

**Call for evidence: Umbrella company market  
Response from the Low Incomes Tax Reform Group (LITRG)**

**1 Executive Summary**

- 1.1 We are a group of tax specialists with interest and expertise in the tax and related issues of the low paid, which includes agency workers that work through umbrella companies. We welcome the opportunity to respond to this call for evidence.
- 1.2 Our work in this area draws heavily on the experiences of TaxAid<sup>1</sup> who assist low-income individuals to comply with their taxation obligations, including around the loan charge and disguised remuneration (DR) (within which some umbrella companies have been involved). TaxAid have inputted into, and endorse, this call for evidence response.
- 1.3 Umbrella companies are used increasingly by low-income workers in the labour market. We have devoted significant time and resource over the past few years in trying to understand the umbrella company marketplace. This work culminated in our 2021 labour market intermediaries report<sup>2</sup>. The report sought to draw together evidence from a range of sources, to help form an overall picture of the current umbrella marketplace.

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<sup>1</sup> TaxAid is a charity that provides free tax advice to vulnerable people on low incomes: <https://taxaid.org.uk/>.

<sup>2</sup> <https://www.litrg.org.uk/latest-news/reports/210324-labour-market-intermediaries>

- 1.4 Some people think that umbrella companies exist only to exploit the tax system and lower-paid workers. Our report showed that this is not always the case, however it showed that there is a real and urgent problem in relation to the proliferation of disguised remuneration (DR) arrangements by some umbrella companies.
- 1.5 As set out in Chapter 11 of our report, previously, DR schemes may have been ‘sold’ to umbrella company workers as a way of them increasing their take home pay (although they may not have fully understood what they were getting involved in). But DR has advantages for others in the supply chain, and we think this is likely why we are now seeing umbrella companies paying workers through DR schemes, with no or negligible impact on workers’ net pay and without the worker having any knowledge of it whatsoever.
- 1.6 The best way we can contribute to this call for evidence is to provide an update on the developments in the umbrella company marketplace we are aware of since the publication of our report in 2021. We hope these updates, when taken together with our recommendations, will be useful input to the call for evidence team.
- 1.7 We frame our updates under 4 broad headings:
- Recent issues (as reported in trade press and mainstream media), including holiday pay abuses, cloning and cyber-attacks on umbrella companies. We offer some brief commentary and extra observations, for example, around the recent press stories on DR, where it seems to us that headlines such as ‘Medical staff are prolific tax avoiders’<sup>3</sup> and ‘It’s not just the rich that avoid tax: it’s teachers and nurses too’<sup>4</sup> are an unfair oversimplification.
  - LITRG/TaxAid queries – since we wrote our report, we and TaxAid have continued to receive contact from taxpayers who are having problems with umbrella companies (particularly DR related). We include a selection in this response.
  - HMRC’s own data – statistics released in November 2021<sup>5</sup> show that despite the ‘loan charge’, DR arrangements continue to proliferate. The data supports the case for decoupling the DR schemes from HMRC’s other efforts and presumptions in tackling tax avoidance, and for HMRC to explore alternative strategies.
  - Other organisations’ reports and data – for example, the Loan Charge All Party Parliamentary Group (APPG) recently issued a report<sup>6</sup> on their inquiry into ‘How Contracting Should Work’, which exposes the issues of ‘commissions’ paid by umbrella companies to agencies to incentivise them to refer workers; and comments on the extent to which this may have driven the operation of DR schemes. Of note is the ongoing industry led work trying to tackle the problems that exist due to the operation of DR schemes.

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<sup>3</sup> <https://www.thetimes.co.uk/article/medical-staff-are-prolific-tax-avoiders-i2cctr60x#:~:text=Nurses%20and%20NHS%20medical%20staff,to%20reduce%20their%20tax%20bills>

<sup>4</sup> <https://www.thetimes.co.uk/article/its-not-just-the-rich-that-avoid-tax-its-teachers-and-nurses-too-lb5jr5tf9>

<sup>5</sup> <https://www.gov.uk/government/publications/use-of-marketed-tax-avoidance-schemes-in-the-uk>

<sup>6</sup> <http://www.loanchargeappg.co.uk/wp-content/uploads/2021/04/How-Contracting-Should-Work-Inquiry-Report-April-2021-min.pdf>

- 1.8 The updates provided in this response, when added to the negative practices of non-compliant umbrella companies highlighted in our own earlier report, make it clear that some action is urgently needed.
- 1.9 We know that since the publication of our report, the single enforcement body (SEB) has been announced<sup>7</sup>. This is a very welcome step in the right direction and we sincerely hope that this call for evidence helps determine the shape of the SEB; however, it does not offer a complete solution as DR is a tax issue not an SEB issue. We believe that it is within HMRC's power to do something about DR **now**.
- 1.10 Although this is a call for evidence, and not a consultation looking at specific solutions, we make the following immediate recommendations:
- As required by the PAYE regulations, HMRC should pursue umbrella employers in the first instance for any underpayment. See Appendix 2 – an extract of an article we wrote outlining the legislation in more detail. HMRC failing to take action against umbrella companies and chasing workers for unpaid PAYE (against their own regulations), means there is no real incentive for the employers to stop using these schemes to pay people and the cycle continues.
  - HMRC should appoint someone with an overall responsibility for umbrella companies. Their remit could include developing an action plan to tackle non-compliant umbrella companies (rather than the workers) from a tax perspective and forming a formal stakeholder group (which could include compliant umbrella companies) to help challenge and guide HMRC in this area and hold HMRC to account.
- 1.11 We look forward to continuing to engage with HMRC on these issues and would be happy to discuss any element of our response in more detail if that would be useful.

