, no more I said, that’s it. My staff do not pay enough in tax and NI contributions so I have to apply for additional funding. It is a lot of work, all the form filling, and then the hours are set for the next six months, that’s no good to me. They have to be flexible.” (Convenience Store, 6 staff, 2 TCRs)

Employers in other businesses also claimed a reluctance to employ tax credit recipients in future. For employers who need staff to be prepared to work flexible hours, tax credits are perceived to be a disincentive to employee flexibility. For some this has caused them to reconsider employing anyone eligible for tax credits in future. This owner, of a residential care home, sums up these concerns:

“In fact, if there were two people presenting themselves [for interview] ...If they were both equally qualified then that [eligibility for tax credits] would be a deciding factor. I need somebody who has got the flexibility. These people [tax credit recipients] don't. I need somebody who can work a few hours and then more the next week. It is hard for

them. They have got their hands tied.” (Residential care home, 17 staff, 5 TCRs)

The impact of the tax credits on recruitment, therefore, appears to vary, often depending on the type of working hours required by the businesses concerned. One owner manager has been unable to advertise jobs in the local job centre because they claim it is not worth while advertising a job of less than 16 hours. She is therefore now using word of mouth for recruitment because of these difficulties with job centres:

“Recruitment is now more difficult – we now specify ‘16 hours available’ in Job Centre adverts. Job Centres won’t advertise jobs now if they are only two to three hours. That’s having a profound effect.” (Cleaning Company, 80 staff, 4 TCRs)

## 6.5 Employer/employee Relations

Several employers mentioned the effects that the tax credits were having on pay between staff doing similar work and on differentials between staff and managers. It was felt by some that the concept of “an equal day’s pay for an equal day’s work” was being undermined by tax credit payments, which upset this balance.

There appears to be a great deal of openness in some small firms about tax credits. It is often common knowledge who is receiving tax credits and sometimes how much they receive, which can fuel perceptions about disparities in pay. The disparities in pay are perceived to exist between employees doing similar work. A book-keeper described how she thinks some employees feel about these disparities in pay:

“Well, I think some of the girls think it is unfair. They say well I am doing the same work as her [the tax credit recipient] but she is getting paid more than us. It’s just difficult to explain it to them, that the extra money is not really wages but a benefit. (Travel Agent and tour operator, 21 staff, 3 TCRs,)

In some firms tax credits were also perceived to erode the pay differentials that exist between staff and managers. In one business, the employer described how one of his drivers, who receives tax credits, earns nearly the same amount when the tax credit is included, as a manager earns. The employer explains how he feels this is unfair and how the manager also perceives the reduction in pay differential as unfair:

“I’ve got a manager who takes home £300 a week. Now this driver [the tax credit recipient], isn’t too far short of that. Now do you think that’s right?.. That manager has got himself a good education, is hardworking and honest, finds that someone who is just a normal driver is taking about the same amount of money home as he is. That’s not fair. He doesn’t think it’s fair I can tell you.” (Drinks wholesaler, 10 staff, 1TCR)

## 6.6 Conclusions

The extra income provided through the tax credits has enabled employers to retain valuable members of staff who may otherwise have left. The boost to income from the tax credits has also had a positive impact on the morale of tax credit recipients at work. However, the 16 hour qualifying criterion for the tax credits has had a mixed effect on these firms. In some businesses, where hours are low and relatively stable, the provision of tax credits is viewed by employers as a bonus.

In other businesses, where working hours are often changeable, the 16 hours criterion has proved to create problems, particularly as a barrier to labour force flexibility. There is a perception by these employers that their staff would rather work the minimum number of hours needed to qualify for tax credits than work longer hours. This decision may be driven by family commitments which require staff to be at home.

Recruitment has been helped in a few businesses by the additional income provided by the tax credits. Training new recruits can be made easier through the additional income provided by tax credits. Some businesses have found that the top-up to wages provided by tax credits has helped them recruit staff into low-paid jobs.

However, some employers were prepared to avoid recruiting tax credit recipients in future. The combination of problems forecasting additional funding and an unwillingness by staff to work inconsistent hours has led these employers to decide not to recruit tax credit recipients in future. This particularly affects businesses that employ mainly part-time staff.

