



HM TREASURY

# The Taxation of Controlling Persons

## **Consultation document**

Publication date: 23 May 2012

Closing date for comments: 16 August 2012

<b>Subject of this consultation:</b>	This is a consultation about the engagement practices of controlling persons. It proposes that a provision is introduced to ensure that controlling persons have income tax (PAYE) and National Insurance deducted at source by the engaging organisation.
<b>Scope of this consultation:</b>	The purpose of this consultation is to explore whether this is a necessary and appropriate way of achieving this aim and to test whether the provision is sufficiently targeted and without unexpected detrimental effects.
<b>Who should read this:</b>	
<b>Duration:</b>	Start date 23 May 2012 Finish date 16 August 2012
<b>Lead official:</b>	Sarah Radford
<b>How to respond or enquire about this consultation:</b>	Comments on this consultation should be sent by 16 August 2012 by email to Sarah Radford at the following email address: <a href="mailto:sarah.radford@hmrc.gsi.gov.uk">sarah.radford@hmrc.gsi.gov.uk</a> Or alternatively by post to: Sarah Radford 1E/09 100 Parliament Street London SW1A 2BQ
<b>Additional ways to be involved:</b>	We will hold meetings with relevant stakeholders to discuss this provision if you wish to be involved in one of these meetings please contact Sarah Radford using the details above.
<b>After the consultation:</b>	We will publish the results of the consultation. Dependent on the results of this consultation there may need to be a further consultation on the draft legislation. If appropriate, the intention is that any provision would then be legislated for in Finance Bill 2013

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## Foreword

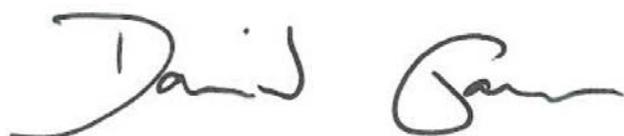
As a Government, we want there to be a simple and transparent tax system. This is why we have brought forward a number of measures aimed at simplifying the tax system and helping people to understand what tax they are paying and what their tax money is being spent on.

At the same time, we want to ensure that everybody pays the right amount of tax, at the right time. This is why at the last spending review we increased HMRC's funding by £900 million over the spending review period to tackle tax avoidance, evasion and minimisation.

The Chief Secretary to the Treasury launched a review into the tax arrangements of public sector appointees on 31 January 2012 with a view to ascertaining the extent of arrangements which could allow public sector appointees to minimise their tax payments. The review has concluded that there is a lack of transparency around the tax arrangements of public sector appointees, where the worker is not on the payroll of the engaging organisation.

The recommendations from the review are that the most senior public sector staff should be on the payroll, and that departments should have the right to seek assurance in relation to the tax arrangements of long term contractors. It is especially important in the public sector that it is transparent that tax obligations are being met.

Equally we believe that where people are in a position to control the major activities of an organisation the organisation, whether in the private or the public sector, should be able to have an assurance that the worker who is in a controlling position in the company is meeting their tax obligations. This is why we are publishing this consultation today.

A handwritten signature in black ink, appearing to read 'David Gauke', written in a cursive style.

David Gauke  
Exchequer Secretary to the Treasury

# 1. Executive Summary

- 1.1** There are many cases where the use of an intermediary, often a personal service company, is for legitimate commercial reasons. Indeed, many businesses start as small limited companies. The Government is very supportive of intermediaries, including personal service companies as a cornerstone of developing business, and it does not believe that personal service companies are necessarily avoidance devices.
- 1.2** However, it has become increasingly clear that there is an established and growing problem with people using intermediaries to disguise employment. Working through an intermediary provides an opportunity to minimise, or in some cases avoid completely paying income tax and National Insurance that would otherwise be correctly payable.
- 1.3** Where someone is using a personal service company to disguise their true employment relationship with their engager, there is already high profile anti-avoidance legislation to ensure that they do not gain a tax or National Insurance advantage. The intermediaries' legislation: Chapter 8 Part 2 Income Tax Earnings and Pension Act (ITEPA) 2003, is commonly known as IR35. This legislation requires the intermediary to pay income tax and National Insurance on all income from a contract which would be a contract of employment if it wasn't for the interposition of the intermediary.
- 1.4** When IR35 was introduced 10 years ago, it was unusual for a senior/controlling person to be engaged through their own limited company. It is the Government's view that where an individual has the requisite level of control to direct the activities of the organisation and they are engaged at a senior level (through an intermediary) then that individual should be taxed as an employee.
- 1.5** The Government's intention is to ensure that where an organisation engages a controlling person the engaging organisation will be required to deduct the income tax (PAYE) and National Insurance at source, as they would for their employees. This ensures that the taxation of the worker is transparent to the engager.

