



UK Government

Tackling non-compliance in
the umbrella company
market

**Government response to the
consultation**

March 2025

OFFICIAL



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Tackling non-compliance in the umbrella company market
Government response to the consultation

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Executive Summary

There is evidence of widespread non-compliance in the umbrella company market, depriving workers of the employment rights to which they are entitled, distorting competition in the labour market and leading to significant tax loss to the Exchequer. Following an earlier Call for Evidence, the previous government launched a consultation on Tackling non-compliance in the umbrella company market which ran from June to August 2023.

The consultation made proposals with the aim of gathering responses from stakeholders about the most effective way to address issues of tax and employment rights non-compliance by umbrella companies. Addressing these issues would enable the delivery of improved outcomes for workers, support a level playing field in the umbrella company market, and protect taxpayers from the significant revenue losses arising from non-compliance, while also supporting economic growth.

The consultation put forward suggestions for the definition of umbrella companies with the purpose of subsequently regulating them and also laid out three options for improving tax compliance in the umbrella company market.

Summary of consultation responses

Seventy-five responses were received from a range of stakeholders. Officials also ran 16 stakeholder roundtable events to discuss the proposals. In this document, the Government will summarise the views of the respondents, showing which of the options put forward in the consultation were preferred, and why they were favoured.

The Government will then respond and set out the actions it will take to ensure workers get comparable rights and protections when working through an umbrella company as they would when taken on directly by an employment business. The Government will also set out its plans to tackle tax avoidance in the umbrella company market, which were first announced at Autumn Budget 2024.

These goals align with the aims of the Make Work Pay plan, a core part of the Government's strategy to grow the economy, raise living standards and create equal opportunities in the workplace.

Government priorities and next steps

The Government considers that timely action in the umbrella company market is imperative to protect the most vulnerable workers.

Informed by the responses to this consultation, the Government is therefore legislating to define umbrella companies, to allow for their regulation and to bring them within scope of the Employment Agency Standards Inspectorate's (and subsequently, the Fair Work Agency's) remit, through an amendment to the Employment Rights Bill.

The Government is also committed to closing the tax gap and making the tax system fairer by ensuring temporary workers are protected from large, unexpected tax bills caused by unscrupulous behaviour from non-compliant umbrella companies. As announced at Autumn Budget 2024, where an umbrella company is used in a labour supply chain to engage a worker, the Government will bring forward legislation to move the responsibility to account for PAYE from the umbrella company that employs the worker, to the recruitment agency that supplies the worker to the end client. Where there is no agency in a labour supply chain, this responsibility will sit with the end client. This will take effect from April 2026. More details about this measure can be found here: www.gov.uk/Government/publications/tackling-tax-non-compliance-umbrella-company-market¹.

Chapter 2: Regulating umbrella companies for employment rights

This chapter of the consultation set out two proposed methods for defining umbrella companies. It sought views on which would be the more effective against two main success criteria, notably its precision and longevity. The responses received highlighted the complexity of defining umbrella companies in a way that achieves the stated objectives, with no consensus emerging around either of the given options. Respondents felt that neither option would successfully capture the range of umbrella company arrangements that exist. Some stakeholders proposed alternative ways of defining umbrella companies.

The Government also sought views on the substance of umbrella regulations that would be introduced once a legal definition is established and how they might be enforced. Responses indicated a consensus that the Government should concentrate on addressing financial detriments, worker understanding of the umbrella arrangement and ensuring genuine businesses operate in the umbrella market. There was support for the principle that the Employment Agency Standards (EAS) Inspectorate should be responsible for enforcing regulation of umbrella companies.

¹ Policy paper – Tackling tax non-compliance: umbrella company market. October 2024. HM Revenue & Customs.
[Tackling tax non-compliance: umbrella company market - GOV.UK](https://www.gov.uk/government/publications/tackling-tax-non-compliance-umbrella-company-market)

Chapter 3: Tackling tax non-compliance in the umbrella company market

This chapter of the consultation outlined strategic options for preventing tax non-compliance in the umbrella company market by changing behaviours in the temporary labour market. It invited views on how these options could be developed and what their impacts could be on non-compliance. Other questions looked at impacts on the umbrella company and wider labour markets.

Option 1: Mandating due diligence.

Most respondents thought that a mandatory due diligence regime for businesses that use umbrella companies would have a positive impact on non-compliance in the umbrella company market, though there was less consensus about the specific aspects of designing this regime. Respondents were clear that they would value certainty and support from the Government if required to undertake mandatory due diligence. Some respondents did not think that this option went far enough and said it would have a limited impact on non-compliance, either because non-compliant umbrella companies would find a way to avoid scrutiny, or because there were already clauses in place between clients and agencies on supply chain liability.

Option 2: Transfer of tax debt that cannot be collected from an umbrella company to another party in the supply chain.

Respondents had mixed views on whether introducing a power to transfer umbrella company tax debts would be effective at tackling tax non-compliance. Some thought that this would have the anticipated behavioural impact of encouraging employment businesses to take greater care when choosing an umbrella company, but others were concerned that this approach could embolden umbrella companies to be non-compliant. Respondents were clear that there should be protection for businesses that could show that they had completed due diligence checks.

Option 3: Deeming the employment business which supplies the worker to the end client to be the employer for tax purposes where the worker is employed by an umbrella company, moving the responsibility to operate Pay As You Earn (PAYE).

Although opinions were mixed, the largest group of respondents thought the introduction of this option would reduce non-compliance. The next largest group suggested that this approach would likely result in businesses moving away from using the umbrella company model to engage labour. While several downsides and risks to this were raised, not all respondents thought that this would be a bad outcome, with some arguing that it would improve compliance.

Chapter 4: Targeted options to address tax non-compliance

This chapter invited views on targeted options to address the abuse of specific tax reliefs by some umbrella companies. Specifically, the Value Added Tax (VAT) Flat Rate Scheme, and the Employment Allowance have both been targeted by so-called mini umbrella companies (MUCS), who abuse both schemes to benefit from lower levels of VAT and employer National Insurance Contributions (NICs).

Many respondents suggested that the VAT flat rate scheme is largely used for financial benefit rather than its intended purpose of simplification. It was also acknowledged that the VAT Flat Rate Scheme was abused by umbrella companies. Almost half of respondents suggested that the scheme should be removed to prevent abuse while some suggested a new scheme which reflected modern accounting practices.

Similar to the VAT Flat Rate Scheme, the Employment Allowance is simple to use and relies on self-assessment of eligibility making it easier for umbrella-style companies to abuse. Some umbrella companies fraudulently exploit the Employment Allowance by splitting businesses into multiple smaller companies (MUCS) and ensuring the company's employer NICs liabilities for the year are covered by the Employment Allowance, meaning no employer NICs is paid. While there was some support from stakeholders for the targeted proposal outlined in this chapter, given the anticipated impact of the umbrella company measure announced at Autumn Budget 2024, the Government will not take forward targeted measures to address VAT and Employment Allowance abuse at this time. The Government will continue to monitor levels of abuse and whether further action is needed at a future date.

Chapter 1

Introduction

Background

1.1 The [Tackling non-compliance in the umbrella company market](#)² consultation was launched by the previous government in June 2023 and closed on 29 August 2023. The options presented were based on information received via the earlier [Call for Evidence](#)³, which ran between November 2021 and February 2022. This document summarises the responses to the consultation and sets out the Government's response and proposed action.

1.2 The consultation document set out how umbrella companies work, and how they interact with both the recruitment sector and other hirers. Umbrella companies are employment intermediaries that employ temporary workers on behalf of recruitment agencies and end client businesses. Typically, they employ workers under contracts of employment. They are responsible for paying individuals and operating Pay As You Earn (PAYE), deducting income tax and National Insurance contributions (NICs). As employers, they are also responsible for providing employment rights. Umbrella companies do not find work for those they employ or engage.

1.3 The use of employment intermediaries – whether employment agencies, employment businesses, umbrella companies, or a combination of one or more – has made the landscape of employment relationships increasingly complex for workers to navigate. It is not always clear to workers whether they are entitled to employment rights and, if they are, who is responsible for providing them.

1.4 Unlike employment agencies and employment businesses, which are regulated under the Employment Agencies Act 1973 and the associated Conduct of Employment Agencies and Employment Business Regulations 2003, umbrella companies are generally unregulated. Umbrella companies can be used (though are not

² Consultation – Tackling non-compliance in the umbrella company market. June 2023. HM Treasury.

<https://www.gov.uk/government/consultations/tackling-non-compliance-in-the-umbrella-company-market>

³ Call for Evidence Outcome – Call for Evidence: umbrella company market. November 2021. HM Treasury.

<https://www.gov.uk/government/calls-for-evidence/call-for-evidence-umbrella-company-market>

exclusively used) to evade obligations to provide employment rights.

1.5 There is also evidence of widespread tax non-compliance in the umbrella company market. HMRC data shows that £500 million was lost to disguised remuneration tax avoidance schemes in 2022 to 2023, almost all of which was facilitated by umbrella companies. These schemes can leave taxpayers with substantial tax bills. Hundreds of millions more was lost to so called 'mini umbrella company' fraud and other fraudulent attacks by people abusing umbrella company structures. This tax non-compliance can leave workers facing substantial tax bills and enables non-compliant umbrella companies to undercut their competitors, threatening the viability of those businesses that do the right thing, as well as the functioning of the market itself. HMRC takes robust action against non-compliant umbrella companies using its compliance powers. However, there is a clear case for strategic action to prevent these forms of non-compliance from occurring at all.

1.6 The proposals in the consultation were broken down into three chapters:

- **Chapter 3: Regulating umbrella companies for employment rights** – sought views on two proposals for defining umbrella companies. The Government also sought early views on the substance of the regulation and how it could be enforced.
- **Chapter 4: Tackling non-compliance in the contingent labour market** – set out three strategic options for addressing the tax non-compliance by changing incentives and behaviours in the labour market.
- **Chapter 5: Targeted options to address tax non-compliance** – focused on the Employment Allowance and VAT Flat Rate Scheme, which are tax easement available to small businesses that are subject to fraud by so-called 'mini' umbrella companies.

Summary of consultation responses

1.7 Seventy-five responses to the consultation were received from a range of stakeholders, although not all respondents answered every question posed. Feedback and responses were also received from stakeholders at 16 roundtable events chaired by HMRC or HM Treasury officials. Respondents to the consultation consisted of:

- 14 Agencies/Employment businesses
- 11 Umbrella companies
- 11 Accountancy/Auditors
- 7 Individuals

- 6 Tax and legal advisors
- 4 Public bodies
- 4 Trade Unions
- 3 Each of Charities, Employment business representative bodies, lobby groups, worker representative bodies
- 2 Each of Umbrella company representative bodies, Policy/Think tanks.
- 1 Each of Business representative body, End clients.

1.8 This document summarises all these responses, illustrating which of the options put forward were favoured and why they were preferred. The Government will respond to each section and then set out the actions it will take to address the issues raised in the consultation.

1.9 The Government will act to ensure that workers get comparable rights and protections when working through an umbrella company as they would when taken on directly by an employment business.

1.10 And the Government has already, at Autumn Budget 2024, committed to tackling tax non-compliance by umbrella companies. The option implemented will be that which the Government considers will have the maximum impact on reducing tax non-compliance.

1.11 The statistical information provided on each question is expressed as a percentage of those who responded to that question, rather than as a proportion of the 75 total respondents.

Government Priorities and Next Steps

1.12 The Government is committed to restoring the principle that work should always pay. The plan to Make Work Pay is a core part of the mission to grow the economy, raise living standards across the country and create opportunities for all. The plan will boost fairness in the workplace, ensure equality of treatment and opportunity, and support low-paid workers, and the Government is wholly committed to ensuring the balance of power between workers and business is fair to all. Crucially, this means that where workers are engaged in an employment relationship – whoever their employer is – they should be able to easily access the rights that they are entitled to.

1.13 The Government's aim is to ensure that workers get comparable rights and protections when working through an umbrella company as they would when taken on directly by an employment business.

1.14 Informed by stakeholder views, the Government intends to take action through amending the Employment Rights Bill to define and regulate umbrella companies for the purpose of employment rights. In developing this amendment, the Government has taken into account the views and concerns expressed by stakeholders through the responses to this consultation and balanced these against the need for prompt action.

1.15 The Government is also committed to closing the tax gap and ensuring that everyone is paying the tax that they owe. This is fair, essential for a well-functioning economy, and will help to keep taxes on working people as low as possible. As announced at Autumn Budget 2024, the Government will therefore bring forward legislation to change who has responsibility to account for PAYE where an umbrella company is used in a labour supply chain to engage a worker. This will move the responsibility to account for PAYE from the umbrella company that employs the worker to the recruitment agency that supplies the worker to the end client. Where there is no agency in a labour supply chain, this responsibility will sit with the end client. This takes effect from April 2026 and is expected to raise £500m in 2029-30.

