

# Tax rules for employment intermediaries - what this means for agencies and employment businesses



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## Introduction

Anti-avoidance measures came into effect on 6 April 2014 in response to the increasing number of businesses using employment intermediaries to disguise employees or workers as self-employed, primarily to avoid paying employer's National Insurance Contributions (NIC).

The measures are concerned with the PAYE and NIC position where UK individuals are provided to a UK business via any third party or intermediary whether based onshore or offshore (such as an agency or employment business). There are separate rules for the oil and gas industry which are not covered by this Inbrief.

## Onshore employment intermediary rules

Under the rules, if a UK-based intermediary supplies a individual to an end client, the individual is treated as an employee of the intermediary which has the direct contractual relationship with the end client ('**Intermediary 1**') unless one of the exceptions below applies.

This means that (subject to a limited exception in the case of fraud by the end client or another entity in the supply chain with which Intermediary 1 has a direct contractual relationship) Intermediary 1 is required to make PAYE and employee NIC deductions from the remuneration paid to the individual and pay employer NIC (regardless of who pays that remuneration). If Intermediary 1 fails to operate PAYE and NIC, Intermediary 1 will be liable for arrears together with interest and penalties. Whilst Intermediary 1 can use a payroll provider to operate PAYE and NIC on its behalf, as far as HMRC are concerned, Intermediary 1 remains liable for any PAYE and NIC errors made by the payroll provider.

The rules only apply for tax and NIC purposes. Accordingly, it is still possible to engage an individual on self-employed terms for employment law purposes provided that PAYE and NIC are operated. Please note that an individual engaged on self-employed terms may still be an individual for the purposes of employment legislation and therefore benefit from working time rights including paid holiday, national minimum wage, the right to be auto-enrolled, the right to statutory maternity pay, protection in respect of discrimination, whistleblowing and data protection.

## What are the exceptions?

The individual is not treated as an employee of Intermediary 1 if:

- The intermediary has "satisfactory evidence" to show that the individual is not subject to (or to a right of) supervision, direction or control ("SDC") by any person (see below).
- The individual is already an employee of another UK entity e.g. an umbrella company or personal services company ("PSC") (a PSC is a company owned and controlled by the individual), in which case the actual employer is liable to operate PAYE and NIC not Intermediary 1.

- The individual provides their services wholly in their own home, or at other premises which are not controlled or managed by the end client, unless the individual is required to do so at those premises because of the nature of the services and work being provided to the end client.
- The individual provides their services as an actor, singer, musician or other entertainer or as a fashion, photographic or artist's model.

## Supervision, direction or control

HMRC has published extensive guidance regarding the meaning of SDC. In accordance with that guidance:

**Supervision** is overseeing a person doing work to ensure that the person is doing the work they are required to do and the work is being done correctly to the required standard. Supervision can also involve helping the person to develop their skills and knowledge.

**Direction** is making a person do his or 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 how the work is done, as it is being undertaken.

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

HMRC guidance also sets out several examples to illustrate how these definitions apply in practice. The examples confirm:

- The SDC test is not satisfied if the individual is subject to SDC or the right of SDC by any person as to the manner in which he or she provides their services.
- The SDC test is not satisfied if someone has the right to subject the individual to SDC even if the right is not exercised in practice.
- A contract term that states that the individual is not subject to the right of SDC is not conclusive evidence. HMRC will consider how the arrangements operate in practice.

The fact that an individual is required to comply with statutory requirements, like health and safety procedures, does not indicate that the individual is subject to the right of SDC.

## Offshore employment intermediary rules

If a UK-based individual is employed by a non-UK employer or a non-UK intermediary and is providing services to a UK end client or is providing services to a UK end client through a foreign intermediary and:

- There is a UK intermediary in the contractual supply chain, the UK intermediary is responsible for operating PAYE and NIC.
- There is more than one UK intermediary in the contractual supply chain, Intermediary 1 is responsible for operating PAYE and NIC.
- There is no UK intermediary in the contractual supply chain, the UK end client is responsible for operating PAYE and NIC.

Separate NIC rules apply if the employer is based in the EU or the Isle of Man.

## Reporting requirements

The UK intermediary (or Intermediary 1 if there is more than one UK intermediary in the supply chain) is required to make quarterly returns to HMRC. The quarterly returns must give personal details of all individuals whom the intermediary places with clients and for whom the intermediary does not operate PAYE and NIC. It must provide details of the dates and hours worked by each of those individuals and the payments the individuals have received.

The UK intermediary (or Intermediary 1 if there is more than one UK intermediary in the supply chain) should keep and preserve 'non PAYE records' (i.e. records and documents which evidence the information that has been provided to HMRC in the quarterly returns). The records do not have to be sent to HMRC but must be retained for three tax years following the end of the tax year to which they relate.

The UK intermediary (or Intermediary 1 if there is more than one UK intermediary in the contractual chain) will be subject to automatic penalties if it fails to comply with the requirements.

## What is the impact of intermediaries?

Intermediaries face a significant administrative burden and additional cost as a result of these rules, in particular:

- The relevant intermediary needs to establish whether individuals are subject to the right of SDC. There is a presumption that there is a right of SDC so the intermediary will need to prove otherwise and keep satisfactory evidence of the lack of SDC. The combination of the presumption of SDC and proof requirement means that showing the lack of the right of SDC is extremely difficult in practice.
- Where the relevant intermediary does not operate PAYE and NIC for an individual, the quarterly record keeping requirements means additional administration and cost. To minimise penalties, if all necessary information is not available by the due date, intermediaries should submit an incomplete return and make subsequent corrections, as a return may be amended up to the submission deadline for the following quarter's return. Although HMRC may impose manual penalties for incorrect and incomplete returns, it is unlikely to do so if the intermediary has replaced the incomplete return within the permitted period.
- It is not possible to "get around" these rules by requiring individuals to provide their services through a PSC. A targeted anti-avoidance rule (TAAR) applies where a individual personally provides services (which are not excluded services) to a client and a third person enters into the 'arrangements', under which the main purpose, or one of the main purposes of the third person's involvement, is to ensure the individual's arrangement does not fall within the provisions of the intermediary legislation. If the TAAR applies, the third person will be responsible for operating PAYE and NIC for all remuneration received by the individual. HMRC has suggested that the TAAR will apply where an intermediary requires individuals to set up PSCs.

- In certain industries where profit margins are lean, intermediaries might struggle to absorb the additional costs and cope with the additional compliance burden.

## What can intermediaries do to protect themselves?

There are a number of steps intermediaries may be able to take to try to minimise the impact of the measures including:

- Ascertaining which entities are in the supply chain, where they are based and whether they are solvent;
- Identifying the entity which has the obligation to operate PAYE and NIC;
- Ensuring relevant warranties and indemnities are obtained from the entity which has the obligation to operate PAYE and NIC (and from any payroll company operating PAYE and NIC on behalf of the intermediary);
- Ensuring that if the individual is supplying their services through a PSC that the PSC exists and that the individual has a contract of employment with the PSC;
- Reviewing any warranties or indemnities that the intermediary is asked to give by the end client or another entity in the contractual supply chain and seek to limit them as appropriate;
- Carrying out an audit on a quarterly basis to identify the individuals for whom the intermediary is not operating PAYE and the reason for this; and
- Where reliance is being placed on the SDC exemption, obtaining written confirmation from the relevant intermediaries and the end clients that the individual is not subject to the right of SDC and retaining the confirmation on record.

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