Fixing the furlough headache

Employment Tax



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Carolyn Brown and *Susan Ball* examine the details of what you need to know about implementing the Coronavirus Job Retention Scheme

Key Points

What is the issue?

On 7 June, 8.9 million employees from 1.1 million employers were furloughed at a cost of £19.6 billion. This eight month scheme is in two parts: one for four months from 1 March to 30 June; and then another on different terms from 1 July to 31 October 2020.

What does it mean for me?

New CJRS from 1 July 2020 is intended to operate more flexibly to support those employers getting their employees back to work. Furloughed employees will be able to actively work for part of the period but be on furlough for the rest of the period, for example.

What can I take away?

Unless the furloughed employee will be fully furloughed, a new or varied furlough agreement is needed. If this includes a change of working hours, this will either need to be agreed with the employee individually, by collective agreement or imposed by a dismissal and offer of reengagement on the changed basis.

On 20 March 2020, the Coronavirus Job Retention Scheme (CJRS) was introduced to provide a support grant for all employers who could not maintain their workforce because their operations had been affected by Covid-19. On 7 June, 8.9 million employees from 1.1 million employers were furloughed at a cost of £19.6 billion.

This eight month scheme is in two parts: one for four months from 1 March to 30 June; and then another on different terms from 1 July to 31 October 2020. From 30 June, employers will only be able to furlough those they furloughed for a full three-week period prior to 30 June, requiring them to have furloughed employees by 10 June, sparing some caveats to accommodate those where this would be hard to achieve.

Subject to that, the employer can use the scheme at any time during this period. Claims can be started from the date that the employee finishes work and starts furlough.

HMRC would not expect to agree a Time to Pay Arrangement that includes the NICs (employer and employee) and PAYE payments due on monies received through the furlough scheme.

The legislative framework is covered in:

- 15 April 2020 The Coronavirus Act 2020 Functions of Her Majesty's Revenue and Customs (Coronavirus Job Retention Scheme) Direction (under powers conferred by the Coronavirus Act 2020 ss 71 and 76);
- 20 May 2020 Revised Direction effective for claims made from 22 May 2020; and
- 29 May 2020 published Taxation of Coronavirus Support Payments – Draft (Finance Bill) legislation.

Old CJRS up to 30 June was to support employers who could not operate during lockdown. Furloughed employees could not work at all, with limited exceptions. New CJRS from 1 July 2020 is intended to operate more flexibly to support those employers getting their employees back to work (see Changes to the Coronavirus Job Retention Scheme). Furloughed employees will be able to actively work for part of the period but be on furlough for the rest of the period.

The maximum CJRS grant

1 March to 30 June: The maximum grant reclaim value is 80% of a furloughed employee's wages up to a cap of £2,500 per person per month plus employer's NICs and employer's auto enrolment minimum pension contributions on those wages.

1 July to 31 July: As above, but only for furloughed hours, thereby allowing employees to work part time.

1 August to 31 August: 80% of a furloughed employee's wages up to a cap of £2,500 per person per month.

1 September to 30 September: The taxpayer will contribute 70% and the employer 10% of furloughed employees' wages during furlough periods.

1 October to 31 October: The taxpayer contribution will be 60% and the employer contribution will be 20%. (In August, September and October, the employer will be required to contribute employer's NICs and employer's pension contributions.)

How will hours worked and furlough hours interact?

When making a claim from 1 July, normal hours worked will need to be recorded, as well as hours worked and furlough hours. Normal hours worked will be on the same basis as 'reference pay', where we consider:

- for fixed rate employees: the last pay period before 19 March; and
- for variable pay employees: the higher of the average for 2019/20 or the same period last year.

The challenge for employers and those assisting with completing claims is access to information for fixed rate employees where the payroll system only records hours worked in bandings and not the actual hours. This is going to need employers to pull records from other sources.

In April 2019, the payslips of workers whose pay varies depending on the number of hours they have worked were required to show the number of hours paid on this basis (i.e. the amount of time worked), so these can be used for variable pay employees.