1.16 This measure will support a level playing field for compliant businesses who already ensure that their labour supply chains are free of tax fraud and avoidance; decrease large sums of money going to organised criminal gangs involved in labour supply chain fraud; and protect workers from large, unexpected tax bills in the future as a result of tax fraud and avoidance by their employer. More details about this measure can be found here: www.gov.uk/government/publications/tackling-tax-non-compliance-umbrella-company-market.⁴

1.17 The Government will continue to review further policy options and engage with stakeholders as appropriate.

⁴ Policy paper. Tackling tax non-compliance: umbrella company market. October 2024. HM Revenue & Customs.
<https://www.gov.uk/government/publications/tackling-tax-non-compliance-umbrella-company-market>

Chapter 2

Regulating umbrella companies for employment rights

Introduction

2.1 The priority in Chapter 3 of the consultation was to gather views and evidence on which of two potential approaches to establishing a legal definition of an umbrella company would be the most effective, and to seek views on the scope and enforcement of regulations relating to umbrella companies.

2.2 In questions 1 to 3, the Government sought respondents' views on which of two proposed definitions would be most effective against two main criteria for success. These options were:

- Option 1: Defining umbrella companies and limiting acceptable engagement structures.
- Option 2: Defining umbrella companies by applying three tests.
- Respondents were also invited to provide their own proposals.

2.3 In questions 4 to 8, the Government sought views on what aspects of umbrella company operations should have specific regulations attached to them as well as the approach to enforcing these regulations. The suggested proposals were:

- Option 1: Introduce regulations to set the minimum legislative standards in a few key areas (for example, handling of pay and holiday pay).
- Option 2: Introduce regulations that go beyond these key areas.
- Respondents were also asked whether starting with a targeted set of standards before expanding them would be most appropriate.

Summary of responses (questions 1 to 3)

Question 1: Which of the two options would be the most effective way to define umbrella companies to ensure only they are brought in scope now and ensure future regulations/standards can be targeted to the right business in the supply chain?

2.4 Of the 61 respondents that answered this question, Option 1 was viewed as the more effective option, with 30% of respondents feeling that this option was more effective, compared with 20% for Option 2. However, these findings should be treated with caution. This is because some stakeholders' views did not reflect substantive support but rather, they felt the option they selected was the more effective of two otherwise limited options.

2.5 Stakeholders who expressed the view that Option 1 would be more effective tended to agree with the rationale that the four permitted engagement methods largely captured those currently in use. They also tended to agree that it would require minimal adaptation, would give certainty for businesses and enforcement purposes, and would bring more transparency into umbrella company arrangements. Common concerns with Option 1 also largely reflected concerns the Government was previously aware of, including the potential reduction of flexibility in the recruitment sector and the reliance on concepts of "Corporate work-seeker" and "personal service company (PSC)" (which were not being defined, and which were not consulted on).

2.6 The common reasons for Option 2 being viewed as more effective were its specificity and that it would avoid unnecessarily reducing flexibility in the sector through not limiting engagement methods. The main concern identified with Option 2 was that it was easier for non-compliant businesses to (re)structure to avoid regulation, because it would provide companies with a list of conditions to avoid complying with. This was not always considered a reason to abandon this policy approach (one leading law firm felt that it might still be preferable provided there were targeted anti-avoidance provisions). There was also a concern that Option 2 could drive umbrella companies offshore, putting more beyond UK Government jurisdiction.

2.7 Some respondents were critical of the requirement for an employment business to be in the supply chain as it could lead to common arrangements, which they thought should be in scope, being excluded. Additionally, one trade union argued that this would deprive a growing population of freelancers working through umbrella companies from receiving protections. This was generally cited as the main reason why neither option was likely to be effective either in the short term or in the longer term.

Question 2: Which of the definitions would be the most future-proof? Please explain your answer.

2.8 Just over 30% of the 54 respondents who answered felt that Option 1 would be the more future proof. However, there were concerns that Option 1 did not capture all the current ways in which individuals might be engaged by umbrella companies and some current and widely used models (such as Professional Employment Organisation (PEOs) and joint employment) would be made unlawful. Moreover, some respondents felt that simply rendering something unlawful would not necessarily solve the issue given that non-compliant actors would seek to find routes to circumnavigate the definition and regulations.

2.9 Some respondents felt that the limited scope of Option 1 would make it ineffective, whilst others argued that its narrow scope made it more future proof, because it would effectively force employment businesses to carry out more due diligence, in turn leading to businesses proactively rooting out bad actors, making the need to update legislation less pressing. It was also suggested that Option 1 would work most effectively when combined with debt transfer and mandatory due diligence which were proposed in chapter 4 of the consultation.

2.10 A similar number of respondents (just under 30%) felt Option 2 would be the most future proof as it would be easier to understand. However, this would depend on the Government adjusting the conditions it had set out under Option 2 for businesses to be considered umbrella companies. In addition, some industry experts reported that Option 2 would provide a higher level of clarity about pay structure.

2.11 Several respondents felt that neither option would be future proof. This was in part because both require the involvement of an employment business. Some also considered the definitions to be too complex and focussed, causing confusion around scope and ultimately enabling deliberately non-compliant companies to be able to “game the system”. With neither option therefore being considered wholly fit for purpose now, respondents thought they were incapable of being “future proof”.

Question 3: Are there any unintended consequences of either option and/or are there alternative ways of defining umbrella companies the Government should consider?

2.12 The summary of responses to this question will be in two parts: respondents' views on i. the unintended consequences of the previous Government's two proposals, and ii. the alternative approaches to defining umbrella companies where they were put forward. 42 stakeholders responded regarding the unintended consequences of Option 1, with 2 of these respondents providing

alternative approaches to defining umbrella companies. 34 stakeholders responded regarding Option 2, with 2 of these respondents providing alternative approaches to defining umbrella companies.

2.13 In addition to the unintended consequences of both options already set out in responses to earlier questions, some respondents were concerned with regard to Option 1 that other contracting models that the previous Government was not intending to regulate through these proposals would be brought in scope (and subject to regulation) simply because they involved a contract with an agency. The main unintended consequences identified for Option 2 were similar, but a small number of stakeholders also highlighted the risk of it stifling innovation and restricting direct engagement by the end-client.

2.14 Few stakeholders proposed alternative ways of defining umbrella companies but there were similarities where such proposals were advanced. Some of the responses suggested incorporating drafting from the other pieces of legislation such as Agency Workers Regulations 2010 (“AWR”) or from the definition of a managed service company. The logic was that they are established and understood definitions and, in the case of the AWR (which it was argued was always intended to cover umbrella companies), have not been subject to challenge. There was also the suggestion that the Government does not actually need to specify the umbrella company activities that are in scope and could instead define umbrella companies as businesses that had registered under a government-run registration scheme. One of the general criticisms made by some stakeholders was that both options were too specific and did not capture the range of umbrella company arrangements, and so a suggestion was to broadly define umbrella companies based on them providing payment services and the worker they employ being in scope of IR35 or choosing to work through an umbrella company. Lastly, one proposal was made that the Government defines umbrella companies by describing the characteristics of the supply chains they operate in.

Government response to questions 1-3

2.15 Protecting the most vulnerable at work is a priority for the Government. The Government is seeking to eliminate the most egregious abuses by umbrella companies in the recruitment sector, where it is understood there has been an increase in the use of non-compliant umbrella companies in recent years. It is also where the potential detriment is greatest as affected individuals are typically agency workers who may have little or no choice about agreeing to be employed by an umbrella company when accepting a role.

2.16 The consultation responses highlighted the complexity of successfully defining umbrella companies, and there was no clear

consensus around either of the two proposed definitions. Whilst recognising this complexity, the Government considers that timely action in this space is imperative to meet the aims to make work pay.

2.17 The Government has therefore tabled an amendment to the Employment Rights Bill to define umbrella companies and allow for their regulation.

2.18 The Government has listened to the respondents of the consultation and recognises the issues with the original two options proposed. Further policy development has taken place, and a new definition has been developed that takes into account the responses received to the consultation, and the need for timely Government action in this space. This definition takes a simpler approach in focusing on two key elements which are indicative of an umbrella company. Firstly, that an entity is in the business of employing a person with a view to them being supplied to a hirer; secondly, that an entity is in the business of paying for, receiving or forwarding payment for the services of persons with a view to them being supplied to a hirer.

2.19 A small number of stakeholders argued that umbrella companies were not capable of holding genuine employment relationships. If true, this would have rendered umbrella company regulation for employment rights largely unnecessary. This has been carefully considered and is a view that the Government does not agree with. An umbrella company can engage in a genuine employment relationship with the workers who provide their services to a hirer.

Summary of responses (questions 4 to 8)

Question 4: What aspects of the umbrella company's role in the supply chain should the regulations cover?

2.20 45 respondents answered this question. There was significant unity across respondents regarding the requirements the Government should apply to umbrella companies which fell into three broad categories: (1) addressing financial detriments; (2) worker (especially agency workers) understanding of the umbrella arrangement; and (3) ensuring genuine businesses operate in the umbrella market.

2.21 To address the genuine and widespread financial detriment to workers, stakeholders agreed that regulations are needed to prevent non-payment of holiday pay, provide clarity about pay rates and ensure umbrella payslips are more user-friendly. One stakeholder argued that pay transparency and protection could be achieved if the Government adopted the model used in the Netherlands, where umbrella companies are required to use client accounts. Preventing wage skimming and banning the use of

financial incentives or ‘kickbacks’ (sometimes reportedly funded by withholding holiday pay or skimming) were also noted as financial issues that regulations should seek to address.

2.22 To ensure workers’ better understanding of the reality of umbrella engagement, some respondents suggested a specific duty on umbrella companies to make sure agency workers know what employment rights they may be entitled to. There was also a general feeling that regulations should prevent workers from being required to pay to be employed and have their pay processed, and that if working through an umbrella company, workers should be able to choose which umbrella company will handle their pay.

2.23 The last broad grouping of issues that stakeholders felt regulations should address concerned ensuring that only genuine businesses were active in the market. Some stakeholders thought that this could be achieved by specifying minimum capital requirements and by employment businesses carrying out appropriate due diligence.

2.24 There were other general comments about the regulations that should be noted. Some stakeholders thought that most of an umbrella company’s relationship with a worker was already subject to wider employment law requirements, suggesting these specific regulations only need to be targeted. Further, some felt that the regulations needed to reflect the specific function that umbrella companies play in the supply chain and that the division of labour between the umbrella company and employment businesses should be clear. Lastly, some set out that the business obligations and any sanctions for non-compliance should be proportionate.

Question 5: Is there a rationale for starting with limited regulations and reviewing them before potentially expanding them to cover other areas of umbrella company involvement? Please explain your answer and illustrate with examples.

2.25 Around 60% of the 41 respondents who answered this question felt that the Government should stagger the introduction of regulations to help avoid further delays and help businesses adapt in a cost-effective way. This would also enable the Government to undertake a formal post-implementation review and avoid “double regulating” umbrella companies. An argument was also made that a smaller set of regulations would be more easily enforceable, particularly in a new and complex sector.

2.26 However, almost 40% of those that answered this question reported that there was no rationale for staggering the introduction of regulations. Some felt the sector had already demonstrated that the current self-regulation was not delivering high standards and that the sector was well-enough understood that there was no need for partial regulation to get these complex regulations right.

Some felt that the gradual approach, rather than helping businesses, could burden them due to the likelihood they would need to regularly adapt to new obligations. There was also a fundamental point that implementing targeted regulations, while curbing some of the worst excesses, would not take a view across the entire supply chain and would risk perpetuating bad practices by leaving loopholes.

Question 6: Are there reasons the Employment Agency Standards (EAS) Inspectorate should not enforce umbrella company regulations? And if so, are there other bodies or approaches the Government should consider? Please explain your answer.

2.27 46 respondents answered this question. Nearly two thirds of responses were firmly of the view that EAS should enforce umbrella company regulations. Common reasons given were EAS' existing expertise regulating the recruitment sector where the consultation document proposed to regulate umbrella company involvement. It would avoid unnecessarily complicating the enforcement landscape or creating delays likely to arise from seeking to set up a separate body. Stakeholders also noted that EAS should work with other enforcement bodies, such as the Financial Conduct Authority (FCA), which have relevant expertise in areas where umbrella conduct should be regulated. Some supported EAS taking on this role, but only in the absence of a single enforcement body.

2.28 A smaller proportion, equating to just over one third of respondents, argued that EAS would not be the most effective body, mainly due to insufficient resourcing. Stakeholders expressed a view that EAS was already under-resourced, and this would only become more challenging if its remit were expanded without a corresponding increase in resource.

2.29 Numerous respondents stated that a Single Enforcement Body would be better placed to enforce umbrella company regulation. For example, one legal and technical expert responded that the money that would have been spent on a single enforcement body could be spent increasing EAS resource to the level required to effectively police umbrella regulations on top of their existing functions.

Question 7: Does the Employment Agency Standards (EAS) Inspectorate have sufficient enforcement powers to regulate umbrella companies or would changes need to be made? Please explain your answer.

2.30 Of the 35 respondents who answered this question, there was a roughly even split between those who felt EAS had sufficient powers and those who did not. Some reflected that EAS alone did

not have sufficient powers and would need to work with other enforcement bodies, while others thought that EAS should be given the power to issue civil penalties. In contrast, some responded that EAS' current powers would be sufficient if they could be used to act against umbrella companies.