## 2. What is the issue?

### What is meant by an intermediary?

**2.1** For the purposes of this document an intermediary is any structure that is put in place between the party for whom the work is undertaken the 'client' and the worker. For the purposes of this document an intermediary does not include Employment Businesses and Employment Agencies. In the situations described in this document the intermediary is usually a small limited company known as a personal service company, but it can also be a partnership or limited liability partnership.

**2.2** A personal service company (PSC) is a limited company where the main shareholder is also the director and is also typically the only employee. In some cases friends and relatives are also directors, shareholders and/or employees. The PSC contracts with the client to supply the services of the director and invoices for the services of the director. For the rest of this document PSC will be used to refer to intermediaries including partnerships and limited liability partnerships.

**2.3** There are a variety of different industries where it is usual for people to work through PSCs. PSCs are often used for entirely legitimate commercial reasons. The PSC may source its own work or may use a recruitment agency to source work on its behalf.

### What are the tax and National Insurance implications of using a PSC?

**2.4** When a limited company is engaged and paid for the services of a worker, the payment from the engaging organisation is made without the deduction of income tax and National Insurance. This is because the payment is a legitimate, invoiced, commercial transaction and there is no requirement for the payments to have income tax and National Insurance deducted even where the individual doing the work is working on terms and conditions that would otherwise make them an employee of the engaging organisation.

**2.5** The PSC can deduct any allowable expenses from their gross profit and pay Corporation Tax on the net profits in the normal way. The rate of Corporation Tax for small companies is currently 20 percent increasing for larger companies to 24 percent.

**2.6** Depending on how the director/shareholder then chooses to withdraw the profits from the PSC the profits can be withdrawn:

- as earnings with income tax and National Insurance deducted from the money they withdraw; or

- by distributing dividends, where payments will be subject to income tax but not to National Insurance payments; or
- as a directors loan.

Again, these arrangements are all perfectly legitimate and many people will use a mixture of these methods to take money out of the PSC. They can do this even where, in the absence of the PSC, they would have been an employee of the engaging organisation – and doing so in such cases means that the individual can maintain their contributory benefits and take advantage of their personal allowance. This is where the problem of tax and National Insurance may become an issue.

## Growth in the use of PSCs

**2.7** Individuals and businesses are always looking to operate in the most cost effective way. For a business, one of the ways that they are able to do this is by engaging people through a PSC.

**2.8** A business choosing to engage people through a PSC achieves greater workforce flexibility. For example, there is no minimum notice period or requirement to make redundancy payments if the engager decides that they no longer have a requirement for that skill set. Normal commercial contracting arrangements apply.

**2.9** Engaging people in this way can also generate a financial saving for the engaging business. This is because there is no requirement for the engaging business to make employer National Insurance payments for the workers – saving them 13.8 percent on earnings in excess of the secondary threshold. There are also further financial savings because there is no requirement for the engager to provide other benefits such as holiday pay, sick pay and pension contributions as they would for their other employees.

**2.10** Working through a PSC also provides the worker with choices of how to withdraw the profits from the PSC, which can be done in a tax efficient way; meaning more money taken home and less money to the Exchequer. Working through a PSC also provides the benefit of more generous expenses.

## Existing Legislation

**2.11** During the 1990's there was rapid growth in the number of PSCs, in many cases, for tax and National Insurance purposes. In some sectors, it was also very difficult for individuals to secure work unless they were working through PSCs as engagers sought to minimise their own National Insurance liabilities. To address this problem the then Government brought in 'IR35' in April 2000.

**2.12** IR35 says that where the relationship between the end client/engager and the worker would be one of employment if it wasn't for the interposition of an intermediary (often a PSC) then the intermediary must account for the income tax and National Insurance on monies earned from that contract.

**2.13** This can be done in one of two ways. The worker can simply take out of the PSC as salary the money earned from that contract and pay tax and National Insurance on those salary payments in the normal way. Where the worker chooses not to do this then, at the end of the year, the PSC is required to calculate a 'deemed payment' on which employee National Insurance Contributions and income tax (PAYE) are due and a deemed employer National Insurance payment.

**2.14** The way of computing the deemed payment is prescribed by legislation and it ensures that what would have been income derived from employment if it wasn't for the interposition of an intermediary is taxed as such, in the event that the worker does not choose to take the money from the contract as salary.

**2.15** The example calculation below shows the difference between the amount of tax and National Insurance which can be achieved if someone is on the payroll as opposed to being paid through an arrangement where someone is working through a PSC where IR35 does not apply or has not been applied and all the profits (from that year) have been withdrawn in the most tax efficient manner. This example is based on 2010/11 tax rates.

<b>Payment to PSC</b>	120,000
Expenses	10,000
Salary	0
PAYE	0
Class 1 NIC primary	0
Class 1 NIC Secondary	0
Corporation Tax @ 21%	23,100
SA liability on dividends <sup>1</sup>	11,205
<b>Total Tax Paid</b>	<b>£34,305</b>

<b>Salary to Employee</b>	120,000
Expenses	N/A
Salary	120,000
PAYE	37,928
Class 1 NIC primary	4,960
Class 1 NIC Secondary	14,629
Corporation Tax	N/A
SA liability on dividends	N/A
<b>Total Tax Paid</b>	<b>£57,516</b>

The difference in payment to the Exchequer in this example is £23,211.

