

Improving the operation of the Construction Industry Scheme (CIS) Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

- 1.1 We broadly welcome the Government's intentions to improve the operation of the Construction Industry Scheme (CIS). We can see that on-line CIS filing by contractors and the associated provision of on-line accounts to workers will be of benefit to many subcontractors paid under deduction, who frequently lose or mislay their monthly statements showing their pay and tax (that is, if they are even provided in the first place).
- 1.2 However we urge HM Revenue & Customs (HMRC) to remember that some individuals may struggle to engage with CIS online services and digital accounts and would recommend the provision of easy, quick and simple alternatives for filing information and accessing their records, for those that need it.
- 1.3 Problems with receiving or retaining monthly subcontractor payment statements (and lack of an annual summary document) can mean that subcontractors are forced to pay agents to source lost or missing CIS documents. In addition, as CIS deductions are usually higher than the final tax and Class 4 bills and CIS workers' tax returns often show a substantial refunds at the end of the tax year, there can be other problems with certain less scrupulous unaccredited tax return preparation agents.
- 1.4 As such, it is essential that when Government are considering 'simplifying end to end processes' for those involved in the CIS system, thought is given to the *workers*, who are often unskilled, in elementary roles and struggle with the sophisticated self-assessment regime unaided. In this regard, we note with interest the entry on page 13: 'A further possibility is that sub-contractors reclaim overpayments using an online account'. We hope that this refers to the provision of a 'self-serve' route outside the current complex system for

those with basic tax affairs and would definitely urge the Government to explore this option further (and make equivalent arrangements for those who are 'digitally excluded').

2 About Us

- 2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.
- 2.4 We have only commented on specific areas of the consultation which we consider to be relevant to the key aims of LITRG, and therefore have answered Questions 4, 5 and 6 only.

3 Question 4: Will removing the option to make monthly returns by paper present your particular business with any issues. How could HMRC help you overcome any difficulties?

- 3.1 We are not a construction business, but answer this question as an organisation with significant experience and understanding of digital exclusion and related matters¹.
- 3.2 Whilst we recognise that a shift to digital channels can save businesses time and money and the potential enabling benefits for many citizens of being able to communicate with government departments online, in general we do not agree with the mandation of online systems – we think that *choice* must be considered when designing processes and systems as otherwise there is a risk of disengaging taxpayers. This is particularly so when dealing with a group of taxpayers that, due to the manual nature of their trade and/or work, may not be IT savvy.²

¹ See for example: <http://www.litrg.org.uk/submissions/2014/a-call-for-evidence-labours-digital-government-review>

² We question for example, the wisdom of making the booklet CIS340 (which explains the CIS system to contractors and subcontractors) only available via a downloadable pdf. In order for as many people as possible to be aware of their obligations and responsibilities under the system, we would have thought it sensible to make CIS340 also available in hard copy.

- 3.3 From Government's own figures, 20% of contractors are currently not filing online – so there could be 30,000 taxpayers who prefer a paper process – not to mention that a potentially significant number of these will be without digital access and/or capabilities. We urge government to consider the case of *LH Bishop Electrical Co Ltd & Others v HMRC Commissioners* [2013] UKFTT 522 (TC) in which three appellants, supported by the LITRG, won their appeal against an HMRC requirement that they file their VAT returns online. The judge held that the HMRC regulations which required mandatory filing of VAT returns online were in breach of the appellants' human rights and were unlawful under the EU law as there were no exemptions for older people, those with disabilities or those who lived in parts of the country which were not well served for internet access.
- 3.4 This tells us that at the very least, there should be an alternative paper process where it is not reasonably practicable for the taxpayer to file online. We would suggest that HMRC bear the work of the PAYE RTI paper filing team in mind when shaping their non-digital option for 'excluded' contractors to file information. They worked very closely with representatives of employers who were exempt from online RTI filing (for example, care and support employers) to ensure that the best paper-filing solution and guidance was fully tested and developed. Many of the principles for dealing with paper filing customers are overarching and we would tend to think, apply across the board – hopefully you will be able to build on the work already carried out in this area rather starting from scratch.

4 Question 5 – Would you welcome an online appeals service?

- 4.1 We accept that penalties are needed to encourage compliance. However broadly speaking, we are not in favour of automatic computer generated penalties which are disproportionate to the offence and which the taxpayer needs to be appeal against in order that they may be cancelled or reduced to an appropriate level. No-one should be charged a penalty unless it is actually properly due in the first place.
- 4.2 Specifically, with regards to this consultation document, we understand that an online appeals service is a development that would come with an upgraded CIS online service. However, the consultation document goes on to say that this would not mean an improvement to the existing system but its replacement with something based on the current RTI channel used for PAYE returns.
- 4.3 If this is the case, then we seek reassurances from HMRC about the continuing availability of free software (that would not be limited to only the smallest contractors) and monthly filing (rather than the introduction of 'on or before'). An RTI based system could be a big change for many contractors and HMRC will need to consider a 'soft-landing' for in-year late filing and payment penalties to give them time to adapt to carrying out their CIS functions using the RTI system. This is particularly relevant to the 50,000 contractors who are not currently employers and so may have had no previous contact with the RTI system – particularly if thus far, they have managed a paper based system and will not fall within one of the exclusions from mandatory online usage.
- 4.4 Further, there are still a lot of unsolved problems with RTI and shortcomings in the system. We do not suggest RTI is rolled out to CIS until the teething problems are fixed. In the meantime, HMRC should work on the new system guidance for contractors, making it as

clear and easy to navigate as possible. HMRC must recognise that poor information could affect contractor payments and compliance³.

