

Championing Compliance Series:

Fact sheet: Compliant Umbrella Companies

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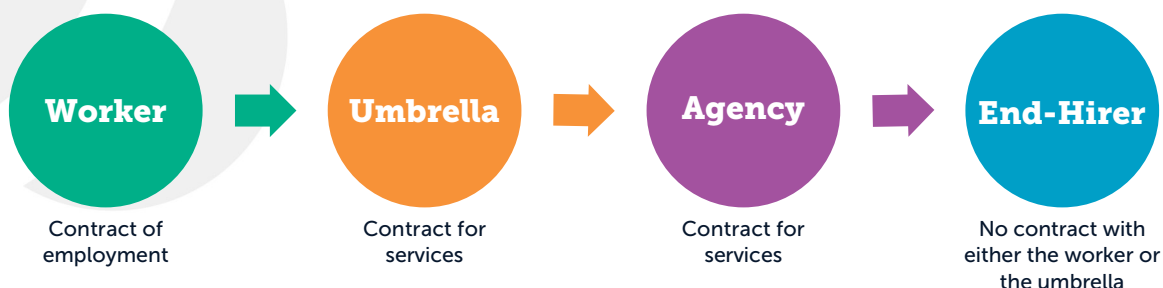
Background

As the largest independent trade association for umbrella firms and contractor accountants, the Freelancer & Contractor Services Association (FCSA) is committed to setting standards for umbrella employers and we want to stamp out any poor or exploitative practices. This factsheet has been prepared primarily for umbrella employees and aims to explain how a compliant umbrella firm operates, and the benefits of choosing to work in this way.

What is an umbrella?

An umbrella company is an employer of contractors and freelance professionals who complete numerous different assignments at various locations for recruitment agencies and/or end hirers. The umbrella enters into an employment contact with the worker, and a service contract with the agency.

The Supply Chain



This mechanism gives the worker freedom to undertake a series of temporary assignments via a variety of agencies/hirers whilst having continuity of employment with all statutory rights and benefits.

Key benefits of umbrella employment to the agency or end-hirer

A fully compliant umbrella employer manages the commercial, employment, taxation, and statutory risks associated with the use of temporary workers for the supply chain. This minimises the overheads, employment risk and administrative burden of managing temporary workers in-house.

The alternative would be to process a significant amount of paperwork each and every time a temporary worker wishes to be redeployed to a different role, agency or hirer. In a fast-paced project-driven environment where workers frequently change assignments, the resulting red tape of treating each change as a new employment would quickly become unmanageable.

Key benefits of umbrella employment to the worker

- **Employment rights**, including all statutory rights and benefits such as holiday pay, maternity, paternity, sick leave, pension etc
- **Employment history** whilst working on a contingent, multi-location basis (notably to support access to finance, housing/mortgages, etc.)
- **Joined up pay from fragmented working:**
 - Many workers will perform multiple assignments during a week or a month
 - Umbrellas consolidate their workers earnings and ensure appropriate taxes are paid
- **Peace of mind that tax is paid appropriately**, with no need to submit an annual self-assessment return to HMRC
- **Employee/HR support**, in the unlikely event that an individual needs HR advice, such as a grievance case, as their employer the umbrella firm will have processes to support them
- **Ability to claim travel and subsistence expenses** subject to status

How pay is calculated

The umbrella firm receives assignment income paid by the agency for the work undertaken. Like any employer, the umbrella must cover employment costs which includes employers national insurance, holiday pay and pension contributions. These employment costs are deducted from the assignment income. Umbrellas also retain a small margin to cover their costs for the services they provide. This is also deducted from the assignment income, and the balance is the workers' gross pay.

The Agency Workers Regulations 2010 provide that umbrella employees receive at least equivalent rights to their full time equivalents, including pay. This means that the assignment rate must usually be greater than the rate which the equivalent employees of the recruitment agency or hirer receive in order to achieve that.

Assignment Income



- Employment costs
- Umbrella margin
- Worker income

Why have umbrella firms become prevalent?

Onshore Intermediaries legislation, set out in the Finance Bill 2014, resulted in agencies being liable for workers PAYE, including employers NICs, unless it is shown that the individual is genuinely self-Employed. This was a significant change for agencies who now needed to either pay their temporary workers via PAYE, or assure themselves that workers are genuinely self-employed. Umbrella firms provided a solution because they employ their workforce and pay them via PAYE.