## 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

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<sup>7</sup> On Tuesday (8 June) the Department for Business, Energy and Industrial Strategy said it will launch the SEB to tackle modern slavery, enforce the minimum wage and protect agency workers – including delivering on prior commitments to 'regulate umbrella companies': <https://www.gov.uk/government/news/government-to-protect-workers-rights-and-clamp-down-on-workplace-abuse-with-powerful-new-body>

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.

### **3 Introduction**

- 3.1 We welcome the opportunity to respond to this call for evidence. We would like to commend the various government departments involved for producing a well thought through and balanced call for evidence and for thinking creatively about how to gather vital, first-hand insight directly from workers.
- 3.2 In March 2021, LITRG released a research report entitled 'Labour Market Intermediaries: a technical report outlining how umbrella companies and other intermediaries operate in the labour market and the implications for workers who use them'.<sup>8</sup>
- 3.3 There are many high emotions and strong opinions about umbrella companies. They tend to generate a lot of 'noise', misconceptions, and confusion. The aim of the report was to cut through it all by obtaining and collating evidence from a range of sources – and then standing back and looking at the overall picture that emerged.
- 3.4 LITRG's research included talking with sector experts, reviewing umbrella company offerings and posts in contractor forums, and mining our own query database for evidence. The result was a factual report exploring the benefits and complexities of umbrella companies.
- 3.5 Without repeating the entire report, our key findings were:
- Umbrella companies perform a number of useful and legitimate functions in the labour market – traditionally they existed to provide an alternative route for freelance contractors who would otherwise have to work through a limited company; however now umbrella companies can also take on the payroll and HR function of temporary work agencies who can't or won't do this in-house.
  - There is no single definition of an umbrella company – anyone can set up a company and label itself an umbrella company.
  - Some agencies do not offer workers the ability to be paid through an agency payroll, with appropriate PAYE and NIC deductions. If workers want to accept an assignment, they have no choice but to work through an umbrella company.
  - At the same time, some agencies are incentivised by a commission into encouraging workers to join up to certain umbrella companies' schemes.
  - Many umbrella companies adhere to certain standards and are concerned about the welfare of their workers. However undoubtedly, there is a sizeable number of umbrella companies

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<sup>8</sup> <https://www.litrg.org.uk/latest-news/reports/210324-labour-market-intermediaries>

whose bad practice and non-compliance (particularly with respect to DR) sadly tarnishes the rest of the industry.

- There is a huge amount of money that flows through supply chains in which an umbrella company may be present. Umbrella companies can have a multi-million pound turnover, for example, we found one umbrella company had a turnover of £287million<sup>9</sup>.
- For traditional, compliant, umbrella companies, the vast majority of income is paid out in the form of worker salaries and on top employment costs (such as employers' national insurance), with the company retaining a small 'margin'. For example, in the £287million example above, £280 million was paid out in salaries and other employment costs, like employer NIC and pension. This left £7million gross profit, however after operating expenses, the overall profit was actually about £1million. With around 6,500 workers on their books in that year – this meant around £150 profit per worker.
- Most traditional umbrella companies do not get involved in DR schemes. We understand it is more likely that the umbrella companies that use DR schemes to pay workers, will have been specifically set up by promoters to operate their DR schemes.
- Claims by umbrella companies of them 'legitimately' or 'tax efficiently' being able to 'maximise' take-home pay to upwards of 80%, have been abundant in recent years and may appeal to certain highly paid or sophisticated contractors who, as a consequence of the IR35 changes, have seen their take home pay reduce.
- However, while some umbrella companies may be using a DR scheme as part of a bigger avoidance supply chain, others may have simply seen an opportunity to get an advantage in the marketplace or to keep up with competitors– casually concocting DR schemes in house without any real 'promoter' behind them.
- In our experience, these are the types of schemes in which lower paid agency workers mainly seem to become entangled. These schemes do not seem to involve particularly sophisticated or convoluted planning – the umbrella companies involved seem to be designating a portion of otherwise taxable earnings as a non-taxable payment. The umbrella companies involved are not even attempting to hide what they are doing and, in many cases, simply referring to an element of a worker's pay as an advance or loan or other non-taxable element with little or no paperwork to support the 'planning'.
- Where DR arrangements are used, the paying entity can increase their 'margin' significantly. So, for example, an umbrella company agrees a contract rate with an agency of £500 per week for a particular worker. Under normal conditions, where PAYE and NIC are appropriately deducted, they would have to pay £400 of that to the worker for their gross pay and £70 in on top employment costs, leaving them with only a £30 margin. If they use DR arrangements, they deliver the worker a similar level of net pay, out of a lower gross amount and cut their on top employment costs, but as a result, the umbrella company can easily double or triple their margin from a particular contract rate.
- To be clear, as the worker's net pay is often roughly the same or only slightly increased, DR can be totally invisible to the worker.

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<sup>9</sup> Turnover means all the umbrella companies' income – some are not like normal businesses; they don't have a 'normal' trade that generates income. Their income is basically the money paid to it by the agencies and end clients.

3.6 We put together a ‘real world’ example in May 2021<sup>10</sup> to try to illustrate the ‘phenomenon’ of DR being totally invisible to the worker, which can be found in Appendix 1. While we have no interest in protecting those who intentionally seek to minimise their taxes by using DR arrangements, in our view, this example demonstrates how easy it is for innocent agency workers to end up as pawns – in a game being played by their non-compliant umbrella companies.

3.7 As we set out in our response to the Call for Evidence on Tackling DR tax avoidance<sup>11</sup>, this is a completely plausible scenario for the following reasons:

- It should be remembered that many workers are not sufficiently well versed in HR and payroll matters to understand how their pay and taxes should be calculated and delivered and not everyone has ready access to their pay documents anymore – often they are only provided online/are password protected, if at all. (Even if people do have access to their payslips, how many people regularly check (and understand) them?)
- Many agency workers are young and sometimes inexperienced; they may have limited education with lower levels of numeracy and literacy or have English as a second language. In any case, for the majority, it is important to appreciate that the PAYE system discourages employees from engaging with their tax affairs. The employer is the tax gatherer, administering an employee’s tax for them and the employee can become very passive, assuming it is all taken care of. This is an excellent system when it works well, but it can contain pitfalls for the unwary. Certainly, our experience of working with unrepresented taxpayers more generally is that people rarely understand how their net pay is calculated and often don’t question figures because they put trust in their engager.

