

Changes to tax legislation from 6 April 2014

28 March 2014

This notes sets out the REC's analysis of the incoming changes arising from the Onshore and Offshore Employment Intermediaries consultations, which will affect how and when employment businesses are responsible for the deduction of PAYE tax and NICs and the payment of employers' NICs. We are currently also reviewing the REC model contracts so see what changes are required.

This note has been written based on the Government's response to the Offshore Employment Intermediaries consultation published on 14 October 2013, the Onshore Employment Intermediaries consultation published on 13 March 2014, the legislation published on 27 March 2014 and related guidance.

There are still a number of points where we are lacking definitive guidance or clarity from HMRC; the REC has submitted a number of further questions to HMRC and we are currently awaiting a response on these. We will update this briefing note when we have those answers. We expect members will also have many more questions – please send them through to Lewina.farrell@rec.uk.com or Ben.farber@rec.uk.com and we will deal with these in future versions of this guidance.

The consultation documents, HMRC's response and their guidance on control are all available [online](#).

REC Legal and Policy

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1. Overview of changes

(1) Onshore Employment Intermediaries

- **The changes:**

- From 6 April 2014, any temporary worker working through an employment intermediary (defined as any company sitting between client and worker, including employment businesses or limited companies) will be deemed employed for tax and NICs purposes, **unless** that intermediary can demonstrate that the individual is not subject to (or to the right of) direction, supervision or control.
- The business with the direct contractual relationship with the end client for the supply of labour will be liable for accounting for income tax and both employee and employer NICs for all workers ultimately supplied to the end client **unless** they are supplied with fraudulent documentation by clients or other suppliers that misleads as to the nature of control or the manner in which tax and NICs has been deducted, in which case the businesses supplying such fraudulent documents will be liable.
- Agencies will be able to continue to supply workers on a self-employed basis either directly or through an intermediary provided they retain on record evidence that the individual in question will not be subject to (or to the right of) direction, supervision or control. See section 2 for further information on Supervision, Direction and Control.

- **Reporting Requirements:**

- From August 2015, agencies will have to submit a quarterly electronic return to HMRC detailing all payments to all individuals not otherwise accounted for via the agency's own RTI submission.
- This quarterly return will include details of payments made to self-employed workers supplied on a direct basis, umbrella PAYE workers and PSC workers. HMRC are working on the detail at the moment.
- Penalties for failure to report or submitting inaccurate reports will also come into force in 2015. The detail of the penalty regime is still to be confirmed. See Section 3 for further detail on Reporting Requirements.

(2) Offshore Employment Intermediaries

- **The changes:**

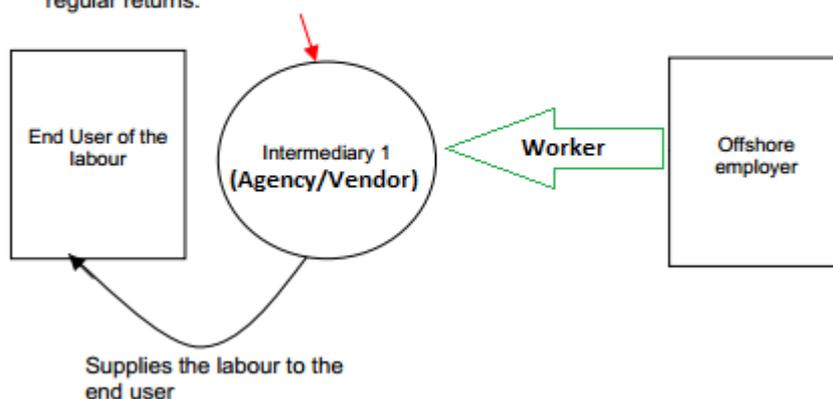
- For the purposes of the new legislation, an offshore employment intermediary is a business in the labour supply chain that is incorporated outside of the EU or Isle of Man e.g. an umbrella company based in the Channel Islands.
- From 6 April 2014 where a temporary worker is supplied to a UK-based client through an offshore employment intermediary, the UK agency with the contractual relationship with that UK-based client (known as 'Intermediary 1') will be liable for accounting for UK tax and

NICs for that temporary worker, even if the worker is employed by that offshore intermediary.