Finally, some employers perceived that tax credits were causing difficulties with workplace relations. In some cases, employers felt that it was unfair that tax credit recipients received more in their take home pay than colleagues doing similar work. Employers also felt that the additional income provided by the tax credits was perceived to erode the differentials in pay between managers and semi-skilled staff. In both these cases employers also felt that other staff were unhappy about this aspect of the tax credits.

## Chapter Seven: Conclusions

This report has sought to present the results of a qualitative study of employers' views and experiences of tax credits.

- 7.1 The attitudes of employers towards tax credits and PVE were complex. As citizens, employers may hold positive views about the principles behind tax credits but as employers they may hold different views. Employers' attitudes can also be influenced by their experiences of paying tax credits, applying for additional funding, and the impact of tax credits on recruitment. When these factors have had either a positive or neutral impact then the introduction and day-to-day management of PVE tended to go smoothly and employers were more likely to accept PVE. Where any of these factors have had an adverse impact, employers are more likely to express negative views.
- 7.2 Most employers were aware that a media campaign about tax credits had taken place during 2000. The best remembered source of initial information was the Inland Revenue video. However, the research identified a lack of awareness among employers about the policy reforms of the tax and benefit systems and the accompanying shift of responsibility from the DSS (now the Department for Work and Pensions) to the Inland Revenue. Accountants and payroll software suppliers were the main sources of information and advice for some employers.
- 7.3 Inland Revenue provides a range of services and advice to businesses but the research suggests that these are often under-used. The helpful manner of the helpline staff was commented upon by several employers. However, many were unaware of this facility. The Inland Revenue website is even less well used than the helpline, though described by those who have used it as a comprehensive source of easily accessible information. Inland Revenue seminars on tax legislation imparted both knowledge and confidence to the people that attended them.
- 7.4 Employers' experiences of introducing PVE into businesses, the day-to-day management of PVE and sources of advice and information were influenced by the type of payroll system they used. In-house payroll systems were either manual or computerised. Where manual systems were used, these tended to be in the smaller firms. In some cases payrolls were externally managed by accountants or payroll bureaux. Although off-the-shelf software was popular amongst all smaller firms, the larger firms were also using bespoke software packages.
- 7.5 Some employers passed responsibility for PVE to external agents. The peace of mind, achieved by delegating to what many perceived as "the experts", was deemed worth the extra cost. Indeed, for many employers the introduction and day-to-day management of PVE was little trouble because they were handled by others. Lack of knowledge about aspects of PVE, by some accountants, did lead to problems for some businesses. The most serious problems occurred when applying, and neglecting to apply, for additional funding.

- 7.6 The use of payroll software eased the introduction and day-to-day management of PVE in many businesses. Information and advice, including software telephone helplines, formed part of the payroll software packages to businesses, making payroll software an effective vehicle for the successful management of PVE. In a few cases, bugs were discovered in the software, which caused delays and difficulties in integrating PVE with PAYE systems. Problems were more likely to occur with bespoke software packages, used in the larger firms.
- 7.7 Some employers, particularly in smaller firms, continued to use manual payroll systems for various reasons including for flexibility in cash-based businesses, and the personal preferences of owner-managers. Some of these employers encountered no difficulties either introducing PVE, or its day-to-day management. They had confidence in their level of education and training and their ability with mathematics and paper work. Those who were less confident found the task of understanding and setting up PVE more onerous. These employers were also more likely to encounter difficulties in the day-to-day management of PVE and spend more time on this task.
- 7.8 The study found that the need for additional funding and associated processes created some of the worst problems for businesses. Unexplained delays in assessing and receiving funding was one of the main problems reported by employers. Lack of knowledge, or inaction, on the part of accountants was another common problem. These two problems are potentially resolvable, but unpredictable working patterns pose a more serious problem to employers when they are making forecasts about additional funding needs. Making estimations about future working hours was especially difficult for businesses dominated by part-time workers and with unpredictable work patterns.
- 7.9 Where businesses had encountered problems with tax credits, whether through additional funding or because of inflexible attitudes by staff towards their working hours, this was likely to generate subsequent negative views by employers. As a result, some employers expressed a reluctance towards recruiting tax credit recipients in future. In some businesses, on the other hand, the tax credits have had a positive impact on existing employees and on the future prospects for recruitment.

