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10 Steps towards umbrella compliance

Many contractors work through an umbrella company to minimise their financial and tax administration. Likewise, working with compliant umbrella companies eases the compliance burden on recruiters. Umbrella companies must complete a periodic audit to become an APSCO affiliate and we work closely with Professional Passport, Saffery Champness, EY and FCSA. However, APSCO wants to ensure that members are aware of non-compliant engagement models being marketed and to reiterate the importance of completing basic due diligence on new providers. The Criminal Finances Act 2017 has led many recruitment companies to reconsider the umbrella companies that they engage with as from 30th September 2017 - recruitment companies, as well as individual consultants, can be criminally liable if they fail to prevent tax evasion. This guidance gives an overview of the main compliance issues that members need to be aware of.

What is an umbrella company?

Umbrella companies are businesses that take on workers as their own employees with continuous contracts of employment.

1) Who is the Umbrella Company?

It can be fairly easy to set up a payroll company without experience or professional advice. You must understand who the umbrella company is and consider the following:

- Who are the owners, directors, shareholders? Do any Directors have any outstanding tax liabilities?
- Is the umbrella UK owned and registered with no offshore affiliations?
- Make sure that the umbrella company does not make use of any sort of offshore payments
- Confirm that all payments made to employees are through PAYE. The umbrella must be able to provide payslips and matching Real Time Information reports (RTIs) to confirm all taxes are being paid directly to HMRC
- Is there a qualified, registered accountant overseeing their activities?
- Can you ask for a screen shot of their HMRC account on PAYE and VAT. Whilst these will often show outstanding balances the important point to look for is whether fines, penalties or interest has been applied as this could suggest an issue. Where this is the case clarification would need to be sought.
- Check VAT registration – ask for their VAT number and check its validity [here](#)

Warning signs

- Not transparent about what they do
- Offer more than 80% of net pay
- State they have been approved by HMRC
- Claim they are IR35 Compliant – IR35 doesn't apply to contractors engaged through umbrella companies.
- Separate deductions for statutory benefits inc: SSP, SMP, SAP and SPP
- Claim they fall outside the AWR
- Encouraged to claim expenses that haven't been incurred
- Offer a self-employment scheme – See [Onshore employment intermediaries](#)
- Based outside the UK – See [Offshore employment intermediaries](#)

Since 2017 there has been a growth in so called umbrella companies partially remunerating workers through a loan scheme or other mechanism which may be offshore. This is tax avoidance, so called “disguised remuneration” and the worker (and potentially the recruiter) will be liable for the unpaid taxes, interest and penalties. HMRC are cracking down on this type of activity but it remains a significant problem, hence the importance of you and your clients controlling your supply chains.

Intermediary reporting means that HMRC knows who has contracted with non-compliant or offshore umbrellas and do investigate up to seven years after the event. Minimise risk by only contracting with APSCo Trusted Partners, FCSA or Professional Passport umbrellas.

2) Appropriate Insurance Cover

The umbrella should have appropriate and adequate insurance cover to protect their employees and have Professional Indemnity insurance for their activities. As an employer, the umbrella must have employer's liability insurance in place for all workers. The recruitment company should request sight of insurance policies and review for any exclusions that the policy might include.

3) Contract Of Employment

Although they might often still be referred to as a contractor the worker must be an employee of the umbrella company and as such they have the same rights as any other employed person.

The following should be included in the employment contract between the umbrella and the worker:

- The employee's and employer's name;
- A job title or brief job description;
- The date the employee's employment began;
- The rate of pay and when the employee will be paid;
- The hours of work;
- Holiday entitlement;
- Where the employee will be working;
- Sick pay arrangements;
- Notice periods;
- Information about disciplinary and grievance procedures;
- Any collective agreements that affect the employment terms and conditions;
- Pension and pension schemes.

Confirmation of an Employment Relationship

- Is the employee given details of grievance and disciplinary procedures and is the Employee made aware of Health and Safety policies?
- Will the Contract of Employment be terminated when this assignment comes to an end- that is not usual?
- What is the notice period required to terminate the contract?
- How many days' holiday is the employee entitled to?
- How is holiday pay paid – is it accrued and paid when taken or rolled up?