**2.16** The Government believes that IR35 remains the correct approach to address this mismatch where intermediaries are used in circumstances which would otherwise be employment between the worker and the engaging organisation. This is why it took the decision to retain IR35 at Budget 2011. However, it recognised that IR35 can be difficult to

<sup>1</sup> Calculation based on the person having no other income in the year so using a personal allowance of £6,475 and 10% relief for tax credits on UK dividends has been given.

understand and it listened to the advice from the OTS that HMRC's administration of IR35 should be improved.

**2.17** Deciding whether the relationship between the worker and engager is one of employment relies on case law principles laid down by the Courts. This applies in IR35 and non-IR35 circumstances. The case law is reliant on the facts of each individual case and people working through PSCs have said that they often find it difficult to establish if IR35 would apply to them.

**2.18** Over the last year, HMRC has worked with external stakeholders to simplify the guidance for IR35 to make it easier to understand, and has also developed 'business entity' tests and scenarios to demonstrate when and why IR35 applies. HMRC published the details of this work on their website on 9 May 2012. Alongside this new guidance HMRC has also made improvements to the way it polices IR35 including strengthening their specialist compliance teams and altering the way they approach investigations in this area.

### **Why isn't the IR35 legislation enough for controlling persons and why does this consultation seek to go further?**

**2.19** When IR35 was introduced 10 years ago it was comparatively unusual for controlling persons of an engaging organisation to be working through a PSC. In the last few years anecdotal evidence suggests that it has become an increasingly common practice in both the private and public sectors.

**2.20** The IR35 legislation places the obligation on the PSC to operate income tax and National Insurance in the relevant circumstances. This means that even where the appropriate tax and National Insurance for the circumstances of the case is being paid, that is not going to be clear and transparent to the engaging organisation. There is no reason it should be as the contract for the work has been made between the engaging organisation and the PSC under normal commercial practices.

**2.21** The Government believes that, because of their role in an organisation, controlling persons should be required to meet their income tax and National Insurance obligations in a way which is transparent to their engager. This is not currently possible where they work through a PSC.

**2.22** The Government has concluded that the most effective way to achieve the right level of transparency is for the engager to deduct income tax and National Insurance at source for payments they make to controlling persons in the same way as they do for their other employees and not to make payments direct to any PSC those controlling persons may work through for any other purposes. This requirement will provide the necessary assurances

to the engaging organisation in a transparent way. It will also reduce the loss of the relevant tax and National Insurance to the Exchequer.

**2.23** The Government recognises that, in the public sector, it is particularly important that off-payroll appointments are made to the highest possible standards. The *Review of the tax arrangements of public sector appointees* also considered this issue, and set out recommendations whereby government departments and their arm's length bodies will also have the right to seek appropriate assurances about the tax arrangements of long-term specialist contractors.

**2.24** The requirement would need to be underpinned by new legislation, more details of which are set out in the following section of this consultation document. The intention would be that HMRC would police the new provision through risk based employer compliance visits during which they would check that everyone who meets the definition of a 'controlling person' of that organisation was on the payroll.

## 3. What is the Proposed Solution?

**3.1** The Government is proposing to create in legislation a provision which would require the engaging organisation to place all controlling persons on the payroll. This provision would apply even where they might be working through a PSC for other purposes and even if the payments made by the engaging organisation were made to the PSC and not directly to the individual worker.

**3.2** This would mean the whole amount paid by the engager to the PSC would be treated as remuneration of the controlling person as if they were an employee. The controlling person would have income tax and National Insurance deducted at source by the engaging organisation. This would effectively mean that the worker would be taxed in the same way as employees of the organisation.

**Q1** Is creating a provision which would require the engaging organisation to deduct income tax and National Insurance at source a correct and proportionate solution to this problem?

**Q2** Does the proposed provision raise any commercial, employment or other issues that would need to be considered before any final conclusions are reached? If yes, please advise.

**Q3** Are there alternative approaches that would better deliver the transparency the Government is seeking in the taxation of controlling persons than requiring them to have income tax and National Insurance deducted at source by the engaging organisation?

### How would the provision work?

**3.3** This provision would take precedent over Chapters 7 and 8 ITEPA 2003 and all extra statutory provisions in the case of 'controlling persons' Only.

**Q4** What are the consequences of this provision taking precedence over IR35 (Part 2 Chapter 8 ITEPA 2003) Part 2 Chapter 7 ITEPA 2003 and all extra statutory provisions?

**3.4** This measure is intended to be targeted only at those who are able to influence the direction of the entity/organisation as controlling persons. We do not intend for this measure to stop genuine commercial arrangements.

