

PAYE Reporting

BETTER ADMINISTRATION OF PAYE



Introduction

The Government is modernising New Zealand's tax system to make it simpler and more certain for New Zealanders. Improving the administration of PAYE is an integral part of this reform.

Employing staff can add significant compliance costs to a business or not-for-profit organisation. The Government wants to do something about this.

Increasingly employers are using payroll software to help them run their organisations. The proposals below would further integrate tax obligations, such as providing PAYE information to Inland Revenue, into employers' own systems and processes. Meeting tax obligations would become part of the process of paying employees rather than a separate and additional activity.

The proposals would make it easier to get an employee's pay right and to quickly address issues, such as using the wrong tax code. The result would be lower compliance costs for employers and improved accuracy of deductions for employees.

The proposed changes are likely to be included in a tax bill for consideration by Parliament in 2017.

Summary

- Employers and payroll intermediaries¹ would no longer be required to file an employer monthly schedule; instead they would file *PAYE information*² on a *payday basis* from 1 April 2019.
- Employers using payroll software would be able to file their information directly from their payroll system.
- Employers would not be required to use payroll software but would have to file their PAYE information on a payday basis.
- The smallest employers would still be able to file their PAYE information on paper if they choose to do so. The *threshold for electronic filing* of PAYE information would reduce from \$100,000 a year of PAYE and Employer Superannuation Contribution Tax (ESCT) deductions to \$50,000 a year.
- The Government is not proposing to change the dates by which *PAYE and related deductions* have to be paid to Inland Revenue. However employers will be able to make these payments on payday if they choose to.
- To improve the workability of the rules minor changes would be made from 1 April 2018 to the PAYE rules for holiday pay paid in advance and to align when rate changes come into effect.
- The payroll subsidy, which subsidises employers to outsource their PAYE obligations to listed payroll intermediaries, would cease from 1 April 2018.

¹ References to employers should be read as including payroll intermediaries

² Terms in italics are included in the Glossary at the end of this document.

What is the purpose of these measures?

The proposals are part of modernising New Zealand's tax administration system and will use business/payroll systems to reduce compliance and administrative costs, for instance:

- Filing directly from payroll software will streamline the process of providing PAYE information. Research into SME compliance costs indicates that similar reforms in GST have already contributed to a reduction in compliance costs of more than 20%.³
- It should be possible for a new employee to fill in a single online form when they join an organisation. The payroll system could then be used to send relevant parts of the information to Inland Revenue without that information having to be obtained and entered separately.
- It is acknowledged that there may be software costs and costs to change processes, but the goal is to reduce the extent to which Inland Revenue imposes separate or additional requirements on employers.

Obtaining PAYE information on a payday basis will enable Inland Revenue to identify problems more quickly, for example when an employee is using two M tax codes. This will improve the accuracy of deductions and reduce the likelihood that employees will miss out on entitlements or incur debt.

Payday PAYE information could also provide opportunities for government agencies to better match social assistance entitlements with periods of need, for example through shorter periods of assessment.

³ Better for Customers: SME's compliance costs in 2016 - Inland Revenue

Payday filing of PAYE information

Employers currently report PAYE information about their employees to Inland Revenue on a monthly basis regardless of how frequently they pay their staff.

Inland Revenue's systems and processes are being redeveloped to take advantage of modern digital technology. Under the proposed changes, the PAYE information-filing process will be integrated into the payroll software that many employers use to pay employees.

Employers would then file their PAYE information each payday directly from payroll software. Employers above the *electronic filing threshold*, all payroll intermediaries and employers using payroll software would be required to file their PAYE information by the second working day after payday. The due date for PAYE information from other employers would be seven working days after payday.

Under the proposed changes, employers would be able to file their PAYE information each payday from 1 April 2018 and would be required to do so from 1 April 2019.

Example 1

Awhina manages the payroll for a firm with six employees. The firm has a high turnover of staff and frequently employs temporary staff. The firm uses payroll software to calculate the fortnightly pay for its employees.