## Appendix A

### Methodology and Sample

Firms were selected from a sample database of 2,000 firms involved with tax credits, supplied by the Inland Revenue. Firms were selected on the basis of three main dimensions. These were region, size and receipt/non-receipt of additional funding. The regions selected and size bands used were:

<u>Regions</u>	<u>Size Bands</u>
North East	1-4
South East	5-9
London	10-49
Midlands	>50

Potential respondents were sent a letter, addressed to a named individual, usually the managing director, describing the research and an opt-out form and SAE. Employers were given the opportunity to opt out of the study by completing and returning this opt-out form.

The first stage of the research was a pilot study carried out in the London area, with six employers, during the Spring of 2001. This stage resulted in one third of employers opting out of the study. The interview schedule was tested and found to be a satisfactory qualitative research instrument for eliciting suitable responses from employers. During the main stage of the research a similar proportion of one third of employers also opted out of the study. After the opt-out phase potential respondents were telephoned to arrange an appointment and confirm business details. During this process almost one fifth of employers declined to participate.

### Additional Funding

Small firms are more likely to receive funding, while those in the South are less likely to receive it than firms in the North. In the main database firms in the North East are most likely to receive funding. In our sample an equal number of firms from the Midlands and the North East have received additional funding. (Table 1).

Table 1 Additional Funding by size of firm

<b>Size Band (number of staff)</b>	<b>London</b>	<b>South East</b>	<b>Midlands</b>	<b>North East</b>	<b>Total</b>
1-4	0	1	3	3	7
5-9	1	2	2	1	6
10-50	1	0	1	1	3
>50	1	0	0	1	2
<b>Total</b>	<b>3</b>	<b>3</b>	<b>6</b>	<b>6</b>	<b>18</b>

Main Characteristics of Businesses

Table 2 North East Interviews

<b>Size Band</b>	<b>Activity</b>	<b>Funding</b>
1	Public House	Yes
1	Electronic retail, installation & repair	Yes
1	Events organiser (conferences, exhibitions)	No
1	Steel distributor	No
1	Software consultancy	Yes
2	Public House (same owner)	Yes
2	Accountant	No
2	Clothing manufacturer	No
2	Child playgroup service	Yes
3	Cheese manufacturer	No
3	Care home for the elderly	Yes
3	Convenience store	No
4	House-cleaning service	Yes

(Size bands: 1= 1-4, 2= 5-9, 3= 10-49, 4= >50)



Table 3 South East Interviews

Size Band	Activity	Funding
1	Tool Merchants	No
1	Estate agents	No
2	Accountants	No
1	Public House	Yes
3	Drinks Wholesaler	No
1	Newsagents/grocers	Yes
2	Public House	Yes
2	Public House	Yes
3	Paper Products Manufacturer	No
3	Nursing Home	No
3	Fruit and Vegetable wholesaler	No
4	Timber Products	No
4	Helicopter operators	No

(Size bands: 1= 1-4, 2= 5-9, 3= 10-49, 4= >50)

Table 4 Midland Interviews

Size Band	Activity	Funding
1	Greengrocers	Yes
2	After school club	Yes
1	Electrical engineering design and development	Yes
1	Occupational health auditors	Yes
2	Clothes manufacturer	No
2	Convenience store	Yes
2	Second hand furniture (charity)	No
3	Residential home for people with learning disabilities	Yes
3	Manufacturer of conveyor systems	No
3	Electronic engineering	No
4	Manufacturer of military accessories (e.g. medals)	No
3	Quantity Surveyors	No

(Size bands: 1= 1-4, 2= 5-9, 3= 10-49, 4= >50)

