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**FALSE SELF-EMPLOYMENT IN CONSTRUCTION: TAXATION OF WORKERS  
HOMES FOR SCOTLAND RESPONSE TO HM TREASURY  
OCTOBER 2009**

**Introduction**

Homes for Scotland is the representative body of the Scottish homebuilding industry, with over 200 full and associate members. Its members build around 95% of all new homes for sale built each year, as well as a significant proportion of the affordable housing output annually. Homes for Scotland makes policy submissions on National and Local Government policy issues affecting the industry, and its views are endorsed by the relevant local committees and technical advisory groups consisting of key representatives drawn from within our members.

Homes for Scotland welcomes the opportunity to respond formally to this consultation, which follows on directly from the wide ranging engagement and contributions provided by Homes for Scotland to the "Construction Employment Forum", Chaired by Val Hennelly, as established by HM Treasury and HMRC (which met on three occasions during mid 2008). Much of the material and issues raised in this response are consistent with and reinforce the industry viewpoints which we outlined during those initial meetings, held during August and September last year.

**The need for new regulation**

Before responding to the particular questions posed, we must point out that we are disappointed that new regulation is proposed without demonstration of the need for change. Insufficient evidence is given within the consultation to convince the reader that the construction industry deserves to be the sole target of additional tests on validity of self-employment.

Homes for Scotland members comply with the CIS system in place. If it is believed that the current CIS system is not working effectively then our members would suggest the most effective solution would be application of additional resources to ensure the existing system is policed accordingly. This, we would hope, will result in the targeting of the few that may well abuse the system, rather than placing additional burden on an legitimate and conscientious industry where the overwhelming majority comply.

Furthermore, given that the tests for employment status in the construction industry are the same for other sectors, with application of the same case law, we question the ability of the Treasury/HMRC to lawfully introduce further systems that ensure construction is treated differently.

## **The solution being proposed**

### **Question 1: do these criteria represent fair indicators of a person who is running his own business and is therefore genuinely self-employed?**

The criteria outlined in the consultation document are legitimate, but do lead to considerable ambiguity and additional risk if they form the sole defining criteria.

#### The provision of plant and equipment

It is not clear how this criteria will be assessed where plant and equipment is not required in order to perform the work? There are many instances where the normal 'tools of the trade' would suffice. On that note it would also be helpful to have a clear definition of "normal" tools of the trade given that these differ significantly between trades.

There are also many instances where the home builder would insist that tools provided are used. This stipulation would essentially be to keep control of health & safety on-site, where the home builder's own tools have been tested as safe to use e.g. lifting gear. The health & safety implications of home builders losing control through the requirement of sub-contractors to provide their own equipment is enough to show flaws in this proposed criteria.

#### The provision of all materials

From a commercial point of view it is not sensible to suggest that a sub-contractor provide all materials required to complete a job. The test would run counter to the industry supply chain management, where materials are generally purchased in volume to ensure competitive pricing. Arrangements made with suppliers also suit the fluidity of the industry, with home builders requiring the ability to 'call off' orders as and when the supplies are required.

From a legal point of view, the choice of material is generally set by the Local Authority as part of the planning and building warrant consent process. To ensure compliance, control over product supply is best left with the home builder.

#### **Example/scenario 1**

Timber frame kits have been ordered by the home builder 6 months in advance to ensure compliance with current building standards and to suit the agreed footprint of the home. The kits were bulk purchased from the same supplier to ensure best value and consistent quality, and are being 'called off' from the supplier when the home builder is ready to start the next home.

With a view to controlling safety, the home builder normally insists that the scaffolding, lifting equipment and safety equipment etc already on site is used for the job.

Two individual self-employed workers are sub-contracted to erect the timber frame kit, or complete the roofing of the new structure for a fixed price, they each work for themselves. They are likely to be on site for not more than 5 days, and have agreed to return in 6 weeks when the home builder is ready to start on the next plot.

By the criteria proposed here these individuals would be deemed employed, yet this is obviously not the case when normal established means of determining employment status are considered.

Given that the materials and equipment are provided by the home builder, and that each of the sub-contractors work on their own without providing additional labour all 3 test would be failed and both workers would need to be classified as 'employed' by the home builder for the entire duration of the work.

Ensuring compliance with the Trades Description Act and providing good customer service also means ensuring what is sold and selected by the customer is delivered in the end result. To ensure control over this the home builder will want to make early arrangements with suppliers, calling in orders at a time that suits.

Turning back to Health & Safety obligations, the quality of the materials and the safe storage of those materials must be left in the control of the home builder. For all of these reasons the 'materials supply' criteria presents significant issues if applied in isolation.

#### The provision of other workers

There will be many occasions where it is unnecessary for the worker to provide other labour because the job only requires one person with the requisite skill set.

#### **Example/scenario 2**

A bathroom tiler or kitchen fitter is contracted to complete 5 homes over a 5 day period, he requires only his normal 'tools of the trade', is using materials supplied by the home builder (as chosen by the customer) and works alone given the scale of the job and the space to work within the bathrooms. Under the criteria proposed the tiler would fail all 3 tests and would be deemed to be false self-employed, resulting in him having to be classified as 'employed' by the home builder, despite the fact that the job is complete in under 5 days.

#### **Question 2: Are there other indicators which ought to be considered?**

If a test is introduced, Homes for Scotland would be supportive of the following indicators:

Acceptance of risk – that a person is taking on an element of risk by accepting a price for a job rather than receiving a daily rate, i.e. home builder agrees to pay a fixed price of £2000 for the fitting of 4 kitchens, the job is expected to take 5 days but in the end takes 8 days, no further payment is made in respect of the additional time on the job.