- There should be no financial advantage to a UK agency in supplying a UK-based worker to a UK-based client via an offshore intermediary. UK tax and NICs (including employer NICs) should be paid in full in such circumstances.

Offshore Employment Intermediaries

The employer's obligations to account for tax and NICs are given to Intermediary 1. Intermediary 1 is also required to submit regular returns.



- **Reporting requirements:**

- From August 2015, Intermediary 1 will have to account for any temporary workers employed offshore and not already accounted for through the agency's Real Time Information (RTI) submission via a quarterly electronic return to HMRC.
- Penalties for failure to report or submitting inaccurate reports will come into force in 2015. The detail of the penalty regime is still to be confirmed. See Section 3 for further detail on Reporting Requirements.

The relevant changes will be made to sections 44 – 47 (for onshore) and 687 – 689 (for offshore) of the Income Tax (Pensions and Earnings) Act 2003 (ITEPA) for tax purposes and the Social Security (Categorisation of Earners) Regulations 1978 for NICs purposes.

Enforcement:

What's clear: Enforcement will be based on the information submitted via the quarterly returns (detailed in section 3). Where agencies continue to report high levels of self-employed or offshore workers HMRC may well investigate to establish how genuine those arrangements are.

What's not clear: HMRC have yet to give an answer on how they will enforce against agencies that simply refuse to engage with the reporting requirements but that continue to supply workers on a self-employed basis.

Anti-avoidance - TAAR:

HMRC will also introduce a Targeted Anti-avoidance Rule to deter businesses from finding new ways to avoid income tax and NICs. One example cited in HMRC's response document is that of employment businesses which require all their workers to work through PSCs to avoid the legislation. In contrast, the TAAR will not apply where the PSC is set up for another reason e.g. to avail of the limited liability protections offered by incorporation¹.

2. Supervision, direction or control

What's clear: Employment businesses will need to know whether temporary workers they supply are subject to (or to the right of) supervision, direction and control by the end user client. Even if the contract under which the temporary worker is engaged states that s/he is not subject to supervision, direction or control, there is a risk to the supplying agency if, on inspection by HMRC, it is determined that in reality control does exist. In such circumstances, the amended legislation will apply i.e. the temporary worker's pay will be subject to PAYE and NICs, and employers' NICs will also be due.

Individuals simply having to comply with general site health & safety rules will **not** be deemed an indicator of supervision, direction or control.

What's not clear: Initial guidance from HMRC suggests that where an employment business has an overarching contract with a client which states that the temporary workers supplied under that contract are under the supervision, direction or control of the client, whether for insurance, health & safety purposes or any other reason, this will be sufficient to render all workers supplied under that contract in scope of this legislation, unless they fall within one of the other exclusions detailed in section 4. However HMRC have confirmed to REC that where such a clause exists purely to ensure compliance with H&S, this by itself would not render the temporary worker under supervision, direction and control. We are seeking further clarification regarding the insurance point.

HMRC definitions & guidance

HMRC have produced guidance on control which will be incorporated into the Employment Status Manual.² That guidance sets out the following definitions:

***Supervision** is someone overseeing a person doing work, to ensure that person is doing the work they are required to do and it is being done correctly to the required standard.*

Supervision can also involve helping the person where appropriate in order to develop their skills and knowledge.

¹ Paras 3.67 to 3.69 inclusive of the response. This is probably new section 46A ITEPA – we are checking this with HMRC.

² Available here:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/290051/Definition_of_Supervision_Direction_or_Control_with_supporting_examples.pdf

Direction is someone making a person do his/her work in a certain way by providing them with instructions, guidance or advice as to how the work must be done. Someone providing direction will often coordinate the how the work is done, as it is being undertaken.

Control is someone dictating what work a person does and how they go about doing that work. Control also includes someone having the power to move the person from one job to another.