#### **4 Recent issues**

4.1 Umbrella companies have been in the news frequently since our report was published. In the following paragraphs we discuss some particularly interesting and noteworthy examples of articles etc. exposing or highlighting various issues (and offer some extra commentary around this).

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<sup>10</sup> <https://www.litrg.org.uk/latest-news/news/210527-received-a-letter-from-hmrc-tax-avoidance>

<sup>11</sup> <https://www.litrg.org.uk/sites/default/files/200922-LITRG-response-Tackling-DR-tax-avoidance-Call-for-evidence-2328.pdf>

- 4.2 At the end of March 2021, there was the furore about an umbrella company withholding holiday pay from workers,<sup>12</sup> where the umbrella workers did not seem to understand the circumstances in which they might lose their holiday pay (for example, if they did not request it before the end of the holiday year).<sup>13</sup> A recent Court of Appeal ruling<sup>14</sup> must surely mean umbrella companies will now need to make certain that they are transparently communicating with their workers regarding the possibility of losing paid holiday. However, given some umbrella companies appear to treat holiday pay as an extra revenue stream, the question must be how will they displace these costs?
- 4.3 In May 2021, there were renewed concerns about the use of mini umbrella companies<sup>15</sup>. Although the Employment Allowance legislation<sup>16</sup> makes it clear that artificially created companies cannot claim the allowance (indeed, back in 2015 – responding to a story about mini umbrella companies – our then Technical Director, Robin Williamson said that they were driving a coach and horses through the legislation: “To use the colloquial – they are having a laugh”<sup>17</sup>), this ‘mini umbrella’ problem seems to be difficult for HMRC to deal with. We are very concerned about mini umbrella companies and not just for obvious reasons (such as the cost to the Exchequer and the impact on workers’ employment histories) – it seems low-paid workers are being targeted to become ‘nominee directors’ of the mini umbrellas, with all sorts of implications for them<sup>18</sup>.
- 4.4 More recently we have had ‘cloning’ – helpfully explained in an umbrella company blog<sup>19</sup> as follows: *‘It appears that umbrella company cloning is taking place to deceive supply chain members into thinking the cloned umbrella is the established umbrella. The reason for doing this is almost certainly to commit fraud by tricking a recruitment agency, for example, to send workers’ payments to a*

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<sup>12</sup> <https://www.bbc.co.uk/programmes/m000tcl7>

<sup>13</sup> The problem being that while not transparently communicating with workers about loss of holiday pay may be unethical, it may not be illegal.

<sup>14</sup> See <https://www.bailii.org/ew/cases/EWCA/Civ/2022/70.html> The Court of Appeal has ruled that a worker can only lose the right to take paid leave within the holiday year when:

- The employer can show it specifically and transparently gave the worker the opportunity to take paid annual leave;
- The employer encouraged the worker to take paid annual leave;
- The employer informed the worker that the right would be lost at the end of the leave year.

<sup>15</sup> The BBC published a piece on mini umbrellas <https://www.bbc.co.uk/news/uk-57021128> and there was an expose by The Guardian [https://www.theguardian.com/business/2021/may/10/tax-dodging-concerns-over-small-firms-used-to-pay-nhs-test-and-trace-workers?CMP=Share\\_iOSApp\\_Other](https://www.theguardian.com/business/2021/may/10/tax-dodging-concerns-over-small-firms-used-to-pay-nhs-test-and-trace-workers?CMP=Share_iOSApp_Other)

<sup>16</sup> <https://www.gov.uk/hmrc-internal-manuals/national-insurance-manual/nim06565>

<sup>17</sup> <https://www.bbc.co.uk/news/business-32914372>

<sup>18</sup> For further information, see this article:

[https://www.contractoruk.com/news/0015047mini-umbrellas-are-major-problem-hmrc-its-agencies-and-workers-who-carry-can.html?utm\\_source=NL&utm\\_medium=News&utm\\_campaign=Comment](https://www.contractoruk.com/news/0015047mini-umbrellas-are-major-problem-hmrc-its-agencies-and-workers-who-carry-can.html?utm_source=NL&utm_medium=News&utm_campaign=Comment)

<sup>19</sup> <https://www.umbrellacompanies.org.uk/umbrella-company-cloning-remains-a-serious-threat-to-the-sector-in-2022/>

*“new” bank account that they believe belongs to the umbrella they have a relationship with. Instead, the cloned umbrella will receive funds – leaving the agency out of money. And the knock-on effect could be very severe because the legitimate umbrella company might not receive the appropriate funds for its employees – meaning temporary workers could be left unpaid.’*