4) Employment Rights

Contractors engaged via umbrella companies are employees with full employment rights just like any other permanent member of staff. These include the right to be paid the national minimum wage, the right to paid holiday, the right to be auto-enrolled into a pension and to statutory benefits such as sick pay and maternity pay (provided the relevant criteria are met).

5) Agency Worker Regulations (AWR)

The AWR ensures agency workers receive equal treatment. Umbrella company employees are classed as agency workers for the purposes of AWR. Under the AWR workers should be allowed to use any shared facilities (e.g. a staff canteen or childcare) from the first day in an assignment location (Day 1). After 12 weeks' continuous employment in the same role, workers should get the same terms and conditions as the end client's own employees. The employment contract should provide for equal treatment once the worker

has been on assignment for 12 weeks. For more information on the AWR APSCo has a [compliance toolkit](#) to help assist members with the AWR.

"Pay between assignment" contracts, commonly called Swedish Derogation contracts, are unlawful since April 2020.

There is a requirement for recruiters to make sure information is obtained from the client usually by way of a questionnaire and to pass the information down to the umbrella company to make any adjustments.

6) Holiday Pay

Umbrella Companies are expected to act as the employer to their contractors, which means they are entitled to a minimum of 28 days holiday per financial year (although they could be entitled to more under the Agency Worker Regulations). The practice of paying the holiday pay with each payroll payment is also known as 'rolled-up holiday pay' and is unlawful. However, where this has specifically been requested by the worker and the holiday pay is clearly shown as a separate line on the payslip there are no financial losses to the worker and this is unlikely to result in any financial awards or penalties being applied. The rate provided to the umbrella will be uplifted to include a relevant amount for holiday pay. The umbrella then takes this as a deduction from the weekly or monthly payments. If the worker leaves the employment having taken fewer holidays than they are entitled to, they should be paid in lieu of the untaken holiday and also they must be encouraged to use holiday leave in the holiday year, just like any other employee.

7) Expenses: Travel & Subsistence

It used to be the case that contractors working through umbrellas were able to claim tax relief and National Insurance Contributions (NICs) disregard on the travel and subsistence expenses they incurred on their commute from home to work. Since 2016 a worker's ability to get tax relief on his/her travel and subsistence costs are restricted unless it can be shown that the worker is not under the supervision, direction or control (SDC) in the way he/she carries out work.

Supervision, Direction or Control

The Supervision, Direction or Control test is multi-faceted and HMRC published guidance on 6th April 2016. This can be found at <https://www.gov.uk/government/publications/employment-intermediaries-personal-servicesand-supervision-direction-or-control>

The Finance Act 2015 introduced a test on 'Relevant Salary Sacrifice' that prohibits any reimbursement of expenses that reduce the workers 'general earnings'. The only exception to this is mileage as it is an allowance and falls outside of the test.

Since 6th April 2016 each assignment falling within the criteria is considered to be a separate employment. This means that workers regularly commuting to a permanent workplace for each assignment (ordinary commuting) are not eligible for relief on travel and subsistence. This change applied irrespective of whether contractors have an "overarching contract of employment" with their umbrella company. Recruitment companies should ask umbrella companies for evidence of how they comply with the changes post April 2016. It is rare for an umbrella worker to now qualify for home to work expenses relief. Contractors may however still qualify for relief on travel expenses incurred while working, as opposed to the commute from home to work.

Where a recruitment company provides an umbrella with reimbursed expenses the umbrella must obtain a completed expense claim form from their employees with all supporting evidence before these can be considered for payment outside of PAYE. Without this evidence the additional monies received would have to be paid via PAYE to the worker, Reimbursed expenses are not automatically tax free to the worker.

Be wary of any umbrella companies that state they can still process home to work travel expenses.

The Bribery Act 2010

Giving or receiving financial incentives to gain a commercial advantage is considered a bribe.