The guidance also sets out 12 scenarios across a range of sectors, including web design, care work, construction, a HGV driver, a chemist and a teacher to help employment businesses understand how these definitions will be applied.

We would appreciate any comments members may have on HMRC's control guidance so that we may feedback to HMRC.

Evidence Requirements

What's clear: From 6 April 2014, agencies continuing to supply workers to a client on a self-employed basis, either directly or via another employment intermediary, must have in their power or possession evidence that the worker is not subject to (or to the right of) supervision, direction or control by any person in relation to the manner in which the worker provides the services. If an agency is unable to produce satisfactory evidence when requested by HMRC, then HMRC may look to recover tax and NICs from the agency.³

If an agency is supplied with a fraudulent document by a client that misleads as to the extent of control the client intends to exercise over the worker, the client, not the agency, will be held liable for tax and NICs.⁴ Likewise, if an agency is provided with fraudulent documents by a subcontracting agency or umbrella company that mislead as to the manner in which tax and NICs has been deducted, the company supplying the fraudulent documents will be liable for any sums owed⁵.

What's not clear: HMRC have not issued definitive guidance on what will constitute "satisfactory evidence" of a lack of direction, supervision or control. As noted previously, where HMRC choose to investigate, they will be looking at the reality of control on a case by case basis in a bid to avoid new contractual avoidance.

It is also unclear what exactly will constitute a 'fraudulent document' and whether an intention to deceive on behalf of the party supplying the fraudulent document will need to be established for the agency to avoid liability. We are checking this point with HMRC.

³ Text taken from draft ESM 2090 at <http://www.hmrc.gov.uk/drafts/draft-esm-manual.pdf>

⁴ Section 44(4)(a)

⁵ Section 44(4)(b)

Please note that REC cannot confirm whether any temporary worker is or is not under the supervision, direction or control of any person. This will depend on the circumstances of the assignment, the nature of the role and the seniority of individual concerned. Ultimately the client should confirm whether the individual is or is not under its supervision, direction or control. If the client insists s/he is not, members should obtain this in writing in order that liability will be transferred to the client if such confirmation is fraudulent.

3. Reporting requirements

Both sets of changes to ITEPA will bring in additional reporting requirements. HMRC envisage that all data required to comply with both the Onshore and Offshore changes will be submitted in a single return.

What's clear: Reporting requirements for both the Onshore and Offshore changes have been delayed until 2015, with the first report due by 5 August 2015, reporting on the period 6 April 2014 – 5 July 2015. Penalties will be introduced for failing to submit reports or for submission of inaccurate information, but the details of this penalty regime have still to be determined.

Reports will have to cover all payments to individuals not otherwise accounted for via the agency's RTI submission. This will include payments to umbrella PAYE workers and PSCs despite these workers being out of scope of this legislation (further information on Exclusions can be found in section 4).

Please note that although the reporting requirements have been delayed to 2015, members must comply with the liability provisions (i.e. to deduct PAYE and NICs) from 6 April 2014. HMRC will be able to go back to this date to reclaim any sums due but not paid.

What's not clear: HMRC is still considering what information it will require employment businesses/vendors to report on and how. In the meantime we set out below what we expect employment businesses will have to report on:

With regards to **self-employed individuals**:

- (1) The name and contact details of the individual;
- (2) The company to which they are supplied;
- (3) The reason why tax and NICs has not been accounted for; and
- (4) The gross sum paid to the individual.

With regards to **PSCs**:

- (1) the name of the PSC the temporary worker worked through;
- (2) the name of the temporary worker; and
- (3) the gross sum paid to the PSC.

With regards to **umbrella PAYE workers**:

- (1) The name of all workers supplied via the umbrella company;
- (2) The name of the umbrella company; and
- (3) The gross sum paid to the umbrella company.

With regards to **Offshore workers**, we expect Intermediary 1 will have to report on:

- (1) The name and contact details of offshore workers;
- (2) The name and contact details of the offshore employer;
- (3) Information about the manner in which they are engaged and paid; and
- (4) Reasons why income tax and NICs has not been deducted by Intermediary 1.