- 4.5 Again, more recently, there have been cyber-attacks on several Freelancer and Contractor Services Association (FCSA) accredited umbrella companies<sup>20</sup> – meaning workers could not be paid as systems were taken offline and there was potentially a breach of their personal data. Of interest is the concluding paragraph in the recent Loan Charge APPG letter<sup>21</sup>, dated 24 January 2022 (in relation to ongoing correspondence about FCSA’s Charter) which states: *‘Lastly we note with concern, the several reports of FCSA accredited companies being hit with cyber-attacks, that have been raised with us. Considering that many UK workers are reliant on their livelihoods by being paid by umbrella companies, who hold confidential data, including bank account details and other sensitive details, this is hugely worrying. Considering this and the huge sums involved overall, this is surely another reason why regulation of the market, something that the FCSA has told us it supports, happens as soon as possible’.*
- 4.6 Disguised remuneration generated several stories towards the end of 2021 – however, headlines such as ‘Medical staff are prolific tax avoiders<sup>22</sup>’ and ‘It’s not just the rich that avoid tax: it’s teachers and nurses too<sup>23</sup>’ (in response to the release of HMRC’s corporate report referenced in the next section) are simply unfair and misleading as they suggest such workers have deliberately set out to avoid tax (which, as we allude to, throughout this response, may not be the case).
- 4.7 The above examples help illustrate:
- 1) there are serious issues in the marketplace (ongoing, new and potential); and
  - 2) issues in the umbrella company industry can often move quickly.
- 4.8 When considering the question of ‘regulation’, it is clearly vital that the government departments involved are clear on exactly which problem (or problems) they are trying to tackle in the industry, so that they are able to formulate appropriate responses, without spending time and money on the ‘wrong’ problems. When it comes to umbrellas, the departments need to be aware of the latest practices and have the richest, most up-to-date information available – which, in our experience,

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<sup>20</sup> For example, see

[https://www.contractoruk.com/news/0015214giant\\_group\\_hacked\\_suspected\\_ransomware\\_attack.html](https://www.contractoruk.com/news/0015214giant_group_hacked_suspected_ransomware_attack.html) and [https://www.contractoruk.com/news/0015341hackers\\_attack\\_parasol\\_and\\_brookson\\_leaving\\_umbrella\\_contractors\\_unpaid.html/](https://www.contractoruk.com/news/0015341hackers_attack_parasol_and_brookson_leaving_umbrella_contractors_unpaid.html/)

<sup>21</sup> <http://www.loanchargeappg.co.uk/wp-content/uploads/2022/01/2022-01-24-Loan-Charge-APPG-reply-to-the-FCSA-about-HMRC-contractors-using-DR-schemes.pdf>

<sup>22</sup> <https://www.thetimes.co.uk/article/medical-staff-are-prolific-tax-avoiders-i2crr60x#:~:text=Nurses%20and%20NHS%20medical%20staff,to%20reduce%20their%20tax%20bills>

<sup>23</sup> <https://www.thetimes.co.uk/article/its-not-just-the-rich-that-avoid-tax-its-teachers-and-nurses-too-lb5jr5tf9>



often comes from responsible umbrella providers who are potentially harmed by poor practices that undercut them.

## 5 LITRG/TaxAid worker queries

- 5.1 LITRG has continually received a trickle of queries into its mailbox about umbrella companies. Despite the significant shift of Personal Service Company (PSC) workers into umbrella companies as a consequence of the April 2021 IR35 changes, we have not seen any notable spikes in connected queries, which is encouraging. It suggests that the welcome investment HMRC made recently in producing guidance for umbrella company workers<sup>24</sup> and the Key Information Document (KID) initiative<sup>25</sup> from April 2020 may be helping some workers navigate the umbrella landscape.
- 5.2 We do know, however, that sometimes problems with umbrella companies can take time to surface. We also have some concerns about the ex-PSC demographic and the use by private sector end clients of Managed Service Providers (MSP) (note – these are not the same as Managed Service Companies). From what we can gather MSPs are retained by end clients to wholly manage their contractor workforces – so in respect of IR35 they would sort the contractors out into inside IR35 or outside IR35 and then act accordingly, e.g., find them an umbrella company or renegotiate the contract. There must be risks for workers moving to umbrella companies, of having *another* entity in their supply chains, with the inevitable downward cost pressure that this must bring, potentially squeezing margins and making questionable practice by umbrellas more likely.
- 5.3 We have also received *a few* queries (although seemingly not from the ex-PSC demographic) that demonstrate there is still some confusion about umbrella companies/the presence of umbrella companies in supply chains (which shouldn't be happening if there was complete transparency/the KID system was working 100% properly). The queries received included:
- one from a person who didn't understand why his gross pay was being paid in two parts (although both parts taxable); and
  - one from an overseas supply teacher, new to UK agency work, (who referred to herself as working through a 'sketchy' umbrella company), who felt completely bewildered and not fully comfortable having been given seven umbrellas to choose from (and given seven different Key Information Documents with no explanation as to what they were or what they meant<sup>26</sup>).

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<sup>24</sup> <https://www.gov.uk/guidance/working-through-an-umbrella-company>

<sup>25</sup> <https://www.gov.uk/government/publications/providing-a-key-information-document-for-agency-workers-guidance-for-employment-businesses>

<sup>26</sup> This indicates that there needs to be better enforcement of Regulation 13A of the 'Conduct Regulations' ([Conduct of Employment Agencies and Employment Businesses Regulations 2003](#)), which introduced the requirement to provide a KID for agency workers. Enforcement needs to include ensuring that each document includes a clear explanation as to what a KID is and what the terms mean, so that even individuals with language or learning issues can better understand their situation.

5.4 Moreover, since our report was issued, LITRG and TaxAid have continued to receive contact from workers who seem to find themselves being paid through a DR scheme. The cases we see are not necessarily from the previously typical groups, such as the IT and oil and gas industry with historic EBT/DR schemes. Individuals are from a wide cross section of industries, including data processors, teachers, social workers, nursing, construction and engineering. They also include people who may have barriers to dealing with their tax affairs for example they may be migrants who don't have English as their first language or in some cases we have seen there is an underlying learning difficulty.

