Budget 2022

A submission from the Recruitment & Employment Confederation (REC)

September 2022

The Rt. Hon. Kwasi Kwarteng MP
Chancellor of the Exchequer
HM Treasury
1 Horse Guards Road
London, SW1A 2HQ

8th September 2022

Dear Chancellor,

Many congratulations on your appointment. On behalf of all of us at the Recruitment and Employment Confederation, I want to wish you every success in your new role, particularly as you come to the job at a critical time for our economy and our country. Securing stable economic growth has never mattered more to our shared prosperity, as it is the only thing that can deliver both lower taxes and public budgets that can sustain high quality public services. The Prime Minister's acknowledgement, in her speech in Downing Street, that it is business that will play a key role in delivering growth was timely and hugely welcome.

We are ready to play our part in this. The recruitment and staffing sector - the members of the REC - represent a professional services sector that is bigger in scale than either law or accountancy. And we reach far into the heart of the UK economy. Placing a million people into new permanent roles every year, and a million temporary workers into workplaces every day, REC members are advisors, planners and partners with businesses in every sector on recruitment, retention and productivity.

When it comes to the role of the workforce in driving growth and productivity, we are at acritical moment. From the pandemic to an ageing population, the shape of our workforce is changing, and firms are facing labour and skills shortages of a type not seen for many decades. As our recent work *Overcoming Shortages* set out that both economic and pay growth would be permanently damaged if businesses do not prioritise addressing these issues. But there is also a vital role for Government in supporting the Investment and change necessary. Our team were pleased to brief your officials on this recently, and we are ready to work with your team in whatever way you need to take this work forward.

Aside from the big, long-term changes necessary to drive growth across the UK, there are also short-term measures which the government could implement as soon as it can to get things moving. These will help households manage the cost-of-living crisis, but also help businesses navigate the increased cost of doing business. The Autumn Budget is the opportunity to provide stability, clarity and much needed support so that businesses can thrive. The first part of our submission looks at some of the policy interventions government can make to help with this. On behalf of our members, we are asking you to:

1. Support businesses to boost productivity by protecting them from extreme energy costs, reversing the National Insurance rise and reforming the business rates systems.
2. Reform the skills system to catalyse more investment by businesses - introducing flexibility to the high-quality training funded by the levy, which Is currently restricted to apprenticeships.
3. Create a tax system that incentivises work by reviewing the application of IR35 rules and providing clarity on employment status for tax.
4. Help parents stay in the workplace by focusing on childcare support and care providers - this will pay for Itself In rising Income tax receipts.
5. Work with REC members to reinvigorate welfare to work schemes, learning the lessons from Kickstart and Restart, to boost labour market participation.
6. Put stable and simple workers' rights at the heart of policy by creating a Single Enforcement Body (SEB) and introducing overdue umbrella company regulation that will protect both workers and compliant businesses.

The second part of our submission gives an oversight of the UK labour market using the data we have based our recommendations on. We are pleased that Treasury officials already cite our data as useful.

It is collected and processed at a faster rate than other similar research, making it the most timely insight on the labour market there is.

If you or your team like to arrange a meeting to discuss any of our policy asks in more detail, Ellie in my office (ellie.goddard@rec.uk.com) can put time in the diary.

Yours aye,

Neil Carberry
Chief Executive

Part one: Boosting firms to drive the prosperity we need.

Support businesses to boost productivity by protecting them from extreme energy costs, reversing the National Insurance rise and reforming the business rates systems.

Protect businesses from rising energy costs

The cost-of-living crisis can't be solved without addressing the cost of doing business. We are pleased that the Prime Minister has set out plans to support households via the Energy Price Guarantee, which will cap bills at £2,500 for each of the next two years. Although it is disappointing that targeted support for the most vulnerable wasn't included in this announcement. While comparable support for business was announced, that support only lasts for six months, meaning businesses only have short-term stability, at a time of significant economic uncertainty.

Our annual *UK recruitment industry status report 2020/21*, showed the impact of the Covid-19 pandemic. Unsurprisingly, we saw a significant drop in activity and revenue, particularly in permanent recruitment. Despite incredibly challenging times, the industry still added almost £36 billion to the value of the UK economy in 2020.[1]

The picture for 2021 appeared more positive, as restrictions eased and businesses could get back to doing business, hiring activity boomed. According to our latest *Labour Market Tracker*, the last week of August signalled the highest number of job adverts posted in the UK for 2022, despite wider economic uncertainty.[2] However, just as businesses have started to get back on their feet, they've been hit by a tsunami of problems including supply chains issues, labour and skills shortages, inflation at its highest rate in over 40 years, rising interest rates, and spiralling energy bills. If not curtailed the cost of doing business will lead to businesses folding and a reduction in tax revenues.