Current process: *At present the payroll software Awhina uses builds up the employer monthly schedule each payday. At the end of the month she has a reminder scheduled in her diary to download the file, log into myIR and use ir-file to upload and file the information with Inland Revenue.*

New process: *Once the payroll has been finalised each fortnight the payroll system would prompt Awhina to file the PAYE information the system has generated. She will use the payroll system to send the information directly to Inland Revenue. Awhina will file the PAYE information for the pay period as part of completing that pay run without leaving the payroll system. Awhina's firm pays its employees by direct credit, the instructions are sent to the bank for the distribution of payment to employees on Wednesday. The due date for the firm's PAYE information is Friday.*

Example 2

Graeme is the administration officer for a small firm with 12 employees; the firm is large enough to be required to file its PAYE information electronically. Graeme uses the calculators on the Inland Revenue site to work out the weekly PAYE and other deductions for staff before he finalises their pay and sends the instructions to the bank.

Current process: *Graeme keeps weekly printouts of PAYE and other deductions and relies on memory to add them up and file them by the 20th of the following month. Once he has added up the totals for each employee Graeme logs into myIR and in ir-File he types the monthly totals into the online form and sends it to Inland Revenue.*

New process: *Once Graeme has finished using the online calculator to calculate the PAYE and other deductions for the weekly pay he will be prompted to send the information to Inland Revenue. He will still need to log into Inland Revenue's myIR to send the information but the process will be easy to use and similar to online banking. Graeme files the PAYE information each week as part of the process of paying staff. Graeme sends the instructions to the bank for the distribution of payments on Thursday and the due date for the firm's PAYE information is the following Monday.*

Example 3

Mary runs a small café business with four part-time employees who are paid using online banking each week. Although she uses internet banking she completes a paper employer monthly schedule. She thinks her business is too small to invest in payroll software and didn't like using my-IR and ir-File when she tried it some years ago.

Current process: *Mary works out the PAYE and other deductions using the tax tables and a wage book. She uses an alert on her phone to remember to calculate the monthly totals and file the information by the 20th of the following month. Once she has added up the totals for each employee she completes the employer monthly schedule and posts it to Inland Revenue.*

New process: *Some of Mary's peers have invested in payroll software and are encouraging her to register for a free trial. However, if she wishes, Mary can continue to use a paper form and post it to Inland Revenue.*

She will however have to complete the form each payday and post it so that it arrives at Inland Revenue within seven working days. Mary sends the instructions to her bank for payment to her employees on Tuesday so she needs to post the paper PAYE information form so that it arrives with Inland Revenue on or before the Thursday of the following week.

If Mary has heard that Inland Revenue's online services have improved she could decide to try electronic filing again. After all internet banking isn't hard and she knows she can go back to using paper if it isn't as straightforward as expected.

Example 4

Di manages the payroll team at a large manufacturing business which runs two different payrolls; a monthly payroll for senior executives, and a weekly payroll for employees in manufacturing, sales, design and administration.

Current process: *Both payrolls run through the same payroll system and produce separate schedules each month. The staff member responsible for filing employer monthly schedules downloads the completed monthly schedules from the payroll system and uploads them again, sending them at the same time to Inland Revenue using myIR and ir-file.*

New process: *The payroll software prepares a PAYE information report each time it runs and sending the information to Inland Revenue has become part of the responsibilities of the staff that finalise each payroll. The due date for the PAYE information from each payroll is the second working day after the bank distributes the payments.*

Reduction in the electronic filing threshold

The electronic filing threshold for PAYE is currently \$100,000 a year of PAYE and ESCT. Employers who withhold this amount of PAYE and ESCT for a year or more, and all payroll intermediaries, have to file their PAYE information electronically. This can currently only be done through Inland Revenue's secure website.

Under the proposals, this threshold will reduce to \$50,000 a year of PAYE and ESCT. As an indication, an employer with fewer than ten full-time staff on the minimum wage or four on the average wage would be below this reduced threshold. The proposals would make it possible to file PAYE information electronically from payroll software or through Inland Revenue's secure online service.