5.5 Here is a query that LITRG have recently received from a social worker:

*I have received a notice to provide information from HM Revenue and Customs as they suspect that my PAYE company may not be paying all my taxes. I am also concerned that my company, may be committing fraudulent action as they pay me 2 separate amounts every week and have stated that I should either just declare one amount to the Inland Revenue or if I declare both amounts to say one is expenses. Are you able to advise as I am really worried as there is amount of £240 which they advise to declare as my income and a amount of £850 which they say to declare as expenses. Could this be correct or is this a way of avoiding tasks by paying 2 amounts and claiming one is expenses.*

5.6 Here is a case study that is typical of the types of calls TaxAid are receiving on DR (this has been shared with HMRC):

*Maya is from Poland. She works as an NHS nurse through an agency. They recommended an umbrella company that provided payroll services and for several years, everything was okay (although she is not a tax expert, she thinks her earnings were taxed correctly). At the end of 2020, the umbrella company got taken over by another umbrella company. Although the new umbrella company did not send out a new employment contract or any paperwork, nothing seemed to change with Maya's net pay, so Maya did not question things any further. She had no reason to suspect anything was wrong with the new umbrella company. Maya has just been sent a letter by HMRC headed 'You may have been involved in tax avoidance' and phoned TaxAid. The TaxAid adviser, having done some research on the umbrella company and a fact find (during which it transpired Maya does not have ready access to her payslips and is receiving two payments into her bank account each payday) advises Maya that her new umbrella company may well be paying her using a DR scheme. Maya will obviously leave the umbrella company concerned with immediate effect if that is the case but is very worried about whether HMRC will chase her for the historic underpayment. Maya also expressed anger and confusion about how, as a law-abiding person, just trying to earn a living, she has been exposed to this situation.*

5.7 These examples help demonstrate that DR may not be an 'active choice' for agency workers. Some agency workers will go along with things but will have little understanding that the way they are being paid is DR. Some may have an inkling that something isn't right but dare not probe as they

need the job. In some instances, workers seem to be being paid through DR schemes by the umbrella companies they are working through with no knowledge or awareness of this.

5.8 Undoubtedly, some historic loan scheme usage will have been rooted in this same ground, with workers unclear of the tax position, which is probably why HMRC are struggling to draw a line under the loan charge<sup>27</sup> and why both LITRG and TaxAid are receiving queries and dealing with cases like the ones below. If people did not know that they were in a loan scheme, then they would not recognise themselves as being affected by the loan charge, let alone be able to fulfil their tax filing and payment obligations.

5.9 Here is a query LITRG received from a supply teacher who appears to have been sent a 2018/19 loan charge tax return to complete:

*I usually work for different agencies I received a letter from Hmrc to do self assessment not self employed but they claimed I have been involved in tax avoidance scheme with (umbrella)... I have done nothing wrong but have been charged £1300.00 for not filling. I have called Hmrc several times asking them to explain but was told they don't know anything about it I ask a lawyer to write to them but they said its my responsibility to deal with the matter. I am stresses (sic) really don't what I can do.*

5.10 Here is a loan charge case study, that TaxAid wrote up for a presentation they gave recently (shared with HMRC already):

*Robert works as a steel erector and he has always avoided going down the self-employed route in the construction industry as he has dyslexia and did not want the worry of filing tax returns and could not afford an accountant to do it for him.*

*Robert, like so many clients that contact TaxAid about the loan charge, did not purposefully set out to save tax through a loan scheme. He simply left it to the agency/umbrella to sort his payroll tax and NIC. He started receiving what he describes as threatening letters from HMRC in 2016. This is his story:*

*"I started trying to deal with this back in 2016 I got nowhere with anyone from HMRC I couldn't get a straight answer why I was due them this money I was promised phone calls back to get an answer but they never happened.*

*I then started getting threatening letters from HMRC again about this debt that I couldn't get answers to why I was due it so I went and spoke to my local (MP) who got onto this for me they didn't get a straight answer either as to why I was due this and I asked for a break down of the debt that never appeared either.*

*I then contacted tax aid to help as I'm not able to do this as I have dyslexia (sic) this is the first time I have been explained why this has come about and you know yourself that's us just starting to get answers and a breakdown of the debt.*

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<sup>27</sup> See our briefing for more information: <https://www.litrg.org.uk/latest-news/submissions/211006-budget-representation-2021-loan-charge>

*Due to me having dyslexia (sic) I always wanted to be PAYE with the agency's that I worked for I was told from the agency I worked for to go PAYE I needed to go through a pay company they would deal with all the paperwork side of it to pay my taxes but at a cost to me they would automatically take that from my wages to cover there fees I knew nothing about loans payed to me until tax aid explained this to me and you explained that there was 2 payments that's when I gave you the figures for the extra payments I had received I have no knowledge (sic) of filling out tax returns and the problem I had filling in tax returns was my dislexia I called HMRC many times about this and explained that I wasn't self employed and that I had no knowledge as to why I kept getting letters to fill in a tax return because I've always been PAYE and I didnt understand the tax system due to my disability but never got anywhere to solving this I've always been met with the attitude from HMRC that they didn't really care or try to help with the situation as you and the MP have seen by the way there also dealing with you they have no clue what's going on as do I*

*I live with my parents now after a break down in my relationship my child lives with my ex partner but I finantually (sic) support my child as I feel I have a responsibility to do so I pay half of my ex partners rent every month so my child has a roof over her head at £500 a month I earn roughly £400 a week I have my usual cost for getting bk and forward to work (car costs) and also board to my parents to keep me"*

- 5.11 We accept that it is more convenient to think of DR (including loan arrangements) as the discrete problem of individuals trying to minimise their taxes rather than a murkier problem that calls into question the health and functioning of the entire temporary labour market, but in these examples at least, the latter appears to be the reality.

## **6 HMRC's own data**

- 6.1 In November 2021, HMRC released their 'Use of marketed tax avoidance schemes in the UK' report for 2019/20<sup>28</sup>.

- 6.2 This data is very insightful. Of note are the following statements and observations that flow from HMRC's own publication:

- Despite the loan charge<sup>29</sup>, disguised remuneration has not gone away – in 2019/20, it made up 100% of all tax avoidance (as opposed to 60% in 2013/14 – with the rest being other tax avoidance schemes such as sideways loss relief schemes).
- 28,000 individuals and 1,000 employers<sup>30</sup> were involved in DR arrangements in 2019/20. This compares to 22,000 individuals and 6,000 employers (which were mainly close companies run by owner directors) during 2013/14.