Provision of a specialist skill – that a person offers a specialist skill, i.e. specialist abilities that are limited or of low availability amongst the general labour market.

Engagement in more than one contract - The analysis HMRC provide of CIS payments show that 24% of sub-contractors receive less than £5k per annum and a further 51% receive between £5k and £25k. This points towards a situation where a high proportion

of supposedly 'false self-employed' subcontractors clearly must have other employment. The consultation seems to ignore the multiplicity of engagements such individuals are likely to have in order to earn a sufficient income.

Length of contract – a time period should be introduced into the criteria so that a person cumulatively contracted by the same organisation for (say) less than 3 months in any single tax year is exempt from the tests. The nature of the length of engagement should be capable of speaking for itself in an industry which is inherently cyclical.

Inclusion of the final two tests would offer a simple approach capturing those single individuals working solely for one builder for long durations, those who arguably should be classed as employed and obliged to pay PAYE and NICs

**Question 3: Are there instances where none of the criteria are met, but a worker would, by reference to the usual case law tests in respect of a true terms of an engagement, otherwise be treated as self-employment? If so, please provide examples.**

See scenarios 1 and 2, noted above.

**Question 4: VAT registration can signal that the worker is in business on his own account, buying materials and investing in plant which takes the turnover of the business over the threshold for registration. Would it be helpful to include the criteria of VAT registration, which would need to be met in addition to one of the three other criteria?**

Given our comments above identifying flaws in the test criteria for provision of plant and materials, having a VAT criteria being met 'in addition' to one of the other three may not be an appropriate approach. However adding this criteria simply as one of the suite of things which would provide exemption would be appropriate.

**Question 5: Is the payer the correct person to have the responsibility for applying the criteria and applying PAYE and NICs?**

The payer may not always be the correct person to have responsibility for applying the criteria as the 'Payer' could be different from the organisation setting the contractual terms i.e. HR/Payroll Department Vs Surveyor/Site manager within home builders.

### **The impact this will have**

The house building industry has been at the forefront of the dramatic impact of the credit crunch with a national reduction in sales to about half of its previously normalized trend levels. Huge jobs and skills losses have been incurred as a result.

National targets set by Scottish government (35,000 new homes per year by the middle of the next decade) are not likely to be realised for a considerable period of time. Indeed Homes for Scotland has predicted that to return to previous trend levels (25,000 per year) could even take until 2025 (at 5% compound growth /year). This will be predicated on a return to more freely available mortgage finance, but crucially, isn't likely to be subject to the kind of year on year double digit house price inflation trends that have characterised the last sixteen years.

Average house prices, especially those related to new build homes, have been significantly falling throughout the past eighteen months and whilst early signs of stability in the market are now appearing the industry is by no means in full recovery mode yet. Therefore for the foreseeable future the industry's focus will simply be on re-growing baseline supply, and meeting consumers' expressed core needs, in a trading environment where affordability (in its widest sense) is significantly constrained.

The consultation describes a situation where it is claimed that false self-employment is estimated to cost the Exchequer £350m per annum. Without accepting this claim, it is our responsibility to make HMRC aware of the financial situation in the house building industry at this time. If this were the true scale of this problem then the practical response is that it is simply not possible for the industry to absorb any additional costs of such magnitude at present and the Government must bear this in mind when assessing the overall level of impact on tax take that the proposed changes will have.

**Question 6: Are there instances where the introduction of the deeming provision could bring about a significant additional burden? If so, please give examples.**

The proposed changes would add significantly to the direct and indirect costs of home builders. Clearly the NICs employer Class 1a payments would be an additional burden on the sector as supply chain costs increase.

Deeming operatives to be employees for tax purposes will inevitably lead to demands for additional benefits currently reserved for employees. The costs of sick pay, holidays, maternity and paternity leave, pension contributions etc will all surely follow and have major cost burdens for the industry. It is difficult to envisage a situation where worker's pay is subject to PAYE and NIC due to deemed employment status but they are not entitled to other equivalent employment benefits and rights e.g. jobs seekers allowance and redundancy benefit. This creates confusion within the industry.

The changes would also add greatly to the administrative requirements, requiring additional costly resources. Applying the criteria will be particularly time consuming and cumbersome for home builders who typically engage workers for a short period of time. The proposed changes could also result in instances where a worker needs to be treated as an employee for one engagement and CIS for another, a home builder could therefore have CIS reporting requirements and PAYE deductions for the same worker in the same year on different projects.

**Question 7: Are there occasions when the deeming provision could impact on the adaptability and flexibility of the labour market? If so, please provide examples.**

The home building sector is highly cyclical and requires a supply of self-employed operatives in order to quickly turn on and turn off as the market economy determines. The proposed changes would risk the creation of a 'hire and fire culture' because the industry cannot sustain employment through ups and downs. Labour market flexibility is a key feature of the industry and the flexibility must not be allowed to suffer through the introduction of these proposed changes.

The consultation outlines a relationship between false self-employment and problems relating to long term job security and career opportunities for workers. There is no detail

to support the assertion that the proposed changes could resolve or improve these problems or that they were the in fact a causal effect in the first place.

There is a serious danger that the changes could force genuine self-employed sub-contractors out of the legitimate industry if their net income is reduced by changes. Furthermore it could result in an increase in the 'black economy', where workers are paid cash in hand by domestic home owners or unregistered gang masters, to avoid the administration of the regulatory regime.

**Question 8: What avoidance routes might be available and how should these be countered?**

We do not support the proposal and have no comment to add here; other than those noted above in relation to overall impact.