

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



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Over recent years a number of anti-avoidance measures have been introduced in a bid to tackle “disguised employment”. Disguised employment refers to those situations where arrangements are implemented to falsely treat employees or workers as self-employed, primarily to gain a tax or National Insurance Contributions (NICs) advantage.

This Inbrief focuses on the employment intermediary or agency rules. These measures, which were introduced in April 2014, are concerned with the PAYE and NICs 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 intermediaries in 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 *an individual* to an end user, the individual is treated as an employee of the intermediary which has the direct contractual relationship with the end user (‘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 user 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 NICs deductions from the remuneration paid to the individual and pay employer NICs and the apprenticeship levy (regardless of who pays that remuneration). If Intermediary 1 fails to operate PAYE and NICs, Intermediary 1 will be liable for arrears together with interest and penalties. While Intermediary 1 can use a payroll provider to operate PAYE and NICs on its behalf, as far as HMRC are concerned, Intermediary 1 remains liable for any PAYE and NICs errors made by the payroll provider.

The rules only apply for tax and NICs purposes. Accordingly, it is still possible to engage an individual on self-employed terms for employment law purposes. Please note that an individual engaged on self-employed terms may still be a worker for the purposes of employment legislation and benefit from various rights including paid holiday, national minimum wage, the right to pension auto-enrolment and protection in respect of discrimination and whistleblowing. For more detail see our [Inbrief on employment status](#).

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, in which case the actual employer is liable to operate PAYE and NICs 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 user, unless the individual is required to do so because of the nature of the services and work being provided to the end user.
- ▶ 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 their 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 user or is providing services to a UK end user through a foreign intermediary, the following applies:

- ▶ If there is a UK intermediary in the contractual supply chain, the UK intermediary is responsible for operating PAYE and NICs.
- ▶ If there is more than one UK intermediary in the contractual supply chain, Intermediary 1 is responsible for operating PAYE and NICs.
- ▶ If there is no UK intermediary in the contractual supply chain, the UK end user is responsible for operating PAYE and NICs.

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 the 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 chain) will be subject to automatic penalties if it fails to comply with the requirements.

What steps should intermediaries take?

There are a number of steps intermediaries should take to comply with, and minimise the impact of, the rules. For Intermediary 1 this includes:

- ▶ Ascertaining which entities are in the supply chain and completing appropriate due diligence including ascertaining where they are based and whether they are solvent.
- ▶ Ensuring relevant warranties and indemnities are obtained from any payroll company operating PAYE and NICs on behalf of Intermediary 1.
- ▶ Reviewing any warranties or indemnities that Intermediary 1 is asked to give by the end user or another entity in the contractual supply chain and seeking to limit them as appropriate.
- ▶ Carrying out an audit on a quarterly basis to identify the individuals for whom the Intermediary 1 is not operating PAYE and the reason for this.
- ▶ Establishing whether the individuals supplied to the end user are subject to the right of SDC. There is a presumption that there is a right of SDC so Intermediary 1 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 reliance is being placed on the SDC exemption, obtaining written confirmation from the relevant intermediaries and the end users that the individual is not subject to the right of SDC and retaining the confirmation on record.



- ▶ Where Intermediary 1 does not operate PAYE and NICS for an individual, complying with its quarterly record keeping requirements. To minimise penalties, if all necessary information is not available by the due date, Intermediary 1 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 Intermediary 1 has replaced the incomplete return within the permitted period.

Other intermediaries in the supply chain will want to ensure that they undertake appropriate due diligence on the supply chain and that they negotiate appropriate warranties and indemnities from Intermediary 1. Any warranties and indemnities given by the intermediary will also need to be carefully considered to ensure that they are as limited in scope as possible.

Interaction with IR35

The intermediary rules only apply where the intermediary is contracting directly with an individual and generally do not apply if the individual is supplying their labour via their personal services company or partnership ("PSC"). That said, it is not possible to "get around" the employment intermediary rules by requiring individuals to provide their services through their PSC. A targeted anti-avoidance rule (TAAR) applies where an 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 NICS 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 any event, where an individual is providing their labour via a PSC, the IR35 rules need to be considered. IR35 is another tax anti-avoidance rule designed to combat disguised employment. IR35 applies when the individual would be an employee (or officeholder) for tax purposes if they were hired directly by the end-user. If IR35 applies, PAYE and NICS must be operated in respect of the fees paid to the PSC.

Under the current IR35 rules, end users in the public sector and large and medium-sized end users in the private sector are responsible for assessing whether IR35 applies. If the end-user determines that IR35 applies, the responsibility for operating PAYE and NICS generally rests with the "fee payer" – that is, the entity which contracts directly with and pays the PSC. For more detail see our [Inbrief on IR35](#).

If no PAYE/NICS is operated on the fees paid to the PSC under IR35 (e.g. because the end user determines that the individual is not a disguised employee and is therefore outside IR35), Intermediary 1 will need to include the individual on its quarterly reports to HMRC under the intermediary rules.

For more information on this subject please contact:



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