4. Exclusions from changes

(1) Onshore Employment Intermediaries

The Onshore Employment Intermediaries legislation will **not** apply in the following circumstances:

- For income tax purposes, if the remuneration the worker receives in consequence of providing the services is otherwise chargeable as employment income, or
- When the worker is legitimately self-employed (i.e not subject to supervision, direction or control), or
- if the worker provides their services wholly in their own home, or
- if the worker provides their services wholly at premises which are not controlled or managed by the client, unless the worker is required to do so at those premises because of the nature of the services and work being provided to the client, or
- if the worker provides their services as an actor, singer, musician or other entertainer or as a fashion, photographic or artist's model.

The legislation is **not** intended to apply to genuine PSC arrangements, where HMRC is satisfied revenue extracted from PSCs is taxed appropriately already – either as employment income in the form of a salary, or via dividend. Payments to PSCs will still have to be reported from April 2015. Further information on PSCs can be found in section 5.

(2) Offshore Employment Intermediaries

Oil & Gas workers – separate provisions apply to those working in the oil and gas sector. These will be covered in a separate briefing.

5. How the changes affect different engagement models

Direct PAYE engagement by employment business – no change required



Employment businesses can engage temporary workers either (1) on contracts for services or (2) on contracts of employment. In both of these scenarios, the employment business will be responsible for deduction of PAYE and NICs, and for payment of employer NICs.

REC has produced model contracts for both scenarios, together with partner client terms. These contracts acknowledge that the temporary worker works under the supervision, direction and control of the end user client. The temporary worker will also be an agency worker for the purposes of the Agency Worker Regulations 2010 (AWR), and subject to meeting the relevant criteria, may also be entitled to be auto-enrolled for a pension.

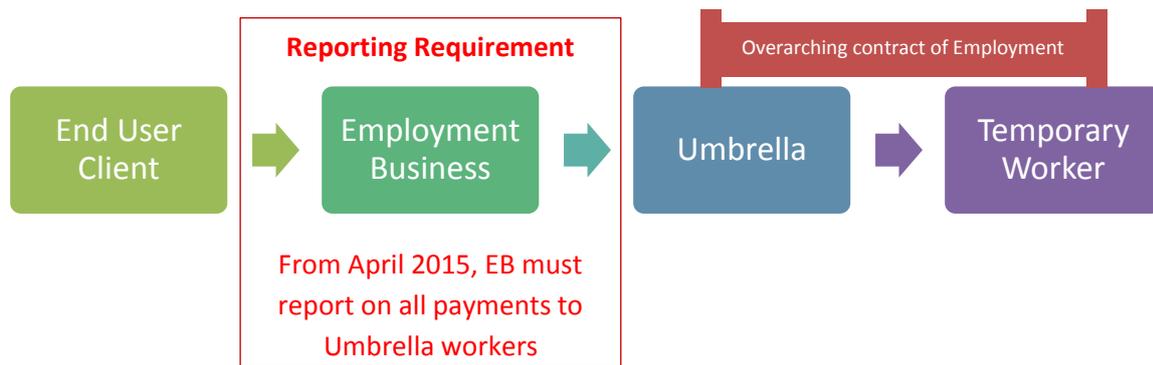
In both scenarios, the employment business deducts PAYE and NICs from the temporary worker's pay and pays secondary (i.e. employers') NICs. The employment business also reports on payments made to the temporary worker via Real Time Information (RTI).

If you already engage a temporary worker in this manner, you do not need to change your contracts or processes.

See REC model contracts:

- Contract for services
 - Contract 3 (client terms) and 4 (temporary worker terms).
- Contract of services
 - AWR Regulation 10 (aka Swedish Derogation or Pay between assignments contract) – contracts 13 (client terms) and 14 (temporary worker terms)
 - Zero hours contract – contracts 15 (client terms) and 16 (temporary worker terms).