8) Referral Fees

Referral fees paid to recruitment firms by umbrella companies for the referral of contractors' business are not uncommon in the recruitment sector. Neither the Act nor any previous legislation implies that referral fees are illegal; however, employers must consider whether the intention of a referral fee is to induce improper performance by their employees. The expression "improper performance" or to "act improperly" means performance which amounts to a breach of an expectation that a person will act in good faith, impartially or in accordance with a position of trust. If umbrella companies are offering cash or pre-loaded credit cards to consultants in exchange for referrals there would most likely be a contravention of the Bribery Act.

The Bribery Act still applies if an arrangement exists between an umbrella company and a consultant without the company's knowledge. In addition, if referrals or gifts in kind are given to them the employer may have a PAYE tax liability. In extreme cases and since the Criminal Finances Act implementation in autumn 2017 recruiters may have corporate criminal liability for tax evasion. The Criminal Finances Act also introduces obligations on recruitment companies to have adequate processes to prevent tax evasion. Where it is known that workers are receiving referral fees a company must have processes in place to ensure this additional income is being reported to HMRC via a consultants SATR. Failure to report is tax evasion.

Recruitment companies should have 'adequate procedures' in place to prevent bribery, which is usually in the form of an anti-bribery policy. As long as companies are transparent in their payment and acceptance of appropriate referral fees and the transactions are clearly documented there should be no contravention of the Bribery Act. APSCo provide a model Anti-Bribery Corporate Policy to members available [here](#). Referral fees are also included in the APSCo Codes of Conduct which members and Trusted Partners are obligated to comply with.

9) Criminal Finances Act & HMRC Crackdown

The Criminal Finances Act 2017 introduced the new corporate criminal offence of failure to prevent the facilitation of tax evasion. The Act has therefore imposed a criminal risk for recruitment companies utilising non-compliant umbrella companies. In our opinion the best way to minimise risk and to avoid engaging with a non-compliant model is to carry out substantial due diligence on all umbrellas. Not all members will have the resource or means to carry out such due diligence so we would therefore suggest using APSCo affiliates, FCSA or Professional Passport umbrellas. Since the changes there may well be recruitment companies who are open to risk without even realising it. If you come across umbrella companies who are advertising a high retention rate, sometimes as high as 85-90% it is likely that the umbrella may be paying a small salary and loaning the balance of the income. No umbrella can be compliant and yet still provide its clients with above 80% net take home pay.

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HMRC is aware that loan repayments and other similar schemes are still prevalent in the umbrella sector. Loan schemes normally involve the employee/contractor being paid a small amount of earnings with the balance by way of a loan from a third party which is not usually repaid. You can see a full list of tax avoidance schemes that HMRC believes are being used to avoid paying tax due here:

<https://www.gov.uk/government/collections/tax-avoidance-schemes-currently-in-the-spotlight>.

Should I create a PSL?

Creating a Preferred Supplier List may be a useful way to limit risk. You may choose to create a PSL by simply using umbrella companies that already have an accreditation or alternatively you may choose to create your own. Members must be aware that setting up a successful PSL system takes time and you must be confident with your auditing and due-diligence process.

You must always be sure that you are not recommending an umbrella

HMRC are pursuing action against the users and promoters of these schemes and recruiters: some members have received HMRC court claims, known as Schedule 80 determinations, claiming the unpaid taxes, interest and penalties from the recruitment company.

10) Documentation

Opt out: The Conduct Regulations also apply to umbrellas. For an opt-out to be effective, any declaration of intent to opt-out must be signed by both the contractor as the "work seeker" and a representative of the umbrella company.

Right to work: Umbrella companies have a responsibility to ensure that their employees are legally entitled to work in the UK. You should ensure that the umbrella confirms that it carries out these checks and you may also want to ask if they have ever been found by the Home Office to have supplied illegal workers or fined by the UKBA.

Timesheets: There must be appropriate timesheet administration fees which are proportionate to cost of processing.

Disclaimer

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This update was prepared by APSCo with the expert input and advice of our affiliate Professional Passport. Professional Passport has been providing compliance support services for over 10 years and cover umbrella, accountancy as well as CIS.

<https://www.professionalpassport.com/>

