

## **TAXREP 33/04**

### **DRAFT LEGISLATION FOR REFORM OF THE CONSTRUCTION INDUSTRY SCHEME**

*Memorandum submitted in July 2004 by the Tax Faculty of the Institute of Chartered Accountants  
in England and Wales in response to an invitation to submit comments to the Revenue announced  
in February 2004*

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## DRAFT LEGISLATION FOR REFORM OF THE CONSTRUCTION INDUSTRY SCHEME

### INTRODUCTION

1. We welcome the opportunity to comment on the draft Statutory Instrument, The Income Tax (Sub-contractors in the Construction Industry) Regulations 2004, published in February 2004 at <http://www.inlandrevenue.gov.uk/cis/cis-secondary-regs.pdf>

### WHO WE ARE

2. The Institute of Chartered Accountants in England and Wales ('ICAEW') is the largest accountancy body in Europe, with more than 125,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.
3. The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy (which includes taxation).
4. The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter 'TAXline' to more than 11,000 members of the ICAEW who pay an additional subscription.

### GENERAL COMMENTS

5. The Institute welcomes the opportunity for further consultation and discussion prior to the implementation of the revised CIS scheme.
6. We remain concerned that the structure of the CIS scheme places a considerable administrative burden on all firms.
7. As we stated in our earlier response, submitted as TAXREP 16/04, many contracting businesses see the CIS as paperwork for the sake of it. The comments we made in our earlier TAXREP are still applicable and are therefore reproduced below

*'Extract from TAXREP 16/04:*

8. *Where gross payment applies, vouchers follow in parallel with invoices. Many firms do not bother to issue them or collate their receipt. This lack of compliance*

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*has lead to subcontractors being refused new sets of vouchers, on the grounds that the previous sets have yet to be issued and returned.*

9. *Some businessmen have spent days travelling round presenting cards to clients, without return or recompense, which we believe leads to considerable loss to the UK economy.*
10. *The Revenue has had difficulties in implementing the new scheme. The supply of vouchers, surely a predictable matter, gave rise to significant problems early on. The judgement of individual inspectors in reviewing exemption certificate applications has shown a wide divergence of opinion. Consistency is an essential element in the running of the self assessment system of which the CIS scheme forms a part.*
11. *There have been amendments in the past few years, such as the reduction in the turnover limit for CIS5 certificates, and the offset of deductions against current PAYE liabilities. We have welcomed these amendments, which deserve recognition.*
12. *However, there is scope for further improvement. There is insufficient gradation between recognisably small failures and errors, and the outright denial of the scheme. The Institute supports the efforts of the Revenue in identifying the black economy that remains within the industry, which should be the focus of the resources available.*
13. *This is an opportunity for a fresh look at the scheme. The finished article should retain the principles that those involved should be able to demonstrate a good record of compliance, and that Revenue officers should use discretion and common sense in their dealings with contractors and sub-contractors.'*

## **SPECIFIC COMMENTS**

### *Regulation 4 Monthly returns*

14. The completion of these forms is essentially a substitution for the completion of vouchers. However, no formal system has been proposed for contractors to inform subcontractors of tax deducted. Where a contractor fails in record-keeping and submissions, there does not appear to be any protection for the subcontractor.
15. We believe that there is need for a standard format for proof of deduction of CIS tax. It would be inappropriate to use copies of monthly returns, as this would breach confidentiality for the other subcontractors. Furthermore, compliance officers will need to ensure, in order to protect the subcontractor's interest, that tax deducted by the contractor coincides with the net payment.
16. There is a real need for the Revenue to respond to this issue by setting out exactly what will be done with these returns.

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17. Currently, Form CIS36 is submitted with the PAYE and CIS annual returns, summarising the payments made to, and deductions made from, subcontractors in the tax year. However, anecdotal evidence suggests that there is no overall review of these forms.
18. In order to identify subcontractors who derive the majority (or all) of their income from one source, we would expect the forms to be monitored on an annual basis so that trends can be spotted. However, we do not think that such analyses are being done. If annual trends are not being monitored, we question how monthly snapshots will help in the monitoring process and we would welcome clarification?
19. Therefore, if the best use is not being made of current levels of information, the completion of these forms appears merely to result in a further burden on businesses. We do not see why a form this form is necessary if it is merely filed and archived.