Question 8: Should EAS mirror its current enforcement approach for employment agencies and employment businesses if it enforces umbrella company requirements? Please explain your answer.

2.31 36 respondents answered this question. Almost 80% of those who responded to this question disagreed that an ombudsman or purely reactive approach to enforcement (i.e. not engaging in proactive or "outward bound" visits to businesses) would work. The scale of bad behaviour in the market was reason enough to justify a proactive enforcement model. There was also concern that if launching enforcement activity relied on complaints, it would be infrequent and leave the sector largely unregulated in practice. This was because those who most needed active state enforcement were also the least likely to make the complaint that would be needed to trigger enforcement activity under an ombudsman-style arrangement.

2.32 Moreover, if EAS was empowered to undertake reactive and proactive enforcement and compliance activity, this should be based on good quality intelligence and its own risk matrix. This could be strengthened by combining EAS own risk data with insights from HMRC's quarterly reporting submission.

2.33 Some also reported that EAS should continue to focus on educating businesses (rather than immediately applying significant penalties) so that enforcement is proportionate and distinguishes between accidental non-compliance and deliberate and repeated breaches of the legislation. EAS should also continue its approach of working closely with key enforcement agencies in other sectors.

2.34 In contrast, a minority of respondents reported that EAS should not follow its current enforcement approach with umbrella companies. This was mostly because it would, in their view, unnecessarily replicate the job being done by accreditation bodies that cover most of those operating. Adopting a reactive approach to umbrella company enforcement could also ensure EAS' limited resource was more effectively deployed.

Government response to questions 4-8

2.35 As set out in the response to questions 1-3, the Government's intention is to legislate, through an amendment to the Employment Rights Bill, to both define and allow for the regulation of umbrella companies. The Government's view is that umbrella

companies should be subject to regulation in the same way that employment businesses are.

2.36 The Government agrees with the broad consensus among respondents on the areas which regulations should cover, as well as with the point that many respondents made about the need to consider any new regulations in the context of those that currently apply to employment businesses. The views expressed in the responses to this consultation have been carefully considered during the drafting process. Umbrella companies will be regulated in a similar way to the existing Conduct Regulations. There is a statutory duty to consult before making any amendment to the Conduct Regulations, and the Government will consult again prior to any amendments to these. Responses to these questions, alongside further stakeholder engagement, will continue to support ongoing policy development in this space.

2.37 The Government notes that there was support among respondents in the consultation for EAS to be the body responsible for enforcing umbrella regulations and agrees with this. The plan to Make Work Pay, which is a manifesto commitment, promised to establish a single enforcement body – the Fair Work Agency (FWA) – where the previous Government had not. The previous Government had publicly committed to including regulation of umbrella companies within scope of the proposed single enforcement body. Through amending the Employment Rights Bill, the Government intends to fulfil this commitment. EAS's functions will fall within the new FWA's remit, which will be – once operational – responsible for enforcing the relevant regulations.

Chapter 3

Tackling tax non-compliance in the contingent labour market

Introduction

3.1 Chapter 4 of the consultation outlined strategic options for preventing tax non-compliance within the umbrella company market by changing behaviours in the temporary labour market. It invited views on how these options could be developed and their impacts on non-compliance. Other questions looked at impacts on the umbrella company and wider labour markets.

Option 1: Mandating due diligence.

3.2 The first option in this chapter explored the introduction of a mandatory due diligence requirement for businesses that use umbrella companies. The consultation invited views on where in the labour supply chain such an obligation should sit if it were introduced and what an appropriate penalty regime to support the requirement would consist of.

3.3 The Government would support businesses by providing guidance setting out due diligence principles, how compliance can be demonstrated and the potential penalties for not completing due diligence or being unable to demonstrate that due diligence was carried out.

Summary of responses (questions 9 to 20)

Question 9: Do you agree that a requirement to undertake due diligence upon any umbrella companies which form part of a labour supply chain would reduce tax non-compliance in the umbrella company market, and to what extent?

3.4 Although not all respondents expressed an opinion on every question, around four out of five responses to this initial question expressed a positive view towards the introduction of mandatory due diligence. Respondents from the recruitment industry generally agreed that a mandatory due diligence requirement would reduce tax non-compliance in the umbrella company market, though some did note that it was important for HMRC to continue to hold umbrella companies ultimately responsible for their tax compliance.

3.5 A number of replies from employment businesses stated that they already carry out due diligence on the umbrella companies they engage with, however the nature of these checks can vary greatly as can the frequency of them. Some thought that merely mandating due diligence would be enough of a deterrent to reduce non-compliance in the umbrella market, while other respondents suggested that it wouldn't have any further impact on non-compliance than their own due diligence checks currently did.

3.6 Respondents from the recruitment industry suggested that the effectiveness of a due diligence requirement would hinge on how well businesses carried out due diligence checks. They raised the importance of obtaining the information that they would need to support their checks, with some suggesting that there would need to be some compulsion in law to make umbrella companies comply with requests to make certain information available.

3.7 Respondents also raised the importance of having a clear expectation as to how a mandatory due diligence requirement would be met. Most respondents favoured a prescriptive set of checks that would provide them with certainty.

3.8 However, others suggested that overly prescriptive guidance could create a burden for the end client or employment business, particularly smaller ones, and questioned whether mandatory due diligence on its own would be sufficient to deter fraudulent operators. The conclusion being that they could not be sure the additional time and expense was justified. There were also suggestions that adding a further layer of administration may lead to delays in supplying a worker.

3.9 Although most replies were in favour of the introduction of mandatory due diligence, some questioned its effectiveness as an option on its own. They suggested due diligence could be a first step with other measures such as debt transfer following. Others thought the impact on compliance may be limited by non-compliant umbrella companies finding ways to avoid scrutiny, or that clients and agencies already had clauses in place on supply chain liability.

Question 10: Would a mandatory due diligence requirement focused on tax non-compliance also improve outcomes for workers engaged via umbrella companies?

3.10 Respondents expressed an overall positive view, with most indicating there would, or may be, an improved outcome for workers after the introduction of mandatory due diligence.

3.11 Respondents suggested that the new requirements would provide agencies with more information about the umbrella companies that they choose to contract with. Agencies would therefore be able to provide better information to workers to ensure that they receive transparent and accurate information about their pay and deductions. This would enable workers to make better informed decisions on which companies to work with. Workers would be more likely to receive the employment rights they are entitled to, such as National Minimum Wage, holiday pay, and other statutory benefits.

3.12 It was also suggested that because of increased compliance in the umbrella company market, workers could benefit indirectly from not facing the possibility of large tax underpayments after working through a rogue umbrella company. There could also be benefits for workers in accruing a complete National Insurance record towards receiving state benefits and pension.

3.13 Some doubted that workers would benefit from mandatory due diligence because many workers already benefit from the non-compliant activities of some umbrella companies by receiving higher rates of pay than they would through legitimate umbrellas. That is, by avoiding tax, some non-compliant umbrella companies can offer higher rates of pay to their workers.

3.14 Some respondents suggested that due diligence should go beyond tax compliance and include looking at worker protection and verifying that fair and transparent payment processes are in place. This approach could ensure that both tax compliance and workers' rights are protected.

Question 11: Which parties in a labour supply chain should be required to comply with a due diligence requirement?

3.15 This question asked which single or multiple entities in the labour supply chain should be responsible for completing the due diligence checks on the umbrella company. This can be complicated by the length of some labour supply chains which can contain multiple agencies. This led to different views on which part of the chain should hold the responsibility for due diligence.

3.16 Approximately three quarters of those who replied to this question indicated the agency should in some way be responsible.

A large part of that group said the end client should also bear some level of responsibility.

3.17 The main answers given for which entity should be responsible for completing due diligence can be broken down into the following:

- both the agency and the end client
- the agency that decides to use an umbrella
- the agency at the top of the chain that has a contract with the end client
- the agency at the bottom of the chain that has a contract with the umbrella company
- the agency as part of joint and several liability throughout the chain
- the agency (no place in the chain specified)
- the end client

3.18 A narrow majority of respondents to this question thought responsibility should be shared between the agency (unspecified place in the chain) and the end client. The argument for this is that the end client directly receives the benefit from the labour provided and so they should also bear some responsibility for the compliance of their labour supply chain. It was noted that ensuring there is no tax fraud in the labour supply chain is a requirement set out in the Criminal Finances Act 2017. Passing the responsibility onto those lower down the chain can allow end clients to turn a blind eye to non-compliance by other entities and enable them to benefit while their workers suffer the consequences of being employed by a non-compliant umbrella company.

3.19 Some respondents suggested the agency, at any unspecified position in the chain, should be responsible for the due diligence checks. Reasons for this view included the agency being best placed to carry out the checks due to their having ready access to the information that may be required, and having a better understanding of how the labour supply chain interacts at each stage. Also, for agencies that already carry out due diligence, adapting existing processes to fit the new guidance should be relatively straightforward, although it was accepted that some may need to build new due diligence systems from scratch. Some responses suggested that at the point of completing checks it should be mandatory for the agency to make the end client aware that an umbrella company is involved in the labour supply chain.

3.20 A small percentage of respondents specified that the agency at the top of the chain or the agency that supplies the worker to the end client should be responsible for undertaking due diligence checks. There were concerns around the end client lacking the

expertise or visibility to carry out effective checks, although it was suggested that they should bear some responsibility for using a compliant labour supplier and not pass all of the burden to the employment business. It was also pointed out that mandating due diligence checks for anything other than the top agency in the chain would open the possibility of non-compliant umbrella companies inserting false intermediaries into the chain to circumvent the requirement.

3.21 With a longer labour supply chain, it was suggested that the agency nearest to the umbrella should complete due diligence. Some respondents who suggested this option also felt that although this may be the easiest way to avoid unnecessary additional admin, it would not ensure the integrity of the entire labour supply chain. Some respondents suggested that the agency that is in a direct contractual relationship with the umbrella company could be involved in any non-compliance and may not undertake the required due diligence checks.

3.22 Some respondents took the view that the entity that chose to engage the umbrella company should bear the responsibility for due diligence. Depending on the circumstances, this could mean that the responsibility would sit with the end-client, an agency or even the worker.

3.23 Views were also mixed from within the recruitment sector. Some suggested that all parties in the labour supply chain should be responsible, while others suggested that a particular agency would be best placed. Several respondents commented that the agency that engages directly with the umbrella company would be best placed to gather information to complete due diligence checks, although some respondents also thought that placing responsibility on the agency that supplies the worker to the client could have a greater impact on compliance.

Question 12: Which due diligence checks are most effective for identifying potential tax non-compliance in labour supply chains?

Question 13: What due diligence checks could end clients or employment businesses be reasonably expected to carry out upon umbrella companies within their labour supply chains? Which tax heads should the checks cover (e.g. employer duties, VAT, Corporation Tax, etc.)?

3.24 These questions focused on a similar theme: the types of checks needed to ensure due diligence is completed both in terms of the effectiveness of the checks and the ease of doing so for those completing them.

3.25 Many organisations that contract with umbrella companies said that they already conduct thorough due diligence checks.

These ranged from a full audit of the umbrella company, to simply relying on the accreditation of the umbrella company by an industry body without completing any specific checks themselves.

3.26 There were numerous suggestions as to what should be included in any due diligence requirement. The more frequently suggested are listed first.

- **Full audit:** incorporating some of measures listed below.
- **Industry body accreditation:** receiving an accreditation from an industry body such as the FCSA, Professional Passport or APSCo.
- **Review of Payslips:** review a percentage of payslips at set times during the year.
- **Employer Costs:** NICs, pension contributions, and statutory employer obligations.
- **Review of Contracts, Processes, and Policies:** covering compliance with employment laws, data protection, and financial reporting standards. Copies of all reviewed contracts and policies should be kept as evidence of compliance.
- **Company Information:** company registration details, director information, other relevant data to establish the legitimacy of the umbrella company.
- **Credit Check:** a credit report should be obtained and kept, establishing the financial strength of the umbrella, particularly for new companies.
- **Cross-Referencing:** with independent data or HMRC records.
- **Due Diligence Questionnaire:** questions to the umbrella company with responses.
- **Summary Report:** a final summary report outlining the due diligence process, findings, and any actions taken.

Full audit

3.27 A third of respondents said they already complete an audit on the umbrella companies they contract with. The method of audit varied between agencies but included variations of the measures suggested above.

Review of payslips

3.28 It was suggested that reviewing payslips and the calculations shown could help establish if the worker is being paid correctly. To help establish the accuracy of a worker's payslip, HMRC has recently

published a pay tool: <https://www.gov.uk/guidance/work-out-pay-from-an-umbrella-company>.⁵

3.29 Workers can use this tool to estimate what their gross and net pay should be from an umbrella company for a particular role. The tool can also be used by an agency to estimate pay for an umbrella company worker.

Quote:

Our current audit process involves a detailed check of current payslips that also must match the RTI submission. We can request this information at any point. If we do not receive the payslips in the period stipulated in our agreed terms, then the umbrella company are removed from our preferred supplier list.

