

The Construction Industry Scheme

The Construction Industry Scheme (CIS) sets out special rules for tax and national insurance (NI) for those working in the construction industry. Businesses in the construction industry are known as 'contractors' and 'subcontractors'. They may be companies, partnerships or self employed individuals.

The CIS applies to construction work and also jobs such as alterations, repairs, decorating and demolition.

Contractors and subcontractors

Contractors include construction companies and building firms and also government departments and local authorities. In fact any business spending more than £1 million a year on construction is classed as a contractor for the purposes of the CIS.

Subcontractors are those businesses that carry out work for contractors

Many businesses act as both contractors and subcontractors.

How The Scheme Works

Contractors pay subcontractors for construction operations. Subcontractors must hold either a registration card or subcontractors' tax certificate to be paid under the CIS.

Employees

The CIS applies to workers who are self employed for a particular contract and **not** employees. Employment status depends on general law and it is for the contractor to decide when engaging the subcontractor whether the worker should be treated as employed or self employed. Revenue leaflets IR56 and IR48 help to explain the general principles.

If a contractor takes on a worker as an employee, the contractor should deduct tax and NI from the worker's pay through the PAYE system. If the worker is not an employee they should be paid in accordance with the CIS rules. Broadly if the subcontractor has a registration card (CIS4) the contractor makes a deduction on account of the worker's tax and NI when making payment. If on the other hand a subcontractor has a tax certificate (CIS5 or CIS6) they can be paid gross.

Registering as a Subcontractor

Contractors can only pay subcontractors who have registered with HM Revenue and Customs (HMRC). Most subcontractors qualify for a registration card. Tax certificates are only issued if the subcontractor's business meets certain detailed criteria relating to turnover, business needs and previous compliance with tax law. There is a subcontractors' HMRC helpline on 0845 300 0581.

Registering as a Contractor

Contractors taking on workers who are genuinely self employed or subcontracting work to other businesses must register as a contractor with HMRC. A new contractors pack will then be sent including the necessary stationery as well as guidance.

Cards and Certificates

There are five types of registration cards and certificates used in the CIS.

Registration Cards.

The permanent Registration Card CIS4(P) bears a NI number and does not have an expiry date.

The temporary Registration Card CIS4(T) does not bear a NI number and has an expiry date.

Tax Certificates

The Subcontractors Tax Certificate CIS6 is issued to a qualifying individual in business on his or her own, a qualifying partner in a firm and directors and company secretaries of companies entitled to gross payment.

The Construction Tax Certificate CIS5 is issued only to companies that meet certain requirements.

The Construction Tax Certificate CIS5(Partner) is issued only to partnerships that meet certain requirements.

Registration Cards

Contractors should verify that a registration card is genuine before making payment:

- check the photograph
- check whether the card is permanent or temporary.

When making payment the contractor should:

- make a deduction (currently 18%) on account of the subcontractor's tax and NI
- complete a voucher (CIS25) each month showing pay and deductions; one copy goes to HMRC and the other to the subcontractor.

Should the deduction be made from the whole payment?

Not necessarily. The following items should be excluded when entering the gross amount of payment on the voucher:

- VAT charged by the subcontractor if the subcontractor is registered for VAT
- any Construction Industry Training Board levy.

The following items should be deducted from the gross amount of payment when working out the amount of payment from which the deduction should be made:

- what the subcontractor actually paid for materials including VAT paid if the subcontractor is not registered for VAT, consumable stores, fuel (except fuel for travelling) and plant hire used in the construction operations
- the cost of manufacture or prefabrication of materials used in the construction operations
- any travelling expenses (including fuel costs) and subsistence paid to the subcontractor should be included in the gross amount of payment and the amount from which the deduction is made.

Tax Certificates

The contractor should check the certificate is genuine before making payment.

CIS6

The subcontractor should complete a CIS24 voucher and pass it to the contractor within 14 days of the end of the tax month. The contractor is responsible for entering the contractor reference number on the top copy and forwarding it to HMRC.

CIS5

The contractor must complete a CIS23 voucher on making payment and forward to HMRC.

Annual Returns

Contractors need to complete an annual return (CIS36) which summarises the payments and deductions made during the year.

In addition self employed subcontractors and contractors need to complete an annual self assessment tax return. Any tax and NI deductions made during the year will be deducted from the final tax bill. If the amount already paid or deducted is greater than the total liability, a repayment is due.

Companies that have deductions made from their income as subcontractors, set off these deductions against the amounts payable monthly or quarterly for PAYE/NI due from their employees and CIS deductions from their subcontractors.

Reform

The CIS will be fundamentally reformed with effect from April 2007. The system of subcontractor registration cards and tax certificates is to be abolished. Instead:

- subcontractors will need to be verified with HMRC
- those who would previously have had a tax (exemption) certificate will be referred to as 'registered for gross payment'. Others will be known as 'registered for payment under deduction'. A third classification will be introduced for those subcontractors who cannot be verified by HMRC and are 'unmatched'. A new rate of tax deduction of 30% will be introduced for these unmatched subcontractors.

Checking

When a contractor takes on a subcontractor under the new regime, the subcontractor will provide basic identity details which the contractor will check with HMRC to determine whether payment should be made net or gross. The contractor will not then need to check every time a payment is made to the same subcontractor.

Monthly return

All contractors will be obliged to make monthly returns under the new regime summarising payments made under the CIS. In addition the return must include a declaration that none of the payments relates to a contract of employment. In other words, responsibility lies with the contractor to question each and every subcontractor engagement and confirm that it is not one of employment.

How We Can Help

We can advise on the CIS whether you are a contractor or a subcontractor. We can also give further details on the reform taking place next year.

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