Engagement via an Onshore PAYE umbrella – no change in liability, new reporting requirement



When supplying workers via an Onshore PAYE umbrella, those workers should be engaged on an overarching contract of employment whereby the umbrella company assumes all employer obligations, including the obligation to deduct PAYE and NICs, as well as payment of employer NICs. Such an arrangement will satisfy the new Onshore Employment Intermediaries requirements, provided the agency ensures that the umbrella companies with which it engages do deduct and pay UK tax and NICs appropriately.

Umbrella Best Practice

When engaging with an Onshore PAYE Umbrella, REC recommends that members:

- Request and review the contract between the umbrella company and the temporary worker to establish:
 - whether it is an AWR Regulation 10 contract or another contract entitling the temporary worker to equal treatment under AWR;
 - whether the umbrella is meeting its tax obligations, as well as other obligations relating to immigration law, AWR and statutory entitlements such as holiday pay and SSP;
- Request assurances from the umbrella company that it operates any travel and subsistence scheme in compliance with HMRC guidance;⁶
- Establish whether the worker has opted out of the Conduct Regulations or not so that the correct terms of business can be issued to both the end user client and the umbrella company.
- If operating in the GLA regulated sector, ensure that the umbrella has a valid GLA licence.

Engagement via an Offshore PAYE Umbrella

While the changes which take effect from 6 April 2014 will remove much of the value of engaging with offshore intermediaries when supplying UK-based workers, the model is still a valid provided UK tax and NICs is accounted for. Offshore intermediaries are also still a viable option when supplying internationally mobile workers.

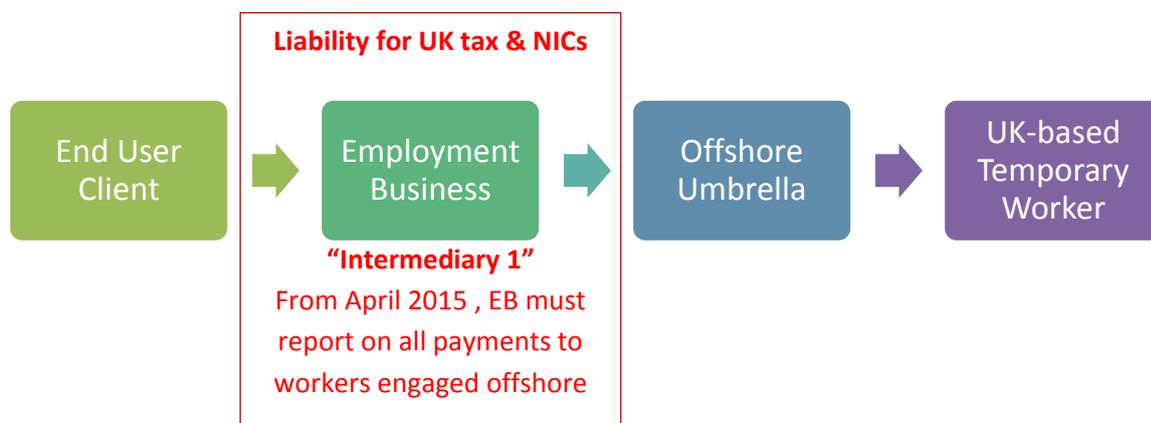
REC advice is to not engage with an offshore intermediary unless you have had specific detailed advice as to the benefits and your potential liabilities of doing so. If, for example, an agency supplies

⁶ We believe that HMRC will review travel and subsistence schemes in 2014.

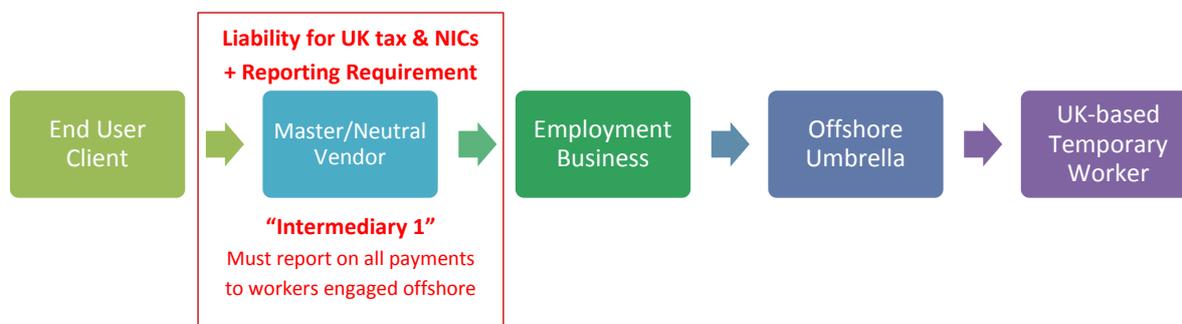
a teacher to work in a UK school or a nurse to work in a UK hospital, there should be no financial advantage for them to work through an offshore company. In contrast, if an agency supplies internationally mobile workers who work for overseas clients, there may be a valid reason for them to work through an overseas business.

