HMRC’s reform of the Construction Industry Scheme (CIS) – the implications on IT Systems.
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1. Executive Overview

In April 2007 a new Construction Industry Scheme (CIS) is being introduced. Like the Scheme it is replacing, it will not only apply to mainstream construction businesses but may also include non-construction businesses and other concerns where their average annual spending on construction operations is £1 million or more.

The introduction is likely to require significant changes to either the contractor’s Accounts Payable processes or Payroll systems. If contractors don't already have plans in place to implement the changes in good time for April 2007, then they must start to plan as soon as possible as penalties for non-compliance are automatic and not trivial.

There are a number of basic questions that organisations will need to answer that are covered in depth by various publications from HMRC such as:

- Do they qualify as a ‘contractor’ under the new CIS?
- How has the CIS changed?
- Why has the CIS changed?
- Can my existing software handle the new CIS?
- What are the associated costs of the change?

This White Paper from BASDA brings together issues from just one aspect of the CIS - namely the implications of the new scheme on IT systems. The main issues to consider are:

What Are the Changes to the CIS?

Monthly Sub-contractor Payment & Deduction Statement

Instead of sending paper CIS25 vouchers every month, each contractor must now send a detailed statement to each Sub-contractor if they have made any deductions from the Sub-contractor’s payment during the tax month.

HMRC regulations allow the contractor to send this statement electronically, but only where the Sub-contractor has agreed to this. Otherwise contractors must produce a written statement (which can be a fax). The sub-contractor statement contains significantly more information than a normal Accounts Payable Statement. Business software will need to be updated to meet the requirements of this statutory statement.

Verification

Newly recruited Sub-contractors will need to be verified with HMRC before payment is made – this process can be undertaken by:-

1. Telephone: 0845 366 7899
2. Internet: http://www.hmrc.gov.uk/new-cis
3. Electronically: using either third party software to undertake verification over the Internet or traditional Electronic Data Interchange (EDI).

In the first year of the new scheme, sub-contractors that have been paid since 6 April 2005 do not need to be verified if the contractor was provided with evidence from the Sub-contractor of one or more of the following:

- CIS4(P) Registration Card,
- CIS4(T) Temporary Registration Card with an expiry date of 04/2007, or later
- Tax certificate CIS5 or CIS6, with an expiry date of 04/2007, or later.

To help contractors identify subcontractors who do not need to be verified, the contractor will receive a file from HMRC in November 2006 and again in March 2007, containing details of Sub-contractors that the contractor has paid in the last two years. The contractor should match this file against the details they have in their database for Sub-contractors. Contractors may find inconsistencies with their database – these should be taken up with the Sub-contractor concerned, and not HMRC.

This is a new process and traditional business software is unlikely to have the functionality to undertake this process.

Monthly Return

Contractors must complete a monthly return, to reach HMRC within 14 days of the end of each tax month, detailing all payments made to all Sub-contractors under the CIS in the preceding tax month. The return is for all Sub-contractors whether or not they were paid gross, paid net of the standard deduction or paid net of the higher deduction.

A Monthly Return can be made by one of three ways:

1. Internet: http://www.hmrc.gov.uk/new-cis
2. Electronically: using either Electronic Data Interchange (EDI) or other third party software
3. Paper Return by Post.

Contractors will receive the paper return in the first month – irrespective of how they plan to file in the future (for example electronic filing) unless they have already agreed with HMRC to file electronically.

Most Contractors will prefer to send the complex form electronically – traditional business systems will need to be upgraded or replaced to handle this new functionality.
Technology Considerations

It is essential that Contractors plan for new CIS changes early. Contractors will need to update their business systems and their current CIS third-party software. In some cases software suppliers will only be supporting these changes in the latest version of their software which may mean upgrading older versions of business software.

It may be easier for companies currently using paper-based systems to consider entry-level CIS software to handle the Sub-contractor statements, the complex data recording and the monthly returns to HMRC.

HMRC is unable to present live data to the HMRC CIS Gateway until 6 April 2007. This makes testing of systems and more importantly ensuring that their contractors’ data is clean, somewhat difficult. However HMRC has developed a ‘Desktop Checker’ which can validate the data held on file to ensure that it meets HMRC’s stringent Quality Standard. The HMRC Desktop Checker will be available through your software supplier.

Contractors will be able to send sample verifications to HMRC between 6 April 2007 and 19 May 2007 to make sure that everyone they intend to pay has been correctly set-up in their system. This will also help confirm that their IT function has successfully applied the live passwords or digital certificates that they need to communicate with the Government Gateway.
2. What are the implications of the new CIS?

Introduction

The key aspects of the reform of the construction industry scheme are:-

- Monthly CIS23, CIS24 & CIS25 vouchers no longer required
- No Sub-contractor CIS4, CIS5 & CIS6 Cards / Certificates
- Detailed record keeping required for all Sub-contractors for payments and deductions
- Monthly return to HMRC – paper or electronic
- New monthly Sub-contractor Payment & Deduction Statement
- Tax Treatment Qualification Test (TTQT) applied to Sub-contractors
- Sub-contractor verification – telephone or electronic
- No annual returns

The new CIS for April 2007 has far reaching implications for Contractors. On a practical level when the scheme is in full flow, Sub-contractors no longer need to present themselves and their card or certificate at the contractor’s offices. This will be welcomed by both parties. The move towards electronic credentials is a bold one, and is one way to tackle the issue of counterfeit cards and certificates.

How can Business Software help?

Be it PAYE, VAT, Corporation Tax or Health & Safety, all dealings with Government depend upon accurate record keeping. IT systems are the key tool to keeping consistent and clear records for business activities.

When it is time to complete key monthly and annual returns, efficiency and accuracy are vital – time spent chasing paper or keying data into a spreadsheet is time wasted. Well-managed business software gives the assurance of a single view of the truth, and efficient access to key business data.

Good IT systems with poor procedures supporting them can only generate best guess figures that may lead to penalties or an inspection. The key is to invest in software from BASDA members that can support the changes to CIS.

For the security of all parties, HMRC require that each transaction submitted electronically is encrypted and additionally, carries an “IR Mark”. This is analogous to a wax-sealed envelope to guarantee that the electronic messages have not been interfered with. Many electronic transactions with Government now insist on this form of security.

Most importantly business software can take the grunt out of producing the new complex monthly Sub-contractor statements, which require detailed information to be stored about each Sub-contractor that will also be used for the monthly return to HMRC. Not easy to undertake with paper-based systems – even more difficult to achieve with spreadsheets.

What to look for

Firstly, it is important to be clear about the outcomes that the business needs from the business software. A project manager must be able to measure whether the outcomes have been achieved.

As new CIS will affect many parts of a business, “buy-in” for change from the highest level of management is essential. The project manager will need to define the resources needed and the planned benefits.

Some Contractors will pass their requirements to IT for package selection; in others the business will take responsibility. A good place to start the procurement is the BASDA web site where a broad range of business software able to manage new CIS requirements is listed. See www.basda.org/CIS.

The Project Manager must also consider how new CIS capable business software works with existing systems. There will be no efficiency gains if data is re-keyed from a Payments system into spreadsheets for example - this practice is likely to introduce more errors. It is important that a new CIS system integrates with existing business software.

Success is more likely where businesses work with software vendors to make sure nothing is missed.

Many software vendors will agree to review existing hardware and software to ensure their products will work efficiently, and passing contractual responsibility to the supplier will focus their attention.

It is important to remember that CIS is not unique to the UK, (many other countries operate a “withholding tax” scheme) but the electronic message formats will be specific to the UK. Business software developed overseas may therefore not meet UK requirements.

What difference will a BASDA recognised Business System make?

Using a system from a BASDA member has a number of advantages. Members committed to the “BASDA Code of Practice” will ensure that all of their business software is fit for purpose and thoroughly tested. The Code of Practice brings benefits aside from peace of mind. www.basda.org/codeofpractice

IT Resources

The new CIS being introduced in April 2007 is likely to require significant changes to existing Payments processes and systems. Businesses should have plans in place now to implement the changes in good time.