Table 4 London Interviews

Size Band	Type of Business	Funding
1	Animal feed supplier and tack shop	No
2	Bookshop	Yes
1	Property management	No
2	Mortgage Brokers	No
2	Travel Agent	No
2	Travel agency and tour operator	No
4	Temping agency for telephonists and receptionists	No
3	Debt Collection Agency	No
3	Family Centre (charity)	Yes
3	Prepared fruit and vegetable supplier	No
3	Retail Bathrooms	No
4	Cleaning contractors	Yes
4	Leisure Group	No

(Size bands: 1= 1-4, 2= 5-9, 3= 10-49, 4= >50)

## Tax Credits Research Study

**Employers Interview Guide**Introduction

*Thank you very much for agreeing to take part in this important study. The Small Business Research Centre (SBRC) at Kingston University is conducting research into the tax credits system on behalf of the Inland Revenue. Last year employers became responsible for paying Tax Credits directly to eligible employees. The Inland Revenue wants to find out how this change is affecting employers. All your responses in this discussion will be held in strict confidence by researchers working on the project.*

*We are interested in your experiences with tax credits. I'm not an expert on the tax credit system but I have some information I can leave with you. To save time I would like to tape this interview if you have no objections.*

In some firms two people may be needed to answer all the questions, e.g. the payroll manager and the MD, or recruitment manager.

*(The questions aim to allow respondent to describe their experiences and views at some length rather than simply looking for short yes or no type answers.)*

**SECTION 1 (For either interviewee)**A. Business Details

*I'd like to start by asking for a few background details about the business.*

1. Could you describe to me what you do in the business?
  - Main products or services provided by the business
  - Approximate number of employees (approximate proportions of men/women)
  - As far as you know are any employees currently receiving tax credits? If so, how many? (approximately)

## B. Awareness of the Tax Credits

*I'd now like to move on to talk about some of the aims of the tax credits. The WFTC and the DPTC were introduced in April last year.*

2. Can you tell me a little about your understanding of the tax credits?
  - What do you see as the main aims of these tax credits?
  - As far as you are aware which government department is responsible for administering the tax credits?
  - How do you think it differs from what happened before?
  - Broadly speaking, what does it mean for employers like you?
  - What do you see as your role in the tax credit system?
  
  - How does it affect you?
    - What tasks are you required to undertake?
  
3. Thinking back what was your initial reaction to the changes?
  - Why did you think that?

## C. Initial Information and Guidance

*Now, I'd like to talk about how you heard about the changes to the tax credit system and about any advice you received before the new system came into operation in April 2000.*

***(The questions aim to allow the respondent to describe their experiences and views at some length rather than simply looking for short yes or no answers.)***

### Awareness of changes

4. Where/how did you first hear about the changes to the tax credit system? :  
  
Did it/they tell you what you wanted to know?
  - If not, why not?
  - If yes, what did you find useful about them?
  - How could they be improved?
  
5. Were you given enough information about the changes to the tax credit system?
  - If not, what would you have liked more information about? Why?
  - Did you find any sources particularly useful?
    - Which source of information did you find most useful? Why?
    - Would a different format be more useful, e.g. booklets, CD ROM?

## Employer's Helpline

(Notes for interviewers: clarify that you want to discuss the Tax Credit Helpline rather than other Inland Revenue helplines. If the business is a new business they may have used the 'New Enterprise Support Initiative Helpline' an Inland Revenue Helpline for new businesses. If they have used a Helpline clarify which one when asking the following questions).

### 6. Are you aware of the Employer's Helpline?

- If Yes,
  - Have you ever contacted them?
  - About how many times?
  - Choose one occasion when the Helpline was able to help you and describe what happened.
    - What did you contact them about?
    - What kind of help did you want?
    - How did they help you?
  
- Has there ever been an occasion when you contacted the Helpline but felt they weren't able to help you?
- If Yes,
  - What did you contact them about?
  - What kind of help did you want?
  - What advice did they offer?
  - What help would you have liked to receive?

### 7. Overall, how useful do you find the Employer's Helpline? Why?

- Overall, how would you describe the service you receive from them?
- Is there anyway the service could be improved?

### 8. If not aware of the Helpline do you think you might use it/have used it?

- What for?