~ Large agency

Industry body accreditation

3.30 Some respondents suggested that an accreditation from an industry body could be relied upon as a guarantee of due diligence being carried out on the agency or end client's behalf.

Quote:

To balance the commercial benefits and compliance costs of due diligence, consideration should be given to greater reliance on accreditation from recognised trade bodies.

~ Tax advisors.

3.31 However, some respondents suggested that third party accreditation would not be sufficient to demonstrate compliance.

⁵ Guidance – Work out pay from an umbrella company. December 2024. HM Revenue & Customs.

<https://www.gov.uk/guidance/work-out-pay-from-an-umbrella-company>

Quote:

We also do not believe that any external private sector organisation could safely act or be relied upon as a due diligence checker on behalf of employment businesses.

~ Employment business representative body.

Director checks

3.32 Some respondents suggested a requirement for checks on directors during due diligence. The purpose of these checks would be to identify those that have been, or still are, a director of a failed or non-compliant business.

Which tax heads should the checks cover?

3.33 Only a few respondents directly addressed this question. Of those who did, the most suggested checks were on VAT compliance. Some mentioned both VAT and PAYE taxes, while the remaining responses simply indicated that all taxes should be included within due diligence. The first part of question 13 asked which due diligence checks could reasonably be carried out on umbrella companies. Some of the replies to that related to payslips and a general audit. Those checks would automatically incorporate reviewing compliance with several tax heads.

Question 14: What evidence would you expect would need to be retained, and for how long, to demonstrate that a due diligence requirement has been met?

3.34 Many of the respondents who replied to this question simply said they would retain evidence to match the due diligence requirements once they had been implemented. Others said that they would keep the result of their audit, generally without going into detail of what the audit would include. Specific things mentioned include:

- Payslips (and audit)
- Tax returns
- Compliance/Due diligence questionnaire
- Fit and proper person test
- Key Information Documents
- Employment/Engagement contract

- Credit check report

3.35 Suggestions on the amount of time these documents would need to be retained varied from 1 year to indefinitely. However, to match other statutory requirements the most frequently suggested retention period was 6 years.

Question 15: How could a mandatory due diligence requirement be designed to ensure that compliance burdens remain proportionate?

3.36 Respondents offered numerous suggestions in response to this question. A theme running through around a third of them was that the guidance on due diligence checks should be set out clearly and definitively so that simple processes can be put in place by businesses to comply with them. A number of responses from agencies favoured outsourcing their due diligence responsibilities and relying on the accreditation given to umbrella companies by trade bodies.

Question 16: What would be the appropriate level of penalty to ensure that the requirement is complied with and how should it be calculated?

Question 17: What safeguards, if any, do you think would be required were a due diligence requirement to be introduced?

3.37 Suggestions for how penalties should be calculated varied. Some respondents thought it was important to have penalties that increased to reflect the level of non-compliance. This could either be based on the number of compliance failures or linked to the amount of tax lost through the non-compliant behaviour.

3.38 The suggestions for calculating penalties fell into these categories:

- Increasing penalties, potentially on a points-based system, based on the number of failures.
- Percentage of tax/NICs payable by a non-compliant umbrella company.
- Fixed penalties.
- Basing penalties on those in other regimes such as the Criminal Finances Act 2017.

3.39 Looking solely at respondents from the recruitment sector, there was no consensus on the best approach for penalties, with all the above suggestions present in their responses. Some

respondents did not think that any penalty should arise unless there was non-compliance by an umbrella company following a due diligence failure, but others were concerned that this might not become chargeable until years after the due diligence failure actually took place. Some suggested that in the first instance, the Government should not issue a penalty but should instead support businesses to improve their due diligence procedures.

3.40 One specific approach suggested was to introduce a two-tiered penalty system. First, a fixed penalty for the lack of due diligence checks could be levied even in the absence of any subsequent non-compliance. Second, further penalties linked to the value of tax avoidance/evasion. It was felt that this would ensure stricter adherence to any due diligence requirement.

Quote:

We propose a two-tiered system based on the following aspects:

- *Tier 1: Absence of Due Diligence (fixed penalty)*
- *Tier 2: Presence of Tax Avoidance/Evasion (turnover-based)*
- *A penalty system that is both gradual and based on the level of noncompliance, we can ensure that the due diligence requirement is taken seriously.*

~ Payroll auditor.

3.41 Some respondents thought that the introduction of rules similar to those in the Criminal Finances Act 2017 would provide a penalty framework for failing to mitigate non-compliant practices in the supply chain.

3.42 With regards to safeguards, respondents said that they did not think that there should be a penalty where the party responsible for undertaking due diligence could show that they had met this obligation, even if they had used an umbrella company that was later found to be non-compliant. Some respondents, particularly in the recruitment sector, noted that due diligence checks could unwittingly be based on fraudulent documents prepared by umbrella companies, and suggested that this eventuality could be specifically provided for.

Question 18: What impacts would this option have on the labour market and on the umbrella company market specifically?

Question 19: Would this measure lead users and suppliers of temporary labour to move away from the umbrella company model of engagement? If so, how would end clients and employment businesses engage workers instead?

3.43 Responses to these two questions followed a similar theme, first looking at the effect of this measure on the umbrella company market, and then the temporary labour market in general.

3.44 Almost two thirds of the respondents who answered question 18 said this measure would either increase umbrella company compliance or drive clients towards using compliant umbrellas.

3.45 A similar number of respondents also suggested this measure could reduce the use of umbrella companies, depending on what consequences are introduced for failing to meet the requirement. The main reason given for a move away from umbrella engagements would be that agencies would use their own payroll facilities to pay workers, thus removing any risk of penalties from dealing with a non-compliant umbrella company. Some also suggested it could lead to more direct hires by the end client. Some respondents said that this would ultimately improve compliance. It was suggested that some umbrella companies might become payroll bureaux if agencies were to choose to move away from this engagement model.

3.46 The remaining respondents who replied to this question did not consider that mandating due diligence on its own would affect decisions around whether to engage through an umbrella and would therefore have little or no effect on the umbrella company market. These respondents were typically those who are satisfied with their current due diligence processes, indicating that making it mandatory would make little difference to them.

3.47 Respondents in the recruitment industry generally said that any impact of mandatory due diligence on decisions as to whether to use umbrella companies would depend on the level of administrative burden placed on employment businesses by the requirement and the scale of the potential penalty for failure. It was also suggested that placing requirements on end clients would be more likely to lead to a reduction in umbrella company usage.

3.48 A small number of respondents suggested that mandatory due diligence would drive-up non-compliance by emboldening non-compliant umbrella companies to further disguise the way they operate.

Question 20: Do you have any other comments on the proposal to require a mandatory minimum level of due diligence checks upon umbrella company engagements? In particular, are there any further

risks that the Government should consider before deciding whether to take this option forward?

3.49 This question produced a wide range of comments. Some stressed the extra burdens that could be placed on businesses, while others re-iterated previous views on using industry accreditations to reduce those burdens.

3.50 Some believed the Government should undertake additional actions to oversee the umbrella company market. Suggestions included:

- Working with accreditation bodies within the industry to develop a due diligence checklist.
- Conducting the due diligence checks and providing results to the industry.
- Carrying out additional enforcement activities to back up any due diligence requirements.
- Providing extra guidance for the industry to follow.

Government response to questions 9 to 20

3.51 As set out at Autumn Budget 2024, the Government is committed to closing the tax gap and ensuring that everyone is paying the tax that they owe. This is fair, essential for a well-functioning economy, and will help to keep taxes on working people as low as possible. To support these aims and achieve the objectives set out in the consultation, there is a strong case for intervention to prevent non-compliant umbrella companies from entering labour supply chains.

3.52 Respondents were clear that an enforced penalty regime would be required to create the incentive for businesses to undertake due diligence, but there was little consensus as to how such a regime should be designed or at what level penalties should be issued.

3.53 The Government strongly supports due diligence in labour supply chains and believes that all businesses should take steps to assure themselves that their suppliers will comply with their tax obligations and treat the workers they supply fairly. However, whilst a due diligence requirement might encourage businesses to take greater accountability for the umbrella companies they contract with, the Government does not believe that such a requirement alone would be sufficient to achieve the behavioural change in the market necessary to significantly reduce the widespread non-compliance.

3.54 The Government therefore will not introduce a mandatory due diligence requirement and will instead pursue an option that

will be more effective in closing the tax gap, protecting the interests of workers, and providing a level playing field for compliant businesses.

Option 2: Transfer of tax debt that cannot be collected from an umbrella company to another party in the supply chain.

3.55 The second option included in the consultation was to legislate to give HMRC the power to collect an umbrella company tax debt from another business in the labour supply chain in certain circumstances. This would primarily apply to outstanding amounts of Income Tax and National Insurance contributions (NICs) that should have been collected via Pay As You Earn (PAYE). This would encourage employment businesses and end clients to be more selective in the umbrella companies they contract with by making them potentially liable for unpaid tax debts in the event of non-compliant behaviour by the umbrella company.

Summary of responses (questions 21 to 33)

Question 21: Do you agree that, were this option to be pursued, it would address tax non-compliance in the umbrella company market, and to what extent?

3.56 Although opinion was split, more than half of respondents thought that, to some extent, this option would reduce tax non-compliance in the umbrella company market. Generally, respondents expected that the potential for debt transfer would drive up the quality of choices made by agencies and direct them away from non-compliant operators.

3.57 Some of those who said these provisions could make a major impact in addressing non-compliance thought that the possibility of debt transfer being made to individuals such as Directors of non-compliant umbrella companies, or people of significant influence, could have a greater impact.

3.58 There were a number of reasons put forward to support the opposite view that debt transfer would not have an impact. Some respondents suggested that the type of business that would take a risk with supply chain compliance are unlikely to be dissuaded by the threat of debt transfer.

3.59 Other respondents, particularly agencies, were concerned that there could be a risk of bad actors operating non-compliant schemes in the hope their debts will be collected elsewhere and potentially being able to operate with impunity by closing and re-

establishing as a new umbrella company. Non-compliant operators attract customers by offering lower fees than a compliant business and would not care what damage they caused to other parts of the labour supply chain. Respondents suggested that it would be unfair to 'punish' those businesses that operate compliantly and transparently already with an additional risk.

3.60 Respondents from within the recruitment industry including several umbrella companies did not think that this option would completely address tax non-compliance in the umbrella company market. They suggested that larger agencies may operate payroll themselves and drive smaller competitors out of the market, although they did not elaborate on how this would impact compliance. It was also put forward that it may lead to blanket bans on the use of umbrellas which would drive workers away from compliant umbrellas and could lead to a growing market in insured indemnities.

3.61 Large accountancy bodies disagreed on the effect of debt transfer. One suggested that changes to the intermediaries legislation to introduce the risk of debt transfer to the fee payer had increased compliance. Another said that awareness of any changes would be low and therefore the impact would be limited.

Question 22: Would this option improve outcomes for workers engaged via umbrella companies?

3.62 Over 50% of respondents to this question believed outcomes for workers would be improved to some degree, though some of these responses were equivocal. The main benefit for workers identified with this approach was that it would mean that they would be less likely to have to pay tax that had not been collected from them by their umbrella companies.

3.63 Some considered that if the introduction of debt transfer led to agencies moving away from the umbrella company model of engagement, the workers would be better off due to more secure working conditions. It was suggested that workers may also benefit from a simplification in their terms of employment, particularly in the clarity of deductions made from their pay.

Question 23: In what circumstances do you think HMRC should be able to transfer an umbrella company's tax debt?

3.64 The most suggested scenario for transferring debt centred around the failure to carry out reasonable due diligence checks. As these checks could bring to light potential non-compliance, a failure to have completed them would leave the employment business open to transfer of debt resulting from the non-compliant activities of the umbrella company. Some respondents suggested

that this could be achieved by combining this option with the mandatory due diligence option, including as an additional step for the Government to take if mandatory due diligence did not have the desired effect without more significant consequences of failure being possible. A further, related suggestion was that this could include scenarios in which the agency has turned a blind eye to obvious non-compliance in their supply chain.

3.65 Several respondents said that HMRC should have to demonstrate they have exhausted all options for collecting the debt from the umbrella company before transferring it to another party in the chain.

3.66 Many of the respondents to this question suggested a reasonable care defence. This is covered in more detail below in response to question 30 on potential safeguards.

Question 24: Do you agree that the tax debt should be transferred to the employment business which supplies workers to the end client, with transfer also possible to the end client in certain circumstances?

3.67 Three quarters of the respondents in favour of a transfer of tax debt thought that an agency in the labour supply chain should be involved in some respect, either solely or jointly with other parties in the chain, particularly the end client. Half of respondents said the end client should be liable, including those who said that liability should be joint with the agency. Some said that the debt should only be transferred to the end client (in addition to the agency) if there was evidence of collusion between them and the agency or umbrella company.