**Q5** Are there any circumstances where this measure would prevent genuine commercial arrangements? If yes please explain.

**3.5** This provision would place the responsibility of deducting the tax and National insurance payments on the engaging organisation as well as making them liable for the relevant employer's National Insurance contributions. The IR35 legislation places this responsibility on the PSC. Placing the responsibility back onto the engaging organisation in the case of controlling persons removes some of the incentive for engaging organisations to encourage workers to be engaged through personal service companies as they will no longer make the National Insurance savings.

**3.6** But it does not prevent anyone from working through a PSC; it just ensures that income from employment has the appropriate tax and National Insurance deducted and that the engager achieves the transparency of understanding which the Government considers to be important in these cases.

## 4. Defining a Controlling Person

**4.1** The Government proposes that a controlling person is defined as someone who is able to shape the direction of the organisation having authority or responsibility for directing or controlling the major activities of the engaging organisation during the year. This would be someone who has managerial control over a significant proportion of the organisation's employees and/or control over a significant proportion of the budget of the organisation.

**Q6** Is someone who has managerial control over a significant proportion of the workforce and/or control over a significant proportion of the organisations budget the correct delineation for a 'controlling person'?

**Q7** Should we extend controlling person to bring a larger group within the remit of this provision? If so who and why?

**Q8** Should controlling person be narrowed so that fewer people are within its remit? If so who should be additionally excluded and why?

### Who would we want to exclude

**4.2** We want to exclude 'micro businesses' who engage controlling persons through a PSC from this provision. A micro business, is defined by the EU as a business which employs fewer than 10 persons and whose turnover and or balance sheet does not exceed €2million (approximately £1.7million.) This is because the burden on these micro businesses would be disproportionate and we would not want to discourage enterprise. This exclusion would not apply to micro businesses that are part of a group structure.

**Q9** Is this exclusion a proportionate exception to the proposed provision?

**Q10** Is there any reason we should not exclude micro businesses, who are not part of a group structure from this provision?

## 5. Tax Impact Assessment

### Summary of Impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17
	N/A	N/A	+/-	+/-	+/-
	The Government will set out the Exchequer impact in due course. The final costing will be subject to scrutiny by the OBR.				
<b>Economic impact</b>	This measure has no significant economic impacts.				
<b>Impact on individuals and households</b>	This will have a negligible impact on a small number of individuals. All those this measure will affect are likely to be highly paid.				
<b>Equalities impacts</b>	The proposal is expected to impact on highly paid individuals. No adverse impact on the equality of protected groups has been identified.				
<b>Impact on businesses and Civil Society Organisations</b>	There will be a small reduction in administrative burden on micro businesses/PSC where the engaging organisation will take on the responsibility of paying PAYE and NICs. The increase in administrative burden for the engaging organisation will be negligible as all qualifying businesses will already be operating a payroll system and so the changes needed are expected to be minimal.				
<b>Impact on HMRC or other public sector delivery organisations</b>	This will have minimal impact – the provision will be policed by HMRC as part of its normal risk profiling and employer compliance checking activities.				
<b>Other impacts</b>	Micro businesses (defined by the EU as a business which employs fewer than 10 persons and whose turnover and/or balance sheet does not exceed 2 million Euros) are exempt from this provision.				

## 6. Summary of Consultation Questions

- Q1** Is creating a provision which would require the engaging organisation to deduct income tax and National Insurance at source a correct and proportionate solution to this problem?
- Q2** Does the proposed provision raise any commercial, employment or other issues that would need to be considered before any final conclusions are reached? If yes, please advise.
- Q3** Are there alternative approaches that would better deliver the transparency the Government is seeking in the taxation of controlling persons than requiring them to have income tax and National Insurance deducted at source by the engaging organisation?
- Q4** What are the consequences of this provision taking precedence over IR35 (Part 2 Chapter 8 ITEPA 2003) Part 2 Chapter 7 ITEPA 2003 and all extra statutory provisions?
- Q5** Are there any circumstances where this measure would prevent genuine commercial arrangements? If yes please explain.
- Q6** Is someone who has managerial control over a significant proportion of the workforce and/or control over a significant proportion of the organisations budget the correct delineation for a 'controlling person'?
- Q7** Should we extend controlling person to bring a larger group within the remit of this provision? If so who and why?
- Q8** Should controlling person be narrowed so that fewer people are within its remit? If so who should be additionally excluded and why?
- Q9** Is this exclusion a proportionate exception to the proposed provision?
- Q10** Is there any reason we should not exclude micro businesses, who are not part of a group structure from this provision?

## 7. The Consultation Process

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

- Stage 1 Setting out objectives and identifying options.
- Stage 2 Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 Drafting legislation to effect the proposed change.
- Stage 4 Implementing and monitoring the change.
- Stage 5 Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of a specific proposal, rather than to seek views on alternative proposals.