Employers' confidence in the broader economy has started to drop.[3] According to the Federation of Small Businesses (FSB) firms have experienced a 424% rise in gas costs and 349% increase in electricity since February 2021 with most UK firms due to negotiate their energy bills in October. It's not just SME's struggling, hospitals and schools aren't protected by any kind of energy price cap. Government will have to do more to support both people and businesses through the current crisis. Our recommendation is:

- *Government should introduce an equivalent energy price guarantee for all businesses for at least 12 months, followed by a review.*

Reverse the National Insurance Hike

While it's vital that the social care system is properly funded, the 1.25 percentage point rise in National Insurance, the UK's biggest business tax, was not the fairest way to do it. National Insurance isn't just a tax on jobs, it's a tax on labour market participation rather than profits. That means the lowest earners and labour-intensive sectors get hit hardest. With over half of the revenue coming from business, and falling more heavily on the thin-margin, consumer-facing businesses most affected by the pandemic, raising the rate was the wrong decision, and it should be swiftly reversed.

- *The National Insurance hike will make things worse in the current climate. Now is the time to reverse it.*

Make Business Rates fairer and encourage town centre investment

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[1] Recruitment & Employment Confederation, *UK recruitment industry status report 2020/21*, *15 December 2021*
[2] Recruitment & Employment Confederation, *Labour Market Tracker*, 2 September 2022
[3] Recruitment & Employment Confederation, *JobsOutlook,* 27 July 2022

For years, UK town centres have seen decline, something accelerated by Covid-19 which pushed people online. Transforming town centres simply from places to shop, into places to work is an important part of the levelling up agenda. This needs to be consolidated through investment in transport infrastructure especially buses. It's no good transforming our town centres if people can't get to them.

The other key issue to get right is incentivising businesses to stay in towns. A big part of that is ensuring we've got a business rates system that works and is responsive to economic change. The current system is outdated. It was designed in a pre-digital, pre-pandemic age, and is a significant burden on businesses, relative to comparable taxes in other countries.

Short-term relief, such as freezing the tax rate or multiplier for another year until the next revaluation of properties in 2023, was helpful. But there needs to be a long-term fix; to create a fair and responsive system. The other problem with the current system is that it hits small and medium businesses hardest, particularly those in deprived areas. The previous government acknowledged that SMEs are the backbone of Britain and committed to "doing all it can to help them flourish" [4]. Instead of stoking growth, the current system is pushing many SMEs to breaking point.

Business rates stifle investment in the facilities and innovations needed for changes towards net zero and exacerbate regional inequality. Many businesses in deprived areas get a double hit following a revaluation when economic activity falls, but their business rates bill does not fall immediately to reflect this. Although the previous commitment to hold revaluations every three years, was a welcome first step, it doesn't go far enough to create a fair and responsive system, nor does it protect businesses in times of economic challenge.

- *To help with the immediate cost of doing business, government should freeze business rates for SMEs until 2024.*
- *Government should reform the Business Rates system so that revaluations are conducted annually.*

Reform the skills system to catalyse more investment by businesses - introducing flexibility to the high-quality training funded by the levy, which is currently restricted to apprenticeships.

There is no question that apprenticeships are a great thing. The REC has been a long-term supporter of them, but we have also been calling for a reform to the levy system, so that the scheme can work for everyone in the labour market including temporary workers, who make up an increasing portion of the labour market.

Whilst some businesses fund apprenticeships for their employees via the levy, the very nature of temporary work means the vast majority of our members cannot access the system despite paying into it.

Many of our members have the willingness and resources to support, upskill and retrain their workers. The recruitment industry places one million temporary or freelance workers into work on any given day, but only 2% of temporary assignments last for 12 months or more - making the use of apprenticeships unviable (as apprenticeships are at least 12 months in duration). That means that almost a million working people are automatically cut off from valuable training opportunities, despite funds being available via the levy. This amounts to levelling down not up.