It is possible that existing systems do not have the capability to store necessary additional information about Sub-contractors. In particular, the regulations covering payments to nominees on behalf of a Sub-contractor are likely to present difficulties.

There will basically be two types of software suitable for handling the new CIS scheme.
CIS – Implications on IT Systems - White Paper

1. Payroll software which, in addition to handling normal employee payroll, will incorporate the functionality to handle the online verification of Sub-contractors, the logging of invoice details, the calculation of deductions, the production of Payment Statements, the incorporation of CIS deductions into the monthly HMRC payment, and the online filing of Monthly Returns. Such systems (priced in hundreds of pounds) will be best suited to smaller Contractors, and those starting up for the first time as Contractors within the scheme.

2. Business software which will incorporate all the functionality to handle CIS as an integral part of the Accounts Payable functions. Such systems will be best suited to medium to large Contractors.

Organisations using packaged payments software should be consulting their business software supplier now, to find out if their systems will support the changes needed, or if there is no direct line of contact, representatives from IT must be fully briefed to represent the business. Many businesses will find that an upgrade for the new CIS is available only with the latest version of the integrated business system. As a consequence the Contractor may have to upgrade or change its whole business system in order to meet the requirements of the new CIS.

The ability to verify Sub-contractor CIS tax credentials on-line is being promoted and actively encouraged by HMRC. Contractors intending to use this facility should have plans in place for IT departments to build the necessary infrastructure to ensure that communications work.

Registration for CIS on-line Filing

Even if a Contractor is presently registered to submit data to HMRC, the company and designated employees must be registered specifically for CIS. The CIS registration is used to authenticate electronic and online CIS transactions with HMRC. BASDA recommends that registration for online CIS should be provided to more than one person to allow for holidays, sickness and meetings – existing PAYE logins will not work! Either the credentials must be shared amongst trusted individuals or the Government Gateway Users and Assistants functionality can be used to set up additional users. Registration for CIS on-line starts on 6th April 2007.

Resources in the business

Not all Contractors will have tax experts to hand, but the detailed knowledge required to run CIS must be disseminated. Accounts staff will need education to use new facilities and should be briefed thoroughly about the new CIS. From October 2007, penalties for non-compliance are automatic and punitive. Organisations should view training as an insurance policy and an investment, rather than just cost.

Operational Managers may see CIS as a back-office problem, but before issuing a contract to a Sub-contractor, whether formally or informally, it is vital to understand whether the Sub-contractor has acceptable tax credentials, because business and business relationships will to suffer if payments received do not meet expectations.

It may seem obvious to the majority, but it is imperative that the business understands when they are treating a worker as an employee. From a legal viewpoint, this complex area is full of subtleties, but should a tax official dispute the status of a Sub-contractor, contracting companies may become liable for tax and NI on payments made.

Rigorous testing of any new systems and procedures is vital. It is important to consider all of the scenarios covered by the new CIS whether individual to a specific Contractor or not, and to ensure that they can be accommodated by modified CIS compliant processes. This inevitably requires that a Contractor must plan to test new systems as well as doing their “day job”.

Tax Treatment and Qualification Test (TTQT)

As part of the new CIS, Sub-contractors will be subjected to a Tax Treatment Qualification Test (TTQT). The purpose of the TTQT is to determine whether a Sub-contractor is entitled to beneficial ‘Gross’ tax treatment or liable to be paid only after deductions have been made at a standard basic rate on the labour charges. The deduction rate will be at a higher rate for ‘un-matched’/unregistered Sub-contractors. TTQT will be initiated when a Sub-contractor applies for registration and at least once a year in the new CIS for all Sub-contractors who are registered for ‘Gross’ payment.

Preparation

Data Integrity

In November 2006 contractors received a list of Sub-contractors (on form CIS333) from HMRC containing details of Sub-contractors that they had paid in the last two tax years. This data was provided to help contractors identify subcontractors who will not need (re) verification and this data should be matched against the details held in payment systems for Sub-contractors. Inconsistencies with payment systems are inevitable: it is incumbent upon contractors to liaise with Sub-contractors to ensure that their systems store the same information as HMRC.

The November CIS 333 showed up those Contractors that had not sent in their recent sub-contractor vouchers, who were then not on the November CIS333. HMRC will be sending out an updated CIS333 in March 2007 so it is important that all the current sub-contractor vouchers are sent in as soon as possible.

For confidentiality reasons, the list will not include any Sub-contractors whose personal details have changed since the last payment where there is no evidence to show that the Sub-contractors had made the contractor aware of the change. For example, if the last payment made to a Sub-contractor was in June 2005 and that Sub-contractor lost their gross payment certificate in January 2006, their name will not appear on the list.

Larger contractors (with over 125 Sub-contractors on file for the last two years) will receive the CIS333 data on a CD, otherwise the list will be sent on paper.

In particular, contractors will need to ensure that personal and trading names, NI Numbers and Company Registration Numbers match with the data that HMRC supply. If a contractor fails to supply a correct reference for their monthly
return, this may raise a compliance warning to be internally investigated by HMRC, and in some circumstances (i.e. if the reference is an invalid format) the return may be rejected, resulting in disruption and possibly a fine. A Sub-contractor may trade under many names, but HMRC systems only recognise one trading name. This is the trading name that new CIS system should use.

Contractors must also act upon the tax treatment listed against each Sub-contractor. Businesses that regularly trade with partnerships should ensure that systems and data reflect the true payment relationships, either to the firm or a specific partner. The March CIS333 will be based on CIS23, CIS24 & CIS25 voucher data for periods up to February 2007 (at the latest), so any new Sub-contractors engaged in the early part of the year should be cross-checked against the CIS333. Any Sub-contractors that start after February, 2007 will almost certainly not be on the list – though they will not need to be verified. (See ‘To verify or not’ below.)

All of this will require effort from both the business and IT: more planning now will pay benefits when the new scheme starts.

Data Protection Act

If an automated system is used to verify Sub-contractors, Contractors should review their Data Protection Registration to cover all of the information stored about their suppliers. Payments to a nominee require that their tax credentials are verified as well, so the registration will also need to cover personal details for third-parties.

Closing off the 2006-07 Tax year

Contractors have until 19 April 2007 to present their 2006-07 CIS payment to HMRC and generate the final CIS23 & CIS25 vouchers. They have until 19 May 2007 to validate and file the (final) annual CIS36 return. Contractors that struggle to do this in good time under normal circumstances should expect that staff working hard to get to grips with the new scheme and changes to payments systems will need extra help to close the old year on time. Resources and workload must be planned carefully and as far in advance as possible.

It is important to reconcile and document the 2006-07 year closing position in as much detail as possible. It will not be possible to make compensating adjustments across the schemes, so it is vital that the cut-over from the old year to the new CIS is as clean as possible. It will save time in the long run.

Change of Tax rate April 2007

Handling the change of deduction rate within a computerised accounting system – notes published by HMRC.

When new CIS begins on 6 April 2007, the standard deduction rate will be 20%. (The rate is currently 18% under the Scheme in force until 5 April).

Where a computerised accounting system is used and where an invoice processed on or before 5 April will not be paid until after that date, the following points should be observed:-

- Where subcontractors are to be paid net, the rate of deduction depends on the date of payment. The standard rate of deduction for payments made on or after 6 April 2007 is 20%

- Where a payment to be made after 5 April is set up on a contractor's accounting system on or before that date, we would normally expect the new rate to be applied

- Where, exceptionally, the system is unable to pick up the new rate in those circumstances, we would not expect the contractor to reprocess the payment after 5 April but we would expect the correct deduction rate to be applied to the next payment.

Where, exceptionally, a contractor’s accounting system has applied the old rate of 18% to a subcontractor’s payment made after 5 April because it was unable to pick up the new rate, the contractor should show the amount of payment and the actual deduction that was made on the monthly return for the month in which the payment was made. Where this has happened, HMRC will not usually regard such action as a compliance failure by the contractor. However, HMRC would not expect to see such under-deductions beyond the return for 5th May 2007, unless there were exceptional circumstances.

