

Treasury to tackle TAX LEAKAGE



Anne Eager outlines the moves to combat 'false self-employment' within the construction industry

The question of status for the self-employed is a long-standing issue for tax advisers and their clients to deal with. True to the announcement in the 2009 Budget, a consultation document that has recently been released aims to simplify the definition of what employment actually is within the construction industry. If the proposed changes go ahead as currently suggested, the practical implications for anyone within the building industry who engages subcontractors could be huge.

This situation has arisen because HMRC have long held the opinion that many of the workers within the construction industry take advantage of the fact that the legislation surrounding employment status is a very grey area. Many workers within the construction industry are self-employed, and HMRC view this as a significant source of 'tax leakage'. HMRC regard this as a high-risk issue because of the

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opportunities for workers to appear and disappear very easily and therefore avoid the tax net, something made even easier, HMRC feel, when payments to the workers are in cash. In the Revenue's eyes the problem is made worse by the fact that self-employed individuals often, legitimately, pay less tax than an employee earning the same amount.

It takes a lot of time and effort for HMRC to investigate cases and potentially take an employer to court or have their workers reclassified as employees, with no guarantee of a result. The consultation document, with its definitive tests, will mean that much of the uncertainty is removed (as well as bringing thousands of formerly self-employed workers into the 'employment' net).

Because this is just at the consultation stage, we do not know when the changes will take effect, but we do know that because there is such a large hole in the Treasury's coffers, there is pressure for HMRC to increase the tax collected. In fairness, the Treasury does acknowledge that now is not the best time to be introducing these changes to an industry sector that has been hit so hard by the recession; because for businesses, the impact of reclassifying workers to employees means an increase in costs of 12.8% (the cost of employers' National Insurance contributions).

Until any new legislation on this issue appears, it is difficult to help clients prepare for any changes because of the uncertainty of what the new rules will say and when they will come into effect. All we can do as advisers in the meantime is keep our clients informed of any developments and continue to alert them to the issues surrounding employment status.

What exactly is the consultation about?

The consultation is aimed at what HMRC describe as false self-

employment within the construction industry. This arises where workers are treated as self-employed for tax and National Insurance purposes despite the fact that the way in which the work is carried out on a day-to-day basis suggests (in the eyes of the Revenue at least) that there is an employment relationship.

What is the consultation proposal – how is employment defined?

The consultation proposes a new deemed employment status for construction workers, who would be deemed to be employees unless they could pass one of the following tests:

- They provide the plant and equipment required for the job that they have been engaged to carry out (excluding any tools that it is normal within the industry for individuals to provide for themselves to be able to do their job). Or
- They provide all materials required to complete a job. Or
- They provide other workers to carry out the work under the contract and are responsible for paying them.

What will this mean for construction workers?

Being reclassified as an employee would mean that the payments would not only have to be subjected to payroll deductions (PAYE and NI), but an employer's NI liability would also arise. The end result would be an increased tax cost for both the newly deemed employee and employer.

Is this fair?

The stated objective of the consultation is to develop the best approach to determining employment status by ensuring that it is fair, clear and can be easily applied. Interestingly, the consultation document does go on

to acknowledge that these would have a financial impact, because it states that it intends that the measures developed as a result of this consultation will take effect when the industry is in a stronger position.

What else is happening in the construction industry?

In addition to the consultation, new information just released shows that a significant number of subcontractors are failing to meet the compliance tests required to maintain their gross payment status. Even after all review and appeal procedures have been pursued, 15.7% still failed to meet the requirements and as a result have lost their gross payment status.

The Tax Treatment Qualification Test (TTQT) is run every month to check whether subcontractors have met the stringent compliance regime. If the tests reveal a compliance failure, then that subcontractor's gross payment status is in jeopardy.

The loss of gross payment status will be declared to all existing clients of a business and will be disclosed to all prospective clients too. As a result it can cause severe damage to the reputation (and cashflow) of that business.

These consequences can be out of all proportion to the compliance failure that gave rise to the loss of gross payment status. On a positive note, it has been agreed that where a late payment of tax is made where this is the subject of a formal arrangement with the Business Payment Support Service, this does not count as late for compliance test purposes.

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