## SECTION 2 (For person who deals with payroll)

### D. Changes to the Payroll System

Next, I would like to hear about your experience of how you went about any changes that you made to your payroll system to fit in with the tax credits and about any advice or help you may have sought.

#### Description of the payroll system and process.

9. First of all could you describe your payroll process to me? (Cover all points)
- In-house payroll or externally managed
  - Manual or a computerised system?
    - If computerised:
      - What is the package called?
      - What does it do?
      - How easy/difficult has it been to incorporate changes in this package? Why?
  - Monthly or weekly payments;
  - Payments: cash; cheque; bank account

#### Changes to payroll system in order to pay tax credits

10. What changes did you make to your payroll system to comply with the payment of tax credits?
- What were the reasons for the particular changes made?
  - How easy or difficult was it to make these changes? (establish which changes were easy or difficult)
  - Why were they easy or difficult?
    - Was this anything to do with the information or advice you received?
  - Have there been any changes that you have made to the payroll system that you have found particularly useful? In what ways?
    - Have there been any changes that have not worked as you'd hoped? Why not?
11. Whilst making the changes to your payroll system did you approach anyone for help/advice?
- If so who?
  - Why did you choose them to approach?
  - What were you seeking advice or help about?
  - Did you receive the advice or help you wanted?
    - If not, what would you have liked to happen?
    - If yes, in what ways was the advice/help useful?

- If respondent didn't use the Inland Revenue? Why not?

Prompt: (for each, explore whether useful or not and why/why not)

- Website?
- 'Notes on PAYE for Computer Users'? (show copy)

12. Did you provide any training for payroll staff?  
If yes, what did the training consist of.

### E. Employer's Experience of Paying Tax Credits

*Now I would like to ask you about your experience of paying tax credits so far.*

***(Once again the questions aim to allow the respondent to describe their experiences and views at some length rather than simply looking for short yes or no answers.)***

13. In general, how well do you find that the tax credit system works alongside the PAYE system? (explore any issues and establish overall view of complexity of tax credits in relation to PAYE/SSP/SMP)
14. Now to turn to the payroll process itself. For instance, how easy or difficult do you find:
- Calculating the tax credits for the pay period from a daily rate?
  - Completing employee/s' payslip/s?
  - Completing the forms (P32, monthly or quarterly) that show the total PAYE tax, NICs and student loan deductions due for all employees (minus what you have paid out in tax credits)

For each:

- If difficult, what in particular is difficult?
  - Have you resolved this difficulty?
  - How?
  - Have you approached anyone for help (IR?)? If so, what happened?
  - Was the advice useful? Why?
15. Looking now at the future. Do you see paying tax credits through your payroll becoming easier or more difficult? Why? (Explore fully)

### Start Notifications

16. How are you first told that an employee is to start receiving tax credits?
17. How useful and clear do you find the start notifications? (Show a start notification)
- What parts are clear?

- Why?
- What parts are not clear?
- Why?
- What could be done to improve them?
- Is there any more information you would like to receive?

## New Recruits

18. Have you taken on anyone recently that receives tax credits?
- How did you deal with this?
  - Did you find it straightforward or not? If not, why was this?
  - Did you seek any advice or help? If so who from?
  - Did you get the advice or help you were looking for? Why/why not?

## Leavers

19. Have you had any employees leave the business who were in receipt of tax credits?
- Had you already started paying tax credits to them?
  - For how long had you been paying them?
  - How did you deal with the process of them leaving?
  - Did you find it straightforward or not? If not, why was this?
  - Did you seek any advice or help?
  - If so who from?
  - What advice were you seeking?
  - Did you get the advice or help you were looking for? Why/why not?

## Holidays, Leave and Sickness

20. Have any employees who are in receipt of tax credits ever been on:
- Holiday
  - Sick leave
  - Maternity leave
  - If yes:
    - What did you do in terms of payment of tax credits? (Did you pay them?)
    - Was this straightforward?
      - If not, why not? What happened?
      - Did you seek help?
      - Who from?
      - Did you get the advice you wanted? Why/why not?



21. If respondent has not experienced any of these circumstances then what would they do if one of these occasions arose? (Would they still pay the tax credits?)
- Seek help?
  - Who from? Why?

