



TAXREP 04/14

(ICAEW REP 15/14)

ICAEW TAX REPRESENTATION

ONSHORE EMPLOYMENT INTERMEDIARIES

Comments submitted on 4 February 2014 by ICAEW Tax Faculty in response to HM Revenue & Customs consultation document *Onshore employment intermediaries: false self employment* published on 10 December 2013

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation document [Onshore employment intermediaries: false self employment](#) published by HM Revenue & Customs on 10 December 2014.
2. We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. On 21 and 30 January we attended meetings with HMRC jointly with other professional bodies in which we were able to put forward some key comments and concerns and discuss aspects of the consultation document (condoc).
4. Information about the Tax Faculty and ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's Ten Tenets for a Better Tax System by which we benchmark proposals to change the tax system.

WHO WE ARE

5. ICAEW is a world leading professional membership organisation that promotes, develops and supports over 142,000 chartered accountants worldwide. We provide qualifications and professional development, share our knowledge, insight and technical expertise, and protect the quality and integrity of the accountancy and finance profession.
6. As leaders in accountancy, finance and business our members have the knowledge, skills and commitment to maintain the highest professional standards and integrity. Together we contribute to the success of individuals, organisations, communities and economies around the world.
7. The Tax Faculty is the voice of tax within ICAEW and is a leading authority on taxation. Internationally recognised as a source of expertise, the faculty is responsible for submissions to tax authorities on behalf of ICAEW as a whole. It also provides a range of tax services, including TAXline, a monthly journal sent to more than 8,000 members, a weekly newswire and a referral scheme.

KEY POINT SUMMARY

8. We support tackling evasion and the principle of moving responsibility for paying PAYE down the chain towards end users where they are paying the workers.
9. However we believe that implementing the proposals in the condoc should be put on hold for a year as to enable agencies and construction companies to:
 - agree new prices, and
 - put into place secure data systems for sharing workers' personal details.
10. We recommend also that the outcome of the current consultation should be a short term measure pending working up a long term solution by way of a holistic review of the whole area of employment/self employment, personal service companies, IR35, managed service companies, umbrella companies and agencies.
11. This is because:
 - The proposals in this consultation document can at best be described as scattergun.
 - We question the piecemeal way in which reforms in this area are being introduced, and the underlying rationale for the changes.

- Evasion should be countered by enforcing the law, rather than simply introducing new laws, especially if it means that tax law definitions will differ from employment law definitions.
 - We think the anticipated behavioural and fiscal impacts have not been properly researched and the proposals if implemented will increase construction costs, which will adversely affect government as one of the biggest customers of the construction industry.
 - The proposals will hit genuinely self employed individuals, particularly those in service industries, whilst not impacting on many of those whom from our reading of the paper are the intended target, ie construction industry tradesmen.
 - The meaning of 'control' is confused.
 - The draft legislation will inter alia require the impossible, namely to prove a negative.
 - We have concerns about data security and the opportunities for cyber identity fraud.
 - An eight week consultation period to settle legislation on a topic which should encompass not only tax and NIC but also employment and contract law is unreasonable.
12. In short, we are doubtful whether the condoc proposals will work in the manner intended, or in any way close to that.