5 Question 6 – Would an integrated online account help reduce costs and reduce the burden of operating the scheme?

- 5.1 We answer this question on behalf of the workers who should, as a result of an online account, be able to digitally access a permanent record of all their payments and tax deductions.
- 5.2 The current monthly statements are frequently and easily mislaid – if they are even provided at all. Much of this is down to workers not understanding the importance of these forms or, indeed, what they should expect from their contractors (which itself speaks volumes about the urgent need for better taxpayer education). When it comes to tax return completion time, often they are not well versed or lack confidence in how to deal with missing or incomplete information. As such, they will pay third parties to obtain missing statements from contractors or to contact CIS Newry on their behalf or if all else fails, perform an estimated gross up calculation from the net amount in their bank accounts.
- 5.3 If their pay and tax data could be instantly visible by logging into an account, then that would be most useful – the cost for them of having to download or print it at their own expense would be vastly offset by their not needing to pay a ‘document retrieval fee’ to a tax repayment organisation. Ideally, such an integrated system would be compatible with smart phones and tablets to make it as accessible as possible. However, we are still talking about a taxpayer population where a significant minority will not have the necessary skills or wherewithal to use an online system, and so provision for them to access their data easily, simply and quickly needs to be made, for example, via a well-resourced CIS helpline – accompanied, of course, by clear promotion so that taxpayers know of its existence (this could also provide the route for workers of paper filing contractors to obtain their details).
- 5.4 In our view, even with this base data at their fingertips, many subcontractors still will be unable cope with the complicated, time intensive and administratively cumbersome task of filing self-assessment tax return – driving them to use tax agents. (It is worth mentioning that the new hurdles of having to decide between accruals vs cash basis, actual vs simplified expenses, so on and so forth, are not helping the perception that tax returns are difficult for individuals to accurately prepare unaided.) Whilst we appreciate that the services of a good accredited tax agent can often be most helpful to taxpayers, we think it should not be necessary for low paid CIS labour-only subcontractors to have to pay for assistance to file a tax return. Charges for this service can be high, and disproportionate if obtained from certain unaccredited agents⁴. With no other income in their tax returns and few expenses,

³ With respect to this, it is worth saying that we are increasingly concerned about the movement of the HMRC guidance to www.gov.uk – we find that there is so much dilution of the material that often important key messages are being lost in transit.

⁴ As noted in our report on Tax Repayment Organisations, we have seen charges range from 8% up to 40% of the overall repayment due:
<http://www.litrg.org.uk/Resources/LITRG/Documents/2013/07/Refund%20Organisations%20report%20CS5.5.pdf>

their tax returns are often basic with refunds calculated mainly based on the availability of the personal allowance.

- 5.5 Moreover, because CIS subcontractors often obtain large tax refunds, they are a target for the less scrupulous, usually unaccredited tax agents who, working on a percentage fee basis, have a vested interest in maximizing the value of the claim (which they might do by inflating the tax refund due by including fictitious or non-tax-deductible expenses, for example⁵). Whilst we and the tax charities⁶ have gone to great lengths to point out the warning signs of unscrupulous advisers⁷, taxpayers still get caught out and it is *they*, rather than the agents, who have to account for the underpaid tax to HMRC's compliance function, perhaps some years later. In such cases, on the basis that a fee will have been deducted already by the tax refund organisation, the HMRC debt may well be more than the financial benefit they received in the first place.
- 5.6 It seems to us that easing the situation of these individuals by allowing them to make a simple claim for repayment (perhaps giving a 10% flat rate expenses allowance automatically for small tools and mileage, etc.) as an alternative to a full calculation on a tax return, could save considerable effort all round. Alternatively (and this would benefit subcontractors that would struggle to make an online claim too) a P800 type automatic reconciliation could occur at the end of the year, with the onus put on the few subcontractors that may have more complex positions to tell HMRC that they need to self-assess.
- 5.7 One step further would be to make in-year claims available⁸ – there is a serious cash-flow disadvantage for many who have to wait until well after the end of the tax year to secure a refund (often driving them to use pay day loan companies to make ends meet in the meantime).
- 5.8 We hope that this is what is meant by 'A further possibility is that sub-contractors reclaim overpayments using an online account' in para 3.22, as this would be a most useful digital enhancement that could help ease the plight of the low paid (accompanied, of course, by an appropriate awareness raising exercise). We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.

LITRG
22/09/14

⁵ A state of affairs that HMRC seem to be well aware of in light of their CIS agent 'memorandum of understanding' exercise discussed here:

<http://www.taxation.co.uk/taxation/Articles/2013/07/03/309981/sign-here-or-else>

⁶ TaxAid and Tax Help for Older People.

⁷ For example, see <http://taxaid.org.uk/guides/information/a-starting-point-for-the-self-employed/cis-subcontractor/inflated-refunds-and-dodgy-advisers>

⁸ Such a facility is currently available via the completion of form CIS40, but the process is little understood and not well in use by taxpayers.