Employment businesses should be aware that master/neutral vendors may in future either contractually prohibit the use of offshore intermediaries, or seek indemnities from employment businesses further down their supply chains, or both.

Offshore Umbrella: Employment business has contract with the end client



Offshore Umbrella: Master/ Neutral vendor has contract with the end client

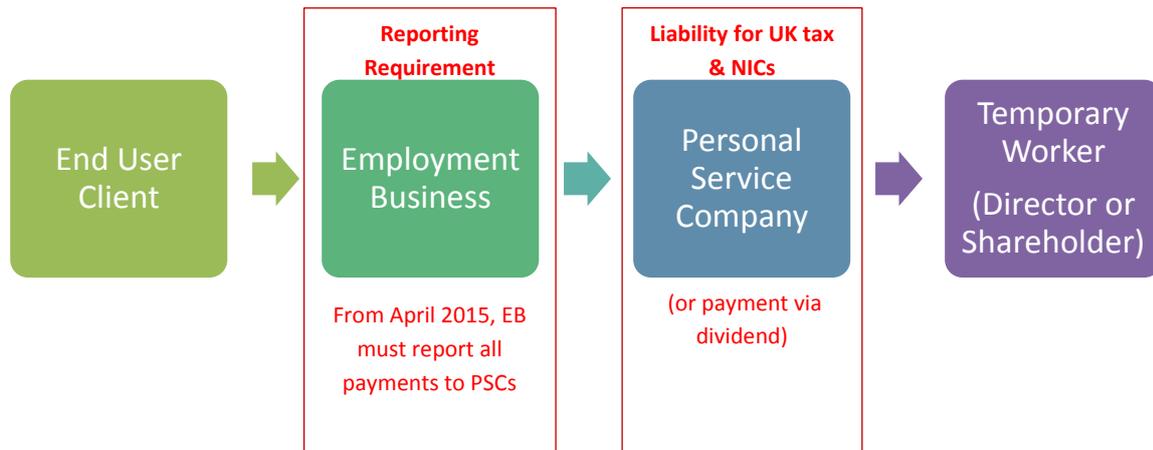


Separate arrangements have been put in place for the oil and gas sector which we will deal with in separate guidance.

REC model contracts:

- Contracts 5 (client terms) and 6 (limited company terms) – inside IR35, opted out of the Conduct Regulations.
- Contracts 7 (client terms) and 8 (limited company terms) – inside IR35, not opted out of the Conduct Regulations.

Engagement via personal service companies



Employment businesses will **not** be liable for tax and NICs on payments made to the PSC unless **all** of the following criteria apply:

1. the PSC worker personally provides services to another person as a consequence of a contract between that person and a third person;
2. the manner in which the PSC worker provides the services is subject to (or to the right of) supervision, direction or control by any person;
3. remuneration is received by the worker in consequence of providing the services (i.e. is not paid as dividends);⁷ and
4. that remuneration does not constitute employment income apart from under the agency legislation (i.e. is not paid as a salary already subject to PAYE and NICs).

Income can only be permanently extracted from a PSC in the form of dividends or salary. Therefore, if the remuneration is received in consequence of the PSC worker providing the services, it would have to be in the form of salary, which **would** constitute employment income subject to PAYE and NICs, thus not meeting criteria 4. If the remuneration is received as dividend, it would **not** be in consequence of providing the services but the shareholding in the PSC, thus not meeting criteria 3.