### How to respond

A summary of the questions in this consultation is included at chapter 6.

Responses should be sent by 16 August 2012, by e-mail to

[sarah.radford@hmrc.gsi.gov.uk](mailto:sarah.radford@hmrc.gsi.gov.uk) or

by post to: Sarah Radford  
1E/09  
100 Parliament Street  
London  
SW1A 2BQ

Telephone enquiries 020 7147 2414 (from a text phone prefix this number with 18001)

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from the HMRC Internet site at <http://www.hmrc.gov.uk/consultations/index.htm>. All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

### Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs (HMRC).

HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

### **The Consultation Code of Practice**

This consultation is being conducted in accordance with the Code of Practice on Consultation. A copy of the Code of Practice criteria and a contact for any comments on the consultation process can be found in Annex A.

# Annex A: The Code of Practice on Consultation

## About the consultation process

This consultation is being conducted in accordance with the Code of Practice on Consultation.

The consultation criteria

1. When to consult - Formal consultation should take place at a stage when there is scope to influence the policy outcome.
2. Duration of consultation exercises - Consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.
3. Clarity of scope and impact - Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.
4. Accessibility of consultation exercise - Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.
5. The burden of consultation - Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.
6. Responsiveness of consultation exercises - Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.
7. Capacity to consult - Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

If you feel that this consultation does not satisfy these criteria, or if you have any complaints or comments about the process, please contact:

Amy Burgess, Consultation Coordinator, Budget & Finance Bill Co-ordination Group, HM Revenue & Customs, 100 Parliament Street, London, SWA 2BQ

e-mail [hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk](mailto:hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk)

# Annex B: Relevant Government Legislation

## Part 8 Chapter 2 ITEPA 2003

### **CHAPTER 8** APPLICATION OF PROVISIONS TO WORKERS UNDER ARRANGEMENTS MADE BY INTERMEDIARIES

Application of this Chapter

#### 48 Scope of this Chapter

- (1) This Chapter has effect with respect to the provision of services through an intermediary.
- (2) Nothing in this Chapter—
  - (a) affects the operation of Chapter 7 of this Part, or
  - (b) applies to payments subject to deduction of tax under section 555 of ICTA (payments to non-resident entertainers and sportsmen).

#### 49 Engagements to which this Chapter applies

- (1) This Chapter applies where—
  - (a) an individual (“the worker”) personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person (“the client”),
  - (b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party (“the intermediary”), and
  - (c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.
- (2) In subsection (1)(a) “business” includes any activity carried on—
  - (a) by a government or public or local authority (in the United Kingdom or elsewhere), or
  - (b) by a body corporate, unincorporated body or partnership.
- (3) The reference in subsection (1)(b) to a “third party” includes a partnership or unincorporated body of which the worker is a member.
- (4) The circumstances referred to in subsection (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.
- (5) In this Chapter “engagement to which this Chapter applies” means any such provision of services as is mentioned in subsection (1).

#### 50 Worker treated as receiving earnings from employment

- (1) If, in the case of an engagement to which this Chapter applies, in any tax year—
  - (a) the conditions specified in section 51, 52 or 53 are met in relation to the intermediary, and
  - (b) the worker, or an associate of the worker—

- (i) receives from the intermediary, directly or indirectly, a payment or benefit that is not employment income, or
- (ii) has rights which entitle, or which in any circumstances would entitle, the worker or associate to receive from the intermediary, directly or indirectly, any such payment or benefit,

the intermediary is treated as making to the worker, and the worker is treated as receiving, in that year a payment which is to be treated as earnings from an employment (“the deemed employment payment”).

(2) A single payment is treated as made in respect of all engagements in relation to which the intermediary is treated as making a payment to the worker in the tax year.

(3) The deemed employment payment is treated as made at the end of the tax year, unless section 57 applies (earlier date of deemed payment in certain cases).

(4) In this Chapter “the relevant engagements”, in relation to a deemed employment payment, means the engagements mentioned in subsection (2).

### **51 Conditions of liability where intermediary is a company**

(1) Where the intermediary is a company the conditions are that the intermediary is not an associated company of the client that falls within subsection (2) and either—

- (a) the worker has a material interest in the intermediary, or
- (b) the payment or benefit mentioned in section 50(1)(b)—
  - (i) is received or receivable by the worker directly from the intermediary, and
  - (ii) can reasonably be taken to represent remuneration for services provided by the worker to the client.

(2) An associated company of the client falls within this subsection if it is such a company by reason of the intermediary and the client being under the control—

- (a) of the worker, or
- (b) of the worker and other persons.

(3) A worker is treated as having a material interest in a company if—

- (a) the worker, alone or with one or more associates of the worker, or
  - (b) an associate of the worker, with or without other such associates,
- has a material interest in the company.