Exemption for employers above the electronic filing threshold but unable to access digital services

The proposals would allow employers who are above the *electronic filing threshold* but who cannot access digital services to apply for an exemption from filing their PAYE information electronically by the second working day after payday. If an exemption is granted these employers will be able to file their PAYE information on paper and it will not be due until seven working days after payday.

It is envisaged that this exemption could be used by employers in locations where suitable internet services are not available and by employers who don't use computers.

Improving the processes for setting up new employees

At present when an employee starts a new job they are generally required to fill in two paper forms for Inland Revenue. The forms include a substantial amount of repetition and often overlap with the information the employer collects for their own purposes. The KiwiSaver enrolment form also requires an employee's contact details.

In future it is intended that software could be used to gather the information required from new employees, and details such as a person's name and IRD number will not need to be repeated.

New employees would be required to provide their date of birth to their employer, who would provide this information to Inland Revenue to help verify the employee's identity. In addition, all new employees, not just those eligible for enrolment in KiwiSaver, would be required to provide their contact details to Inland Revenue via their employer.

Inland Revenue will encourage employers to send "new employee" information to Inland Revenue before the new employee is first paid, but this would not be a requirement.

New employee information could be sent direct from the payroll system or through Inland Revenue's improved e-services. Sending employee details before a new employee is first paid will enable Inland Revenue to automatically check the IRD number, proposed tax code and other deductions, and communicate back in near-real time if changes are necessary.

For employers still using paper it is intended that the two Inland Revenue forms for new staff, the IR 330 and the KS2, will be combined into one.

Example

Awhina's payroll provider has made an integrated employee information screen available for new employees. The online form includes fields for the employee's tax code, IRD number, date of birth and contact details, and other information required by the employer. The screen identifies which information will be sent to Inland Revenue.

New process: *Once the information relevant to Inland Revenue is completed Awhina generally uses the payroll system to send that information to Inland Revenue before the new employee is first paid. She has found that getting their details right from the start saves time in the long run.*

However if the employee doesn't complete the electronic form until the last minute she simply includes the new employee information with the payday submission of PAYE information and deals with any subsequent issues as they arise.

Adjustment and error correction

Making adjustments to or correcting errors in PAYE information after it has been filed, is currently a largely manual process. The proposed requirement to submit PAYE information more frequently means this process will need to be more effective.

Inland Revenue is using feedback from consultation to develop requirements for simpler processes which will reduce compliance costs and work for employers. Once proposals are developed wider feedback will be sought before requirements are finalised. Options include:

- Defining the circumstances in which employers may correct errors in a subsequent return.
- The payroll system automatically generating a schedule of adjustments as a by-product of the employer updating its own records.
- Employers accessing their filed information through Inland Revenue's secure online services and updating the lodged information.

Modernising the PAYE rules

To improve the workability of the PAYE rules the Government is proposing to make some changes affecting the calculation of PAYE and related deductions and contributions, with effect from 1 April 2018. Changes are proposed to the tax treatment of salary or wages paid in advance and to the application of legislated rate changes.

Tax treatment of holiday pay paid in advance

The proposals will give employers the option to treat holiday pay paid in advance as a lump sum as if it was paid over the pay periods to which the leave relates, rather than as an extra pay.

If additional payments are subsequently made for a pay period to which the leave relates, employers will have to calculate PAYE based on all earnings for that period, less the PAYE already collected. This will apply to pay periods partially taken as leave and partially worked.

While this new option is more precise, it could increase compliance costs for employers not using payroll software. Therefore, it will not be mandatory and employers will be able to continue to use the existing extra pay method. For consistency, salary or wages paid in advance will be treated similarly.

Example

After its peak season Awhina's firm closes for three weeks in mid-February and employees are required to take leave.