Even if the temporary worker is subject to (or to the right of) supervision, direction or control by the end client, if s/he is paid via dividend or via salary by the PSC, then the PSC remains liable for all relevant deductions and tax.

Definition of PSC

There is no statutory definition of a PSC though HMRC have defined it in their consultation and response documents as *“a small limited company through which an owner/director provides their own personal services”*.^{8 9}

⁷ HMRC’s response states that genuine dividends would not normally be considered to be remuneration for the purposes of the agency legislation. However in the case of avoidance there may be instances where HMRC will argue that these payments are remuneration either as general earnings or as remuneration for the purposes of the agency legislation.

Due diligence

Employment businesses will need to do appropriate due diligence to ensure that the limited company they have engaged with is a PSC. Recommended due diligence is as follows:

- (1) Check the company has been properly incorporated e.g. by checking Companies House;
- (2) Ensure the individual(s) supplied by the company is/are owners/directors and shareholders of the company;
- (3) Confirm in writing that the PSC will either pay the individual supplied via dividend or salary. This will be required to benefit from the transfer of liability provision set out in section 44(4)(b);
- (4) Check if the company is VAT registered or not (though bear in mind it will only have to be VAT registered if the VAT threshold will be met).

Risks of engaging with PSCs

Agencies must be mindful that PSCs, though in all likelihood out of scope of the Onshore legislation, will still have to ensure they are not caught by the Managed Service Company legislation or IR35.

Agencies should be wary of “PSC solutions” that are mass-marketed to existing self-employed or PAYE workers – there is a high risk HMRC could deem these disguised managed services.

Agencies should also be mindful of the proposed Targeted Anti-Avoidance Rule that HMRC will use to combat avoidance tactics like the forced migration of workers into PSCs.

REC model contract:

Individuals working through PSCs are more likely (though not guaranteed) to be genuinely self-employed and outside IR35. However you must be sure of an individual’s status before you issue contracts.

- Contracts 9 (client terms) and 10 (limited company terms) – outside IR35, opted out of the Conduct Regulations.
- Contracts 11 (client terms) and 12 (limited company terms) – outside IR35, not opted out of the Conduct Regulations.

⁸ Page 20, HMRC “Onshore employment intermediaries: false self-employment: A summary of responses 13 March 2014”.

⁹ We are currently checking the position regarding limited liability partnerships (LLPs). Further tax changes affecting LLPs also come into effect on 6 April 2014.