Monthly Sub-contractor Payment & Deduction Statement

Instead of sending paper CIS25 vouchers every month, contractors must now send a statement to each Sub-contractor paid under deduction, that is, if they have had any deductions made from their payment during the tax month. These statements will not be a feature of general payment systems as they contain information beyond a typical remittance. HMRC regulations allow the Sub-contractor statement to be sent electronically, but only where the Sub-contractor has agreed to this. Otherwise Sub-contractors must be provided with a written statement, which is deemed to include a fax.
CIS – Implications on IT Systems - White Paper

To ensure that Sub-contractors can receive their statements, it is important to communicate with them in advance of the start of the scheme. If they do not respond, follow-up with another letter or a phone call to make sure that data is correct.

It is important to ensure that the Sub-contractors consent for electronic delivery of statements is kept on file, and that the consent specifies the email address to which communications must be sent.

Common sense suggests that is incumbent upon the Sub-contractor to notify their Contractors if their contact details change. However, this should be put in writing so that the Sub-contractor cannot be critical if they fail to do so. A Sub-contractor “self-service” portal will move the initiative to make the changes onto the Sub-contractor.

Starting the New CIS

To verify or not

Sub-contractors that already have a relationship with a contractor will probably not need to be verified for some time after the start of the new scheme. These Sub-contractors will be listed on the CIS333 list (Construction Industry Scheme. Subcontractors you do not have to verify for payment in new CIS).

Any new Sub-contractors taken on after 5 April 2007 will need to be verified with HMRC before payment is made. In the first year of the new scheme, Sub-contractors who have been paid by a contractor since 6 April 2005 do not need to be verified if, when they were paid, they provided evidence of one or more of the following:

- registration card, CIS4(P)
- temporary registration card, CIS4(T) with an expiry date of 04/2007 or later
- tax certificate CIS5 or CIS6, with an expiry date of 04/2007 or later

Any Sub-contractors not on the CIS333 list who provide up to date credentials before 6th April 2007 can be paid according to the tax treatment that would have applied under the old scheme.

Although many systems have the ability to do so, blanket verification of Sub-contractors is discouraged. When a contractor verifies a Sub-contractor they are confirming with HMRC, either implicitly or explicitly, that “a tender is accepted / contract agreed / order placed for all of the Sub-contractors to be verified”. If this is not the case, then the Sub-contractor should not be verified! Remember that the verification process is recorded against the Sub-contractor’s tax records: HMRC should not be led to believe that the Sub-contractor might be paid if there is no good cause.

Just as importantly, HMRC systems may not be able to meet the demand for this workload, especially at month end when returns will also be submitted electronically.

Implications for Accounting

Where payment systems have been changed to cater for new CIS, business procedures will also need to be updated. For example, any cheques cancelled in the new tax year will need to be treated with care. If they relate to the previous tax year, the Payments team will need to make sure that repayment is not counted again, and contractors should not try to adjust the new monthly returns to compensate.

The processing of credit notes also needs to be carefully reviewed. Credit notes may be netted off against new invoices to reduce the payments due, typically for faulty workmanship or materials. But refunds, as such, are not allowed – and never have been. The rules forbid this – HMRC views this as the contractor refunding tax. Credit notes can reduce the value of a payment not yet made, but refunds against an invoice that has already been settled and reported, must be notified to HMRC by mail or telephone, to effect an adjustment to a previous return. (There is currently no electronic means to perform this transaction).

Technology Considerations

HMRC are unable to present live data to the HMRC CIS Gateway until 6 April 2007. This makes testing of systems and more importantly contractors’ data somewhat difficult.

Contractors will certainly wish to make sure that electronic verification works, but will have to wait until 6 April 2007 to do this on their own data. Most will have completed a number of the pre-packaged test scenarios, but they will not be able to check the integrity of their data until after then.

BASDA recommends that Contractors ensure that their systems and security are working and that data is validated to the required standard by submitting a small, selected sample of Sub-contractors for verification some time after 6 April 2007. As many organisations will be doing this, no-one should submit more than 25 Sub-contractors and include a mix of individual Sub-contractors and a small batch.

Between 6 April 2007 and 19 May 2007, Contractors must make sure that everyone they intend to pay has been correctly set-up in their systems so that when their return is submitted on 19 May, all of the information is correct. If the CIS333 data has been implemented correctly, the return should be accepted. However, if the data is not consistent and there are invalid formats, the return may be rejected. Contractors should ensure that they have successfully applied for all of the live passwords or digital certificates needed to communicate with the Government Gateway.

The New processing timetable

Superficially, the timetable for processing CIS will be little different from the old timetable. The basic deadlines are the same.

All deductions must be paid to reach HMRC by the 19th of the month following the end of the tax month to which the deductions relate or by the 22nd where payment is made electronically. Where the 22nd is a weekend or public holiday, the payment must be received by HMRC on the banking day prior to 22nd.
Contractors must also issue statements to Sub-contractors under deduction by 19th of the tax month to which payment relates.

HMRC is making some allowances for the scale of the changes and will not apply penalties initially. To give systems some time to bed in, penalties (based on the number of Sub-contractors employed) for late returns will not be introduced until October 2007.

During the first few months, BASDA recommends that additional time is set aside to quality assure systems, processes and returns.
3. Implementation of the new Construction Industry Scheme

In this section we highlight the different ways in which business software will be affected by the new CIS, and how IT can be used to reduce the administrative burden. The findings apply to all Contractors that have to comply with the scheme, whether considering implementing business software for the first time, or upgrading an existing system.

**Record keeping**

Contractors are responsible for keeping records of their registered Sub-contractors, the payments that they have made to them and the payment deductions made under CIS. The government also keeps records, but up until now they have been held in disparate systems, with different data held in different systems for the same entity. The 3 government databases (used for Self Assessment, Corporation Tax filing and the current CIS scheme) are now being brought together to provide a single record for each CIS contractor and Sub-contractor.

After the introduction of new CIS the data held by HMRC and the data held by contractors must match. If there are significant discrepancies that do not meet the CIS Data Quality standard then the monthly returns will be rejected. See Section 4 below for the potential data issues that may arise from this exercise.

Some key information needs to be kept for each registered Sub-contractor:

- Registered name
- Unique tax reference: UTR
- National Insurance Number: NINO
- Company Registration Number: CRN
- Registered trading name
- Partner’s name (for partnership subcontractors)
- Partner’s UTR or NINO (or CRN if a company)

Contractors may be holding all this information already, in spreadsheets or in disparate business systems. The implementation of the new scheme provides an ideal opportunity to bring all systems together, and replace spreadsheets with suitable Business Software.

**Communication between HMRC, contractors and Sub-contractors**

One of the most significant changes as far as IT systems are concerned is the way in which communications will be handled between the contractor, Sub-contractor and HMRC. IT systems can be used to streamline the process, with various tools being available to handle the different elements.

- New Sub-contractors should be verified against the HMRC records.
- Contractors will be required to provide a monthly statement to those Sub-contractors paid under deduction.
- Contractors have to submit monthly returns to HMRC, with details of the payments and deductions made to each registered Sub-contractor. These replace the existing vouchers.
- HMRC will provide information to Sub-contractors directly. In particular CIS 313.
- Contractors will be notified of any changes in tax status of the Sub-contractor. 30 days’ notice of the change will be given to contractors (90 days’ notice to Sub-contractors), but it can be disputed by the Sub-contractor. Systems should be able to respond to the following details when received from HMRC:
  - the effective date of any change in tax status
  - if the change is under dispute
  - if the change is no longer under dispute
  - the change of tax status (for example, gross to net)

Note: there is no longer a requirement for contractors to submit an annual return to HMRC.

**Verification**

Verification is the process used to ensure that Sub-contractors have the correct deduction rate made on their payments.