Current process: *Employees in Awhina's firm are paid their holiday pay in advance. Awhina calculates the holiday pay as an extra pay and because of the high earnings before the leave period employees may be overtaxed. If so they would need to file a tax return or seek a personal tax summary at the end of the year to obtain a refund.*

New option: *Awhina can use her payroll software to calculate the PAYE for the holiday pay as if it were paid in the future periods when the employees are on holiday. When employees return to work their first pay will be for the part of the pay period they have actually worked (they were paid in advance for the part spent on annual leave). The software will calculate PAYE for this pay taking into account total earnings for the period and the PAYE already deducted. This approach eliminates the possibility of over deduction of PAYE.*

Application of legislated rate changes

Under the proposals the rules about how legislated rate or threshold changes are applied will be aligned across the different types of PAYE income payments and PAYE-related social policy products (such as KiwiSaver contributions and student loan deductions). The rates and thresholds to be applied would be those in force on the date the payment is made.

Aligning the rules will simplify the transitional process for employers when a legislated rate or threshold change occurs.

Payroll subsidy

As part of this package of proposals the payroll subsidy will cease from 1 April 2018.

Currently the Government subsidises the cost of eligible employers engaging a listed PAYE intermediary to meet the PAYE obligations on behalf of the employer. The subsidy is paid at the rate of \$2 per employee, per pay run, for a maximum of five employees.

Because the subsidy incentivises only one model of payroll service the payroll subsidy may distort employers' choices between a range of different types of payroll products and services.

In future these services will include significantly improved electronic services from Inland Revenue which will enable employers who do not use payroll software to calculate PAYE and other deductions and provide PAYE information to Inland Revenue.

Due dates for payment of PAYE and related deductions

From 1 April 2018 employers will have the option of paying their PAYE and related deductions to Inland Revenue on payday however they will not be required to do so.

Employers with more than \$500,000 a year of PAYE and ESCT deductions will continue to be required to pay their PAYE and other deductions twice a month, by the 5th and 20th. All other employers will continue to be required pay their PAYE and other deductions by the 20th of the following month.

Legislation

The proposed legislative changes will be included in the next omnibus taxation bill, which is expected to be introduced into Parliament early next year.

PAYE Questions and Answers

Small employers who do not use payroll software

Q Is Government insisting that all employers use payroll software?

A *No, the Government is not insisting that employers use software. Other options for calculating PAYE information will still be available and the smallest employers and those without access to internet services or computers will not be required to send the information to Inland Revenue electronically. The use of accounting software to file GST has contributed to a more than 20% reduction in compliance costs recorded in the latest survey of small businesses. In the light of these results employers might want to reconsider whether or not investing in software, or using Inland Revenue's electronic services, is worthwhile.*

Small Businesses

Q Won't payday filing increase compliance costs for small businesses that don't use software?

A *This is unlikely. The information required is the same. The difference is when it is provided to Inland Revenue. The changes are largely about making better use of modern digital systems and evidence from GST research suggests significant compliance cost gains for small businesses from investing in software. Employers who choose not to use software already work out the PAYE information for each payday. They need it to pay their staff. Logging onto to Inland Revenue's website or completing a paper form each payday at the end of the payroll process could be easier than putting the information aside only to come back to it at the end of the month, add it up with the other paydays in the month and then send it to Inland Revenue.*

Auto transmission

Q Doesn't filing automatically from software raise the risk that information will be accidentally transmitted before it is finalised or approved?

A *This will be no more of a risk than it is today. Nothing is going to be sent to Inland Revenue automatically. Direct from software means information will be sent much more seamlessly from within the payroll system, but the operator will know they have logged onto Inland Revenue's system and will know that they are sending the information.*

More errors

Q If information is sent more quickly, won't there be more errors and adjustments?

A *Feedback from employers suggests the current processes are inefficient. With payday reporting it will be even more important to ensure that there are easy ways for employers to correct errors and make adjustments. An objective for those with payroll software is to automate the process.*

Compliance costs

- Q** Previously most employers only had one PAYE date to worry about each month, the 20th of the following month. Now with payday reporting and payment by the 20th don't they have more to worry about?
- A** *Employers have always had to worry about getting things done for payday. What these proposed changes mean is that sending information to Inland Revenue can become part of that payday routine. Employers will have the option of paying Inland Revenue then too, but the Government understands that many might prefer to hold onto the deductions until the payment dates required in the current legislation.*