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<sup>28</sup> <https://www.gov.uk/government/publications/use-of-marketed-tax-avoidance-schemes-in-the-uk>

<sup>29</sup> In 2016 Budget speech announcing the loan charge, it was claimed that the policy would 'shut down disguised remuneration'

<sup>30</sup> HMRC say 'These 'employer' figures do not include non-compliant umbrella companies who act as the employer for the majority of individuals involved in avoidance schemes. The individuals who work through non-compliant umbrella companies are counted in the individuals' population'.

- In 2013/14 the typical use of ‘disguised remuneration’ was by employers operating third party Employee Benefit Trusts and Employer Funded Retirement Benefit Schemes for their employees (including owner directors). In more recent times, the arrangements are basically a variation on the theme of an agency worker or contractor being paid a minimal amount of taxable income, topped up with a purportedly non-taxable element (whether it be loans, investment payments, advances, grants, loans, credits etc.).
- The largest group of users of such schemes according to HMRC had an employment categorised as “bookkeeping activities”, which is what a worker would be classed as if they were part of an umbrella company, regardless of what their actual job may be.
- It is therefore not possible to understand exactly which types of workers are getting caught up in DR, although we understand from HMRC that the amount of money ‘locked up’ these days in disguised remuneration is much less than previously – which suggests that those involved tend not to be higher or additional rate taxpayers but basic rate taxpayers, - i.e., those on lower incomes.
- There are about 20 to 30 promoter organisations who are behind most of the tax avoidance schemes that are marketed to the UK public. HMRC estimate there are currently around 60 to 80 non-compliant umbrella companies involved in the operation of disguised remuneration avoidance schemes.

- 6.3 Taking all these figures together, what they appear to be telling us is that HMRC have been very good at shutting down sideways loss relief schemes and Employee Benefit Trusts but that DR arrangements continue to proliferate. One possible reason for this is that HMRC’s efforts to date, which have been largely focussed on targeting promoters and changing taxpayer behaviour (i.e., bolted on to a regime designed to tackle traditional tax avoidance like sideways loss relief), have failed to address the root causes of the use of DR schemes.
- 6.4 The figures also demonstrate that there has been a significant shift in scheme usage towards lower paid workers (which backs up LITRG and TaxAid’s own experiences of agency workers like locum nurses and supply teachers presenting to them with DR problems, as set out in the previous section).
- 6.5 However, the idea that lower paid agency workers like the social worker and Maya reference above – often decent, law abiding, migrant, public sector workers who may never have even used a Ltd company before, let alone have an aggressive tax avoidance motive – are trying to seek out umbrella companies to pay them more through a DR scheme, is far removed from what we see or understand to be going on – such that we do not believe it to be true in the majority of cases.
- 6.6 Something else must be happening. As highlighted on numerous occasions<sup>31</sup>, we think the ‘something’ is that lower paid agency workers are being exploited by some non-compliant umbrella companies for their own gain, by being unwittingly paid through DR schemes. As stated previously in our introductory comments, DR arrangements mean umbrella companies can make a larger percentage return from the amount they turnover. So, it would be logical for this to be now a significant driver of the DR problem as opposed to taxpayers ‘being in the market’ for tax avoidance.

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<sup>31</sup> Including in meetings with HMRC, letters to HMRC, informal discussions with HMRC and formal submissions including to the Clamping down on the promoters of tax avoidance consultation sand the draft legislation.

- 6.7 We are encouraged that HMRC seem more aware of this issue than previously, but we remain concerned that this awareness does not seem to be fully filtering down to HMRC's strategy in tackling DR.
- 6.8 Looking at DR through this lens (that low income workers may be unaware that they are in a disguised remuneration scheme as the motivation and benefits sit with others in the labour market supply chain), what is needed (and as we set out in the conclusion) is action to be taken at the engager level<sup>32</sup> combined with a holistic approach to raising standards across all entities in the supply chain – including end clients and agencies<sup>33</sup>.
- 6.9 We know there are a variety of reasons why people get into DR – the 'unknowing' individuals clearly will not account for all usage – but we think it is incumbent on HMRC to explore all possibilities and tailor their response accordingly. Without such a holistic rethink of HMRC strategy, there is a serious risk that it will fail to have the intended effect and DR schemes will continue to proliferate with individual taxpayers continuing to suffer the side effects.

## 7 Other organisations' reports and data

- 7.1 Since the publication of our report, the Loan Charge All Party Parliamentary Group also issued a report on their inquiry into 'How Contracting Should Work'<sup>34</sup>. It covers much the same ground as our umbrella report. Both reports expose the issues of 'commissions' paid by umbrella companies to agencies to incentivise them to refer workers and comment on the extent to which this may have driven the operation of disguised remuneration schemes.
- 7.2 In May 2021, there was the publication of 'Umbrella Companies – Call for Regulation'<sup>35</sup>, a set of proposals for government action in this area, authored by employment status expert Rebecca Seeley Harris and founder of offpayroll.org James Poyser. The paper draws heavily on our umbrella report, highlights the "*mounting evidence of malpractice*" and "*widespread non-compliance of both tax and employment law*", in the supply chain, and urges a consultative approach to the design of regulation, to be pursued as a priority by government.

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<sup>32</sup> For example, HMRC could take action at employer level (so against the umbrella companies) for failure to operate PAYE correctly. Indeed, it is open to HMRC to issue a Regulation 80 determination against an umbrella company and then when they inevitably fold, use their new 'joint and several' liability powers to pin the liability personally on the director. However, this does not appear to be happening in practice, which is a missed opportunity to stop this type of DR usage.