Broadly speaking, there are three steps to verification:

- The contractor provides HMRC with details of the Sub-contractor.
- HMRC checks the Sub-contractor is registered with them.
- The contractor is given a rate of deduction to apply, if any.

Remember that, from 6 April 2007, Contractors do not have to verify any Sub-contractors if they have already included them on any monthly return in that tax year, or have paid them in the previous two tax years.

In any other case, contractors must verify the Sub-contractor. This has to be done before a contractor is able to make any payment to them.

**The information required about the Contractor is:**

1. Contractor’s name
2. Contractor’s Unique Tax Reference (UTR)
3. Contractor’s HMRC Accounts Office reference

**The information required about the Sub-contractor is dependent on the type of business entity as follows:**

1. Sole-trader
2. Partnership
   a. Partnership’s registered or trading name and UTR,
   b. The partner’s UTR or NINO
   c. If the partner is a company - company’s UTR or company registration number.

3. Company
   a. Registered or trading name of company,
   b. company’s UTR,
   c. company’s registration number (CRN).

HMRC records are checked to see if the Sub-contractor is registered with them and contractors are instructed to pay the Sub-contractor either:
1. gross – no deductions taken
2. net - with a deduction at the standard rate
3. net - with a deduction at the higher rate – reason being here is that there is no record of that Sub-contractor’s registration, or they are unable to verify them for any other reason.

Note that the rate applies on the date that the payment is made, not the invoice date. This is the same rule as in the current scheme.

Verification Reference Number will be issued for each Sub-contractor that is verified at the same time. If it is not possible to verify a Sub-contractor, one or two letters are added to the end of the number making it unique to that Sub-contractor.

In the case of the electronic submission in a third party software application, this is done by a process of matching and verification.

The following chart gives an indication as to how this might be done online, behind the scenes via the government gateway, thus simplifying the process for the user:

Verification process – Example Implementation

Verification can be undertaken over the phone or on the HMRC CIS web-site: http://www.hmrc.gov.uk/new-cis. There is a limit of 10 Sub-contractors that can be verified directly at any one time over the phone. If a contractor wants to verify more than 10 subcontractors by phone, HMRC will ring the contractor back within 24 hours. There is also a 100 Sub-contractor limit on the web site.

Contractors with a large number of Sub-contractors or a high turnaround will find it more efficient to use the electronic communication method. This allows the business software to send a message to the Government Gateway. HMRC will return a Verification Reference Number on successful match and verification.

Sub-contractor Payment & Deduction Statement

This can be printed either monthly or for each payment made. Details to be included in the statement are as follows:
1. Contractor’s name
2. Contractor’s address
3. Contractor’s employer’s reference
4. Tax month to which the payments relate (or the date of the payment)
5. Sub-contractor’s name
Monthly returns

Contractors must complete a monthly return to reach HMRC within 14 days of the end of the tax month of all payments made to all Sub-contractors in the scheme in that tax month. The return is for all Sub-contractors whether or not they were paid gross, paid net of the standard deduction or paid net of the higher deduction.

A Monthly Return can be made by one of three ways:

1. Electronically using third party software to submit XML via the Government Gateway or EDI
2. Internet web-submission: http://www.hmrc.gov.uk/new-cis
3. Paper Return by post.

Contractors choosing to use paper returns will receive return forms partially completed by the last day of the tax month that is by the 5th of the month. The names and taxpayer references of all of the Sub-contractors that the contractor has previously returned or newly verified within the last three months will be pre-printed on the forms. Contractors are required to check the pre-printed names and UTR numbers and leave blank entries for Sub-contractors they have not paid in the month, adding names and UTRs of additional Sub-contractors to whom payments have been made in the month. Additionally, verification numbers need to be added for Sub-contractors where higher rate deductions have been made. Details of the amounts paid to each Sub-contractor and details of materials allowed and deductions made from those Sub-contractors not entitled to receive gross payments must all be entered.

Monthly returns need to be signed and if submitting electronically, by confirming the declarations about verification and the Sub-contractors' employment status.

Nil returns will be required from Contractors who have not paid any Sub-contractors in a month and can be submitted in four ways:

1. Electronically using third party software to submit XML via the Government Gateway or EDI
2. Internet web-site: http://www.hmrc.gov.uk/new-cis
3. Phone: 0845 366 7899
4. Monthly return: by completing the section on the monthly return and returning by post.

N.B. Contractors may notify HMRC of up to 6 months of NIL returns in one submission.

Needless to say the process of submitting a return is made significantly easier by using the electronic submissions options available in the form of third party software applications and by EDI for the larger contractor.

There are other issues surrounding the submission of returns associated with any incorrect entry of details on the return; Sub-contractors underpaid or overpaid in error and correcting these errors - but these are beyond the scope of this document and are covered in detail in the Contractor’s packs issued by HMRC (and in information available on the HMRC website www.hmrc.gov.uk/new-cis).

Monthly Return - Electronic Submission

There are two ways of submitting information to HMRC electronically: either automatically using purpose built application software or directly through an internet site.

If a contractor is managing a large number of Sub-contractors the easiest method of submitting monthly returns is by using a packaged software application that can communicate directly with HMRC which will be in one of two ways:

1. Using XML and the Government Gateway. This method is being used currently for PAYE returns and so is now well established as a secure and accurate method of communication. It requires the contractor to register with the Government Gateway. Messages are encoded and sent directly to HMRC by the application software.
2. Using EDI. This was the traditional method used for electronic data exchange but is not widely used today. It is suitable only for organisations processing a particularly large amount of data as it is expensive to set up and maintain. Few software developers are supporting an EDI method of submission.

If a Contractor is only managing a small number of Sub-contractors, or does not have suitable business software, then it is possible to submit verification requests and monthly returns via the HMRC web site: http://www.hmrc.gov.uk/new-cis. With this method all data has to be keyed manually into online forms, which is likely to be time consuming!

Contractors are required to register for on-line submissions via HMRC’s web-site http://www.hmrc.gov.uk. Registration will start on 6th April 2007. Even though the Contractor may already be registered for on-line submissions of other forms e.g. PAYE, they will still need to re-register for new CIS.

All contractors will be sent a pre-populated paper monthly return on 23rd April, 2007 – irrespective of their intention to file by paper or electronically. The paper return should not be completed it the Contractor files electronically.
4. Data Issues

Introduction

Generally with the new CIS it will be of utmost importance to ensure that the data being held against a Sub-contractor is not only correct but matches the data held by HMRC on that Sub-contractor. A failure in the data being sent to HMRC matching to their records could result in the Sub-contractor having the wrong deductions made from their payments (and a potential disgruntled Sub-contractor and all that can entail!). The trading name is, potentially, the most likely cause of problems.

The data quality can also cause failures – for example, a space in a personal name field will be invalid, therefore any double-barrelled names in a field will need a hyphen not a space.

HMRC and Trading Names

In bringing together the new HMRC CIS database, HMRC has linked to data from a number of different databases, perhaps the two most important being as follows:

For self-employed Sub-contractors HMRC data is from its Self Assessment database. This comprises 5 fields:

1. Salutation,
2. First name,
3. Second name,
4. Surname / Family Name
5. National Insurance Number (NINO)

For registered companies the HMRC data is from its Corporation Tax database. This comprises 3 fields:

1. Registered company name
2. Trading name
3. Company Registration Number (CRN).

For electronic verification and the CIS300 Monthly Return, Contractors have to provide three data items, usually the Unique Taxpayer Reference (UTR), Sub-contractor Name and NINO/CRN. For verifications ALL three items must agree with the HMRC database for a full match. For CIS300 Monthly Returns where a full match cannot be made, a partial match, based on UTR and NINO/CRN, will be made. Failing that, further combinations are attempted such as UTR and Name, Name and NINO/CRN etc.

A full match can only be achieved if the Sub-contractor name sent can be matched to that held on the HMRC database. Even the partial match includes a search on a name held by HMRC which may not match any name held on the Contractor’s database. Delays in processing will be inevitable where partial matches are required, so achieving full matches the majority of the time is a sensible objective.