GENERAL COMMENTS

Overall approach

13. We support the policy objective of reducing tax evasion and recognise that there is abuse going on. However, the proposals are scattergun rather than cohesive. They are latest in a long series of measures that are either missing their targets or would do if they had not been shelved (income shifting, travel expenses, controlling individuals, false self-employment in the construction industry, offshore employment intermediaries, and IR35 itself; see also our recent written evidence to the House of Lords inquiry into personal service companies [TAXREP 60/13](#)). The only one that has really worked is the managed service companies rules introduced in 2007. The condoc proposals will not catch all those who it is intended should be caught but they will catch many who it is not intended should be caught.
14. Given that (as we pointed out in our response [TAXREP 36/13](#) to the false self-employment condoc and what we assume is meant by 'should be an employee' in para 1.6 of the condoc) the problem is one of evasion rather than avoidance, the best way to deal with this would be increased and better-targeted compliance activity by HMRC, rather than new legislation. HMRC state that people try to circumvent the law by putting false substitution clauses into documents, yet the courts are quick to strike these out where they are not warranted (eg in [Castle Construction \(Chesterfield\) Ltd v CRC](#) [2008] SpC 00723 (STC (SCD) 97); [Consistent Group Ltd v Kalwak](#) [2007] UKEAT 0535 06 1805; [JLJ Services Ltd v HMRC](#) [2011] UKFTT 766; and [Autoclenz Ltd v Belcher](#) [2011] SC 41 – the last of these is a recent Supreme Court judgment which gives more junior courts considerable encouragement to disregard bogus substitution clauses). We think that HMRC are proposing new legislation because they do not have enough inspectors dealing with the problem using existing powers.
15. We suggest that onshore and offshore employment/self employment/agency/personal service companies/IR35/etc and the distinction between the supply of staff and the supply of services (other than for VAT which is clear) should be reviewed from scratch across the board on a holistic basis, rather than by way of the current piecemeal approach. As the VAT distinction is clear and well understood, we believe that it should form the basis of this holistic basis.
16. If agencies are not behaving in an acceptable manner, then construction industry scheme (CIS) gross payment status should be withdrawn from businesses that are not directly involved

in construction activities. HMRC could offer a system of accreditation to agencies that provide compliant schemes. This would be similar to the accreditation of software houses that provide approved CIS systems.

17. Insofar as concerns individuals, some may set up personal service companies (with the likelihood of a lack of realisation or advice from off the shelf company providers that accounts and returns should be filed and the company's bank account should not be used as a personal moneybox), but for others the proposals raise the likelihood of managed service companies filling the void, perhaps disguised as something else. We question whether HMRC have the resources to tackle all the different schemes that might be dreamt up.
18. We would also mention the human rights aspect, as the prospect of taxing individuals as if they were employees without giving them employment rights will give rise to the same problems that led to the 2008 deeming proposals being dropped. The common, although sometimes erroneous, perception of the public is that someone who pays tax under PAYE is an employee, and affected workers understandably feel aggrieved when they discover that they are not. We suggest that there should be greater, and more public, co-ordination between HMRC and the Department for Business, Information and Skills (BIS) to ensure that BIS is content, particularly (as here) where HMRC's proposals affect relatively low paid workers.

Impact assessment and construction costs

19. We also question the robustness of the research and the veracity of the anticipated impacts both fiscal (assessed estimated exchequer gain of c.£½ billion pa) and behavioural cited in the consultation document.
20. In particular, there seems to be an implicit assumption in the condoc that it will be the 'CIS umbrella' companies that will be paying most of this. This is unrealistic: £520 million a year spread over 250,000 workers comes to £2,080 a head. An umbrella charging the £25 a payslip stated in the condoc (para 1.7) will only be making £1,300 out of this arrangement, out of which it will have to pay its costs. Furthermore, if £25 is an excessive cost simply for processing a payslip with no tax deducted (and we accept that it looks high), it is a reasonable reflection of the actual costs of running an umbrella company that has to operate PAYE and offer employment rights, which is what these companies will be supposed to be doing when the legislation comes in. Typically, once the overheads of bespoke IT systems, marketing costs and staff are included, an umbrella company will be left with about a third of this sum as profit. A £25 charge is unlikely to cover such costs and in our view the costs will have to be met in the form of lower pay in the short term, and higher construction costs later on.
21. Bearing in mind that in the construction industry the worker will already have had 20% of his pay deducted on account of tax and NI, and that the lower paid ones will frequently get tax rebates at the end of the year as a result of this, it seems to us that virtually all of the extra money raised from the construction industry is in fact going to represent employer's NI. It is only fair and reasonable that this should be paid, in economic terms at least, by the people for whom the workers work – that is, the construction industry. It seems unjust that this should be paid for by the worker, yet that (in the short term at least) is the likely result as the industry will not be able to raise its prices to cover the extra costs at such short notice.
22. The estimated impacts need to take into account the practical problems of construction firms having to work together and the inevitable downtime in such a fluid industry, for example where materials or the right tradesmen are not available or the weather is too poor for work to take place, all of which makes it uneconomic to pay workers when nothing is done. Every construction project is unique and there is rarely any steady and regular fall-back work. If there is pressure on large construction businesses to increase prices then this may lead to cartel behaviour.