<sup>33</sup> We set out some ideas in our response to the Call for Evidence on Disguised Remuneration: <https://www.litrg.org.uk/latest-news/submissions/200923-call-evidence-tackling-disguised-remuneration-tax-avoidance>

<sup>34</sup> <http://www.loanchargeappg.co.uk/wp-content/uploads/2021/04/How-Contracting-Should-Work-Inquiry-Report-April-2021-min.pdf>

<sup>35</sup> <https://www.inniaccounts.co.uk/2021/05/policy-to-regulate-umbrella-market-submitted-to-the-treasury/>

- 7.3 In June 2021, sector expert and founder of Professional Passport<sup>36</sup>, Crawford Temple published<sup>37</sup> a report entitled 'The Good, the Bad and the Ugly', containing helpful suggestions for quick win interventions to address the issues of tax non-compliance in the umbrella sector. For example, he suggests that HMRC have access to huge volumes of information through both umbrella payroll and agencies' monthly intermediary reporting data, which if cross-referenced could provide significant intelligence enabling them to identify potential disguised remuneration schemes quickly. HMRC should then work quickly to protect themselves and the workers from losses, by demanding PAYE security deposits from umbrellas.
- 7.4 It is worth saying that we have heard so many things about umbrella companies in our work – that they are unscrupulous and unethical and will do anything they can to bend the rules. We have even heard them described as no better than loan sharks. However, there are many responsible providers in the umbrella industry that are desperate to find consensus with HMRC as to 'what good looks like' and to raise standards.
- 7.5 In terms of industry led calls/solutions trying to highlight/fill the gaps that exist with state enforcement/regulation – more recently, we have come across SafeRec<sup>38</sup> – a startup concerned with underhand umbrella practices.
- 7.6 SafeRec have spent the past 18 months developing an AI that can read and audit umbrella payslips<sup>39</sup>. They then cross-reference the audit with the assignment rate (i.e., the amount paid by the agency to the umbrella company) and also how much PAYE Tax and NIC has been paid to HMRC. The combination of these 3 steps means that SafeRec can quickly identify when workers are being paid through DR schemes; in addition, also it can spot other potentially 'invisible' pay and tax abuses/skimming by umbrellas.
- 7.7 Very recently, SafeRec relayed (in general terms) some of the data that the payslip tool has thrown up<sup>40</sup>. The information is very insightful and should be of huge interest to HMRC in terms of helping to build HMRC's evidence base and getting a better idea of the nature and scale of various issues. It also shows how technology can be utilised to understand some of these issues and help workers understand their position.

## 8 Conclusion

- 8.1 It is clear that low-income workers continue to be at risk due to working through non-compliant umbrella companies, particularly with regards to DR. Indeed, that risk might be growing. It has long been our view that the low-paid require their positions to be protected through effective state

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<sup>36</sup> One of the two main umbrella accreditation bodies: <https://www.professionalpassport.com/>

<sup>37</sup> [https://www.professionalpassport.com/pdfs/Professional\\_Passport\\_Good\\_Bad\\_Ugly\\_Final-web.pdf](https://www.professionalpassport.com/pdfs/Professional_Passport_Good_Bad_Ugly_Final-web.pdf)

<sup>38</sup> <https://saferec.co.uk/>

<sup>39</sup> <https://saferec.co.uk/payslip-checker>

<sup>40</sup> For instance, that 1 in 3 or 4 umbrella payslips that are audited 'fails' the process. Even allowing for a number of false positives, this is a startling figure.

enforcement and we can now say with some certainty: this can be no truer than when it comes to umbrella companies.

- 8.2 The new single enforcement body (SEB) has the potential to have a really positive impact on umbrella workers. But it will not offer a complete solution<sup>41</sup>. For example, although its role in supporting and protecting worker rights may help bring improvements for umbrella employees in key areas over time<sup>42</sup>, DR is primarily a tax, not an SEB, issue.
- 8.3 In the longer term, there is a clear and unequivocal need for HMRC to share information and work closely with the SEB. In the short term, we urge HMRC to use their existing powers to act **now** against tax non-compliant umbrella companies, particularly those which use disguised remuneration to pay workers. If HMRC consider that these powers are inadequate then they should be swiftly reviewed and improved where appropriate.
- 8.4 What underlies a DR scheme is a failure to operate PAYE correctly on behalf of the umbrella company employer. As we set out clearly in a recent article (an extract of which is contained as Appendix 2), the PAYE regulations say that in most instances, HMRC should pursue the employer for any underpayment. In our view, HMRC failing to take action against umbrella companies and chasing workers for unpaid PAYE (against their own regulations<sup>43</sup>), means there is no real incentive for the employers to stop using these schemes to pay people and the cycle continues. This has a significant impact on the well-being of the workers involved but also wider implications for the reputation of the tax system.
- 8.5 In pragmatic terms, one of the ways that HMRC could start to translate thoughts and ideas about how to tackle DR, into a tangible reality, is for HMRC to appoint someone senior to take overall responsibility for umbrella companies. Their remit should include developing an action plan to tackle non-compliant umbrella companies from a tax perspective. This should include the formation of some kind of trusted, expert stakeholder group (which could include the compliant umbrella companies) to help challenge and guide HMRC in this area and hold HMRC to account.

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22 Feb 2022

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<sup>41</sup> The SEB will combine the Gangmasters and Labour Abuse Authority, the Employment Agency Standards Inspectorate and HMRC's National Minimum Wage Enforcement into one body. It doesn't include HMRC tax.

<sup>42</sup> Regulation would drive away those umbrella companies that do not respect employment law, which will help protect lower paid agency workers who are vulnerable to exploitation. As they are likely to be the umbrella companies that are also non-compliant with tax law, there is a potential double benefit. There are also wider impacts. For example, non-payment of holiday pay is likely to be impacting considerably on gross wage levels, meaning lower receipts for the Exchequer.