Sub-contractors registering on new CIS will be allowed to specify two names; their Taxpayer name and a separate Trading Name. The Taxpayer name is not held on new CIS but is simply checked against the existing known taxpayer name (held on Corporation Tax or Self-Assessment systems as appropriate).

The Trading Name is held locally on New CIS. On current (Live) CIS, HMRC hold the CIS Record Holder (CRH) Name and an optional Trading As Name. Currently only 13% of Sub-contractors have nominated a Trading As Name. Where a Trading As Name is not provided the Card Name (the name printed on the Sub-contractor’s card) is usually a shortened version of the CRH unless the Sub-contractor has nominated a different card name.

For example:

CIS Record Holder (CRH) = MR J MCLAUGHLIN
CIS CARD NAME = J MCLAUGHLIN
Or
CRH = MR J SMITH
CIS CARD NAME = JAMES SMITH (nominated name)
Or
CRH = JOHNSONS ROOFING & CLADDING LTD
TRADING AS NAME = JOHNSONS
CIS CARD NAME = JOHNSONS ROOF & CLAD LTD (nominated name)

The information held on the Self Assessment and Corporation Tax databases will be brought together for HMRC’s new CIS database and as part of the migration from current CIS to new CIS, HMRC will – as a general rule - be populating the Trading Name field with either the Trading As Name or (where no Trading As Name exists) the Card Name (where this is different from the CRH Name). Sub-contractors who register from 6th April 2007 will receive a notification following registration (CIS313). This will confirm their registered tax treatment and the details they need to pass to the contractor to allow them to be verified. This notification will give their UTR, NINO/CRN and a registered name.

So, what does that mean in practice?

Under the existing CIS for manually produced vouchers (handwritten or printed) returned to HMRC, the name recorded in the computer system to pay Sub-contractors and that used in the production of the vouchers is not critical because any mismatch can be dealt with manually. Those companies currently sending this data via EDI may already have encountered the thorny problem of matching the information required for the voucher with that stored in their software. In the new scheme, matching will extend to every Contractor, whether they make returns electronically or not, because the information for the monthly return will be based on the Sub-contractor’s UTR, name and
NINO/CRN held by HMRC. If the return cannot be matched by HMRC this has compliance implications for the individual Sub-contractor by changing their tax status and, in the near future, financial penalties levied on the contractor for failing to file accurate returns on time. **Initially, matching will be based on two out of the three items but eventually may be changed to all three.**

The details used to set up the account in the business system will not necessarily be the same as the limited information held by HMRC. For Sub-contractors starting with a contractor after 5th April 2007 great care will be required when creating a Sub-contractor account to ensure that the UTR, NINO/CRN and HMRC registered name is entered correctly, as well as the name the payment is to be made to if it is different. The CIS specific element is not standard Purchase Ledger or Employee Record information, so any business software choice will have to be one that is not only CIS orientated, but new CIS compliant as well.

Unless existing Sub-contractor records were set up and updated adhering strictly to the CIS4/5/6 Card details, the bulk of the problems will be encountered when trying to match those records with the information appearing on the pre-printed paper CIS 300 Monthly Return produced by HMRC or its electronic equivalent.

**Don’t despair Help is at Hand!**

Fortunately, HMRC have been prevailed upon by BASDA to send all contractors a Sub-contractor List (CIS333) showing Sub-contractors paid by them in the last two tax years. This will allow them to check their existing records and, where necessary, update them before April 2007.

For confidentiality reasons, the list will not include any Sub-contractors whose personal details have changed since the last payment where there is no evidence to show that the Sub-contractors had made the contractor aware of the change. For example, if the last payment made to a Sub-contractor was in June 2005 and that Sub-contractor lost their gross payment certificate in January 2006, their name will not appear on the list.

Larger contractors (defined by HMRC as having more than 125 Sub-contractors over the two-year period) will receive a CD which can be compared electronically with their data to produce an exceptions report identifying those records that require amendment.

Two mailings of the sub-contractor list are scheduled, one in November 2006 with the final update in March 2007. The data that will be provided in CIS333 will be:-

1. Sub-contractor’s Unique Tax Reference (UTR)
2. Sub-contractor’s name, (- up to 28 char)
3. Sub-contractor’s NINO/CRN,
4. Tax Month last paid
5. Tax treatment (Gross or Net).

N.B. HMRC only records the first 28 characters of the Sub-contractors name – it will have truncated longer names. The longer names can still be used for returns to HMRC.

The CIS333 will have an asterisk (*) in front of each Sub-contractor’s trading name – the asterisk is for information purposes and should be ignored.

Sounds straightforward enough, but remember the Sub-contractor name being quoted is the one held by HMRC not necessarily the trading name recognised by the contractor, making it highly likely it will be different from what is recorded on the contractor’s system. Sensibly, the verification search criteria will have to be based on the UTR.

Where differences are identified the Contractor cannot notify HMRC direct, only the Sub-contractor can initiate changes to HMRC’s database. Thankfully, confirmation of the data held on an individual subcontractor will be sent to both the Sub-contractor and the Contractor. Until then, the name HMRC recognises for the Sub-contractor (or longer than 28 char where applicable) must be recorded for use on any monthly return that might be due. If using the pre-printed CIS 300 Monthly Return - no amendments can be made to the pre-printed items.

**In March 2007, as well as the mailing to contractors, HMRC will be sending confirmation of details held on their files directly to Sub-contractors.** Contractors would do well to make their Sub-contractors aware of this and how important it will be to note the details HMRC will be using.

New Sub-contractors taken on from October 2006 should have their vouchers returned to HMRC as early as possible to ensure they are included in the March 2007 mailing; they almost certainly will not appear in the November 2006 list. Sub-contractors taken on in February 2007 will not appear in the final mailing in March. For these Sub-contractors it would be sensible for Contractors to ask to see their HMRC confirmation letter before April 2007 to ensure information held in their records will allow HMRC to verify their tax treatment for new CIS, otherwise it may be expedient to verify their tax status and include the verification number in the first return of the new CIS.

**What else can go wrong with the data?**

Unfortunately, there is another aspect of ‘data cleansing’ to be considered. To take full advantage of the time saving element of this new scheme, contractors will naturally want to send the CIS 300 Monthly Return electronically. Those already making end of year returns electronically from their payroll will already be aware how sensitive the system is to the quality of the data being sent. In fact, currently, there is a 54 page document – the CIS Data Quality Standard - which details (amongst other things) mandatory fields, maximum field size, validated formats and invalid characters.

Returns not complying with the standard are rejected. A quality standard has been produced for the new CIS which covers everything from the Contractor’s own UTR and Accounts Office Reference number to the Sub-contractor first name, surname, NINO/CRN and UTR. Again, far sighted software companies will have incorporated the means to validate existing data in advance of April 2007. Failing that, contractors will have to trawl through all their records manually to try and spot anything that will fail the standard. Not such an easy task, because something as simple as
having a space as the first character of a mandatory field will cause all the data to be rejected (not just an individual item) yet will not be that obvious to the person doing the checking.

The temptation will be to ‘hope for the best’ and deal with problems as they arise on the first return after April 2007. OK if one or two are returns are problematical but not so good where there are substantial numbers, and that strategy will also rely on the quality of the information coming back from HMRC on which Sub-contractor has been rejected and why. Ask your colleagues in the Payroll Department how ‘user friendly’ HMRC’s error message system is!

