



Construction Industry Scheme

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Introduction

The Construction Industry Scheme (CIS) is designed to ensure that subcontractors in the building industry do not avoid paying income tax.

Unless the subcontractor is registered by HMRC, the contractor must deduct an amount of income tax and pay it to HMRC. The subcontractor is required to submit self-assessment tax returns in the normal way, but is credited with the tax deducted by the contractor.

CIS only applies to individuals who are self-employed. If a construction company employs people, they will be taxed under PAYE on a normal payroll. In 2009, HMRC raised the issue of “false employment” in the construction industry where workers were taxed under CIS instead of PAYE. It should be noted that whether a worker is employed or self-employed depends on the facts of the working relationship; it is not a matter of choice.

The tax collected from subcontractors is paid monthly to HMRC. The contractor must keep records, and notify HMRC of changes to its business.

Unlike PAYE, CIS does not attempt to collect the correct amount of tax, so paying tax under CIS is not excuse for a subcontractor not completing a tax return.

CIS was first introduced in 1972 to counter a practice known as “the lump” where tax evasion was rife and building site safety standards were compromised. The scheme has been amended several times since in 1977, 1980, 1992, 1999 and the current system introduced in 2007.

The scheme covers all parts of the UK, including Northern Ireland and British territorial waters.

Contractor

The contractor is the person who is responsible for the construction work.

There are two types of contractor. A **mainstream contractor** is someone who is in the construction business. A **deemed contractor** is someone who is not in the construction business but who has spent an average £1 million on construction work over three years. Deemed contractors can include local authorities, government departments and housing associations.

A contractor can be a sole trader, partnership, company or other type of entity. The organisation does not have to be a commercial one. A local authority or public body can be a contractor, though there is a list of excepted public bodies.

A householder having work done on his or her own property is not a contractor. There are also some exceptions for charities, trusts and schools.

CIS does not apply to small contracts where the value of the work (excluding materials) does not exceed £1,000. There are also some exceptions for work on agricultural property.

Subcontractor

A subcontractor is any person who undertakes construction work for a contractor. This includes a gang leader and a foreign business operating in the UK.

A contractor can be a sole trader, partnership, company or any other form of legal entity.

For tax purposes, a subcontractor is construed widely. It includes employees of the subcontractor and any sub-subcontractor.

The rules apply to all contractor and subcontractors working in the UK, even if they are based outside the UK.

Construction work

Construction includes:

- demolition and dismantling anything on site
- preparing the site, such as digging foundations
- building work
- alterations, repairs and decoration
- installing heating, lighting, power, water and ventilation
- cleaning the inside of the building after construction work.

Construction does not include:

- architecture and surveying
- scaffolding hire without labour
- carpet fitting
- delivery of materials
- non-construction facilities on site, such as an office or canteen
- signwriting, murals, sculpture and gardening
- delivery of materials.

Registration

A contractor must be registered with HMRC before engaging a subcontractor. A contractor need not register if they do not use sub-contracted labour. Registration is done online from GOV website.

Each subcontractor should also register with HMRC but may work before being registered.

A subcontractor is registered for either gross or net payments.

A registered contractor may engage any subcontractor, including one who has not yet registered with HMRC.

Payments to subcontractors

The contractor pays the subcontractor in accordance with the contractual arrangements agreed between them.

A contractor must check with HMRC whether the subcontractor is registered, and whether any registration is for gross or net payment. This is now done by using HMRC's free CIS online service or by using commercial software.

The subcontractor must provide him or her

The payment for the subcontractor is made:

- with no tax deducted, if the subcontractor is registered for gross payments
- with 20% tax deducted, if the subcontractor is registered but not for gross payments
- with 30% tax deducted, if the subcontractor is not registered.

Tax is deducted for payment for the subcontractor's labour. The taxable amount therefore excludes charges for materials, plant hire, fuel (other than for travelling), Construction Industry Training Board levy and VAT.

Registration by subcontractor

The subcontractor registers with HMRC by providing such details as HMRC may require. HMRC may refuse to register a subcontractor and may cancel an extant registration.

A subcontractor has 30 days from such a decision to appeal to a tribunal. Otherwise a registration is indefinite.

Many contractors will only engage subcontractors who have gross certificates. A loss of gross payment certificate can have the effect of making the worker almost unemployable.

Registration for gross payment

To be registered for gross payment, the subcontractor must satisfy three sets of tests:

- business test
- turnover test
- compliance test.

The **business test** is to demonstrate that the subcontractor is engaged in construction work, has a bank account, and keeps proper accounting records.

The **turnover test** is that the subcontractor earns at least £30,000 a year from construction work. For a partnership or company, that figure is multiplied by the number of partners or directors. Alternatively the partnership or company must earn £200,000 a year from construction work.

The **compliance test** means that the subcontractor has in the previous 12 months submitted all tax returns and paid all tax due. It is not sufficient that a subcontractor is bringing his or her tax affairs up to date when applying for registration. It is also a condition that HMRC reasonably believes that the subcontractor will keep his or her affairs in order in the future.

There are some exceptions to the compliance test for minor breaches or where there was reasonable excuse.

Companies must also be up to date in submitting their annual returns to Companies House.

Paying subcontractors

The contractor must check in advance whether a subcontractor is registered and, if so, whether that is for gross or net payments. This must be done for a new subcontractor or where the contractor has not included that subcontractor on a return in the current tax year or either of the previous two tax years.

The subcontractor must provide him or her national insurance number, name or company name, UTR tax reference and (if a partnership) trading name of the partnership and the nominated partner.

Once a contractor has checked on a subcontractor, that check remains valid for two years or until HMRC notifies the contractor of a change. If a subcontractor's position changes, HMRC notifies all contractors who have used that subcontractor in the previous two years.

The subcontractor is paid directly or through a third party, as the contractor and subcontractor agree. If a tax deduction has been made, the contractor must provide a payment and deduction statement within 14 days of the end of each tax month. Tax months end on 5th of each calendar month.

Paying HMRC

The contractor must pay the tax collected under CIS to the HMRC Accounts Office by the 22nd of the tax month in which the amount was deducted. This date is 19th if payment is not made electronically. The payment is made against the return form CIS300 which may be posted or sent electronically. There are penalties for making mistakes or being late.

CIS payments are separate from PAYE and self-assessment payments that the contractor may be making.

If a contractor reasonably believes that the monthly total of CIS payments, PAYE payments, national insurance and student loan repayments will not exceed £1,500 a month, the contractor may make payment quarterly instead of monthly.

HMRC may raise an assessment if the contractor does not submit a return. The contractor may also be liable to interest and penalties.

A contractor who knows that he or she will not be engaging subcontractors in the next six months may notify HMRC of that fact. Otherwise, a contractor must make a nil return for any month where no tax was deducted under CIS.

There is no annual return form required by HMRC from the contractor.

The contractor and subcontractors are all required to keep proper accounting and tax records.

The subcontractor may offset tax deducted under CIS against other tax liabilities. The scope of such offset for companies differs from that for sole traders and partnerships.