Misunderstandings about umbrella

Despite the important role that umbrella firms play in supporting contractors, providing all employment rights and ensuring tax and NICs are paid, there are numerous misunderstandings about how umbrellas work in practice. As the trade body for umbrella firms, we strive to ensure that there is transparency regarding how they operate, and here we dispel some of the common misunderstandings:

Misunderstanding 1 – payment of employers national insurance and other hidden charges

When unions first became aware of umbrella firms they were concerned about the apparent deduction of employers' national insurance from workers' pay, however this deduction should be factored into calculating the assignment rate, i.e. it is in addition to workers' gross pay. All employers are legally required to pay employers national insurance, as well process employee deductions.

Umbrellas have always been transparent about how they calculate gross pay, i.e. that employment costs are deducted from the assignment rate. However in some instances this has led to the misunderstanding that employees are paying employers national insurance whereas in fact this amount does not constitute any element of the workers' gross pay.

If a worker is paid via the agency or end hirer payroll, the employers national insurance (and associated employment costs) will still need to be paid in addition to the gross pay – it needs to be factored in somewhere within the supply chain.

Good umbrella companies explain and provide illustrations of these deductions prior to the employment contract being entered into.

Misunderstanding 2 – that umbrella firms are a "scam"

Umbrella firms have never been a scam, they offer a legitimate contractor management solution that enables individuals to receive all benefits of employment whilst working on a numerous different assignments. Good umbrella firms are wholly transparent in their dealings with workers, providing them with a clear contract of employment, all statutory rights and benefits, and transparency in how their pay is calculated.

Misunderstanding 3 – no advantages to working for an umbrella

Contractors working for an umbrella firm are by definition employed by that umbrella firm, and therefore have access to all statutory rights and benefits of employment. This includes annual leave, maternity, paternity, sick pay and pension contributions, and all of these rights are provided for by the umbrella firm.

Misunderstanding 4 – that umbrella employees are self-employed / can't access pension

This is fundamentally incorrect: umbrella firms employ contractors. Anyone working through an umbrella is by definition employed, and not self-employed. By being employed, anyone working for an umbrella firm has the same pension rights as any other type of employment, and all of these rights are provided for by the umbrella firm. Every umbrella firm must provide a pension scheme and automatically enroll employees into it, as every UK employer does, under the Pensions Act 2008.

Misunderstanding 5 – that umbrella firms are a new entity

Umbrella firms have been in existence for some 15+ years. They were formed to service the requirements of professional contractors undertaking a series of assignments who needed specialist back-office support to take care of their tax affairs. Umbrella firms evolved to meet this requirement, enabling contractors to carry out their assignments without also needing to become skilled financial specialists to run their own affairs.

Recent changes in legislation affecting umbrella firms

Legislation changes introduced in April 2016 have resulted in some umbrella employees being placed at financial disadvantage. In short, the changes mean that umbrella employees can no longer receive tax deductible travel and subsistence expenses unless there is evidence that they are not subject to the right of supervision, direction or control as to the manner in which they work. It is difficult to prove the absence of supervision, direction or control, which means that most umbrella employees have now lost this tax deductible benefit.

From April 2017 legislative changes make the public sector liable for tax and NICs for their contractor workforce if they are falsely self-employed. See our factsheet on IR35 changes for more detail.

Umbrellas are a solution because they employ contractors and pay them via PAYE payroll, so we are expecting an increase in people choosing umbrella as a result. It is essential that contractors who are employed by an umbrella firm receive clear information about their gross pay rate and deductions, and all FCSA members are committed to ensuring such transparency.

FCSA tirelessly campaigned against both of these changes. However Government was unwilling to accept our arguments regarding the impact that these changes would have on the very workforce that has supported the UK throughout recent economic recovery. Unfortunately we are now seeing our predictions come to fruition with umbrella employees being financially worse off in many cases.

Many individuals are choosing umbrella employment for the numerous benefits, such as statutory rights, simplicity of tax administration throughout numerous assignments, and consolidated pay with no need to complete an annual self-assessment tax return. We are committed to setting standards for umbrella employers and we want to stamp out any poor or exploitative practices.