**Limited Companies that currently hold CIS4 cards.**

Currently contractors’ records will hold a NINO for the company representative. The CIS333 shows the company registration number. Contractors will probably want to update their records with the Company Registration Number (although it is not mandatory to disclose it on the CIS300 monthly return). Some software packages will provide a facility to upload the Company Registration Numbers from the CIS333 for these subcontractors.
5. Contractors’ Business System Infrastructure

When implementing business software (or changing existing business software) to cope with the new CIS, the factors which need to be considered are similar to those for any other IT system implementation. These factors can be grouped under four headings:

1. Hardware
2. Software
3. Data
4. Users

Successful IT implementation projects are those which give appropriate priority to each of these. Failure to deal adequately with any one of these four areas can lead to a failure of the system implementation as a whole. All four areas require forward planning in order to avoid problems and delays. Remember that depending on the scale of your organisation, implementing change may take several months, so it is wise to check what changes may be required. The detail of what is required is dealt with in other sections of this document. In this section there are some simple checklists of factors to consider under each of these four headings. The amount of time and effort which needs to be spent on each item will vary between organisations dependent on the size and complexity of the organisation. However, these checklists are generally applicable to all contracting organisations that pay a sufficient number of Sub-contractors to consider computerised operation of the new CIS.

1. Hardware

In some cases no change may be required to computer and communications systems, but the areas listed below should be reviewed.

- **Server**: The server on which the system will run (this will often be an existing server but a system upgrade or replacement may sometimes require a new server).
- **Communication**: Connectivity between the server and the internet to allow access to the Government Gateway (this may have already been established for payroll year-end returns or may need to be a new connection).
- **Peripherals**: PCs and printers for users with access to the server (these will generally be existing equipment if new equipment needs to be procured then there may be a lead time involved, so do not leave this too late. Before committing to the purchase of any hardware, compatibility with software and with other hardware needs to be carefully considered).

2. Software

There will be action required under this heading for nearly every Contractor who regularly pays a number of UK Sub-contractors.

- **Upgrade**: Existing business software (which could be a Sub-contractors ledger, payroll or Accounts Payable) will generally require upgrades, patches or fixes to be applied to operate the new CIS scheme (contact your software supplier to check for availability).
- **Replacement**: If existing business software cannot be suitably upgraded, it may require replacement with a suitable alternative
- **Operating System**: Check whether new or upgraded business software will require upgrades to operating system software on the server or on users’ PCs.
- **Compatibility**: Check whether new or upgraded business software will be compatible with other linked software such as BACS or fax software.
- **Manual operation**: If you currently operate the CIS outside of your accounting software (manually or in spreadsheets), you need to consider very carefully whether this will continue to be a practical option for the new CIS. This is only likely to prove practicable for very low volumes of subcontract transactions.
- **Non-UK Sub-contractors**: If you also pay Sub-contractors outside of the UK, you will need to ensure that your existing or proposed accounting software can simultaneously handle the rules for each jurisdiction. This is particularly likely to be an issue for contractors in the Isle of Man and also Northern Ireland who have contracts both in the UK and in Eire.
- **Installation & Configuration**: Software needs to be installed and configured appropriately. Your business software supplier should provide details of any configuration and set-up required.
- **Testing**: Software needs to be tested to ensure that it is correctly installed and operating as required.
- **Test environment**: Testing of software may require the use of a separate copy of the software and data so that testing can cover all relevant scenarios without interfering with live operation of the existing scheme or live data relating to the new scheme.

If new software needs to be procured then there may be a lead time involved in implementation, so do not leave this too late. In this case, remember to also consider the appropriate issues related to Hardware, Data and Users as there are some differences under these headings for new systems compared to upgrading existing systems. It would be advisable to ensure that new or upgraded systems are installed and working at least three months (and preferably longer) prior to the start of the new scheme in April 2007. This will give adequate time for testing and staff training. It will also provide a contingency if implementation is unavoidably delayed.
3. Data

Both static data (such as Sub-contractor name and address records) and transactional data (such as payment details) will need to be considered for nearly every Contractor who regularly pays a number of UK Sub-contractors.

- **Volumes:** The volume of data will be an important factor in planning for the transition to the new scheme. This could affect the choice of hardware and software required as well as the amount of work involved in handling the data issues. Start by gathering statistics on the number of Sub-contractors that are paid each month and how many new Sub-contractors are engaged each month. This will give an idea of the size of your monthly return and the number of Sub-contractor verifications which will be required on a regular basis.

- **Transitional Data:** Consider how you will handle transitional data at the start of the new CIS. You will need to check your existing records against details provided by HMRC in November 2006 and March 2007. One of the main areas to be addressed is the potential mismatch between the Sub-contractor names held on your business system and the trading names used by HMRC. The CIS333 details provided by HMRC will be in electronic format for contractors paying more than 125 sub-contractors or on paper for those paying fewer than this.

- **Data Transfer:** If new business software is being implemented, consider how the initial data will be transferred into it (electronic conversion or manual re-input). This will depend on a number of factors including data volumes, data quality, compatibility of formats, etc.

- **Quality:** System testing needs to include testing the quality of the data. This is particularly important because the data is electronically communicated to HMRC and data errors could ultimately result in penalties.

- **Input:** Consider the responsibility for on-going data input. Remember to include both maintenance of static data (e.g. Sub-contractor names and addresses) and input of transactional data (e.g. payments). Do not assume that these responsibilities can remain the same as under the current scheme: because of the change from viewing physical certificates and registration cards to telephone and/or electronic verification of new Sub-contractors this may need to be different from current responsibilities.

- **Security:** When considering the security of data, remember to consider the back-up and recovery routines for the database which will include the CIS scheme data. Also consider the measures to prevent unauthorised access to the data and your responsibilities under data protection legislation.

Data issues frequently receive insufficient attention in system implementation. It is wise not to underestimate the amount of time and effort required to cover these. There is no need to delay addressing data issues – start as early as possible: certainly when you will receive details of your existing Sub-contractors from HMRC – CIS333.

4. Users

There will be action required under this heading for every Contractor who regularly pays a number of UK Sub-contractors.

- **Scheme training:** Users need to be trained in the requirements of the new CIS so that they understand what HMRC expects and what the implications of non-compliance are.

- **Software training:** Users need to be trained in how to operate the new CIS within the business software.

- **Procedural training:** Users need to be trained in company procedures related to the new CIS. This will normally include authorisation procedures for new Sub-contractors and for monthly returns, also filing of paperwork, etc.

- **Training environment:** Training of users may require the use of a separate copy of any software and data so that they can be trained in all relevant scenarios without interfering with live data.

- **Security rights:** Users need to have the necessary security rights within the software to operate the scheme, while unauthorised users are prevented from such access.

- **Responsibilities:** Users need to know who within the organisation is responsible for the various aspects of compliance with the scheme (because of the change from viewing physical certificates and registration cards to telephone and/or electronic verification of new Sub-contractors this may need to be different from current responsibilities).

- **Help contacts:** Users need to know who to contact for help with different aspects of the operation of the scheme (this may be a mixture of internal staff, HMRC help lines, IT infrastructure supplier and software supplier). Training may be provided internally within the contracting organisation, by software suppliers, by HMRC or by third party training organisations. Different types of training may be provided separately – in this case planning and co-ordination are required to ensure that all relevant areas are covered.

Training for users should not start too early so that it is still fresh in their mind when they start to operate the new scheme. February 2007 would be the ideal time for training. However training will need to be planned and booked well in advance depending on the number of users involved. Between three and six months before the main training, staff should be made aware of the forthcoming changes and how they are being dealt with in outline.