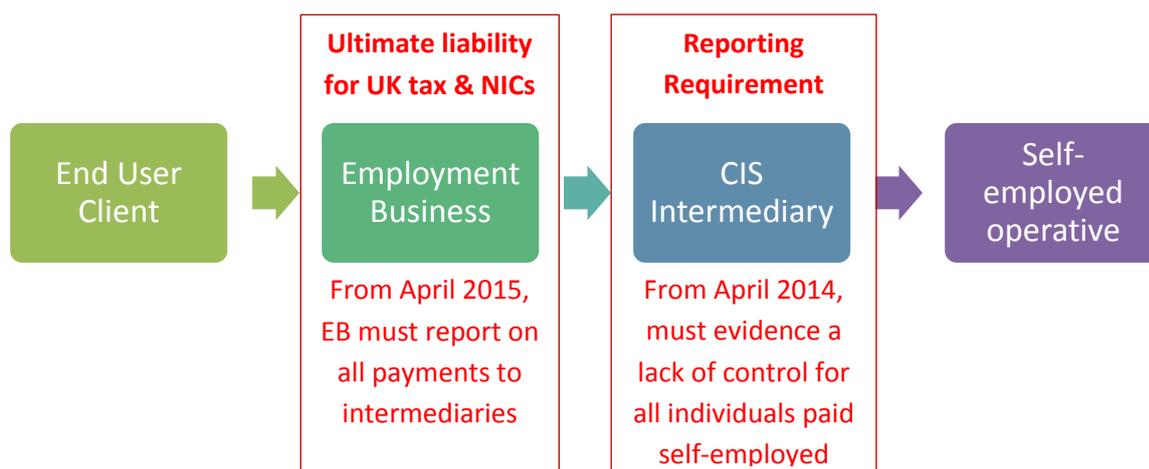
Engagement on a self-employed basis

Engaging with sole traders



Individuals may claim to be genuinely self-employed though they have not incorporated a limited company. They may indeed be genuinely self-employed and therefore responsible for their own tax and NICs. However, in the absence of a limited company (or other corporate entity) should the individual not pay the appropriate tax and NICs, HMRC could pursue the employment business if it deems the individual should have been deducted PAYE and NICs. Equally, should the individual work under (or be subject to the right of) supervision, direction or control, the employment business should deduct PAYE and NICs. For this reason REC has not produced model contracts for engagement with sole traders.

Engaging via CIS intermediaries



It will be possible for employment businesses to continue to pay individuals via CIS intermediaries provided those individuals are **not** subject to (or to the right of) the supervision, direction or control by the end user client, and the supplying agency can evidence this. If the employment business does not have sufficient evidence, it will be liable for the deductions together with payment of employers' NICs. Should the client provide false information regarding supervision, direction and control, the

liability will transfer to the client.¹⁰ We recommend that members review HMRC's guidance on supervision, direction and control for further advice.

The Government considers that the construction sector is the sector with the largest false self-employment problem and we expect HMRC to focus enforcement efforts on this sector from an early stage. Members should be aware and should ensure that their candidates are aware that **having a Unique Tax Reference number (UTR) does not by itself make a construction worker genuinely self-employed and does not automatically mean that s/he should be paid via CIS.**

REC model contracts:

We anticipate that where members recognise that individuals should no longer be paid via CIS they will either (a) engage them directly on a PAYE basis, (b) engage them via a PAYE umbrella or (c) engage them via a PSC.

Members must be satisfied that an individual does/will not be working under the control of the end user client before they can supply them under CIS, in which case members can use model contracts 9 to 12 identified at section 4 above. These contracts have not been drafted specifically for the construction sector and will need to be amended to take into account construction related health and safety issues, lengthier supply chains and sub-contracting arrangements. REC legal business partners, Brabners, can assist you at discounted rates.¹¹

¹⁰ New section 44(4)(a) ITEPA

¹¹ For details see <https://www.rec.uk.com/business-support/business-partners/legal-and-compliance-support/brabners-chaffe-and-street>

Summary of REC contracts to use

Please read the guidance notes to each contract to ensure that you use the appropriate contract.

Supply model	Client terms	Temporary worker terms	Liability to deduct PAYE and NICs	Reporting requirements
Engagement by the employment business (EB)				
Direct PAYE engagement	3	4	EB	As now via RTI.
Employed on an AWR Regulation 10 contract	13	14	EB	As now via RTI.
Employed on a Zero hours contract	15	16	EB	As now via RTI.
Engagement via a limited company				
Working inside IR35 (i.e. under the supervision, direction and control of the client), <u>not</u> opted out of the Conduct Regulations	5	6	<ul style="list-style-type: none"> The limited company if UK based. Intermediary 1 if an offshore limited company 	<ul style="list-style-type: none"> The limited company via RTI if UK based. Intermediary 1 if an offshore limited company
Working inside IR35 (i.e. under the supervision, direction and control of the client), opted out of the Conduct Regulations	7	8		
Working outside IR35 (i.e. <u>not</u> under the supervision, direction and control of the client), <u>not</u> opted out of the Conduct Regulations	9	10	The limited company	The limited company via RTI.
Working outside IR35 (i.e. <u>not</u> under the supervision, direction and control of the client), opted out of the Conduct Regulations (more likely to a PSC situation)	11	12	The limited company	The limited company via RTI.
Working as a Master/ neutral vendor	19		<ul style="list-style-type: none"> The EB or umbrella company where they are UK based. The master/ neutral vendor where the temporary worker works through an offshore intermediary	
Terms with second tier suppliers	20			

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