Pensions and salary sacrifice

Employers need to check the rules of the scheme to determine what contributions are due and how they fall during furlough (for normal hours not worked). For example, must they be calculated by reference to the pay that the employee actually receives during furlough, the employee's normal pay or some other amount? The problem is that many are set up to convert a percentage of pay. Salary sacrifices for pension payments create an added complication. The Pensions Regulator has issued detailed guidance, stating that it is intended for large employers but applies to all with such schemes. This impacts:

- reference pay under the legislation (which is the amount after the salary sacrifice), unless the employee opts out as a life event change (where HMRC has agreed that Covid-19 is a reason for a life event change);
- pay to the employee as salary sacrifice, which cannot be deducted from furlough grant pay (and where deducted from top-ups, employers need to make sure employees are still paid NMW for training or working hours); and
- the pension contributions paid over to the scheme, which need to be correct as per the pension scheme rules, might be different again from what's been paid.

This has created complications for those making grant claims, and making sure that both the payroll and the pension contributions are correct. It could result in incorrect grant claims and possible employment claims.

Other key features

From 1 July, the maximum number of furloughed employees that an employer can claim for cannot be higher than the maximum number it has claimed for previously. This would appear to prohibit one obvious way to get more of the workforce back to work through furloughing more personnel on short-time flexible furloughed hours in the same pay period(s).

From 1 July, employers cannot claim for overlapping pay periods but only for one pay period at a time.

Employers have until 31 July to make a claim for any periods of furlough up until 30 June. This applies to both employees furloughed for the first time in June and those previously furloughed.

Employers who overclaimed in error in a previous claim should inform HMRC and reduce the amount of a new claim to take account of a previous error.

Deductions from grant received

The employer must pay the employee all the grant they receive for an employee's gross pay in the form of money. Authorised deductions their salary can continue while they are furloughed, provided that these deductions are not charges, fees or other costs in connection with the employment.

The employee will still pay income tax, NICs, student loan repayments and any other deductions (such as pension contributions) from their wages.

Annual leave

Statutory holiday entitlement continues to accrue during furlough leave. The Department for Business, Energy and Industrial Strategy (BEIS) issued guidance on 13 May outlining how employers can operate workers' holiday entitlement and holiday pay during the pandemic. If a furloughed employee takes holiday, the employer should pay their usual holiday pay in accordance with the Working Time

Regulations or contractual pay, if higher.

Redundancy costs

Employers can claim under CJRS for employees given notice of termination by reason of redundancy (in its widest definition) serving notice during the period for which a furlough scheme claim is made. Furlough pay may also support wages during collective and individual consultation redundancy periods. Pay in lieu of notice, statutory or contractual redundancy payments cannot be claimed.

National minimum wage

As usual, national minimum wage (NMW) pay rates increased from 1 April 2020. Where employees were furloughed under old CJRS, NMW rates needn't have been paid. However, employers of furloughed employees who undertake permitted activities should ensure they meet NMW requirements.

From 1 July, employers using flexible furloughing need to ensure their NMW and national living wage (NLW) obligations are met. HMRC has announced that it is resuming NMW and NLW enquiries.

Furlough agreements and employment contracts

Employment contract changes by the employer during furlough, such as a reduction in wages, should have been agreed with the employee and any existing workforce collective consultation agreements met. Equality and discrimination laws apply.

Claims made from 22 May require that the employer and employee have agreed or confirmed in writing (or email) the terms and conditions on which the employee will cease all work, and that that agreement is incorporated in the employee's contract of employment. Such agreement can also be made by collective agreement with a recognised trade union.

In terms of new CJRS, unless the furloughed employee will be fully furloughed, a new or varied furlough agreement is needed. If this includes a change of working hours, this will either need to be agreed with the employee individually, by collective agreement or imposed by a dismissal and offer of reengagement on the changed basis. Where larger numbers of employees are in scope, prior collective consultation

obligations may be triggered.

Record keeping

An employer must keep a written record of all communications with the employee regarding the furlough arrangement, including all copies of the agreement, for five years. Where a claim is made under the second Treasury direction, the agreement or confirmation of furlough must be retained by the employer until at least 30 June 2025.

An employer must also keep a record of the claims for reimbursement it makes for furloughed employees' wages under the CJRS. An employer should keep a copy of all claims records for six years, including:

- the amount claimed and claim period for each employee;
- the claim reference number for your records; and
- the calculations used, in case HMRC need more information about the claim.

Where an employer claims more than it should have done in a claim period, it should keep records of any notification to HMRC and records of the adjusted amount for six years.

Penalties for getting it wrong

HMRC reportedly received around 1,900 reports of potentially fraudulent claims under CJRS to the end of May and will be investigating claims.