(4) For this purpose a material interest means—

- (a) beneficial ownership of, or the ability to control, directly or through the medium of other companies or by any other indirect means, more than 5% of the ordinary share capital of the company; or
- (b) possession of, or entitlement to acquire, rights entitling the holder to receive more than 5% of any distributions that may be made by the company; or

(c) where the company is a close company, possession of, or entitlement to acquire, rights that would in the event of the winding up of the company, or in any other circumstances, entitle the holder to receive more than 5% of the assets that would then be available for distribution among the participators.

(5) In subsection (4)(c) “participator” has the meaning given by section 417(1) of ICTA.

## 52 Conditions of liability where intermediary is a partnership

(1) Where the intermediary is a partnership the conditions are as follows.

(2) In relation to any payment or benefit received or receivable by the worker as a member of the partnership the conditions are—

(a) that the worker, alone or with one or more relatives, is entitled to 60% or more of the profits of the partnership; or

(b) that most of the profits of the partnership concerned derive from the provision of services under engagements to which this Chapter applies—

(i) to a single client, or

(ii) to a single client together with associates of that client; or

(c) that under the profit sharing arrangements the income of any of the partners is based on the amount of income generated by that partner by the provision of services under engagements to which this Chapter applies.

In paragraph (a) “relative” means husband or wife, parent or child or remoter relation in the direct line, or brother or sister.

(3) In relation to any payment or benefit received or receivable by the worker otherwise than as a member of the partnership, the conditions are that the payment or benefit—

(a) is received or receivable by the worker directly from the intermediary, and

(b) can reasonably be taken to represent remuneration for services provided by the worker to the client.

## 53 Conditions of liability where intermediary is an individual

Where the intermediary is an individual the conditions are that the payment or benefit—

(a) is received or receivable by the worker directly from the intermediary, and

(b) can reasonably be taken to represent remuneration for services provided by the worker to the client.

The deemed employment payment

## 54 Calculation of deemed employment payment

(1) The amount of the deemed employment payment for a tax year (“the year”) is the amount resulting from the following steps—

### *Step 1*

Find (applying section 55) the total amount of all payments and benefits received by the intermediary in the year in respect of the relevant engagements, and reduce that amount by 5%.

### *Step 2*

Add (applying that section) the amount of any payments and benefits received by the worker in the year in respect of the relevant engagements, otherwise than from the intermediary, that—

(a) are not chargeable to income tax as employment income, and

(b) would be so chargeable if the worker were employed by the client.

*Step 3*

Deduct (applying Chapters 1 to 5 of Part 5) the amount of any expenses met in the year by the intermediary that would have been deductible from the taxable earnings from the employment if—

(a) the worker had been employed by the client, and

(b) the expenses had been met by the worker out of those earnings.

If the result at this or any later point is nil or a negative amount, there is no deemed employment payment.

*Step 4*

Deduct the amount of any capital allowances in respect of expenditure incurred by the intermediary that could have been deducted from employment income under section 262 of CAA 2001 (employments and offices) if the worker had been employed by the client and had incurred the expenditure.

*Step 5*

Deduct any contributions made in the year for the benefit of the worker by the intermediary to a scheme approved under Chapter 1 or 4 of Part 14 of ICTA that if made by an employer for the benefit of an employee would not be chargeable to income tax as income of the employee.

This does not apply to excess contributions made and later repaid.

*Step 6*

Deduct the amount of any employer's national insurance contributions paid by the intermediary for the year in respect of the worker.

*Step 7*

Deduct the amount of any payments and benefits received in the year by the worker from the intermediary—

(a) in respect of which the worker is chargeable to income tax as employment income, and

(b) which do not represent items in respect of which a deduction was made under step 3.

*Step 8*

Assume that the result of step 7 represents an amount together with employer's national insurance contributions on it, and deduct what (on that assumption) would be the amount of those contributions.

The result is the deemed employment payment.

(2) If section 559 of ICTA applies (sub-contractors in the construction industry: payments to be made under deduction), the intermediary is treated for the purposes of step 1 of subsection (1) as receiving the amount that would have been received had no deduction been made under that section.

(3) In step 3 of subsection (1), the reference to expenses met by the intermediary includes—

(a) expenses met by the worker and reimbursed by the intermediary, and

(b) where the intermediary is a partnership and the worker is a member of the partnership, expenses met by the worker for and on behalf of the partnership.

(4) In step 3 of subsection (1), the expenses deductible include the amount of any mileage allowance relief for the year which the worker would have been entitled to in respect of the use of a vehicle falling within subsection (5) if—

(a) the worker had been employed by the client, and

(b) the vehicle had not been a company vehicle (within the meaning of Chapter 2 of Part 4).

(5) A vehicle falls within this subsection if—

(a) it is provided by the intermediary for the worker, or

(b) where the intermediary is a partnership and the worker is a member of the partnership, it is provided by the worker for the purposes of the business of the partnership.