The current focus on year-long+ apprenticeships also disadvantages many businesses trying to fill vacancies quickly or at entry level. Take HGV drivers as an example. There is a shortage of almost 70,000 drivers in the UK[5]. Money from the levy could be used to fund some of their training requirements,

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[4] Cabinet Office and The Rt Hon Oliver Dowden CBE MP, *Small businesses are the backbone of our economy*, 10 April 2018

[5] Recruitment & Employment Confederation and Brabners LLP, *HGV Driver Shortage – The Causes, the Facts and the Potential Solutions, 1 February 2022*

which only take a few weeks, but qualified HGV drivers would have a job for life. The opportunity to upskill whilst maintaining some flexibility could make a significant difference to the earning potential of many temporary workers.

The economic cost of this rigid system is clear. Nearly £2 billion of employers' levy funds expired and was returned to the Treasury between May 2019 and March 2021. Opening up apprenticeship levy funding so businesses can use it for shorter, modular training courses would be a win-win for the industry, workers and government.

- *Government should redesign the apprenticeship levy to make it flexible so that more people can access high-quality, early-career apprenticeships, good retraining opportunities and modular options.*

Create a tax system that incentivises work by reviewing the application of IR35 rules and providing clarity on employment status for tax.

Review IR35 and provide clarity on employment status for tax

The Government's focus on free markets and enterprise as drivers of growth is hugely welcome. Diverse forms of engagement in our labour market show how powerful this can be - they stand behind the UK's excellent employment record. Ensuring policy does not penalise those who work flexibly should be a vital part of the Government's armoury in building a pro-enterprise approach.

Getting taxation right for contractors must be part of this. Understanding and complying with the off payroll working (IR35) rules is challenging. Many businesses, including our members and their clients find off-payroll working legislation the most difficult tax legislation to understand. Although the legislation has been reviewed and amended several times since its inception, it is still overly complex and does not place sufficient impetus on the end-client to provide their assessment and take responsibility for it. Trying to ascertain if and how it applies to recruitment agencies, in the context of limited client engagement and a lack of regulation on payroll companies adds to the bureaucracy and financial burdens on fee payers.

At a time when businesses are struggling because of severe labour market shortages, the impact of IR35 is made worse. As the competition to recruit from a limited pool rumbles on, businesses need contingent labour, to continue to operate effectively and fulfil demand. Businesses want to be compliant with IR35 but ambiguity over employment status for tax purposes increases the risk of falling foul of the rules and being fined.

- *IR35 is still not working so we need a full overhaul of the legislation. Businesses need a system that supports the use of flexible labour and works fairly for everyone involved.*
- *Government should reduce ambiguity over employment status for tax for businesses, to improve compliance and lower tax risks.*

Further improvements must be made to HMRC's CEST tool

Although some minor improvements have been made to HMRC's CEST tool, there is broad consensus that it is still not fit for purpose. HMRC's view that mutuality of obligation should not form part of the questions in the CEST tool, does not reflect the reality of how contractors work. This was reflected in the Professional Game Match Officials Ltd (PGMOL) case, which concluded that the referees were not employees of PGMOL. Despite this, HMRC's position is that the question of mutuality of obligation only goes to whether a contract exists at all – an assumption which has been built into the CEST tool.
In addition, the questions are often too vague. The examples in the CEST guidance such as painting and decorating, or market research are generally irrelevant in sectors where consultancy arrangements are most common. For example, where contractors deliver professional services, IT solutions, or media advice.

There also concerns about the accuracy of the CEST tool. Often changing a response to a single question changes a determination from "inside IR35" to "outside IR35". Case law on employment status for tax is clear that one factor is unlikely to determine a change in status, and that all relevant factors should be considered. As a result, the CEST tool is not sophisticated enough for hirers to rely on it and meet their obligation to use "reasonable care" when reaching a conclusion. The sheer number of "undetermined" outcomes shows us the tool isn't working as it's meant to. The Department for Work and Pensions (DWP) owing HM Revenue & Customs (HMRC) nearly £87m for "historic errors" in assessing tax liability for DWP off-payroll workers demonstrates why the CEST tool needs to be improved.

- *Improve HMRC's CEST tool so that all factors relating to a particular period of work are taken into consideration, and unrealistic assumptions are not built into the tool.*

Help parents stay in the workplace by focusing on childcare support and care providers - this will pay for itself in rising income tax receipts.