3.68 It is common for labour supply chains to include multiple agencies. A number of responses indicated that the debt should be transferred to the agency without specifying which agency this would be if there were multiple agencies. Some respondents were more specific as to where the debt should be transferred. Suggestions included the agency directly below the end client or the entity that decided to use the umbrella company. Some respondents suggested the closest agency to the umbrella company. There was no clear consensus among those respondents who set out these more specific approaches.

3.69 Another view was that the debt could be transferred after it had been calculated who had benefitted from the non-compliant activities, with the debt being distributed accordingly. The debt could be split between the parties further up the chain if appropriate.

3.70 Although it was not proposed in the consultation, around 20% of respondents said the debt should be transferred to the directors of the umbrella company and their associates. These

individuals would be deemed to be personally liable in the event of deliberate non-compliance. HMRC already has powers to transfer liabilities to company directors in certain circumstances. It was not clear from responses whether the suggestion was that these powers should be expanded, or that respondents were unaware of their existence.

Question 25: What processes would employment businesses and end clients use to identify tax risks within their labour supply chains?

3.71 The most prevalent responses revolved around due diligence and how it was carried out. Respondents gave insight as to what these processes might look like in relation to question 13 above and again in question 28 below. Around a third of respondents said their current due diligence processes would be enough for them to identify tax risks. Around a fifth of respondents said they would base their approach around the Government's guidance on due diligence. A similar number said they would prefer to have a third party complete their checks for them.

Question 26: Do you agree that this option should apply to employment taxes as set out above? Which other taxes could, or should it apply to?

3.72 Most respondents suggested that the debt transfer should only apply to employment taxes, however a significant minority thought that VAT should also be included. Some suggested VAT should not be included as input tax relief can already be denied by HMRC in circumstances where the Kittel principle can be applied.

Question 27: How should the Government define the engagements to which this option would apply?

3.73 There was a low response rate to this question. Of those that did respond, the majority view was that this option should apply to all umbrella company engagements. Some respondents suggested that HMRC should use the same definition of 'umbrella company' as is ultimately used for rights purposes (see previous Chapter).

Question 28: What steps should businesses using umbrella companies take to assure themselves that they are engaging with a compliant umbrella company? How could the Government support businesses to minimise the impact of these actions?

3.74 This is a similar question to question 25, based on what procedures can be used to check the compliance history of an umbrella company through which an agency or end client is

engaging workers. The most common suggestion was for HMRC to set out guidance for due diligence and businesses to follow this. It was also put forward that standardising due diligence checks across the supply chain would make them easier to comply with.

3.75 There were several specific responses as to the support that the Government could offer:

- **Clear Guidelines:** on what constitutes a compliant umbrella company, making it easier for businesses to conduct due diligence.
- **Certification Programs:** support for or endorsement of third-party certification programs that meet Government standards for compliance.
- **Online Registry:** create an online registry of compliant umbrella companies that have met Government or endorsed third-party standards.
- **Educational Resources:** provide resources and workshops to educate businesses.
- **Legal Support:** offer templates or examples of contract clauses that can be used to ensure compliance.
- **Financial Incentives:** offer tax incentives or grants to businesses that engage with certified compliant umbrella companies, thereby encouraging best practices.

3.76 Some also linked this with a due diligence checklist from industry accreditation bodies, while others felt that an accreditation from an industry body would be sufficient.

Question 29: Would businesses stop using umbrella companies as a result of the introduction of a transfer of debt? How many businesses would do this and what wider impacts would there be?

3.77 There was a large response to this question with over half who responded saying that if debt transfer was introduced, businesses would stop using umbrella companies. Adding the number of respondents who thought business *may* stop using umbrella companies, that figure rose to almost nine out of ten. Some suggested that the shift in the market would result in the engagement and payment of the workers being handled by other providers and other models that could introduce unforeseen new risks to the Exchequer. The anticipated response was that there could be a shift to the use of agency payrolls or direct employment by the end client. Smaller agencies raised concerns about the administration costs if they brought workers onto payroll rather than using umbrella companies.

3.78 The number of responses that indicated a move away from umbrella companies rose even further when counting those who had a mixed view. These respondents suggested that the factors that would influence any change would include reliance on umbrella companies for payroll expertise, shortage of labour from other avenues and the difficulty of complying with any new rules.

Question 30: What safeguards, if any, do you think should be included if this option is taken forward?

3.79 By far the most suggested safeguard was that a transfer should not be possible where reasonable due diligence had been completed and evidence of doing so could be demonstrated. There were also some suggestions that the transfer should only apply to those who act in concert with a non-compliant operator rather than just engage with them. It was suggested that limiting the power in this way would act to prevent a large-scale move by businesses away from using the umbrella company model.

3.80 Others mentioned that clear Government guidelines on the debt transfer would be essential, including:

- **Clear Criteria:** establish a timescale for the transfer of debt to occur, with adequate notice given.
- **Appeal Mechanism:** an appeal process should be established.
- **Shared Liability:** where multiple parties are involved.

3.81 A further safeguard suggested was having a phased introduction of the measure, for example introducing a due diligence requirement one year and then the possibility of debt transfer a year later.

Question 31: Would this option change behaviour of businesses using umbrella companies in the way that the Government expects?

3.82 There was no consensus in the replies to this question with respondents roughly divided by their position in the market. Those who agreed that it would have the effect the Government intends, such as tax experts and unions, were satisfied that the possibility of a debt transfer would lead to businesses that use umbrella companies improving their due diligence checks leading to improvements in compliance as intended.

3.83 More than half of respondents were unsure of the potential outcome. Some thought that the introduction of debt transfer provisions would act as intended to some extent but could embolden rogue umbrella companies to increase non-compliance knowing that their tax debt would be transferred to the agency or end client. Others thought that the success of the measure

depended on the ease of its implementation and subsequent enforcement.

3.84 Less than 30% of respondents disagreed that the measure would work as expected, which were mainly umbrella companies or their representative bodies, citing a general move away from umbrella company use if it was introduced. They argued that this could affect compliant operators and have a negative effect on overall compliance and the amount of tax collected on behalf of the Exchequer by umbrella companies.

3.85 Several respondents, including some umbrella companies, were open minded, indicating that the success of this option would depend on the clarity of the guidance which accompanied it.

Question 32: How likely is it that the temporary labour market would move away from using umbrella companies entirely, were this option taken forward?

3.86 Similar to question 29, approximately 70% of respondents thought it was likely or very likely that there would be a move away from the use of umbrella companies. Some likened the situation to the introduction of the off-payroll working reforms in 2021 and the reported increase in using the umbrella company model over personal service companies. Some respondents suggested that while it was unclear what could ultimately replace the umbrella company model, this could lead to a move back towards the use of agency payroll and direct employment, which they did not see as a negative outcome. However, there was a concern that if the market moved away from using umbrella companies, and employment businesses moved to using their own payroll, there could be a negative impact on the smaller agencies who may not have the resources to run their own payroll.

3.87 There was a small percentage of replies that thought a move away from umbrellas was unlikely. They said that agencies may be satisfied with their current due diligence procedures and if the new due diligence was manageable, it would override the threat of debt transfer.

Question 33: Are there any further risks that the Government should consider before deciding whether to take this option forward?

3.88 This broad question attracted many different responses, although a third of respondents thought that the possible risks had been captured through the earlier questions in this section.

3.89 However, this question did generate a number of suggestions that respondents had not made previously, including:

- **Smaller agency failure:** larger agencies would have the resources for inhouse payroll provisions, leaving smaller agencies vulnerable due to increased costs.
- **End client and agency failure:** tight margins in sectors such as transport could leave agencies and clients at risk without umbrellas. Debt transfer is also difficult to quantify as a contingent liability risk.
- **Penalties on innocent parties:** there is a danger that this legislation would disproportionately affect the “compliant” operators in the market and “favour” non-compliant operators who have a more aggressive attitude to risk and a disrespect for the law. Unless there is a personal risk for the directors/shareholders of a non-compliant company, the efforts to improve compliance would not be successful. As noted earlier in response to question 24, HMRC do already have some powers to transfer liabilities to company directors in certain circumstances.
- **Lack of Government resource:** HMRC and businesses would need enforcement and compliance resource. The focus on umbrellas could direct the market towards other engagement models that are equally susceptible to non-compliance. This could simply shift the problem rather than solve it.

Government response to questions 21-33

3.90 Respondents generally favoured this option less than mandatory due diligence. Some respondents suggested that introducing this option would not be effective as it could embolden umbrella companies to be non-compliant, on the basis that this approach would lead to any tax they owed being transferred to another party in the labour supply chain. In practice, HMRC would continue to act against umbrella companies for their non-compliant behaviour in the first instance and would only consider transferring the tax debt if it became clear that collecting it from the umbrella company was highly unlikely.

3.91 There was also an argument that threat of debt transfer simply would not register on an umbrella company that was non-compliant. It would not influence their behaviour and have no effect on overall compliance. The objective of this approach, however, was to change behaviour among businesses that use umbrella companies and incentivise them to take steps to prevent non-compliant umbrella companies from entering their supply chains.

3.92 Many respondents, particularly agencies, had concerns about acquiring debt that they considered they had taken every possible step to guard against. There was a strong view that if this option

were to be taken forward, there should be protection for businesses that could show that they had undertaken due diligence checks into the non-compliant umbrella company. This approach would make this option analogous with option 1, with the prospect of debt transfer where HMRC is unable to collect outstanding liabilities from a non-compliant umbrella company effectively replacing a penalty regime for failing to undertake due diligence.

3.93 Respondents strongly favoured incorporating due diligence as a defence against a transfer of tax debt from a non-compliant umbrella company. Although debt transfer may be a stronger incentive than the penalties considered for option 1, the Government believes that this approach would not drive the requisite behavioural change to significantly reduce the widespread non-compliance in the market. The inclusion of due diligence as a factor in this option would also increase complexity and could lead to more uncertainty for business as to their exposure to tax risk.

3.94 The Government also considers that this option could create a protracted and complicated process both for businesses and HMRC in which the transfer of a tax debt could only be carried out after an umbrella company had been proven to be non-compliant. This could lead to the debt transfer happening a long time after the non-compliant behaviour had taken place and result in a great deal of uncertainty being introduced for the agency. This could be exacerbated by including a defence where due diligence could be shown, as this may need to be demonstrated several years after the checks had actually taken place, not only extending the length of time before a case could be resolved but also leaving any inadequate due diligence processes unchallenged.

Option 3: Deeming the employment business which supplies the worker to the end client to be the employer for tax purposes where the worker is employed by an umbrella company, moving the responsibility to operate PAYE.

3.95 The third and final option in this chapter was to place the responsibilities of the employer for tax purposes with the agency that supplies the worker to the end client, removing these legal responsibilities from the umbrella company. This would not prevent an agency from engaging an umbrella company to operate payroll on their behalf but would mean that the agency would be legally responsible for the tax shortfall if the umbrella company failed to make the correct deductions.

3.96 At Autumn Budget 2024, the Government announced that it would take forward a version of this option as part of its package to

close the tax gap. More details about this measure can be found here:

<https://www.gov.uk/government/publications/tackling-tax-non-compliance-umbrella-company-market/tackling-non-compliance-in-the-umbrella-company-market--3>.⁶

3.97 Questions for this option explored how it would work in practice, the impact it would have on non-compliance in the umbrella company market and the potential for wider labour market impacts, such as agencies choosing to stop using the umbrella company model when supplying labour.

Summary of responses (questions 34 to 41)

Question 34: Do you agree that, were this option to be pursued, it would address tax non-compliance in the umbrella company market, and to what extent?

3.98 Responses to this question were split between three viewpoints (though the third is compatible with either of the other two answers):

- It would address non-compliance;
- It would not address non-compliance; or
- It would lead to umbrella companies leaving the market.

3.99 The most popular of the three views was that this option would address non-compliance. Some respondents thought that the most likely response from an agency would be to bring the payroll function in house. If they still used an umbrella company to pay workers, they would only allow the umbrella company access to a worker's net pay, minus tax and NICs. This would prevent the operation of payroll fraud and under-deduction of employee's taxes by non-compliant umbrella companies. As set out in the consultation, if the worker's full gross pay was paid to the umbrella company and it did not correctly account for PAYE, then the agency as the entity with ultimate responsibility for the operation for PAYE would be liable.

3.100 Although many respondents thought that being responsible for operating PAYE would mean that the employment business would have to take payroll in house, the policy also allows employment businesses to continue using umbrella companies. The policy intention is that because the employment business holds

⁶ Policy Paper – Tackling non-compliance in the umbrella company market. October 2024. HM Revenue & Customs. <https://www.gov.uk/government/publications/tackling-tax-non-compliance-umbrella-company-market/tackling-non-compliance-in-the-umbrella-company-market--3>

responsibility for PAYE operation, they would only use highly trusted umbrella companies with which they already contract or have completed stringent due diligence checks on.

3.101 The respondents that did not think this measure would improve compliance, a majority of which were umbrella companies, referred to a loss of expertise held by umbrella companies in running payroll and the amount of tax that is currently collected for the Exchequer. The suggestion was that if agencies were to be required to administer payrolls, they would be more likely to make mistakes than umbrella companies and any non-compliance would be more difficult to detect, whether deliberate or accidental.