The above checklists can be used both initially when starting to plan for compliance with the new CIS, and later to help review progress.
6. Customer Test facilities

- Before focusing on the new CIS reforms, it is important to check the new upgraded system. Whether the system is large or small, test the upgrade thoroughly - in the case of the CIS reforms, it would be prudent to ensure any 3rd party applications (such as internet gateways and E-mail systems) are functioning as expected.
- If difficulties are encountered contact the system provider(s) immediately.
- Once you have tested that your business software and any third party applications are working correctly, and users have become familiar with the user interface changes or enhancements (however subtle), it’s important to then focus on a number of items relating to the system and the new CIS reforms.
- The quality of data must be considered paramount. Prior to the 6th April 2007, there is the opportunity to ensure that the application is recording details relating to sub-contractors correctly.
- A Desktop Checker has been made available by HMRC for Software Developers and in-turn their customers to test the quality of data against the pre-determined business rules as determined by HMRC.
- It was hoped that HMRC would provide the means for contractors to send test submissions after 6th April. This facility will not be available.
- The following is a list of areas that are critical for the successful compliance with the new CIS

Configuration

- Assuming your business software is configured to be operating as a ‘Contractor’ system, ensure that the system has been updated within its general systems configuration to accommodate the Contractor references (such as the UTR).
- Ensure that all the appropriate Sub-contractors and their details are correct.
- Produce a sample Sub-contractors Statement,
- If filing online, ensure that the online registration has been completed and it is possible to generate a test submission (the level of test submission options will vary between systems) of the new monthly return.
- From 6 April 2007, companies will be able to submit verifications online which will provide confidence that their systems are set-up correctly, credentials are working properly, their data is valid and communications are functioning between the Government Gateway and HMRC. It will be critical to complete registration as close to the 6 April 2007 as registration will take up to 5 days to process prior to being able to send submissions.
- If on-line submissions are not applicable, then produce a facsimile of a monthly return and ensure the information contained within the report is correct.

Accuracy of information

It is critical that the Trading name and supporting information regarding Sub-contractors are correct within the system.
- Ensure that the correct UTR is correct for each Sub-contractor, and is appearing on the monthly return and Sub-contractor’s statement
- Ensure that the NINO is correct for each Sub-contractor, and is present on the monthly return and Sub-contractor’s statement.
- Ensure that the correct verification status has been applied to each of the existing Sub-contractors within the system.
- Ensure that any ‘new starter’ has been applied for a verification status, and the appropriate verification number has been recorded against their record within the system.
- Check to ensure that any payments made that are applicable previously to the CIS reforms are not included on either the monthly return or Sub-contractors statement.

Throughout the transition to the CIS reforms, and indeed the on-going compliance with the scheme, the quality of the data that the return is based on should be validated on a regular basis. Should inaccuracies of data be present, the HMRC has the powers within its remit to levy financial penalties.

What to do if the tests highlight a problem

Should difficulties be encountered with any of the recommended tests listed above, it is imperative that the appropriate system provider is contacted immediately.

If difficulties are encountered, the source of the issue could relate to any one of the number of distinct types of providers of your IT environment. The providers are:
- HMRC
- Business software provider
- Reseller of business software
- Infrastructure provider
- Sub-contractor
- Internal / External IT support

Typically the following examples of difficulties will help determine the appropriate provider.

Contact HMRC for difficulties such as:
- No response from the Government Gateway
CIS – Implications on IT Systems - White Paper

- On-line registration information has been rejected
  Contact your Business Software provider or reseller for difficulties such as:
  - Inaccurate information being reported on the monthly return
  - No Sub-contractor payments are present on the monthly return

Contact the Infrastructure provider for difficulties such as:
  - It is not possible to connect to Internet
  - It is not possible to connect to your network environment
  - The printer is off-line

Contact your Sub-contractor:
  - If HMRC does not recognise the Sub-contractor during verification
  - Sub-contractor not recognised in the monthly return
  - If the Sub-contractor’s details are different to those supplied by HMRC

Contact your Internal / external IT support:
  - If online service not available
  - You are having printer difficulties

Please also consider user error!
7. Risk Analysis

Overview of Risk Analysis

The following should be considered in any risk analysis exercise:

- Data problems
- Inadequate testing
- Poor training
- Jeopardising tax status
- Penalties for late filing and data quality – full scale tax enquiry
- Upsetting Sub-contractors
- Sheer scale of the changeover – impact on business systems – e.g. BT
- Internet connections – firewalls - security

Risk Exposure with new CIS

Contractors need to be able to identify the risks and benefits early on and be able to monitor the risks as an upgrade or replacement business software project develops. The more work undertaken to identify where the risks are, the higher the likelihood that the project will be delivered within the timescales set, to the right level of functionality and quality, but with the bonus of minimum disruption to the business.

In the planning process all areas of the business affected by a new system should be analysed and any risks, or the potential impact of the new system measured. It may be that the system is being installed into two areas within the business – one which is already computerised and the other which is moving from a manual process.

The most effective way to measure the impact is to devise a rating system from, for example 0 – 5 or a simple Low, Medium, High. The criteria can range from no impact right through to severe impact.

Risk Reduction

Once identified you need to reduce your risk exposure on any new CIS projects. This can be achieved in a number of ways such as avoiding the risk (changing the requirements for example), passing on or transferring the risk and finally taking responsibility for that risk. The risk should then be prioritised and this is achieved through ranking and ordering the risks using the rating system.

Risk Monitoring

Every area of the project that has some element of risk attached to it needs to be monitored and tracked to make sure that progress is being made in resolving the risk and that corrective action is being taken where necessary.

Risk Management Plan

The most effective way to manage risk is through a proactive plan. This will allow you to identify, analyse, prioritise and track the risks within your implementation and make it easier for you to manage any issues as they occur.

The plan will make you focus on the high risk issues first and monitor the others as they progress.

Following these recommendations will minimise the number of problems occurring with any new system or upgrade implementation associated with new CIS and make sure projects fulfil business requirements. It will also have a positive effect on staff who are the ultimate users of the system - as you will have taken their needs and requirements into consideration from the outset and their acceptance levels will be greatly increased.

CIS Risk Assessment

This list of potential risks to an organisation that arise with the introduction of the new CIS has been compiled by experienced members of the software industry, and can be used as part of the implementation plan to justify investment in resource and as a check list to a full risk management plan.

As a reminder of the importance of achieving a successful implementation of the new scheme it should be remembered that from October 2007 HMRC has the power to apply financial penalties automatically for late returns!
<table>
<thead>
<tr>
<th>Risk factor</th>
<th>Outcome</th>
<th>Impact</th>
<th>Mitigation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contractor’s new CIS software is not implemented correctly on 6 April 2007.</td>
<td>Errors in the monthly submission to HMRC.</td>
<td>Penalties from HMRC.</td>
<td>Implement automated software from reputable supplier (e.g. member of BASDA).</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Negative impact on company’s tax status.</td>
<td>Timely testing of new software.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Upset Sub-contractors.</td>
<td>Follow instructions from software supplier carefully.</td>
</tr>
<tr>
<td>The organisation is not ready to go live on the new scheme on 6th April 2007.</td>
<td>Monthly returns are submitted late. Incorrect deductions are made from Sub-contractors.</td>
<td>Penalties from HMRC.</td>
<td>Make sure adequate resource is assigned to the project at the cut over.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Negative impact on company’s tax status.</td>
<td>Include sufficient time for staff training.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Upset Sub-contractors.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stressed staff.</td>
<td></td>
</tr>
<tr>
<td>Sub-contractors are not ready to go live on the new scheme on 6th April 2007</td>
<td>Additional hassle for Accounts Payable staff and project managers from Sub-contractors queries</td>
<td>Stressed staff.</td>
<td>Keep Sub-contractors informed about the plans to introduce the new scheme.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Upset Sub-contractors.</td>
<td>Ensure they know what changes they will expect to see in the way they interact with the contractor.</td>
</tr>
<tr>
<td>IT policy does not allow access to the internet for validation and monthly returns.</td>
<td>Validation and monthly returns will have to be completed manually.</td>
<td>Additional resource needed to complete paper forms manually.</td>
<td>Involve IT at an early stage in the implementation plan.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Increased likelihood of errors.</td>
<td>Make sure that adequate firewall protection is installed to protect systems.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Increased cost to the business of compliance.</td>
<td></td>
</tr>
<tr>
<td>Existing Sub-contractor information held does not correspond to HMRC data.</td>
<td>Monthly returns will be rejected.</td>
<td>Penalties from HMRC.</td>
<td>Check records in November 2006 against the CIS333 sub-contractor list provided by HMRC.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Negative impact on company’s tax status.</td>
<td>Check records again when updated list is provided in March 2007.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Contractors should make sure that they send in the vouchers for new Sub-contractors taken on after October 2006 as early as possible to ensure that they are on the Sub-contractor list sent out in March.</td>
</tr>
<tr>
<td>The scale and impact of the changes are underestimated</td>
<td>Cost overrun and missed deadlines</td>
<td>Stressed staff.</td>
<td>Plan the transition carefully.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Incorrect returns.</td>
<td>Take advice from a reputable software supplier or IT consultant.</td>
</tr>
</tbody>
</table>
## 8. Time Line of Events