Parents now pay an average of over £7,000 per year for a part-time nursery place. So, it's hardly surprising that parents are dropping out of the labour market or reducing hours to offset this. As the cost-of-living bites, parents are juggling whether to go back to work or step back from the workplace to mitigate childcare costs. For a growing number of parents, it's a complete catch-22. Rising childcare costs will hamper productivity and future growth as fewer people participate in the labour market. Enhanced government support on childcare has the potential to be fiscally positive, as more parents stay in work (or higher paying jobs), pay more tax, and drive more growth for their employer.

The balance between childcare and work also disproportionately impacts women. The number of women with second jobs is at its highest level since before the pandemic and is still rising. There are a few reasons why this might be the case. More women than men work part-time as they often also take on caring responsibilities. For many, it's more realistic to 'top up' hours and earnings with a second part-time role than for someone working full-time. The gender pay gap also plays a role – there are more women working in lower-paid positions and lower-paid sectors like hospitality and healthcare.

Practical policies to help working parents return to and stay in work include schemes like tax-free childcare. But more must be done to promote them, and increase take up. This scheme is currently used by just over 500,000 families in the UK, compared to almost 800,000 that use childcare vouchers.

- *Government should increase the financial contribution to the tax-free childcare scheme so that for every £8 parents put in, government double their current contribution from £2 to £4.*

It isn't just parents and carers that need help with nursery funding though. Nurseries and other childcare providers also need support from government to ensure they can operate in the areas where childcare is limited. It currently costs £7.69 per day for a nursery to look after each child, but government funding is currently limited to only £4 per child per day. This leaves many providers unable to operate in certain parts of the UK. This, in turn, has an impact on the number of people in work.

- *Government should increase funding for nurseries and childcare providers so that no-one in the UK is left without provision.*

Work with REC members to reinvigorate welfare to work schemes, learning the lessons from Kickstart and Restart, to boost labour market participation.

Activation programmes, similar to Kickstart and Restart, are an excellent way of engaging those furthest from the labour market. The REC was pleased to be a Kickstart Gateway organisation and we are also a supplier to one of the lead providers for Restart. We'd like to see new and improved schemes introduced. Kickstart and Restart had the right intentions but were often let down by administrative challenges.

As a Gateway organisation, we were advocates for Kickstart and alongside many of our members, were passionate about making it work. The same emphasis on engaging business in Kickstart needed to be equally directed towards the young people Kickstart was designed to help. If government are to sponsor similar, follow up schemes, this time they need to put in place the right processes and resources to deliver a labour market activation programme. There is much that can be learnt from private practice - this is something that recruiters do day in and day out.

Although the number of unemployed young people has fallen, the number of young people in employment remains below pre-pandemic levels by 84,000, a 2% fall. This is because more young people are classed as economically inactive. 137,000 more young people have become economically inactive compared to pre-pandemic levels, an increase of 5%.

We know that the UK's NEET (not in employment, education, or training) rate for 20–24-year-olds is 14%, with the UK ranking 18 out of 38 OECD countries for labour market opportunities for young people. We need to do better for the workforce of the future and recognise the importance of getting this right if we are to create a sustainable labour market.

- *Government should introduce new and improved labour market activation schemes, learning from the past, to offer the best value for taxpayers and participants.*

Put stable and simple workers' rights at the heart of policy by creating a Single Enforcement Body (SEB) and introducing overdue umbrella company regulation that will protect both workers and compliant businesses.

In December 2019, the previous government announced its intention to publish an Employment Bill to protect and enhance workers' rights. This Bill was meant to address several issues from umbrella company regulation to the creation of a combined single enforcement body (SEB) – all with the aim of modernising compliance and enforcement frameworks. Unfortunately, the long-awaited Bill never materialised. Now is the time to get that Bill on the statute book.

Introduce umbrella company regulation

Without proper regulation, employers and workers risk being exploited by unscrupulous umbrellas offering tax avoidance solutions to people on their payrolls, a problem that increased after the introduction and extension of IR35. One example is Mini Umbrella Companies' (MUCs) which are set up as limited companies incorporated in the UK with British directors and a small number of temporary workers. The directors are typically replaced after a short period by an overseas director with minimal responsibilities.