23. We do not think that the anticipated exchequer gain will accrue to any great extent from reduced profits of intermediaries and agencies as they will still need to be paid to cover their costs. Such additional costs will instead be passed as price increases onto end users/ customers, of which government departments such as the NHS and local government are amongst the biggest. Attempts to fund these additional costs by reducing the net pay of workers is likely to prompt those workers to move to other areas of work (including abroad), to be replaced by people from overseas.

Targeting of the proposals

24. We believe that the proposals will hit genuinely self employed individuals whilst not impacting on many of those who from our reading of the paper are the intended target.
25. The Castle Construction case featured tradesmen who were not subject to supervision, direction or control as to how the work was done. This was one of the main reasons why Castle Construction won the case. The building trades are ones where people learn their trade as young men and then are able to do a job that does not radically change for the rest of their lives, so there is no need for a third party to control how someone goes about their work.
26. Workers who the proposal is intended to cover but will not include drivers. Like construction, this activity is something that people learn when young, and they then know how to do it thereafter. We understand that it may even be illegal to supervise, direct or control how a driver drives his van.
27. People that the proposal does not intend to encompass but will include all self-employed sales forces, such as used in the insurance, double glazing and timeshare industries, maintenance people paid by the item (eg white goods repairmen), telecoms installers, couriers, short-term subcontractors who help out accountants in the January self assessment tax return filing rush, and events managers. A partner in a partnership will be affected if he receives some of his remuneration by reference to the turnover in his department or division, or even an individual job. It will even include liquidators and insolvency administrators, and could even include a sole practitioner accountant who helps out a client or an individual who sells his business and after the sale provides on a consultancy basis the benefit of his knowledge and knowhow. In short, most self-employed people in service industries would be at some risk. We should welcome confirmation that this is not the intention, and an explanation of why the legislation does not affect them.
28. This is because the proposed provision does not require the paying party to be an agency or umbrella company, as is doubtless intended: all that new section 44(1)(a)-(c) requires is that:
- the worker is personally involved in the provision of services to someone else – this means anyone who works on providing a service, for example a life assurance salesman arranging a policy for one of his firm's clients;
 - there is a contract between the client and a third person (in this example, the insurance company) under which the client pays for the services – obviously there will be; and
 - remuneration is receivable by the salesman in consequence of being involved in the provision of services – this would catch any commission based on the premium being received.
29. The best way of dealing with this would be to confine the legislation to cases where the paying party is an employment business, as defined by the Employment Agencies Act 1973, or an umbrella company. That would require defining 'umbrella company', which might give rise to attempts at circumvention; however the success of HMRC's definition of a managed service company in 2007 suggests that this could be done.

Control

- 30.** We are concerned that the meaning of control and its implications are being confused. Control over what the worker does is being muddled up with how the worker does his job. For example, in Example 3 the end user asked painter C to work in various different buildings. This is not controlling the manner in which the work was undertaken as envisaged in para 4.2 of the condoc, ie how the painter applies the paint, but is controlling what work is done, which is always the prerogative of a customer of anyone who is self employed, and indeed it is a feature of, for example, building work that different tasks need to be carried out in a certain order.

The need to do the impossible, ie prove a negative

- 31.** New section 44(2) requires the taxpayer to prove that there is no control. Control is an abstract concept, so, whilst it is possible to prove control is there when it is present, if there is no evidence either way, it is impossible to prove that control is not there when it is not. This requirement is oppressive, and may prove unenforceable.