(6) Where, on the assumptions mentioned in paragraphs (a) and (b) of step 3 of subsection (1), the deductibility of the expenses is determined under sections 337 to 342 (travel expenses), the duties performed under the relevant engagements are treated as duties of a continuous employment with the intermediary.

(7) In step 7 of subsection (1), the amounts deductible include any payments received in the year from the intermediary that—

(a) are exempt from income tax by virtue of section 229 or 233 (mileage allowance payments and passenger payments), and

(b) do not represent items in respect of which a deduction was made under step 3.

(8) For the purposes of subsection (1) any necessary apportionment is to be made on a just and reasonable basis of amounts received by the intermediary that are referable—

(a) to the services of more than one worker, or

(b) partly to the services of the worker and partly to other matters.

## **55 Application of rules relating to earnings from employment**

(1) The following provisions apply in relation to the calculation of the deemed employment payment.

(2) A “payment or benefit” means anything that, if received by an employee for performing the duties of an employment, would be earnings from the employment.

(3) The amount of a payment or benefit is taken to be—

(a) in the case of a payment or cash benefit, the amount received, and

(b) in the case of a non-cash benefit, the cash equivalent of the benefit.

(4) The cash equivalent of a non-cash benefit is taken to be—

(a) the amount that would be earnings if the benefit were earnings from an employment, or

(b) in the case of living accommodation, whichever is the greater of that amount and the cash equivalent determined in accordance with section 398(2).

(5) A payment or benefit is treated as received—

(a) in the case of a payment or cash benefit, when payment is made of or on account of the payment or benefit;

(b) in the case of a non-cash benefit that is calculated by reference to a period within the tax year, at the end of that period;

(c) in the case of a non-cash benefit that is not so calculated, when it would have been treated as received for the purposes of Chapter 4 or 5 of this Part (see section 19 or 32) if—

(i) the worker had been an employee, and

(ii) the benefit had been provided by reason of the employment.

## 56 Application of Income Tax Acts in relation to deemed employment

(1) The Income Tax Acts (in particular, the PAYE provisions) apply in relation to the deemed employment payment as follows.

(2) They apply as if—

(a) the worker were employed by the intermediary, and

(b) the relevant engagements were undertaken by the worker in the course of performing the duties of that employment.

(3) The deemed employment payment is treated in particular—

(a) as taxable earnings from the employment for the purpose of securing that any deductions under Chapters 2 to 6 of Part 5 do not exceed the deemed employment payment; and

(b) as taxable earnings from the employment for the purposes of section 232.

(4) The worker is not chargeable to tax in respect of the deemed employment payment if, or to the extent that, by reason of any combination of the factors mentioned in subsection (5), the worker would not be chargeable to tax if—

(a) the client employed the worker,

(b) the worker performed the services in the course of that employment, and

(c) the deemed employment payment were a payment by the client of earnings from that employment.

(5)The factors are—

- (a)the worker being resident, ordinarily resident or domiciled outside the United Kingdom,
- (b)the client being resident or ordinarily resident outside the United Kingdom, and
- (c)the services in question being provided outside the United Kingdom.

(6)Where the intermediary is a partnership or unincorporated association, the deemed employment payment is treated as received by the worker in the worker's personal capacity and not as income of the partnership or association.

(7)Where—

- (a)the worker is resident in the United Kingdom,
- (b)the services in question are provided in the United Kingdom, and
- (c)the client or employer carries on business in the United Kingdom,

the intermediary is treated as having a place of business in the United Kingdom, whether or not it in fact does so.

(8)The deemed employment payment is treated as relevant earnings of the worker for the purposes of section 644 of ICTA (relevant earnings for purposes of permissible pension contributions).

Supplementary provisions

### **57Earlier date of deemed employment payment in certain cases**

(1)If in any tax year—

- (a)a deemed employment payment is treated as made, and
- (b)before the date on which the payment would be treated as made under section 50(2) any relevant event (as defined below) occurs in relation to the intermediary,

the deemed employment payment for that year is treated as having been made immediately before that event or, if there is more than one, immediately before the first of them.

(2)Where the intermediary is a company the following are relevant events—

- (a)the company ceasing to trade;
- (b)where the worker is a member of the company, the worker ceasing to be such a member;
- (c)where the worker holds an office with the company, the worker ceasing to hold such an office;
- (d)where the worker is employed by the company, the worker ceasing to be so employed.

(3)Where the intermediary is a partnership the following are relevant events—

- (a)the dissolution of the partnership or the partnership ceasing to trade or a partner ceasing to act as such;
- (b)where the worker is employed by the partnership, the worker ceasing to be so employed.

(4) Where the intermediary is an individual and the worker is employed by the intermediary, it is a relevant event if the worker ceases to be so employed.

(5) The fact that the deemed employment payment is treated as made before the end of the tax year does not affect what receipts and other matters are taken into account in calculating its amount.