Non-compliant umbrella companies and MUCs engage in fraudulent activity by abusing two UK government incentives (VAT flat rate scheme and the Employment Allowance). This enables them to escape their responsibilities of paying PAYE, National Insurance Contributions and other taxes. As a result, temporary workers don't receive all they are entitled to. Once the MUC has grown and no longer qualifies for tax relief, the payroll duties are shifted to the next MUC, and the pattern continues.

Lack of regulation allows for the constant evolution of tax dodging schemes, leaving workers vulnerable and costing the taxpayer millions in lost revenue. The latest iteration is to use a Joint Employment Model to reduce VAT bills.

Create a Single Enforcement Body

As first proposed in the Taylor Review, we need to see the creation of a Single Enforcement Body (SEB), that is well resourced. A SEB would act as a one-stop shop for labour market enforcement, combining the existing remits of the Employment Agency Standards Inspectorate, the Gangmaster's Labour Abuse Authority and HMRC's National Minimum Wage team.

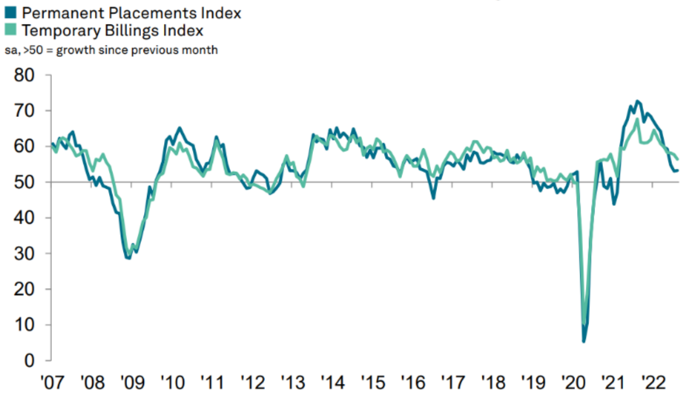
- *Government should re-commit to introducing an Employment Bill which would strengthen workers' rights and protections, create a SEB and introduce umbrella company regulation – benefitting workers and taxpayers alike.*

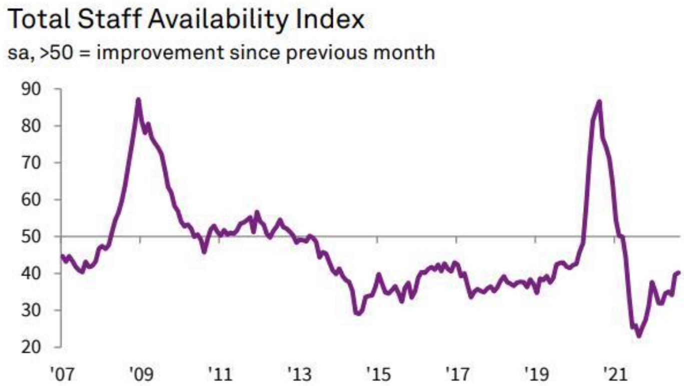
Part two: REC research reports - the current state of the labour market.

KPMG and REC UK Report on Jobs[6]

The latest UK *Report on Jobs* showed hiring activity growth slowing amid increased economic uncertainty.

- Though sharp by historical standards, the latest increase in **demand for staff** was the weakest seen for 18 months.
- Nursing/Medical/Care topped the **permanent staff demand** league table in August, followed closely by Hotel & Catering.
- All monitored job categories recorded higher **temporary vacancies** midway through the third quarter. Nursing/Medical/Care signalled by far the steepest increase in demand for short-term workers.
- All four monitored English regions recorded marked increases in temp billings, with the sharpest expansion seen in London.
- **Candidate availability** continued to fall sharply in August, with permanent worker availability deteriorating at a quicker pace than that seen for short-term staff.
- **Starting salaries** for permanent staff continued to rise rapidly in August, though the rate of inflation softened further from March's survey record. Temp wages meanwhile rose at a slightly sharper pace in August. Higher rates of pay were frequently linked to intense competition for candidates and the rising cost of living.





JobsOutlook[7]

The REC's latest *JobsOutlook* showed that employers' confidence in both the UK economic outlook and their own ability to invest in their business dropped quickly in the second quarter of 2022, with inflation and labour shortages causing widespread concern.

In April-June 2022, employer confidence in making hiring and investment decisions for their own business hit net: -13. This is the same level as April-June 2020, at the height of the pandemic. Meanwhile, business confidence in the economy fell by 40% from January-March 2022 to net: -50.