What incentives will Government offer to get employers onto the new systems

- Q** What support and incentives will Government be offering to encourage take up of the new systems?
- A** *The best incentive is that it should be simpler for everyone concerned. There will be lots of communication and Inland Revenue will target support for customers who might have most difficulty.*

Will Inland Revenue provide free payroll software

- Q** Will Inland Revenue be providing free payroll software?
- A** *No, payroll software does much more than provide information for tax purposes and it is not the Government's intention to have Inland Revenue provide payroll software when existing providers make products and services available at a variety of price points. For employers with very simple payrolls, the PAYE calculators will still exist on Inland Revenue's website and the website will be improved so that filing without using payroll software will be easier and more intuitive.*

Costs to upgrade

- Q** Will Government subsidise the cost to upgrade payroll software?
- A** *No, the Government is not proposing to subsidise costs. Employers pay for upgraded software either through a subscription or contract fee or by paying for an upgraded version. The changes the Government is proposing will require software to be upgraded but these changes are often bundled together with upgrades the provider is making for other reasons. Employers who choose to file electronically through the Inland Revenue website will not face additional costs.*

Dates

- Q** Will there be enough time for employers and software developers to be ready before the new system goes live?
- A** *Enough time has been allowed for an orderly introduction. Inland Revenue will be ready to accept PAYE information on a payday basis from 1 April 2018 but under the proposals employers won't be required by law to provide it until 1 April 2019.*

Support for the proposals

- Q** Did the Government receive universal support for payday filing of PAYE information in response to the consultation document?
- A** *The response was mixed. Many employers using payroll software were supportive or supportive with some caveats, such as automated error correction. On the other hand many small employers were uncomfortable with the prospect of being required to change their existing processes and were opposed to being required to invest in payroll software – which will not be required. However, as feedback from new the GST filing insights shows, moving to digital systems should reduce compliance costs.*

Avoiding software problems

- Q** There are recent examples of where Government-run software changes have caused problems. How can we be confident that this won't happen again?
- A** *This is entirely different as Government is not proposing to build payroll software and there are no significant changes to how PAYE and other deductions are calculated and paid. The changes are largely about how and when information is provided to Inland Revenue, and Inland Revenue will work closely with payroll providers to ensure success. Much of the information the Government wants to receive on a payday basis is already held by employers, but rather than being aggregated it is to be transmitted each payday.*

Penalties and interest

- Q** Will payday filing increase employers' exposure to late filing penalties?
- A** *Some submitters expressed that concern, but this is not intended. By integrating the filing of information with paying employees it is less likely that employers will forget or overlook their filing obligation. The late filing penalty will remain a monthly penalty so the maximum late filing penalty an employer could be subject to remains \$250 a month.*

Glossary

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| PAYE information | <p>The information employers are required to provide to Inland Revenue when they make payments of PAYE income, including the information on the employer monthly schedule and the KiwiSaver 1 form.</p> |
| Payday basis | <p>“Payday” means the day on which an employer makes a payment of PAYE income to an employee.</p> <p>Instead of being aggregated across a month PAYE information will be provided each payday.</p> <p>The due date for PAYE information from employers above the electronic filing threshold, from payroll intermediaries and for those using payroll software, will be the second working day after payday.</p> <p>The due date for employers below the electronic filing threshold who do not use payroll software and for those who have an exemption from the requirement to file electronically will be seven working days after payday.</p> |
| PAYE and related deductions | <p>PAYE, including ACC earners levy and where relevant, student loan deductions, KiwiSaver contributions and child support payments.</p> |
| Electronic filing threshold | <p>The electronic filing threshold for PAYE is currently \$100,000 a year of PAYE and employers superannuation contribution tax (ESCT). Employers who withhold this amount of PAYE and ESCT a year or more have to file their PAYE information electronically. This can currently only be done through Inland Revenue’s secure online service.</p> <p>The announcements include the reduction of this threshold to \$50,000 a year of PAYE and ESCT. In future it will be possible to file PAYE information directly from payroll software or through Inland Revenue’s secure website.</p> |

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