Identity security and cyber fraud

- 32.** We are concerned about the identity security implications of requiring agencies to make returns. Quite apart from the compliance burden and real difficulties in obtaining the information if people are recalcitrant, and the need for HMRC to enable agents and HMRC to liaise with one another (another box on form 64-8?) and agents where agents complete and submit returns on behalf of clients, it will in some cases be necessary for agencies to obtain the data needed to complete the returns in bulk from umbrella companies. Identity thieves could hack into emails containing large amounts of valuable and confidential information, eg emails with spread-sheet attachments containing names, addresses, dates of birth, national insurance numbers, passport/identity card numbers, etc.
- 33.** The requirement to pass on national insurance numbers is a particular concern as they are frequently the last pieces of information to be obtained by criminals when cloning identities.
- 34.** The passing across of such data between businesses should take place in a secure document exchange environment similar to that used when submitting returns to HMRC.
- 35.** We believe that an extra year should be given before the quarterly reporting requirements are brought in, to enable agencies to set up secure document exchanges. Whilst we appreciate that HMRC cannot control what happens between third parties, we recommend that HMRC guidance should emphasise the importance of passing this information in a secure manner.

Items for guidance

- 36.** If the legislation goes ahead as planned, we believe that the following areas will need to be covered comprehensively in HMRC guidance:
- the meaning of 'supervision' and 'direction'. Although these terms have always been there, not much attention has been paid to them. With the absence of a requirement for personal service, the focus will shift and make these terms much more important, and whilst there is a great deal of precedent on the meaning of 'control' there is hardly any on the meaning of these two other terms. For example, it would seem to us that whilst control connotes the right to command how something is done, supervision would indicate the right to suggest how something is done, which is much wider. Also, 'control' indicates that there will be some sort of follow-up to see that the work has been done properly and a right to insist that defective work be corrected, whereas 'direction' does not require this. Control will also emanate from a person or an identifiable group of

people, whereas directions can be laid down in a rule book produced by people who have no control at all (such as a regulatory agency);

- the examples should be very comprehensive and geared towards major public sector construction projects, which is where we expect the most serious differences of opinion to be. There need to be a good many more of them than appear in the condoc – for example as in Booklet 490 on travel expenses;
- they should also explain why self-employed sales and maintenance forces, such as the ones mentioned in the section above on Targeting of proposals, are not included (assuming that that is the intention);
- bearing in mind the need to prove that supervision, direction and control do not exist, the evidence that HMRC will expect businesses to collect in order to demonstrate this; and
- we would also welcome confirmation that this will not (for NIC's at least) apply to people working abroad, as we understand is the case, as that would put British businesses at a severe competitive disadvantage.

Consultation period

37. We object to having only an eight week consultation period covering both the Christmas period and the self assessment tax return filing period. The government's own guidelines say twelve, and whilst the guidelines have been watered down since they were first introduced by the Cabinet Office, there is nothing in the condoc to suggest that a shorter period is warranted.

RESPONSES TO CONSULTATION QUESTIONS

Question 1: Would the definition of intermediary as proposed in the draft legislation cause any practical difficulties e.g. to genuine commercial arrangements? Please provide details and examples.

38. Yes – see the paragraphs under Targeting of proposals above. As with the managed service companies, the legislation should describe the kind of intermediary whose gross payments HMRC object to and apply the law to that kind of intermediary only. There is already a definition of employment businesses, so only one of umbrella companies would be required in addition. Otherwise it risks taking in all service industry personnel paid by results.

Question 2: Are there likely to be any commercial difficulties with the proposed definition of employment intermediary? If so please say what they are likely to be and provide examples.

39. Yes – see our answer to question 1.

Question 3: Do you have any general comments on the legislation as drafted and if it will achieve the stated policy objectives? If so please provide reasons

40. See our General Comments above. We believe that these proposals will miss targets that they are intended to hit, and hit targets that they are intended to miss.

Question 4: Is the interaction with IR35 likely to cause any issues? If so please state what they are likely to be.

41. No, except that the proposals may drive more people into personal service companies. In the case of construction workers and the others mentioned in the condoc this would not generally be desirable.

Question 5: Would ensuring the intent of this legislation is maintained, such as with a TAAR, be helpful in preventing attempts to avoid this legislation?

42. We think that the legislation needs to be better focussed before a TAAR can be contemplated.

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APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/-/media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)