### **58 Relief in case of distributions by intermediary**

(1) A claim for relief may be made under this section where the intermediary—

(a) is a company,

(b) is treated as making a deemed employment payment in any tax year, and

(c) either in that tax year (whether before or after that payment is treated as made), or in a subsequent tax year, makes a distribution (a “relevant distribution”).

(2) A claim for relief under this section must be made—

(a) by the intermediary by notice to the Inland Revenue, and

(b) within 5 years after the 31st January following the tax year in which the distribution is made.

(3) If on a claim being made the Inland Revenue are satisfied that relief should be given in order to avoid a double charge to tax, they must direct the giving of such relief by way of amending any assessment, by discharge or repayment of tax, or otherwise, as appears to them appropriate.

(4) Relief under this section is given by setting the amount of the deemed employment payment against the relevant distribution so as to reduce the distribution.

(5) In the case of more than one relevant distribution, the Inland Revenue must exercise the power conferred by this section so as to secure that so far as practicable relief is given by setting the amount of a deemed employment payment—

(a) against relevant distributions of the same tax year before those of other years,

(b) against relevant distributions received by the worker before those received by another person, and

(c) against relevant distributions of earlier years before those of later years.

(6) Where the amount of a relevant distribution is reduced under this section, the amount of any associated tax credit is reduced accordingly.

### **59 Provisions applicable to multiple intermediaries**

(1) The provisions of this section apply where in the case of an engagement to which this Chapter applies the arrangements involve more than one relevant intermediary.

(2) All relevant intermediaries in relation to the engagement are jointly and severally liable, subject to subsection (3), to account for any amount required under the PAYE provisions to be deducted from a deemed employment payment treated as made by any of them—

(a) in respect of that engagement, or

(b) in respect of that engagement together with other engagements.

(3) An intermediary is not so liable if it has not received any payment or benefit in respect of that engagement or any such other engagement as is mentioned in subsection (2)(b).

(4) Subsection (5) applies where a payment or benefit has been made or provided, directly or indirectly, from one relevant intermediary to another in respect of the engagement.

(5) In that case, the amount taken into account in relation to any intermediary in step 1 or step 2 of section 54(1) is reduced to such extent as is necessary to avoid double-counting having regard to the amount so taken into account in relation to any other intermediary.

(6) Except as provided by subsections (2) to (5), the provisions of this Chapter apply separately in relation to each relevant intermediary.

(7) In this section "relevant intermediary" means an intermediary in relation to which the conditions specified in section 51, 52 or 53 are met.

## **60 Meaning of "associate"**

(1) In this Chapter "associate"—

(a) in relation to an individual, has the meaning given by section 417(3) and (4) of ICTA, subject to the following provisions of this section;

(b) in relation to a company, means a person connected with the company; and

(c) in relation to a partnership, means any associate of a member of the partnership.

(2) Where an individual has an interest in shares or obligations of the company as a beneficiary of an employee benefit trust, the trustees are not regarded as associates of the individual by reason only of that interest except in the following circumstances.

(3) The exception is where—

(a) the individual, either alone or with any one or more associates of the individual, or

(b) any associate of the individual, with or without other such associates,

has at any time on or after 14th March 1989 been the beneficial owner of, or able (directly or through the medium of other companies or by any other indirect means) to control more than 5% of the ordinary share capital of the company.

(4) In subsection (3) "associate" does not include the trustees of an employee benefit trust as a result only of the individual's having an interest in shares or obligations of the trust.

(5) Sections 549 to 554 (attribution of interests in companies to beneficiaries of employee benefit trusts) apply for the purposes of subsection (3) as they apply for the purposes of the provisions listed in section 549(2).

(6) In this section "employee benefit trust" has the meaning given by sections 550 and 551.

## **61 Interpretation**

(1) In this Chapter—

- “associate” has the meaning given by section 60;
- “associated company” has the meaning given by section 416 of ICTA;
- “business” means any trade, profession or vocation and includes a Schedule A business;
- “company” means a body corporate or unincorporated association, and does not include a partnership;
- “employer’s national insurance contributions” means secondary Class 1 or Class 1A national insurance contributions;
- “engagement to which this Chapter applies” has the meaning given by section 49(5);
- “national insurance contributions” means contributions under Part 1 of SSCBA 1992 or Part 1 of SSCB(NI)A 1992;
- “PAYE provisions” means the provisions of Part 11 or PAYE regulations;
- “the relevant engagements” has the meaning given by section 50(4).

(2) References in this Chapter to payments or benefits received or receivable from a partnership or unincorporated association include payments or benefits to which a person is or may be entitled in the person’s capacity as a member of the partnership or association.

(3) For the purposes of this Chapter—

(a) anything done by or in relation to an associate of an intermediary is treated as done by or in relation to the intermediary, and

(b) a payment or other benefit provided to a member of an individual’s family or household is treated as provided to the individual.

(4) For the purposes of this Chapter a man and a woman living together as husband and wife are treated as if they were married to each other.

