WAKING THE DEAD

David Heaton considers the new NIC holiday and its chances of success

With the holiday season, it seems appropriate to look at a holiday topic, but with a twist. The furnished holiday letting rules have been reprieved for a time, while somebody works out a better way to meet EC Treaty obligations, but the more interesting announcement in the Emergency Budget was the new NIC holiday.

Although I am not ordinarily one to rush to judgement, I do wonder whether the proponents of this scheme have either very short memories, or no idea what happened in the 1990s. In a government avowedly committed to cutting waste and unnecessary legislation, it will be interesting to see which other rules are removed to make way for this, and what replaces it when it flops.

Why the scepticism? The old NIC holiday died a quiet death when virtually nobody used it. A brief recap might help to understand the context.

April 1996 saw the Mark 1 version launched, as the latest initiative to remove the long-term unemployed from the misery of the dole queue. Employers were offered freedom from contribution liability for a year in respect of anyone they hired who had been unemployed for at least two years and who worked for the claimant employer for at least 13 weeks. The employee needed a certificate from the Benefits Agency to cover the two-year qualification, followed by another certificate from a department at the Contributions Agency created specifically for the purpose of checking and certifying the employment requirements. Because of the minimum 13-week employment hurdle, employers initially had to account for all the contributions as normal and then make a refund claim (subject to a six-year time limit), eventually showing a negative 'Table P' contribution on the year-end returns to account for the difference between NIC credited to the record and NIC paid over. In some cases, depending on the timing of recruitment and application for certification, the refund affected two year-end returns. The value to the employer was 10% of the employee's earnings above the lower earnings limit for 52 weeks, and since most long-term unemployed would have been taken on only in low-paid jobs, this frequently did not amount to much.

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A DSS research report (No. 76) into the scheme in 1997 reached a number of conclusions:

- Awareness of the scheme was low.
- Where employers were aware, the level of understanding varied, and while payroll people might have understood, their HR colleagues often did not and had taken no account of the scheme in their recruitment policies.
- For large employers, the return was not worth the effort.
- For small employers, the risk of taking on someone who might not stay or prove to be unreliable outweighed the value of the NIC refund.
- The scheme did not affect whether a recruit could do the job, which is an employer's prime concern, and few employers were willing to relax their criteria for a small cash benefit. If the recruit could do the job, the scheme could only tip the balance away from an equally suited but non-holiday candidate.
- Employers also favoured those unemployed candidates who had done something worthwhile during their period on the dole, which showed the right attitude.
- The scheme was seen as a bonus after recruitment rather than an incentive to recruit.

Some of those lessons appear to have been learned, judging from the information so far released about the new scheme.

Under the new NIC holiday, the recruits need not be from among the long-term unemployed, who were sometimes in that position precisely because they would not ordinarily have the skills and attitudes that employers needed, so that is one hindrance removed.

The new scheme is also unlikely to appeal to large businesses, as it is limited to the first 10 recruits in a new business, although it is not clear what will in fact count as a 'new' business, and large employers might be able to find a way to qualify for some of their business units by spinning them off. Anti-avoidance rules in this area are inevitable.

The savings have a headline cap of £50,000 spread over 10 employees at £5,000 each. £5,000 represents earnings of about £45,000 at current not contracted out rates, and about £43,000 next year, so it has to be questioned how many new businesses will be paying all of their first 10 recruits anywhere near the figures quoted (except perhaps the spin-out businesses suggested above). Will it really be worthwhile to jump through all the inevitable hoops? Is that desirable or sensible? The self-employed will not qualify on their own earnings, but so what? They don't currently pay secondary NICs anyway.

And what happens about contracted out rates? It is highly unlikely that any new business will immediately set up a contracted out pension scheme, but if it did and the measure of contribution saving was purely the cash value of employer contributions, higher earnings would count, so the rules will presumably aim for a level playing field by using only standard rates.

Some obvious anti-avoidance measures have already been indicated: IR35 and managed personal service companies will not qualify, but that will not catch properly organised spin-outs. Domestic employees such as nannies and chauffeurs will not count, but chauffeurs employed through a real new business ought to be different. There will be restrictions in the coal, agriculture and fisheries sectors, although details are not yet known.

It is a matter of mild controversy that the new scheme is also restricted in geographical scope: employers in London, the East and the South East will not qualify, because the scheme is intended to promote employment in areas to be affected by public sector cuts. Demarcation disputes are inevitable: what makes a business an Eastern Region business? An office in Norwich might be an obvious disqualifying factor, but what if the 'head office' or registered office of the new business is in one founding director's Birmingham home and there is also a Norwich office where the other founding director lives and works? More anti-avoidance steps to consider.

The paperwork will presumably need a redesign to cope, although it may just be that Table P is raised from the dead. Some employers who have received unjustified penalty notices for non-existent payroll errors – or even for perfectly promptly e-filed corporation tax returns that were simply not processed – will question whether HMRC's IT will be able to handle the new scheme correctly. How long before the system issues its first penalty for an alleged underpayment caused by deducting the correct amount under the NIC holiday?

The 'new' NIC holiday will clearly differ from the 'old' one, so my pessimism might be totally misplaced (I hope that is the case), but even if the idea is neat and simple in concept, it is unlikely ever to be worth £50,000 to any business. Once we factor in the inevitable pages of legislative paranoia that will accompany the new relief to ensure that it is not abused by employers, and the form-filling and double-checking that the qualification and audit criteria entail, and the internal cost at HMRC to publicise, manage and police the scheme, we may see the new going the same way as the old, maybe even to a similar timescale. Waking the dead is rarely a fruitful exercise.

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