3.102 There were also concerns that it would encourage non-compliance by encouraging businesses to use models such as 'joint employment', which, it was suggested, would lead to a loss of VAT revenue. These models already exist but some claimed they may proliferate if this option were pursued.

3.103 Another view was that deeming the employment business to be the employer for tax purposes would likely result in a contraction of the umbrella company market. This view was particularly prevalent among umbrella companies themselves. By removing one of the main benefits (for the agency) of engaging through an umbrella, some thought that many would leave the market or adapt to become payroll bureaux.

3.104 If this were the case, the proposed loss of expertise in the market would not occur due to the repurposing of some businesses which currently operate as umbrella companies. This is reinforced by the suggestion that the market would simply adapt by coming up with a new model which may make use of the expertise available. It should be noted that umbrella companies are a relatively recent addition to the supply chain and historically employment businesses would have run their own payroll.

3.105 Other respondents said that it would address non-compliance by umbrella companies by simply removing those non-compliant umbrellas from the market. However, there were also concerns that the non-compliance may just shift to the agency that engaged with that umbrella company. This could be the case, for example, if the agency and umbrella company were controlled by the same individuals.

Question 35: Were this option to be taken forward, which entity in the labour supply chain would be best placed to be the deemed employer, and why?

3.106 There were fewer responses to this question than some of the others in this section that considered the detailed design of this option.

3.107 The most suggested response was that the agency would be the appropriate party to be the deemed employer. As with question 24, many respondents did not specify which agency this should be if there were more than one in the labour supply chain.

3.108 Some respondents suggested that the agency that contracts with the umbrella company would be best placed to act as deemed employer. Reasons advanced for this included the close relationship between these two parties and that this would align with the approach taken for the reformed off-payroll working rules.

3.109 Another option put forward was the agency or 'master service provider' immediately below the end client should be the deemed employer. The reason given being that that this entity will be unlikely to face cashflow issues and would also be likely to dictate to lower entities in the chain which umbrella company would be used.

3.110 There was some support for the responsibility falling to the end client as this would ensure a clear line of responsibility and incentivise compliance throughout the supply chain. Another suggestion was that the responsibility could fall to the agency in the first instance with the end client as a back-up in the event of the agency also being non-compliant.

Question 36: How would businesses manage their obligations as deemed employers following this change? What could the Government do to support them with these new obligations?

3.111 Around 40% of those who commented on how businesses would manage their responsibilities suggested the best option would be to either use their own payroll or outsource it to a payroll bureau to account for the employment tax before paying the worker's net pay to the umbrella company. Respondents in the recruitment industry suggested that employment businesses might lack the capability to take workers onto their own payrolls due to a lack of expertise and the additional cost. It was also pointed out that end clients may decide to change the agencies they contract with to avoid those that have had dealings with non-compliant umbrella companies.

3.112 In terms of what the Government could do to support businesses, the main demand from respondents was guidance to help employment businesses with their obligations. Some replies stated that the changes would not be difficult to implement as most medium to large agencies have at least some internal payroll systems. The ones who do not would probably be the smaller agencies, meaning any new guidance would need to be aimed at them to be most effective.

3.113 There were other suggestions on how the Government could help. These included giving tax relief to employment businesses to improve their payroll systems, and mandating umbrella companies to provide information to the employment business.

Question 37: Would businesses stop using umbrella companies as a result of this change? How many businesses would do this and what wider impacts would there be?

3.114 There was a large response to this question with a majority of responses indicating that there would be a move away from the use of umbrella companies if this were taken forward. A minority of these thought that businesses would start using an outsourced payroll. Around three quarters of respondents thought that this option would remove a key incentive to use an umbrella company and could lead to a contraction of the umbrella company market. A number of respondents, including both umbrella companies and employment businesses, commented that it could have a disproportionate effect on smaller employment businesses due to their current lack of payroll resource. It was suggested that this could have the effect of pushing these smaller players out of the market, allowing larger businesses that are better equipped to offer a payroll function to become more dominant in the market.

3.115 According to some responses, if the market was to move towards employment businesses operating their own payroll, it could affect enforcement within the market. These respondents suggested that non-compliance would simply move to another party in the labour supply chain if this measure were implemented. It was put forward that monitoring the sector and enforcing any new rules would be much more difficult if workers were employed by a large number of employment businesses rather than a smaller number of umbrella companies.

Question 38: How would the temporary labour market respond to this option being taken forward?

3.116 Similarly to the previous question, the majority of respondents thought the temporary labour market would react to the implementation of this option by reducing the use of umbrella companies. Many respondents either raised the same points here or simply pointed to their responses to the previous question. It was also suggested that the reaction of the temporary labour market would be led by the preferences of end clients who may find new ways to outsource their employer responsibilities.

3.117 One respondent suggested that from a worker's perspective it would be a positive, as the responsibility for administering PAYE would move to a regulated business. Similarly for the end client,

reputational risk would be reduced, and due diligence made easier.

Question 39: Would this option improve outcomes for workers engaged via umbrella companies?

3.118 Respondents who said that this measure would benefit workers generally did so quite strongly, mainly citing the increased security workers would have around issues related to their net pay, and income tax deductions such as:

- **Compliant PAYE and NICs payments:** greater peace of mind regarding income tax and NICs being properly accounted for.
- **Reduced risk of selecting a non-compliant umbrella:** workers protected from the promotion of disguised remuneration 'loan' schemes.
- **Clear, accurate pay:** one step less in the pay chain would reduce the deductions made from the assignment rate and help workers understand their payslips which would also lower the risk of payroll skimming.
- **Simplified supply chains with fewer intermediaries:** moving to agency payrolls could give workers greater certainty about where to turn to with problems.

3.119 Respondents that argued that this approach would not improve outcomes for workers put forward several different reasons. Some thought that taking forward this option would lead to confusion for workers as they would be dealing with one employer for tax purposes and a second employer for rights purposes. It was suggested that this could lead to complexity for workers looking to assert their employment rights. This is at odds with the view above which suggested that fewer links in the labour chain would simplify things for workers.

3.120 Other respondents considered the potential impacts if this measure resulted in businesses moving away from the umbrella company model. They suggested that fewer umbrella companies in the market could lead to workers losing the opportunity of continuity of employment that is often put forward as the main advantage of working through an umbrella company. This in turn would mean that the worker would be unable to make pension contributions to the same provider and could lose access to certain employment rights that require a minimum period of service and other benefits such as being able to show a continuous employment record when applying for finance.

3.121 It was also suggested that a move away from using umbrella companies would reduce choice for workers in how they are engaged.

Question 40: Are there any further risks that the Government should consider before deciding whether to take this option forward?

3.122 Respondents identified a number of issues in response to this question, some of which have been touched upon in the replies to other questions:

- **Disguised umbrella companies:** ensure that umbrellas do not simply start employment businesses to get around the new rules.
- **Non-compliance would move to agencies:** non-compliance issues would still occur, albeit within employment businesses, or whatever intermediary subsequently evolves to replace umbrella companies.
- **Disruption to the market:** this could skew the existing market, possibly to the disadvantage of workers.
- **Undermine the umbrella market:** putting the jobs of people working in or supporting the umbrella market at risk.
- **Increased costs:** enhancements to agency payroll systems would be costly, which could add to the cost of hiring temporary labour.

Question 41: Are there any other options that have not been covered in this chapter that you think could reduce non-compliance in the umbrella company market?

3.123 This question was intended to ensure all suggestions which may not fit into previous categories could be considered. This attracted a large variety of comments, some only suggested by single respondents.

3.124 Some common themes that ran through responses included:

- Increased action taken against directors of non-compliant umbrella companies.
- Government registration and/or assurance of umbrella companies.
- Preventative measures to stop umbrella companies being set up as companies in the first place.
- Banning umbrella companies.

Government response to questions 34 to 41

3.125 Although the consultation produced conflicting opinions on this option, the largest group of respondents thought this option would increase compliance. Taking on board the responses received, the Government believes that this option would do the most to address tax non-compliance in the umbrella company market, improving outcomes for workers and protecting the Exchequer.

3.126 As announced at Autumn Budget 2024, the Government therefore intends to introduce legislation to move the responsibility for accounting for PAYE from the umbrella company to the agency that contracts with the end client to supply the worker's services. In the event that there is no such agency in a labour supply chain, which is expected to be a minority of cases, this responsibility will be placed on the end client. The measure will take effect from April 2026. The Government will consult on draft legislation this year, ahead of introducing legislation to Parliament.

3.127 The Government recognises that concerns have been raised about the impact this measure could have on the sector and is grateful to those who raised them in response to the consultation. These concerns largely focused on the changes that businesses might make to how they engage labour, particularly the possible reduction in contracting with umbrella companies. Not all respondents thought that these changes to the way labour is engaged would represent a bad outcome. Some thought that they would improve compliance.

3.128 Whilst many umbrella companies operate diligently, supporting their employees and providing convenience and administrative benefits for agencies, too many are used to facilitate non-compliance including tax avoidance and tax fraud. HMRC analysis shows that umbrella companies were used to engage at least 700,000 workers in 2022-23. This analysis also shows that at least 275,000 of these workers, and likely significantly more, were engaged at some point in 2022-23 by umbrella companies that failed to comply with their tax obligations. This incurs significant losses for taxpayers and can leave workers with unexpected tax bills. In addition to causing significant harm to workers and taxpayers, non-compliant umbrella companies undercut compliant firms, threatening the viability of those businesses that do the right thing, as well as the functioning of the market itself. The Government believes that this measure is a proportionate response to the scale of the problem faced. It is forecast to raise £500m in 2029-30.

3.129 Some respondents raised concerns that the payroll expertise of umbrella companies would be lost if this option were to be taken forward. However, this option will not prevent businesses from

engaging other entities to operate payroll on their behalf in the same way that other employers are able to. What this option does is ensure that while businesses can continue to outsource the operation of payroll to umbrella companies (or other, similar entities), they will no longer be able to outsource the underlying obligation and will be ultimately responsible if the umbrella company operating payroll on their behalf fails to do so correctly. It is the Government's expectation that those businesses that choose to continue to outsource payroll operation to umbrella companies will take steps to ensure that these obligations will be properly discharged on their behalf.

3.130 In many ways, this option brings the tax position for umbrella company workers into line with other agency workers. Since 2014, the legislation at Chapter 7, Part 2 of the Income Tax (Earnings and Pensions) Act 2003 has placed employment responsibilities for agency workers with the agency that supplies the worker to the end client. These rules do not apply where an umbrella company is used to employ the worker and as such are circumvented by the umbrella company model. This has been cited as a reason for the growth of the umbrella company model. By placing employment obligations for tax purposes with the same agency when an umbrella company is used, this option ensures that the approach to taxation is consistent across these two engagement models.

3.131 Some respondents argued that this option would simply shift the non-compliance from umbrella companies to other entities in the supply chain such as employment agencies. The Government expects that placing the PAYE obligations on the employment agency that supplies the worker to the end client should help mitigate this risk. It is expected that these client-facing businesses are the least likely to be structured, and able to behave, in ways designed to frustrate HMRC's compliance activity. HMRC will continue to monitor the temporary labour market and take strong action against those who fail to meet their tax obligations. If necessary, the Government will consider further strategic policy options to crack down on tax non-compliance in the temporary labour market.

3.132 The Government is grateful to respondents for their views on the potential impacts that this option could have for workers. Respondents pointed out that were this option to be introduced, workers who continue to be employed by umbrella companies could have different employers for tax and rights purposes, leaving them facing additional complexity in their engagements. The Government will update its guidance for workers employed by umbrella companies to make clear what these changes mean for them.

3.133 Some respondents also focused on the benefits, such as a continuous employment record, that workers could lose out on if

they are moved from umbrella company employment to some other form of engagement. However, views from workers in relation both to this consultation and the previous Call for Evidence indicated that many people do not find that they receive these benefits in practice due to regularly having to change umbrella company when they start a new engagement. It is not clear therefore that other forms of engagement would provide for less continuity of employment. The Government's Employment Rights Bill also provides for workers to have basic rights from their first day in a new job.

Chapter 4

Targeted options to address tax non-compliance

Introduction

4.1 This chapter invited respondents' views on targeted options to address the abuse of specific tax reliefs by some umbrella companies. Changes designed to prevent this abuse could be taken forward in conjunction with the strategic options in Chapter 4 of the consultation.

4.2 The VAT flat rate scheme and the Employment Allowance have both been targeted by so-called mini umbrella companies who abuse both schemes to benefit from lower levels of VAT and employer NICs.

VAT flat rate scheme

4.3 The VAT flat rate scheme is a simplification measure designed to reduce the administrative burdens of VAT compliance for small businesses. The scheme relies on self-assessment of eligibility which makes it easier for umbrella-style companies to abuse. These companies are known to disaggregate into smaller entities (also known as mini umbrella companies) to meet the eligibility requirements of the scheme. They exploit the lower flat VAT rates available, often by relying on incorrect trade classifications.

4.4 The consultation invited views on how further action could be taken to combat abuse of the flat rate scheme. It set out that introducing further measures into the scheme would add complexity to VAT simplification and it noted that the limited costs trader test added a further calculation for users to carry out.

