

Contractor guide to the Construction Industry Scheme (CIS)

Contractors working, or hiring other contractors to work, on construction operations may have to register for the [Construction Industry Scheme \(CIS\)](#). This requires the hirer to deduct income tax directly from the contractor's or worker's gross earnings.

"Special arrangements for the construction industry have been around for many years but the CIS scheme has been in its present form since 2004," explains Neil Awbery, Senior Tax Manager at [ClearSky Business](#).

"The CIS scheme only applies to genuine self-employment, and one of HMRC's main objectives has always been to prevent self-employed subcontractors avoiding tax by simply not registering as self-employed."

'Contractors' and 'subcontractors' both have to register with HMRC

Awbery notes that it is important to understand the terminology used by CIS: "In a CIS context, when HMRC uses the term 'contractor', it does not mean a classic one-person company as we know it, but a construction contractor that delivers construction services and may employ workers or hire subcontractors."

And according to Awbery, subcontractors are typically the worker, and they could be trading as a one-person [limited company contractor](#) or, as is more commonly the case, a self-employed sole trader.

"So, using CIS terminology, both contractors and subcontractors who perform the construction operations defined by HMRC as qualifying for the CIS must register with HMRC under the scheme."

When hiring or being hired, subcontractors must be verified

Awbery continues: "When a contractor wants to hire a worker, then they must first check by phone or online with HMRC that the worker is registered under the scheme. This is not only a legal requirement, but also determines how much tax is deducted from the subcontractor's fees."

Most payroll software now includes the ability to check a worker's status online. That means if a contractor of the one-person limited company kind wants to hire other contractors to work on a construction project, they can easily determine whether the contractors they want to hire are CIS registered.

The CIS requires income tax deductions from gross fees

If the subcontractor/worker is registered with the scheme and performing construction operations, then the contractor/hirer needs to deduct 20% of the subcontractor's gross fees as income tax.

"If the status of the subcontractor/worker cannot be verified, and she/he is not registered with HMRC, then the contractor/hirer is obliged to deduct 30% of the subcontractor's gross fees," says Awbery. "This provides a significant financial incentive for subcontractors to register with HMRC."

How the payments and deductions are processed

In addition to basic status checking and making the deduction, hirers must also make a monthly HMRC return detailing the amounts that they have deducted under the scheme, and also pay the amount deducted to HMRC.

If the contractor has suffered a CIS deduction, it can be recovered from the CIS deductions it has made and only account for the net amount to HMRC. If the deductions it has suffered exceed the CIS deductions it has made it can recover the balance from any Pay As You Earn (PAYE) and National Insurance Contributions (NICs) deducted from any employees it may have.

"If a single-person limited company contractor is hiring other contractors to work on a construction project, they must make the payment and submit the return by the 19th of every month, or face an automatic £100 penalty. HMRC is very strict about this," warns Awbery.

Limited company subcontractors who have deductions by their hirer can choose to set any amounts still unrecovered against their corporation tax liability and they may find that once their corporation tax return is completed, their company is owed a tax rebate by HMRC. "Contractors who are affected could think of it as an advance payment against their corporation tax," adds Awbery.

Although most single-person limited company subcontractors are [VAT](#) registered, Awbery notes that this makes no difference: "If a subcontractor's monthly fees are £10,000 plus £2,000 VAT, they would pay the £2,000 VAT to HMRC as normal via their quarterly tax return. And they would simply receive £8,000 in net fees from their hirer after the 20% CIS deduction."

How subcontractors can receive gross payments

Awbery highlights that it is possible for subcontractors to apply to HMRC to receive their money gross with no deductions: "To receive their full gross fees, the subcontractor must satisfy certain criteria.

"A self-employed sole trader has to demonstrate that their sales turnover for subcontracting activities is £30,000 a year or higher. For a limited company, in broad terms the business must have a sales turnover of at least £30,000 a year for each director or £200,000 for the company as a whole.

"Furthermore, for the 12 months prior to the application for gross payment, the subcontractors must be able to demonstrate that they have complied with all of their tax obligations, and that includes personal tax returns and liabilities. If the subcontractor employs or hires workers, they must also be fully up-to-date with PAYE and CIS returns and payments."

What construction activities qualify for the CIS

As Awbery explains, tax legislation clearly defines which construction activities are covered by the CIS, and HMRC provides [detailed guidance](#): "The good news is that the construction professions, such as architecture, planning, surveying, building services and civil/structural engineering are not within the scope of the scheme."

That means the vast majority of construction contractors (of the one-person limited company kind) only have to worry about CIS if they are hiring other contractors as subcontractors who are within scope.

But Awbery urges contractors to check the rules carefully, as there are some oddities. For example, ship building is not within the scope of CIS, but building offshore platforms is. There are also rules that exempt large companies from having to register as contractors if their construction operations are only a small and non-core part of their operations.

HMRC has published a [comprehensive guide in PDF format](#) that details how the scheme works, what activities are covered and the responsibilities of contractors and subcontractors.

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