[6] Produced by S&P Global on behalf of the REC and KPMG, this monthly survey of 400 recruitment businesses provides analysis of permanent and temporary recruitment, vacancies and earnings in the UK labour market.
[7] Monthly survey detailing the hiring intentions of UK employers, featuring analysis of workforce demand and candidate shortages across all sectors. The survey includes data from 600 employers about their short and medium-term hiring plans.

Despite this, labour shortages mean that many firms are still trying to hire new staff. The hiring outlook stayed positive, although it slowed slightly from the first quarter of this year. In the short term, hiring intentions for permanent staff decreased by 5 percentage points to net: +23, while demand for temporary workers fell by 4 points to net: +12.

Labour Market Tracker[8]

- In the last week of August 2022, there were **2.08 million job adverts** in the UK, a new record high for 2022
- There were **269,000 new job postings** in the same period – the second highest figure on record
- All occupations in the UK, except dancers, actors and entertainers, recorded notable increases in job adverts
- All regions in the UK recorded an increase in job adverts
- Four out of the UK's top ten hiring hotspots were in the West Midlands in the week of 22-28 August

Occupation Sectors	July 2022 Unique Postings	Aug 2022 Unique Postings	% Change July to August
Logistics and Drivers	149,937	156,484	+4.4%
Construction	137,388	135,688	-1.2%
Industrial	37,504	36,555	-2.5%
Sales and Retail	130,716	127,211	-2.7%
Hospitality	155,687	150,767	-3.2%
Engineering and Technical	297,440	287,925	-3.2%
Business and Accounting	1,149,364	1,078,512	-6.2%
Health and Social Care	476,852	442,650	-7.2%
Information Technology	307,743	274,599	-10.8%
Education and Training	267,441	230,253	-13.9%

[8] Labour Market Tracker is a tool to help recruiters, businesses and policymakers see how the jobs market is evolving. It aims to spot signs of growth through job vacancy data from all local areas and occupations across the UK.

Regional Comparison

Gov't Office Region Name	July 2022 Unique Postings	Aug 2022 Unique Postings	% Change July to August
Yorkshire and The Humber	189,002	200,166	+5.9%
North West	264,666	272,243	+2.9%
West Midlands	194,894	199,085	+2.2%
Northern Ireland	45,802	45,930	+0.3%
Scotland	214,681	214,373	-0.1%
East Midlands	157,137	156,226	-0.6%
South East	332,131	329,345	-0.8%
East of England	197,433	195,496	-1.0%
South West	207,427	204,113	-1.6%
North East	69,275	67,341	-2.8%
Wales	85,715	82,260	-4.0%
London	552,850	482,246	-12.8%

Other Research Content: Labour and Skills Shortages

Many firms are still struggling with labour and skills shortages, and these will constrain economic growth over the longer term. The REC's latest report, Overcoming Shortages, shows exactly how much damage could be done if we don't take the necessary steps to solve these shortages and get the UK economy growing strongly again. With a 10% surge in demand across the economy, and the labour market restricted by shortages, we could see a 1.2% fall in expected GDP and productivity from 2024 – costing the economy anywhere between £30 billion and £39 billion a year. This figure is just short of the entire current defence budget, or two whole Elizabeth Lines.

In this report we turned to businesses across the UK for their views, as well as looking to Canada and Germany for things we could learn. The best outcome for the UK labour market is for both businesses and governments to change behaviour and put people planning at the top of their list, rather than dealing with recruitment as a cost to be minimised.

The government will need to dedicate resources to create a future workforce strategy, outlining the skills that the UK economy will need over the coming years. This means putting in place policies for skills, immigration, regional investment, and labour market activation. But many of the actions lie with businesses, which need to push workforce planning up the agenda at leadership and board level. By engaging in workforce planning in partnership with various stakeholders including recruiters; investing in skills; implementing equality, diversity and inclusion policies; and making sure they provide attractive working conditions, businesses can ensure they have the workers they need to grow sustainably and succeed in the long-term.

For further information on this submission please contact:
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The REC is the voice of the recruitment industry, speaking up for great recruiters. We drive standards and empower recruitment businesses to build better futures for their candidates and themselves. We are champions of an industry which is fundamental to the strength of the UK economy. Find out more at www.rec.uk.com