

MSC Tax Tribunal outcome could have wider repercussions for contractors, warns expert

Contractors providing their services through third party service providers without conducting due diligence could unwittingly be at risk from the Managed Service Company (MSC) legislation.

This is according to [Andy Vessey](#) of [Qdos Consulting](#), who says that the MSC rules pose a very real threat to contractors due to the broad interpretation of the legislation that has been adopted by HMRC, as well as Tax Tribunal judges.

In the first case brought to the Tax Tribunal using MSC legislation – [Christianuyi Ltd & Ors v Revenue & Customs](#) - five medical contractors had their appeals against extra tax bills determined by HMRC rejected. This was on the basis that their companies and earnings were controlled by MSC provider Costelloe Business Services Ltd (CBS) during the 2007/8 and 2009/10 tax years.

As a result, the contractors face backdated tax payments of £160,000 between them, whilst HMRC also intends to transfer tax debts to CBS. However, Vessey notes that the verdict may have broader implications for both contractors and service providers.

First MSC appeals case was “doomed to fail”

“The case was pretty clear-cut in terms of what CBS were doing and the mistakes they were making,” highlights Vessey. “The appeals were doomed to fail from the start.”

Whilst tax tribunal cases don't set legal precedents, Vessey does acknowledge that this case provides contractors with an idea as to how the courts will consider the legislation. Unfortunately for contractors, the view of the tax tribunal judges in this case aligned quite accurately with HMRC's interpretation.

“One of the most alarming things was the wide manner in which the tribunal considered factors such as influence and control,” he adds. “When HMRC wrote the legislation, it was very open to interpretation – and quite deliberately so.

“The actual legislation was a stroke of genius for HMRC, because it did away with composite companies with the stroke of a pen. Similarly, the broad manner in which its definitions can be adopted might open the way for a lot more of these cases.”

CBS dealings were error-strewn

Vessey points out that the dealings of CBS were littered with errors, and so appeals from clients of other MSC providers – of which there are expected to be many – may not suffer the same fate. However, it also reinforces the importance for contractors to carry out their due diligence with regards to their financial affairs.

Long before the appeals were brought to a tax tribunal, an inquiry into CBS was launched by HMRC under the [MSC legislation](#). From this inquiry it was found that each set of accounts provided by CBS had the company name listed as the company secretary, an activity that falls foul of the legislation.

During the tribunal, it was found that one of the contractors, Dr Jacek Trzaski, was unaware that he needed both a company secretary and a registered office for his company.

‘Control’ and ‘influence’ the determinate factors

Vessey explains that CBS also offered bank accounts to all of its clients, the large majority of which were accepted, without proffering little alternative. CBS set up mandates to withdraw funds from its contractors' accounts in order to pay necessary taxes without seeking permission from the contractors themselves.

“In HMRC's eyes, if you do anything more than simply view a client's bank account, you are in control. CBS set up a mandate that they thought was sufficient, but by making deductions before notifying clients, they were in breach of MSC legislation,” adds Vessey.

“Further, the money sat in an interest-bearing account which racked up interest of £127,000, but no interest was passed onto the clients. This was another huge error.”

As a result of these errors, amongst others, CBS was found to be in breach of three of the five necessary criteria for determining an MSC. It was considered to be benefiting financially from its clients, asserting influence over the way payments to clients were issued, and assuming control of the finances of its clients' companies.

Sufficient paper trail could satisfy courts

Vessey explains that, whilst the conclusiveness of this case will leave some MSC providers sweating over their fate in a similar case, due diligence in the way of documentation will likely aid the cause of both company and contractor.

"If the service provider happens to have documented every mandate - and has a watertight audit trail - as a client I would be a lot less concerned. On the other hand, any contractor whose MSC can't provide that body of evidence should be worried, as HMRC will just pick holes in their arrangement."

What is an MSC?

HMRC defines an MSC as: "a person who carries on a business of promoting or facilitating the use of companies to provide the services of individuals". In order for the legislation to apply, the provider must fulfil the definition of an MSC Provider (MSCP) and be involved with their client companies.

MSC legislation highlights five ways in which an MSCP may be deemed to be involved with a client. Falling foul of any of these will result in a negative judgement at a tax tribunal for a contractor and MSC:

Benefitting financially on an ongoing basis from the provision of the services of the individual

Influencing or controlling the provision of services of the worker

Influencing or controlling the way in which payments to the worker are made

Influencing or controlling the client company's finances or any of its activities

Giving or promoting an undertaking to make good any tax loss

In engaging with an MSC, a worker claims remuneration and avoids Pay As You Earn (PAYE) and National Insurance Contributions (NICs) payments in the process.

Contractors who are concerned about the legitimacy of their service provider are advised to seek assurances from their provider, as well as requesting expert advice.

Vessey concludes: "Contractors will need to find out whether the ruling will have any repercussions for them.

"If the provider feels that they sit outside the MSC legislation, the contractor needs to firstly ask why, and what the provider intends to do if they are found to be within the legislation. After seeking assurances from their provider, contractors should seek third party professional advice."

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