4.5 The consultation also sought views on the extent to which the VAT flat rate scheme continued to offer administrative simplifications in light of the introduction of Making Tax Digital (MTD) in 2019, which introduced simplifications for record keeping and automation of calculation processes.

Question 42: What more could HMRC do to prevent abuse of the scheme? Are there any specific options that you believe the Government should consider?

4.6 Twenty-nine respondents commented on this question. Many respondents suggested that the VAT flat rate scheme is largely used for financial benefit rather than for simplification, which is its intended purpose. Just under half of respondents suggested that the scheme be removed to prevent abuse while some suggested replacing it with a new scheme that reflected modern accounting practices.

4.7 A few respondents didn't think the compliance measures suggested in the consultation paper would tackle abuse of the VAT flat rate scheme. It was suggested the cash benefit the scheme provides is too much of an incentive for abuse and it would be likely that any compliance measures adopted by HMRC will be circumvented.

4.8 There were several suggestions of what HMRC could do to prevent abuse such as using legislation to introduce tougher consequences for fraudulent use of the scheme and using data analytics to identify and remove abusive entities. There were also suggestions around allocating more compliance activity to enforcement and using technology to screen VAT flat rate scheme applications with ongoing monitoring of businesses. However, it was acknowledged this would require more resources.

4.9 One respondent suggested that HMRC should avoid diluting or abolishing the scheme and instead use current legislative powers to remove and punish users who abuse it.

Question 43: What benefits does the scheme currently provide when compared to other accounting simplification measures (e.g., the annual accounting or cash accounting schemes) and, in particular, what additional (if any) benefits are there to those enabled by Making Tax Digital (MTD)?

4.10 Many respondents did not have a comment for this question and stated that they do not use the scheme themselves. Those that did respond acknowledged that the VAT flat rate scheme was abused by umbrella companies.

4.11 When comparing the scheme to other accounting simplification measures, some respondents said the VAT flat rate scheme was the only option that offered businesses simplification of their VAT accounting obligations. Some stated that the scheme provided different benefits to making tax digital such as reducing accounting errors and time spent calculating VAT liabilities. Other benefits cited were reducing the need to engage with and

understand complex VAT rules and helping businesses to budget by using a flat rate of VAT. A few respondents said that the VAT flat rate scheme and making tax digital deliver different policy objectives and that making tax digital did not act as a replacement for the VAT flat rate scheme. One reason given was the 1% reduction in the first year of VAT registration which the VAT flat rate scheme provides. Another respondent said that making tax digital and the VAT flat rate scheme complemented each other through digital efficiency and accounting simplification.

4.12 Others held the view that making tax digital, and the advancement of accounting technologies, had reduced the benefits and the need for the scheme. A few stated that the scheme should be scrapped or reformed, whereas some argued that the scheme was still beneficial for small businesses and should not be changed without prior consultation to impact the effects on legitimate users. One respondent suggested that the VAT flat rate scheme would benefit from introducing the same director eligibility requirements proposed for the Employment Allowance.

Question 44: What effect, if any, has the 'limited cost' test had on your VAT accounting obligations?

4.13 There were not many responses to this question. Those that did respond said that the limited cost test was largely ignored by some businesses, including umbrella companies and there was anecdotal evidence of businesses circumventing the rules to avoid using the limited costs rate of 16.5%.

4.14 Some respondents said that the limited cost rate had reduced the financial benefits of the VAT flat rate scheme, and the test could adversely affect some businesses. One respondent said the test had added complexities to VAT accounting and increased administrative burdens for businesses. Other drawbacks reported were the scope for increased errors and anxiety for businesses whose costs hover around the level of a limited cost business. A few respondents said that the introduction of the limited cost test had made businesses re-evaluate their VAT accounting practices, and it was suggested that this was the cause for the reduction in the VAT flat rate scheme's population in recent years.

Question 45: Do you have any other thoughts you would like to share on the VAT flat rate scheme?

4.15 There were few responses to this question. Some suggested removing the scheme would be the only way to prevent abuse by umbrella companies. Some called for a review of the scheme to ensure it still achieves its purpose of simplification and to find ways

to prevent abuse without introducing complexities for legitimate businesses.

4.16 It was suggested that the scheme be integrated with making tax digital software to make compliance with VAT rules easier. Other suggestions included a review of the flat rates as they currently cover broad trade sectors, improving guidance to help businesses understand if they would be eligible to join the scheme, introducing flexible eligibility criteria to help businesses who are suffering from temporary financial struggles, and providing a separate flat rate just for umbrella companies.

Employment Allowance

4.17 The Employment Allowance is a NICs relief targeted at smaller employers. It reduces eligible secondary Class 1 NICs (employer NICs) liabilities by up to £5,000 each tax year and is available where an employer had employer NICs liabilities of less than £100,000 in the previous tax year. At Autumn Budget 2024, the Government announced that it would increase the Employment Allowance from £5,000 to £10,500 and remove the £100,000 threshold, expanding this to all eligible employers. These changes will take effect from 6 April 2025.

4.18 Similar to the VAT flat rate scheme, the Employment Allowance is simple to use and relies on self-assessment of eligibility making it easier for umbrella-style companies to abuse.

4.19 Some umbrella companies fraudulently exploit the Employment Allowance by splitting businesses into multiple smaller companies (mini umbrella companies) and ensuring the company's employer NICs liabilities for the year are covered by the relief meaning no employer NICs is paid. They typically have a UK-based director when they claim the Employment Allowance, before that director resigns and a new offshore director is put in place, to make it more difficult for HMRC to recover any VAT or NICs lost through fraud.

4.20 Legislation already exists to prevent abuse of the Employment Allowance rules, including the connected companies rules and anti-avoidance provisions, and HMRC takes compliance action to address fraud by businesses abusing these rules. However, the rules do not currently provide adequate protection against the type of abuse by mini umbrella companies. The consultation included a proposed legislative change which would require a UK resident director to be in place in order for a company to be eligible to claim the Employment Allowance and asked for views on this proposal.

Question 46: Do stakeholders agree, that if this option were implemented, it would help address abuse of the Employment Allowance?

4.21 There were 27 responses to this question. Two thirds of the respondents agreed that this would be a good way to address the abuse of the Employment Allowance.

4.22 Some of the respondents felt that whilst this was good idea, further measures would be needed to fully tackle the abuse. Suggestions included ensuring a person with significant control is in place, requiring directors to be members of relevant trade bodies for umbrella companies, and requiring mini umbrella companies to be incorporated.

4.23 There was also concern from several respondents that this rule would create a risk of vulnerable UK residents being used as directors.

4.24 Of the respondents who did not agree this change would help, the main concerns were that it simply wouldn't work as fraudsters would find a work around, and that businesses who have a legitimate reason for a non-UK director would be adversely affected.

4.25 There were also some concerns as to how this would be implemented, checked, and enforced by HMRC, and the time and cost associated with this.

Question 47: Are there any ways in which mini umbrella companies could sidestep these changes, and if so, how could this proposal be strengthened to reduce or prevent this risk?

4.26 Many respondents were concerned that this change could be sidestepped by the mini umbrella companies using a nominal UK based director who, in reality, has no direct involvement with the company. This could also exploit vulnerable British residents. Using a UK address also does not necessarily mean the person is UK resident. Respondents also highlighted that this could also result in companies being set up with false names of people who do not exist, or an increase in identity fraud.

4.27 Many felt the proposal could be strengthened by ensuring there is also a UK-based person of significant control, in addition to having a UK based director.

4.28 There were also several suggestions put forward to cross check information against HMRC systems such as checking the Unique Tax Reference (UTR) numbers of directors to ensure they are genuine, residency checks, and checking if individuals have a high number of directorships.

4.29 Another risk area highlighted was that the mini umbrella companies may simply make false declarations and confirm they meet the criteria for an Employment Allowance claim when they do not. Suggestions to overcome this included proper scrutiny of companies claiming the Employment Allowance, making the requirements clear and publicising what enforcement procedures will be, and introducing a check when the claim is made, rather than being self-determined.

Question 48: For limited companies, how would your business be impacted if eligibility requirements were brought in that required your business to have at least one UK director in order to claim or continue claiming the Employment Allowance?

4.30 All but one of the respondents confirmed this change would have little to no impact on their business. One respondent advised non-UK nationals wishing to operate in the UK could be adversely affected.

Question 49: Would there be any barriers to appointing a UK director for those legitimate businesses who do not currently have one in place but who are eligible to claim the Employment Allowance?

4.31 Most respondents felt there would not be any barriers for legitimate compliant businesses.

4.32 Some advised that while possible, it may not be practical from a commercial perspective, and would bring administrative costs, and require operational changes.

Question 50: Are there any wider benefits, impacts or risks involved with this proposal that have not been identified above?

4.33 Aside from what had already been mentioned regarding the risks of new tactics such as companies using nominal UK-based directors and the unintended exclusion of some legitimate businesses who have non-UK directors, respondents also highlighted that the resource allocation to implement and monitor the new requirement could be significant.

4.34 It was also noted that many double taxation treaties the UK has with other countries contain a non-discrimination article that prevents the UK or the other country who is party to the treaty to place non-residents at a disadvantage. Further consideration would need to be given as to whether this may impact any new rule.

4.35 Benefits of the new rule were identified as increased transparency and enhanced accountability, as a UK director would

be more easily reachable, and improved/more stable working conditions for people employed by mini umbrella companies.

Question 51: Do stakeholders consider it would be beneficial to amend payroll software to make explicit that a UK director is required at the point of claiming the Employment Allowance?

4.36 There were 18 responses to this question, and they were evenly split. Half of the respondents agreed that this would be beneficial and serve as a reminder to aid compliance in general. It could also give HMRC more leverage in the case of investigation. However, many recognised that it would not deter those who are determined to commit fraud.

4.37 From the other half of the respondents, the majority of them felt that given the wide range of payroll software products that are available, with many configured to meet clients' needs, any decision to mandate such a change would not be welcomed and could be criticised as overstepping HMRC's remit to mandate such information. They also recognised that a change to software would not deter a fraudster, with one respondent advising that the change would be costly and unnecessary.

Question 52: Aside from the proposed option and wider options discussed throughout this consultation, what more could HMRC do to reduce the abuse of Employment Allowance?

4.38 Six of the 13 respondents suggested that HMRC consider making Employment Allowance claims retrospective following a full year of accounts/submissions.

4.39 Several respondents put forward that HMRC could undertake enhanced vetting, such as real time monitoring, proper scrutiny of claimants, and monthly checks before the Employment Allowance is claimed.

4.40 One respondent suggested that changing the rules for Employment Allowance will not have an effect without addressing the VAT flat rate scheme.

4.41 Another suggested a wider review of Employment Allowance as it is currently too simple to claim. Another questioned if the Employment Allowance remains the most appropriate way to help small businesses.

Government response to questions 42 to 52

4.42 The Government is grateful for the views that were shared about changes that could be made to the VAT flat rate scheme and

Employment Allowance to make it more difficult for non-compliant umbrella companies to abuse them.

4.43 As set out in the previous chapter, the Government announced at Autumn Budget 2024 that it will introduce legislation to move the responsibility for accounting for PAYE from the umbrella company to the agency that contracts with the end client to supply the worker's services. In the event that there is no such agency in a labour supply chain, which is expected to be a minority of cases, this responsibility will be placed on the end client. As a result of this change, the Government expects that businesses that continue to use umbrella companies will take steps to prevent non-compliant umbrella companies from entering their supply chains, including those non-compliant umbrella companies that abuse the VAT flat rate scheme and Employment Allowance.

4.44 As a result of this anticipated impact, the Government is not taking forward targeted options to address abuse of the VAT flat rate scheme or Employment Allowance at this time. The Government will continue to monitor abuse in this sector and will consider whether further action is required in future.

Annexes

List of consultation respondents

Only organisations that provided written responses are listed below. In addition to the responses from these organisations, the government also received seven responses from individual workers.

Acacium Group

ADVANCE

Agency payroll

The Advisory, Conciliation and Arbitration Service

The Association of Professional Staffing Companies

Artemis Contractor Supply Chain Management Limited

Association of Labour Providers

Association of Recruitment Consultancies

BDO Ltd

Brit European

Brookson Group

Carrington Group

Caroola Accountancy

The Chartered Institute of Taxation

The Chartered Institute of Payroll Professionals

Clarity Umbrella Ltd

Clipper Contracting Group

Contractor Calculator

Construction Industry Joint Taxation Committee

Danbro

Deloitte

Driver Hire

Freelance & Contractor Services Association (FCSA)

Giant Group
Grant Thornton
Hays
The Institute of Chartered Accountants in England and Wales
The Association of Independent Professionals and the Self-Employed
Inspiring Teaching Ltd and CareJoy Healthcare Ltd
Investigo
JobsAware
KPMG
Director of Labour Market Enforcement
The Law Place
Low Incomes Tax Reform Group
Liquid Friday
Loan Charge Action Group (LCAG)
Loan Charge & Taxpayer Fairness All-Party Parliamentary Group
Markel Tax
Machtech Group (UK) Ltd
Maxipay Accounting Services
Moore Kingston Smith LLP
Morson International
My Digital Accounts
National Association of Schoolmasters Union of Women Teachers (NASUWT)
National Education Union
Ocado Group
Odgers Interim & Odgers Connect
Orca Pay Group
PayePass
People Group Services Ltd
Professional Passport
National Union of Rail Maritime and Transport Workers
Randstad UK
Recruitment & Employment Confederation (REC)
Re Legal Consulting

RSM UK
Rullion
SafeRec Group Ltd
Federation of Small Businesses
SThree Partnership
TaxAid
Tax Centre of Excellence
Tax Policy Associates
Trades Union Congress: TUC
Unite the Union
WTT Group

Overview of policy options and consultation questions

Regulating umbrella companies for employment rights

Chapter 3 set out the options the previous Government considered to address employment rights issues within the umbrella company market such as pay, or holiday pay, being withheld.