The government has tabled Finance Bill amendments legislation to claw back funds claimed in error or fraudulently. The draft clauses present a problem to employers and agents, as they require the correction or notification to HMRC of errors with previous claims within 30 days; i.e. 30 days of Royal Assent and then 30 days after a claim is made.

As well as being entitled to the furlough-related payment, the employer must have paid the funds to furloughed staff within 'a reasonable period' which has not yet been defined. If the criterion is not met, a 100% tax rate is applied, rather than the usual corporation tax or income tax due on the receipts. Lobbying is ongoing to extend the notifications deadline for errors made beyond 30 days. Claims already made should be checked carefully to make sure they were valid. Where possible,

overpayments should be corrected ahead of the penalty legislation deadline.

Additionally, while the draft legislation contains no specific penalties for errors or mistakes in any claim for support from the government, it does contain rules to penalise those who don't notify HMRC of their error within the time limit explained. The 'failure to notify' penalty has been used by HMRC in other tax enforcement campaigns. The penalties charged assume that the failure is deliberate and concealed, thereby triggering the highest penalty loadings.

Potentially employees may have a claim for breach of contract or unlawful deduction from wages, depending on the issue.

Ultimately, the Treasury Directions take precedence over the HMRC guidance where the guidance deviates from it. From HMRC's perspective, its functions in respect of the CJRS are defined by the Treasury Direction. It remains to be seen what happens where there is conflict. However, what is certain is that this is not something that will be forgotten about any time soon!

Calculating flexi-furlough pay in practice

The employer brings the employee off full-time furlough and they return to work part time from 1 July, working 70 hours in July. The employee works full-time but has variable hours.

Step 1: Work out the reference pay and hours: The equivalent pay period in 2019 was July 2019: 220 hours, gross pay £2,200. The average monthly hours across the whole 2019/20 year was 192.5 hours with average gross pay £1,925.

Step 2: Take the higher amount: The higher of the two figures is July, so £2,200 for 220 hours. The employer must use the same method to calculate the employee's usual hours for each period as they have used to calculate the employee's reference pay.

Step 3: Deduct hours worked to calculate furloughed hours: The furloughed hours are the difference between the usual hours for the period and the hours worked in that period. In July, this amounts to 220 usual hours minus 70 hours worked, amounting to 150 furloughed hours.

Step 4: Calculate furlough pay: Per month, this amounts to:

Reference pay x [furloughed hours/usual hours] x the percentage CJRS grant entitlement.

In July, this is: £2,200 x [150/220] x 80% = £1,200.

Furlough pay is therefore £1,200.

Step 5: Calculate the pay for the hours worked: Employers are responsible for paying employees for hours worked. This is calculated by applying the hourly rate to the hours worked. In July, this is 70 hours at £10 per hour (amounting to £700).

Step 6: Calculate the NIC/pension: This is calculated on a siimilar basis as before (see gov.uk). Total gross pay for the employee is the sum of the working pay and furloughed pay In July, this is £1,200 of furlough pay plus £700 working pay (amounting to £1,900).

	NI liability	NI grant	NI employer	Pension liability	Pension grant	Pension employer
July	£161.18	£96.73	£64.45	£41.40	£25.63	£15.77

What problems have we seen?

- Use of incorrect number of days (working days rather than calendar days).
- Salary sacrifice pension arrangements not correctly applied in relation to pay whilst on furlough and incorrect amounts paid over to the pension scheme.
- Staff working for the employer whilst on furlough up to 30 June and/or after 1 July when it's a furlough day.
- Not factoring top-ups or additional payments into the NIC element of calculations, claiming when no NIC is due or not capping based on the furlough grant element when making a claim for employer's NIC.
- Claims made for ineligible employees (employees not on the last RTI/payroll before 19 March or not previously furloughed before 10 June).
- Staff called back from furlough before 21 days, yet included in claim(s).
- Grant payments not paid over to employees, HMRC and the pension scheme (as appropriate).
- A lack of understanding of employment contracts and the different components through which an employee is paid, as well as of furlough agreement terms,

meaning that grant pay under CJRS is incorrect.

- Furlough agreements don't clearly identify how pay and benefits will continue during furlough; for example, pension, salary sacrifice or net pay benefits under flex schemes.
- A lack of understanding about how to deal with holidays when on furlough.
- Approved training days not being recorded nor working days after 1 July, therefore leading to potential employee underpayments as they are entitled to NMW or contractual pay.
- Inadequate documentation of furlough start and end dates and flexi-furloughing being applied.