

CAMBRIDGE CITY COUNCIL

REPORT OF: Head of HR

TO: Civic Affairs Committee

19/9/2013

WARDS: All

CONSIDERATION OF MEASURES TO DISCOURAGE TAX AVOIDANCE

1 INTRODUCTION

- 1.1 At the Civic Affairs Committee meeting on 30 January 2013, when considering the proposed Pay Policy Statement for 2013/14, which contains a section on Tax Avoidance, the Committee asked for a further report back to Civic Affairs to consider measures to discourage tax avoidance arising from the employment of consultants through companies. This report outlines proposals for consideration.

2. RECOMMENDATIONS

- 2.1 Civic Affairs Committee approve that the Director of Resources, Head of Legal Services, Support Services Manager and Head of HR develop contract clauses and guidance for use by Cambridge City Council managers when employing consultants through companies, in line with the suggested models and guidance set out in this report.

3. BACKGROUND

- 3.1 At the Civic Affairs Committee meeting on 30 January 2013, when considering the proposed Pay Policy Statement for 2013/14, which contains a section on Tax Avoidance, the Committee asked for a further report back to Civic Affairs to consider measures to discourage tax avoidance arising from the employment of consultants through companies.

- 3.2 The wording on Tax Avoidance currently set out in the Council's Pay Policy Statement 2013/14, approved by Council in February 2013 states:

Tax Avoidance

The Council takes tax avoidance seriously and will seek to appoint individuals to vacant positions using the recruitment procedures on the basis of contracts of employment and apply direct tax and National Insurance deductions from pay through the operation of PAYE.

Where consultants are recruited the Council will seek to avoid contractual arrangements which could be perceived as being primarily designed to reduce significantly the rate of tax paid by that person, such as paying the individual through a company effectively, controlled by him or her.

- 3.3 Having obtained advice on what measures the Council could consider to discourage tax avoidance, please see Appendices A and B, the following proposals are made:

- a) When using agency workers where there is a Personal Service Company (PSC) and the person does not pay PAYE/NIC via the agency, the Council could use procedures similar to those adopted by Government Departments and the NHS.

An example of these is set out in Appendix B.

- b) When using interim managers, not employed by the Council but engaged under a contract for services, the Council could verify the tax arrangements and include clauses in the contracts to enable termination of the contract if the information obtained is not satisfactory to demonstrate the person is complying with their tax and NIC obligations.

Suggested model contractual provisions are set out in Appendix B.

- c) When using a consultant for specialist advice the Council could develop and use steps and contract clauses similar to those set out in the example contained in Appendix B.

3.4 Appendix A sets out some background information on this issue.

3.5 Appendix B contains a Procurement Policy Note on Tax Arrangements of Public Appointees, produced by HM Treasury, for use by Government Departments. The guidance note particularly refers to arrangements lasting more than six months and costing over £220 per day.

4.0. **CONSULTATIONS**

4.1 The Head of Legal Services, Director of Resources and Support Services Manager have been consulted on this report.

5.0 **CONCLUSIONS**

5.1 It is proposed that the Director of Resources, Head of Legal Services, Support Services Manager and Head of HR develop contract clauses and guidance for use by Cambridge City Council managers when employing consultants through companies, in line with the suggested models and guidance attached as Appendix B.

6.0 **IMPLICATIONS**

(a) **Financial Implications**

The measures set out in this report are considerations to manage risk and thereby reduce potential financial implications for the Council.

(b) **Staffing Implications**

The staffing implications arising from this report are officer time engaged in developing procedures. There is the potential that a consultant may choose not to work with the Council if checks are requested or the Council may choose not to work with a consultant if the information provided is not deemed satisfactory.

(c) **Equal Opportunities Implications**

An equality impact assessment has not been prepared for this item.

(d) **Environmental Implications**

None

(e) **Procurement**

The procurement considerations relate to the engagement of consultants and further steps which could be put in place.

(f) **Consultation and communication**

This report relates to the engaged of consultants.

(g) **Community Safety**

There are no community safety considerations in this report.

BACKGROUND PAPERS: The following are the background papers that were used in the preparation of this report:

- The Council's Pay Policy Statement 2013/14
- Minutes of Civic Affairs Committee – 30 January 2013
- Advice note on tax arrangements, the appendices are attached to this report.
- Procurement Policy Note – Tax Arrangements of Public Appointees, Action Note 07/12.

To inspect these documents contact Deborah Simpson, Head of HR on 01223 458101.

The author and contact officer for queries on the report is Deborah Simpson, Head of HR on 01223 458101.

Report file:

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Background Information

IR35

The intermediaries' legislation, known as "IR35", was introduced by the Government in 2000 in an attempt to discourage and deter the use of intermediaries or Personal Service Companies ("PSC").

These are the companies set up for the primary purpose of reducing tax, and National Insurance Contributions, for an individual who would otherwise be employed by the organisation, where the individual supplies their services through an intermediary (usually a PSC) and is paid in dividends.

The IR35 legislation shifted the responsibility of ensuring compliance from the employer back to the PSC. Since then there have been announcements about proposed changes to IR35 and measures targeted in the public sector, particularly for Government Departments, to seek assurance that highly paid individuals who are not on the payroll, are meeting their tax obligations, sufficient to prevent the loss of tax/NICs through disguised employment.

Reasons for using a limited company

- The principal benefit of trading as a limited company has always been the limited liability bestowed upon the company's officers and shareholders.
- As a sole trader or other non-limited business, personal assets are at risk in the event of failure of the business, but this is not the case for a limited company.
- As long as the business is operated legally and within the terms of the Companies Act, directors' or shareholders' personal assets are not at risk in the event of a winding up or receivership. Sometimes, such events are not always under the control of the director.
- Operating as a limited company often gives suppliers and customers a sense of confidence in a business in terms of being able to deliver the goods or services efficiently and professionally.
- Larger organisations including public sector entities may prefer not to deal with non-limited businesses where there is a potential risk to it or the good or services it has requested.

HMRC action and Reputational Damage

If it appears to HMRC that an individual has been engaged who should have been on the payroll, HMRC will seek any tax and NICs (plus interest and penalties) from the Council. In addition to the financial cost, there could also be the adverse publicity and reputational damage.

Agency Workers

Where an individual is engaged via an agency and no PSC/limited company is involved then the Agency is required to operate PAYE/NICs on any payments made to the individual.

Where the engagement by the Agency involves a PSC/limited company then the PAYE/ NICs liability will fall on the PSC/limited company.

Contract for Services

If an interim manager is not a temporary employee of the Council, with an employment contract, but is an employee/partner of a consulting firm and the contract is between the Council and the Consulting firm, the Council does not have a requirement to deduct PAYE/NICs through the payroll.

Consultants providing Specialist Advice

Contracts for such advice will normally be between the Council and a partnership or limited company.

In any contract that is in place, other than one with an individual, the Council currently has no obligation to deduct tax/ NICs from payments made. The recipient is responsible for accounting for any tax/NICs.

Where the contract is with an individual, the Council is required to consider the individual's tax status and contract clauses could be used to seek assurances that the worker is complying with his/her tax obligations.

Where the contract is with an Agency directly, clauses could be included in the Agency contract, and the Council could request that similar clauses be included in any contract between the Agency and the PSCs.