

## Contractors who subcontract must comply with HMRC employment intermediary obligations

Contractors who subcontract work to other contractors and freelancers on behalf of a client are classed by HMRC as being an employment intermediary. As a result, they are required to comply with certain tax and National Insurance Contributions (NICs) obligations, according to [guidance published by HMRC](#) in September 2015.

Intermediaries, which can include contractor agencies and umbrella companies, play a major role in the contractor workforce supply chain. However, HMRC is concerned that many are not paying the correct amount of tax and NICs for their workers.

As a result, HMRC has imposed strict guidance in an attempt to ensure that all intermediaries – and this includes contractors who subcontract - fulfil their legal employment obligations.

### What is an employment intermediary?

HMRC describes an employment intermediary as a person or business who makes arrangements for somebody to carry out work for a third party. It goes on to state:

*"You're an employment intermediary if you supply workers to work for an end client or another employment intermediary, and the client then pays you or someone connected to you for the worker's services. The end client is who the worker does the work for."*

This means that contractors who supply other contractors fall into the scope of an intermediary, as they provide another contractors' service to an end client or another party involved, providing a link between the two.

The contractor who subcontracts will typically assume overall responsibility for the project, and will receive the subcontractors' fee from the client on completion, before paying the subcontractor directly from their own company.

### Contractors who subcontract are liable for unpaid tax

Crucially, when a contractor takes on the role of an employment intermediary they assume employment rights and debt transfer risk from the client.

What this means is, should the worker who has been contracted to complete the work be found to have not paid their fair share in tax and NICs, the contractor who subcontracts is liable for any outstanding debt.

This means that it is very much in a contractor's interest when subcontracting to adhere closely to HMRC's guidance.

### Contractors who subcontract may be required to operate PAYE

Employers usually have to operate Pay As You Earn (PAYE) as part of their payroll, which involves deducting income tax and NICs from employees gross pay at source, and then reporting these deductions to HMRC on or before each payday via RTI.

For employment intermediaries, special agency rules apply, known as the agencies legislation. If the rules are found to apply, then the intermediary must treat the worker as if they were an employee and deduct income tax and NICs via PAYE.

This means if a contractor subs out work to another contractor, who is then caught by the agency legislation, then the original contractor must pay their subcontractor via a PAYE payroll, and not simply gross on presentation of an invoice.

For these rules to apply to the subcontractor, four conditions must be satisfied:

Personal service is a requirement

There is a contract between the client and intermediary, or main contractor

The subcontractor must be subjected to, or subject to the right to, supervision, direction and control (SDC)

The subcontractor's fee is not already employment income.

In this instance, it is the responsibility of the intermediary to operate PAYE as if the worker who has been subcontracted the work is an employee. The payments received by the worker are then treated as employment income.

## When employment intermediaries aren't required to operate PAYE

Exceptions are made if the worker provides their service without anybody having the right to supervision, direction or control (SDC) or if personal service is not required. Agency rules are also not applicable if the subcontracted contractor works on a premises not controlled or managed by the client, such as their own home.

Should the intermediary be subcontracting work to a contractor who is either self-employed, in a partnership or limited company, they may also be exempt from operating PAYE, as the contractors' status requires them to announce tax on their income on an annual basis.

When a contractor is part of a contractual chain featuring more than one intermediary, the intermediary that has the contract with the end client must assume the role of 'employer', and decide whether PAYE should be operated.

## Employment intermediaries also have strict reporting requirements

In the circumstance that a contractor who subcontracts is not obliged to operate PAYE on the subcontractors' income, they are instead required to [regularly report on the subcontractor](#) to HMRC. The reporting schedule is quarterly and the details the main contractor needs to send to HMRC include:

The full name, date of birth, gender, NI number and address of the subcontractor

The reason why PAYE was not operated

The workers' Unique Taxpayer Reference (UTR)

The dates within which the contract runs

The fee, currency and whether VAT is included

The party paid by the intermediary

HMRC provides a [report template](#) to ensure that all of the necessary information is gathered, before being uploaded onto its [online upload service](#).

## Intermediaries who do not comply may face penalties

According to the schedule set out by HMRC, the reports must be filed at least once every three months. So if a report is late, incomplete or incorrect, the contractor in the role of employment intermediary may be charged a penalty.

For either not sending a report or for sending a late report, the contractor will initially be hit with a £250 fine. Repeated failure to comply within a 12-month period can result in larger fines.

A second offence within 12 months will result in a £500 and additional offences after that will incur £1,000 fines. For incomplete and incorrect reports, manual penalties may be issued on a case-by-case basis.

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