### Transition Periods

22. Do you know how long these awards to employees are made for?
- How long does the recipient get the award before they are re-assessed?

(If respondent is unsure clarify that it is 26 weeks. After which IR resumes payment until a new notification is sent out to employer)

23. Have any of your employees on tax credits reached the end of one of these payment periods yet?
- If so, what happened at the end of the period?
  - Was it straightforward?

24. Did you approach the Inland Revenue for help/advice?
- What happened?
  - Were they able to help? Why/Why not?
  - In what ways did they help?

If you didn't approach IR, why not?

Did you approach someone else for help or advice? Who? Did you get the advice you wanted? What advice were you given?

25. If you haven't experienced an employee getting to the end of a 26 week period yet, do you know what the process involves?

### Additional Funding

Looking now at the funding for the tax credits.

26. As far as you are aware where does the money come from to pay for tax credits? (If they say from them, explore. In what ways do they pay? Cash? Time? Etc.)

(Clarify that the money comes out of their PAYE tax, NICs and student loan deductions)

27. Has there ever been an occasion when the amount you paid out in tax credits was more than you deducted from the PAYE tax, NICs (and student loans if relevant)? (i.e. have they ever been out of pocket through paying tax credits).
- Did you apply for funding from the Inland Revenue?

- If you didn't apply why not? Did you seek advice? Who from and what were you told?

If you did apply?

- How did you go about applying?
  - Did you ask for help?
  - Who from, were they able to help you? Why/ why not?
  
  - Did you receive the amount of money you needed? Why/ why not?
  - Did you receive the money when you needed it?
  - Why/ why not?
  - Did you incur any bank charges when applying for direct funding? If so, how much was this?
28. Do you know whether you are taxed or not on this funding?
29. Is there anyway in which the process of applying for this kind of funding could be improved? In what ways?

## End Of Year Tax Forms

30. Have you completed your end of year tax forms?
- If yes how have you found this process. (For instance:
    - Recording the total tax credits paid in a tax year?
    - Entering the total tax credits in the year for the employee on the P14 and P60?
    - Entering the total tax credits for all employees in the year on the P35, together with the total amount of Inland Revenue funding in the year)
31. Did you approach anyone for help?
- Who?
  - What happened?
  - Were they able to help? Why/Why not?
  - In what ways did they help?

### Information and advice for employees

32. Do you tell your employees about the availability of tax credits or give them any information or advice?
- Have any of your employees ever asked for advice?
  - What information /advice did they want? Why?
  - Were you able to supply this information? If not why not?
  - Do you think the information and advice provided for employees could be improved? In what ways?

## **SECTION 3 (For Managing Director or Director of Personnel)**

### F. The Effects on your Business of Paying Tax Credits

**Now I'd like to discuss any broader effects on your business the payment of tax credits may have had.**

33. Has the payment of tax credits had any effects on the day-to-day running of your business?
- What effects has it had?
  - How have you dealt with these?

For each type of effect reported:

- Have you made any changes as a result?
- What kinds of changes?
- Why did you make these changes?
- How have these changes worked out? Why?
- What effect/s do you think it/they will have on the business? Why?

34. Do you think that the tax credits have made recruitment easier?
- If yes, for which kinds of staff?
  - In what ways?
  - Why do you think this is? (For instance by offering incentives to people who didn't work before)
35. Has the payment of tax credits made any difference to your thinking about who to employ or on how you manage your staff?
- In what ways do you think differently? About what?
  - Have you made any changes as a result ?
  - What kinds of changes?
  - Why did you make these changes?
  - How have these changes worked out? Why?
  - What effect/s do you think it/they will have on the business? Why?
36. Do you think that the money your staff receive through their tax credits has affected their motivation and morale?
37. Finally, thinking about the business as a whole, how important an issue has the introduction of paying tax credits been in relation to other aspects of running the business?

*That completes my questions is there anything else that we haven't covered that you think is relevant to understanding the changes brought about by the tax credits?*

*Thank you very much for giving up your time to discuss these issues today. If you need any further information about the WFTC or the DPTC I can give you the Tax Credit Helpline number.*