<sup>43</sup> HMRC seem to have an unrelenting and uncompromising stance that 'individuals are responsible for their own tax affairs'.



## Appendix 1

Extract from article: <https://www.litrg.org.uk/latest-news/news/210527-received-a-letter-from-hmrc-tax-avoidance>

*Traditional, compliant, umbrella companies pay out the vast majority of the income they receive from agencies or end clients, in the form of worker salaries and 'on top' employment costs (such as employers' national insurance), with the company retaining a small 'margin' for its services.*

### Example

*Jess is a weekly paid worker. She works 35 hours a week and her gross pay rate is £11 an hour. In order that the umbrella company can deliver £11 an hour to Jess, her agency passes £495.25 to umbrella company in respect of her 35 hours work.*

*Where DR arrangements are used, the umbrella company increases the amount of money they retain as a margin (£26 in the top payslip below), significantly. They deliver Jess a similar level of net pay, out of a lower gross pay amount, and cut their 'on top' employment costs. The umbrella company can easily double or triple their margin from a particular contract rate.*

Jess: normal payslip					
<b>Umbrella Company Ltd</b>					
Employee number	Name			NI Number	Date
123	Jess			QQ123456A	7-May-21
<b>Contractor statement</b>					
Agency receipts	Units	Rate	Amount	Employer deductions	
Normal time	35	14.15	495.25	Pension	7.96
Re services to Agency X				Holiday	46.47
				Employer NIC	29.81
				Margin	26
<b>Payslip</b>					
Employee payments	Units	Rate	Amount	Employee deductions	
Salary	35	8.91	311.85	Tax	28.6
Taxable bonus	35	2.09	73.15	Employer NIC	24.12
				Pension	10.6
<b>Total gross pay for tax</b>			<b>£385</b>	<b>Net pay</b>	<b>321.68</b>
Tax code 1257L				BACS	

*\*Umbrella companies usually use a payment structure where they use the NMW plus a taxable variable bonus or commission to pay their workers. There are two reasons for this structure: 1) To limit financial risk to the umbrella and 2) To allow for pay rates to vary, however both elements should be taxable.*

Jess: disguised remuneration payslip					
Umbrella Company Ltd					
Employee number	Name			NI Number	Date
123	Jess			QQ123456A	7-May-21
<b>Contractor statement</b>					
Agency receipts	Units	Rate	Amount	Employer deductions	
Normal time	35	14.15	495.25	Pension	5.76
Re services to Agency X				Holiday	40.69
				Employer NIC	19.57
<b>Payslip</b>					
Employee payments	Units	Rate	Amount	Employee deductions	
Salary	35	8.91	311.85	Tax	-13.97
				Employer NIC	-15.34
				Pension	-7.67
				Payment	46.81
<b>Total gross pay for tax</b>			<b>311.85</b>	<b>Net pay</b>	<b>321.68</b>
Tax code 1257L					
				BACS	

### More detailed explanation

Suppose Jess' umbrella company above continues to receive £495.25 as per the agreed contract rate, but instead of using this to deliver an £11 an hour gross pay rate to Jess and take a £26 fee, it only delivers a gross salary rate of £8.91 per hour to Jess (the main minimum wage rate in May 2021) and no taxable bonus.

On a weekly gross salary of £311.85 (8.91 x 35 hours), the umbrella company's employment costs are reduced to £66.02 – leaving £117.38 from the received £495.25, for the umbrella company.

It then channels an additional £46.81 to Jess through a **non-taxed element** (received by Jess 'gross', i.e., without tax deducted, in addition to her taxed £311.85) in order to make her net pay up to the same as it was before (£321.68), leaving the umbrella company with £70.57 (£117.38 - £46.81).

Thus, through using a loan arrangement, the umbrella company has made £70.57 rather than its usual £26. Jess is no better off than she would have otherwise been if she had simply received a gross pay of £385.

By using a DR scheme, the umbrella company can increase its profitability very easily and/or pass this money to others in the supply chain to secure future business.

## Appendix 2

Extract from article: <https://www.litrg.org.uk/latest-news/news/211222-umbrella-companies-have-your-say>

### ***What happens in the meantime?***

*Any changes to the umbrella company market that come out of the call for evidence may not take effect for a long time. As such, it is hugely important that workers try and steer clear of problems with umbrella companies that may occur in the meantime.*

*For example, one of the biggest issues is that some non-compliant umbrellas can use disguised remuneration to pay workers. This may not be with the worker's agreement. In fact, as the worker's net pay is often roughly the same or only slightly increased, it can be totally invisible to the worker. We set out the problem in more detail and what to do if you think you are in a disguised remuneration scheme in a [previous article](#).*

*GOV.UK have two new pages of guidance to help you check whether you may be caught up in disguised remuneration – a [risk checker](#) and a [payslip checker](#).*

*You may notice that HMRC's guidance suggests that it is you that could end up having to pay money to HMRC.*

*What underlies a disguised remuneration scheme is a failure to operate PAYE correctly on behalf of the umbrella company employer. The PAYE regulations say that in most instances, HMRC should pursue the employer for any underpayment (HMRC have discretionary powers to disapply the PAYE regulations, but we do not think they would apply in situations like this).*

*If HMRC take that action against the employer, our understanding is that in most cases, the employer will then have a right of action against the employee which – if successful – will end up with the employee being in the same position as if the correct deductions had been made in the first place. We do not think it is for HMRC to make a shortcut straight to the employee – the PAYE regulations must be applied and then it is up to the employer to take any action against the employee that they see fit.*

*Please note that if HMRC ask you to pay back any money as a consequence of being in a disguised remuneration scheme, we suggest you seek some professional advice before doing anything. Take advice from a [professional tax adviser](#) – or if you can't afford one, [TaxAid](#).*