Unlike employment agencies, which are regulated under the Employment Agencies Act 1973 and the associated Conduct of Employment Agencies and Employment Businesses Regulations 2003, umbrella companies are generally unregulated, unless their other activities bring them within the scope of the current regulations that apply to employment agencies and employment businesses. The Government first committed to regulating umbrella companies following the Good Work Plan in 2018, reaffirming this in its Call for Evidence in 2021.

To enable regulation to be introduced, umbrella companies must first be defined in law. The consultation proposed two possible approaches to defining umbrella companies. Both options would enable the Government to be precise about the businesses to be brought in scope and ensure subsequent regulations or standards crystallise on the right business at the right point in the supply chain.

Considerations for the previous Government in this area included what aspects of the umbrella companies' involvement in the supply chain should be covered and how any new standards would be enforced.

Option 1: Defining umbrella companies and limiting acceptable engagement structures.

Option 2: Defining umbrella companies by applying three tests.

- **Question 1:** Which of the options would be the most effective way to define umbrella companies to ensure only they are brought in scope now and ensure future regulations/standards can be targeted to the right business in the supply chain? Please explain your answer.

- **Question 2:** Which of the definitions would be the most future proof? Please explain your answer.
- **Question 3:** Are there any unintended consequences of either option and/or are there alternative ways of defining umbrella companies the Government should consider? Please explain your answer.
- **Question 4:** What aspects of the umbrella company's role in the supply chain should the regulations cover?
- **Question 5:** Is there a rationale for starting with limited regulations and reviewing them before potentially expanding them to cover other areas of umbrella company involvement? Please explain your answer and illustrate with examples.
- **Question 6:** Are there reasons that the Employment Agency Standards Inspectorate should not enforce umbrella company regulations? And if so, are there other bodies or approaches the Government should consider? Please explain your answer.
- **Question 7:** Does the Employment Agency Standards Inspectorate have sufficient enforcement powers to regulate umbrella companies or would changes need to be made? Please explain your answer.
- **Question 8:** Should EAS mirror its current enforcement approach for employment agencies and employment businesses if it enforces umbrella company requirements? Please explain your answer.

Tackling tax non-compliance in the contingent labour market

Chapter 4 outlined strategic options for preventing tax non-compliance within the umbrella company market by changing the incentives and behaviours in the temporary labour market. It invited respondents to share their views on how these options could be further developed and what their impacts could be on reducing non-compliance, on individual businesses and on the wider labour market.

Option 1: Mandating due diligence.

The first of these options is the introduction of a mandatory due diligence requirement, with penalties applying to those employment businesses or end clients that do not comply. This requirement could sit with the employment business or the end client depending on the specific arrangements of the contract. The Government would support

businesses by providing guidance setting out due diligence principles and how compliance can be demonstrated.

- **Question 9:** Do you agree that a requirement to undertake due diligence upon any umbrella companies which form part of a labour supply chain would reduce tax non-compliance in the umbrella company market, and to what extent?
- **Question 10:** Would a mandatory due diligence requirement focused on tax non-compliance also improve outcomes for workers engaged via umbrella companies?
- **Question 11:** Which parties in a labour supply chain should be required to comply with a due diligence requirement?
- **Question 12:** Which due diligence checks are most effective for identifying potential tax non-compliance in labour supply chains?
- **Question 13:** What due diligence checks could end clients or employment businesses be reasonably expected to carry out upon umbrella companies within their labour supply chains? Which tax heads should the checks cover (e.g. employer duties, VAT, Corporation Tax, etc.)?
- **Question 14:** What evidence would you expect would need to be retained, and for how long, to demonstrate that a due diligence requirement has been met?
- **Question 15:** How could a mandatory due diligence requirement be designed to ensure that compliance burdens remain proportionate?
- **Question 16:** What would be the appropriate level of penalty to ensure that the requirement is complied with and how should it be calculated?
- **Question 17:** What safeguards, if any, do you think would be required were a due diligence requirement to be introduced?
- **Question 18:** What impacts would this option have on the labour market and on the umbrella company market specifically?
- **Question 19:** Would this measure lead users and suppliers of temporary labour to move away from the umbrella company model of engagement? If so, how would end clients and employment businesses engage workers instead?
- **Question 20:** Do you have any other comments on the proposal to require a mandatory minimum level of due diligence checks upon umbrella company engagements? In particular, are there

any further risks that the Government should consider before deciding whether to take this option forward?

Option 2: Transfer of tax debt that cannot be collected from an umbrella company to another party in the supply chain.

The second option is to legislate to give HMRC the power to collect an umbrella company tax debt from another business in the labour supply chain, in specified circumstances. This would primarily apply to outstanding amounts of Income Tax and National Insurance contributions (NICs) that should have been collected via PAYE. This would encourage employment businesses and end clients to be more selective in the umbrella companies they contract with by making them potentially liable for unpaid tax debts in the event of non-compliant behaviour by the umbrella company.

- **Question 21:** Do you agree that, were this option to be pursued, it would address tax non-compliance in the umbrella company market, and to what extent?
- **Question 22:** Would this option improve outcomes for workers engaged via umbrella companies?
- **Question 23:** In what circumstances do you think HMRC should be able to transfer an umbrella company's tax debt?
- **Question 24:** Do you agree that the tax debt should be transferred to the employment business which supplies workers to the end client, with transfer also possible to the end client in certain circumstances?
- **Question 25:** What processes would employment businesses and end clients use to identify tax risks within their labour supply chains?
- **Question 26:** Do you agree that this option should apply to employment taxes as set out above? Which other taxes could, or should it apply to?
- **Question 27:** How should the Government define the engagements to which this option would apply?
- **Question 28:** What steps should businesses using umbrella companies take to assure themselves that they are engaging with a compliant umbrella company? How could the Government support businesses to minimise the impact of these actions?
- **Question 29:** Would businesses stop using umbrella companies as a result of the introduction of a transfer of debt? How many

businesses would do this and what wider impacts would there be?

- **Question 30:** What safeguards, if any, do you think should be included if this option is taken forward?
- **Question 31:** Would this option change behaviour of businesses using umbrella companies in the way that the Government expects?
- **Question 32:** How likely is it that the temporary labour market would move away from using umbrella companies entirely, were this option taken forward?
- **Question 33:** Are there any further risks that the Government should consider before deciding whether to take this option forward?

Option 3: Deeming the employment business which supplies the worker to the end client to be the employer for tax purposes where the worker is employed by an umbrella company, moving the responsibility to operate PAYE.

The third option would deem the employment business that supplies the worker to the end client to be the employer for tax purposes. This option would require a party further up the labour supply chain to operate PAYE on payments to contingent workers. This would not prevent the deemed employer from using a payroll bureau or umbrella company to discharge their PAYE obligations, but the deemed employer would be ultimately responsible for ensuring the correct operation of PAYE.

- **Question 34:** Do you agree that, were this option to be pursued, it would address tax non-compliance in the umbrella company market, and to what extent?
- **Question 35:** Were this option to be taken forward, which entity in the labour supply chain would be best placed to be the deemed employer, and why?
- **Question 36:** How would businesses manage their obligations as deemed employers following this change? What could the Government do to support them with these new obligations?
- **Question 37:** Would businesses stop using umbrella companies as a result of this change? How many businesses would do this and what wider impacts would there be?

- **Question 38:** How would the temporary labour market respond to this option being taken forward?
- **Question 39:** Would this option improve outcomes for workers engaged via umbrella companies?
- **Question 40:** Are there any further risks that the Government should consider before deciding whether to take this option forward?
- **Question 41:** Are there any other options that have not been covered in this chapter that you think could reduce non-compliance in the umbrella company market?

Targeted options to address tax non-compliance

This chapter examined two specific reliefs that are subject to abuse and invited views on options to reduce fraud.

The Employment Allowance and VAT flat rate scheme are both targeted by fraudulent umbrella companies that abuse both schemes to benefit from lower levels of employer NICs and VAT. The Employment Allowance is exploited by umbrella companies that artificially disaggregate to ensure the company's employer NICs liabilities for the year are covered by the £5,000 allowance meaning no employer NICs is paid. The same entities defraud the VAT flat rate scheme to exploit the different VAT rates available. HMRC has deregistered tens of thousands of umbrella companies who it believed were involved in abusing either or both the VAT flat rate scheme and Employment Allowance.

The consultation sought views on the benefits of the flat rate scheme and what the Government could do to prevent its abuse. It also set out a proposal to mandate a UK director to be in place for a company to be eligible for the Employment Allowance.

- **Question 42:** What more could HMRC do to prevent abuse of the scheme? Are there any specific options that you believe the Government should consider?
- **Question 43:** What benefits does the scheme currently provide when compared to other accounting simplification measures (e.g. the annual accounting or cash accounting schemes) and, in particular, what additional (if any) benefits are there to those enabled by Making Tax Digital for VAT?
- **Question 44:** What effect, if any, has the 'limited cost' test had on your VAT accounting obligations?

- **Question 45:** Do you have any other thoughts you would like to share on the VAT flat rate scheme?
- **Question 46:** Do stakeholders agree, that if this option were implemented, it would help address abuse of the Employment Allowance?
- **Question 47:** Are there any ways in which mini umbrella companies could sidestep these changes, and if so, how could this proposal be strengthened to reduce or prevent this risk?
- **Question 48:** For limited companies, how would your business be impacted if eligibility requirements were brought in that required your business to have at least one UK director in order to claim or continue claiming the Employment Allowance?
- **Question 49:** Would there be any barriers to appointing a UK director for those legitimate businesses who do not currently have one in place but who are eligible to claim the Employment Allowance?
- **Question 50:** Are there any wider benefits, impacts or risks involved with this proposal that have not been identified above?
- **Question 51:** Do stakeholders consider it would be beneficial to amend payroll software to make explicit that a UK director is required at the point of claiming the Employment Allowance?
- **Question 52:** Aside from the proposed option and wider options discussed throughout this consultation, what more could HMRC do to reduce the abuse of Employment Allowance?

Terminology

The following is an explanation of some of the terms that are used in this Summary of Responses.

Disguised remuneration (DR) – contrived arrangements that pay people amounts that are purported to be non-taxable in place of a salary. These amounts are often described as a loan, annuity, or other payment that is said to be non-taxable. These supposedly ‘non-taxable’ payments are no different to normal earnings and are, and always have been, taxable.

Employment agency - a business which finds permanent roles for work-seekers with an employer or supplies employers with work-seekers. For the precise definition, see the Employment Agencies Act 1973, section 13(2).

Employment business – a business which finds temporary or contract roles for work-seekers and supplies them to work for, and under the control of, the end client. The provision of work-finding services (defined in regulation 2 of the Conduct Regulations) is a distinguishing feature of an employment business. For the precise definition, see the Employment Agencies Act 1973, section 13(3). For tax purposes, such as the agency legislation, these are typically known just as agencies.

Employment intermediary – any person who makes arrangements for an individual to work for a third party or pay for work done for a third party. Employment businesses, employment agencies and umbrella companies are types of employment intermediary.

End client – the party who receives the services of the person supplied to carry out the work.

Key Information Document (KID) – the document which employment businesses must provide to work-seekers when they sign up with them and before any work-finding services can commence. It should set out pay-related information for the work-seeker.

Mini umbrella company (MUC) – a small umbrella company, typically only employing a few workers, set up to commit tax fraud.

Personal Service Company (PSC) – a limited company through which a contractor provides their services. Typically, the contractor is a significant or the only shareholder.

Umbrella company – a business which employs a worker with a view to that worker being supplied to work for, and under the control of, the

end-client. There is no statutory definition of an umbrella company for employment rights or tax purposes.

Umbrella company employee – a work-seeker who is employed by an umbrella company in order to complete work for an end client.

Worker – a person supplied to carry out work, typically used in this document to refer to someone seeking temporary work, often through an employment intermediary (sometimes also referred to as a contractor). Please note that this term does not refer in this context to the technical meaning of the employment status ‘worker’ or ‘limb (b) worker’ for the purpose of assigning employment rights as set out in section 230(3) of the Employment Rights Act 1996.

Work-seeker – for employment law purposes, this refers to the person to whom an employment agency or employment business provides (or holds itself out as capable of providing) work-finding services.