## *Regulation 6 Verification etc of registration status of sub-contractor*

20. In order for this regulation to work, it is essential for contractors to be able to check easily and quickly the status of a subcontractor. In recent years, the Revenue has not had the best record in implementing IT projects and systems. Problems occurring this year in online PAYE registrations appear to indicate a lack of planning and the resources required in order for the project to succeed. We are concerned that if there are problems with the proposed online verification system, this will place further burdens on business and will result in an irrevocable shift to telephone enquiries.
21. The online verification project is crucial to the success of the CIS and the size of the project should not be underestimated: we understand that about 1.3 million registration cards are currently in issue. With a proposed 18 month's lead time, it is essential that sufficient resources are allocated to this project now so as to ensure that it is fully operational and bug-free when the new CIS system comes into operation.
22. We would welcome clarification of the use of the term 'contract'. The term 'contract' rather suggests a written contract but the wording may also cover verbal agreements. We suggest 'agreement to supply services' rather than contract.
23. We understand the logic behind paragraph 6(3) – that a subcontractor's exemption status (or otherwise) should not affect the characteristics of the engagement – but it is impractical. Firstly, a subcontractor is hardly likely to remain silent on this issue. Secondly, in many cases the Revenue will be unable to check whether there was an agreement before the check is made, which makes the regulation unenforceable.

## *Regulation 9 Recovery from sub-contractor of amount not deducted by contractor*

## *Regulation 10 Return and certificate if amount may be unpaid*

## *Regulation 11 Notice and certificate if amount may be unpaid*

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24. No doubt the Revenue guidance booklets and notes will be constructed differently, but these paragraphs are poorly drafted and consequently difficult to understand. Further to the Ten Tenets for a Better Tax System, a copy of which is attached, and in keeping with the intent of the Tax Law Rewrite Project, the Regulations need to be drafted with greater clarity.

## *Regulation 17 In-year repayments of provisional excess credit*

25. One of the problems with the current system of vouched deductions, exacerbated by the continuing failure by the Revenue to supply vouchers promptly, is the difference between the timing of deductions from sums paid and the writing-out and dating of the vouchers. This can give the deducting contractor a cash flow advantage, but can disadvantage the subcontractor when the vouchers fall into a later tax period.
26. The in-year credit facility is a good idea. However, the lack of prescription by the Revenue of the form of deduction notification for April 2006 onwards, linked with the above matter, will undermine this facility.

## *Regulation 18 Small payments*

27. This move is welcome, but given the ongoing burden of the Scheme, needs to be redrafted to ensure that it is properly targeted. It is intended as a de minimis for non-industry payers, but may be exploited as it stands by the use of rolling short-term contracts of just under £1,000.

## *Regulation 19 work carried out on land owned by person to whom payment is made*

## *Regulation 20 Reverse premiums*

## *Regulation 21 Payments as agent of a Local Education Authority*

## *Regulation 22 Payments in respect of property used for business*

28. The definitions in Regulation 2 do not define 'land', which is typically taken to mean land and buildings, or indeed 'property'. Given that this is an important definition, the definition should be clarified.
29. The move to exempt self-builds, schools and non-construction businesses is a sensible proposal which helps to remove the uncertainty of those not accustomed to operating CIS regularly.

## *Regulation 30 Exceptions from compliance obligations*

30. We understand that Table 2 may be changed if it transpires that adjustments are needed. Given that the rules and case law governing certification are potentially the most contentious issue within CIS, this news is welcome, but we think that the review of the CIS is too narrowly focussed and should be more wide-ranging
31. The Revenue's current approach seems to be to review the current situation, to see if the rules are too restrictive rather than look at CIS in the wider picture and consider whether it is justified for all businesses in the construction sector. We are concerned that the new CIS will continue to be discriminatory and unfair for those

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businesses that are predominantly compliant and present no risk of tax failure. A consistent approach to compliance, collection and yield is required across all business sectors rather than focussing on CIS.

32. Table 2 needs to be redrafted so that it is more clearly targeted on those taxpayers who present the greatest risk of tax loss. We understand the need to retain the right to deny or remove exemption status for the worst offenders. However, the current minor and technical definitions, in regulation and case law, will serve only to harm many other businesses where the risk of tax loss is little or no higher than in other business sectors.
33. Steps also need to be taken to centralise the granting of certificates. There is no overall review for consistency across local offices by the Revenue, which has given rise to inconsistencies and unfairness and is in breach of the Charter. The power effectively to terminate businesses should not be vested in local inspectors but be exercised either at the regional or national level.

## *Regulation 49 Contractor in default if specified payment not received by applicable due date*

34. The inability to pay arising from a debtor's failure to make a promised payment, or delaying a payment outside established credit terms is the bane of every subcontractors' life and we believe that this should be recognised when reviewing such cases. The legislation governing payments to small businesses is often weak or unworkable, so exacerbating the problem is unlikely to promote new business start-ups.
35. It is fair to draw the analogy with employed staff whose monthly salary payment is delayed due to computer problems. How would they cope? What steps would need to be taken when the length of delay is uncertain?
36. In the light of the above comments, we request that the definition be redrafted to help bridge the difference between the inspector's and businessman's view of reasonable excuse.

## *Regulation 51 Default surcharge*

37. We have in the past expressed our concern about the requirement for mandatory electronic payments and that failure to make an electronic payment results in a default surcharge which may be much higher than the extra costs of processing a manual payment.
38. The surcharge should be more closely linked to the increased direct costs incurred by the Revenue where a manual payment is received.

AM/FH  
26.7.04