<table>
<thead>
<tr>
<th>Date</th>
<th>HMRC</th>
<th>Contractors / Sub-contractors</th>
<th>BASDA Recommended Actions</th>
</tr>
</thead>
<tbody>
<tr>
<td>February 2007</td>
<td>Second ‘Burst’ of publicity to Media</td>
<td>File outstanding sub-contractor vouchers</td>
<td>Contractor System Testing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Start Contractor Employee Training</td>
<td>Contractor Employee Training</td>
</tr>
<tr>
<td>March 2007</td>
<td>Second Mailing to contractors with details of Sub-contractors who do not have to be verified. If Contractors have over 125 then this will be sent via a CD Sub-contractors mailing with confirmation of the details held on the HMRC database</td>
<td>Review sub-contractor’s details from CIS 333</td>
<td>Contractor System Testing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Contractor final comparison of Sub-contractor details against HMRC listings</td>
<td>Contractor online registration for online monthly returns</td>
</tr>
<tr>
<td>April 2007</td>
<td>Final Media Advertising</td>
<td>6 April – Contractor trial verification up to 25 records.</td>
<td>Contractor Verification for Sub-contractors not used prior to April 2005 or new Sub-contractors added after February 2007.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>6 April – Go Live of online registration and verification service.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>19 April – Final day for submission of 2006-07 payments to HMRC</td>
<td></td>
</tr>
<tr>
<td>May 2007</td>
<td></td>
<td>19 May – Final day for validation and filing of CIS36</td>
<td>Receipt of first Monthly Statement</td>
</tr>
<tr>
<td></td>
<td></td>
<td>19 May – Final day for returns</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>19 May – Final day for payment of deductions made for April if manual</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>19 May – First Sub-contractor statement production</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>22 May – Final day for payment of deductions made to HMRC if payment electronic</td>
<td></td>
</tr>
<tr>
<td>October 2007</td>
<td></td>
<td>HMRC Penalties implemented</td>
<td></td>
</tr>
</tbody>
</table>
9. Glossary of Terms

**HMRC – HM Revenue and Customs**

**Key HMRC Document Terms**

<table>
<thead>
<tr>
<th>Document</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>CIS300</td>
<td>HMRC form reference for Contractor’s Monthly Return, also communication routing name of EDI Monthly Return message</td>
</tr>
<tr>
<td>CIS313</td>
<td>Sub-contractor notification of registered Tax Treatment. This document will also contain the Sub-contractor individual UTR, NINO/CRN and registered name.</td>
</tr>
<tr>
<td>CIS333</td>
<td>Listing provided to each Contractor detailing Sub-contractors paid within the previous two years.</td>
</tr>
<tr>
<td>CIS340</td>
<td>The HMRC Guide for contractors and Sub-contractors setting out the operation and rules for CIS.</td>
</tr>
</tbody>
</table>

**Glossary of Terms**

<table>
<thead>
<tr>
<th>Term</th>
<th>Meaning</th>
</tr>
</thead>
</table>
| Accounts Office Reference / Employer Reference No | This is an HMRC reference number for the contractor which must be quoted on monthly returns and verification requests. It is made up of two separate numbers:-  
  • The Tax office – numeric - 3 numeric  
  • The employer number – alpha numeric – up to 10 char  
    ♦ character 4 must be ‘P’  
    ♦ character 5 must be uppercase alpha  
    ♦ characters 6-13 must be alphanumeric  
  E.g. 123PZ12345678 |
| CIS                                 | Construction Industry Scheme                                                                                                                                                                          |
| Construction Operations             | The scheme covers payments for construction operations which are defined in paragraphs 2.41 to 2.44 and Appendices A and B of CIS340.                                                                    |
| Contractor                          | A contractor is a business or other concern that pays Sub-contractors for construction work. Defined in CIS340 - paragraph 2.4.                                                                          |
| Contracts                           | A contract means any legally binding agreement or arrangement under which one individual or business does work or provides services for another individual or business. See CIS 340 paragraph 2.40 for details. |
| CRH                                 | CIS Record Holder (name) e.g. F J Smith                                                                                                                                                                |
| CRN                                 | Company Registration Number e.g. 1234567                                                                                                                                                               |
| Deductions                          | A deduction is the amount that a contractor has to withhold from a payment made to a Sub-contractor.                                                                                                     |
| Deemed Contractor                   | Under the new CIS, some organisations outside the construction industry which carry out or commission construction work are deemed to be contractors if their average annual expenditure on Contractors exceeds £1 million. See CIS340 paragraph 2.6 for details. |
| EDI                                 | Electronic Data Interchange – this was the traditional method of electronic transfer which is still an alternative to the internet as a means of communicating electronically between a contractors system and HMRC. However, this is no longer supported by most commercially available CIS software packages. |
| Employer’s Reference No Accounts Office Reference | This is an HMRC reference number for the contractor which must be quoted on monthly returns and verification requests. It is made up of two separate numbers:-  
  • The Tax office – numeric - 3 numeric  
  • The employer number – alpha numeric – up to 10 char  
    ♦ character 4 must be ‘P’  
    ♦ character 5 must be uppercase alpha  
    ♦ characters 6-13 must be alphanumeric  
  E.g. 123PZ12345678 |
<p>| Employment Status                   | For a contract to be within the new CIS, it must not be ‘a contract of employment’. This means that the Scheme applies to workers who are self-employed under the terms of the contract, and who are not employees subject to Pay As You Earn (PAYE). Contractors are required to declare on their monthly return to HMRC that the employment status of all Sub-contractors has been considered. |
| Government Gateway                  | Centralised registration service for e-Government filing services allowing the exchange of electronic data.                                                                                           |</p>
<table>
<thead>
<tr>
<th><strong>Higher Rate</strong></th>
<th>The rate of deduction required to be made from unmatched Sub-contractors</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>HMRC</strong></td>
<td>Her Majesty’s Revenue and Customs – the government department responsible for collecting taxes combining the former Inland Revenue and HM Customs &amp; Excise</td>
</tr>
<tr>
<td><strong>IR-Mark</strong></td>
<td>A cryptographic message digest algorithm using Canonicalised XML - means of proving that the data sent was the data received – non-repudiation.</td>
</tr>
<tr>
<td><strong>Matching</strong></td>
<td>Matching is similar to verification, but for those Sub-contractors who are unmatched no unique verification number will be issued (and no payments may be made). This gives the contractor the opportunity to check the details before resubmitting for matching or verification.</td>
</tr>
<tr>
<td><strong>Monthly Return</strong></td>
<td>Each month, contractors must send HMRC a complete return of all payments made to all Sub-contractors within the Scheme in the preceding tax month. This can either be sent electronically or on paper. Nil returns will be required.</td>
</tr>
<tr>
<td><strong>NINO</strong></td>
<td>National Insurance Number – format AANNNNNNA – uppercase only</td>
</tr>
<tr>
<td><strong>P35</strong></td>
<td>Employer’s Annual Return to HMRC which must include the total of deductions from Sub-contractors under CIS as well as from employees under PAYE</td>
</tr>
<tr>
<td><strong>Payment and Deduction Statement</strong></td>
<td>The contractor must provide a written statement to every Sub-contractor from whom a deduction has been made within 14 days of the end of each tax month. There is no set format but certain information must be included. The statement can either be provided for each payment or monthly to cover all payments in the month.</td>
</tr>
<tr>
<td><strong>Payments</strong></td>
<td>A payment is anything paid out by the contractor to the Sub-contractor under a contract for construction operations. This applies whether or not the payment is made directly to the Sub-contractor. See CIS 340 paragraph 2.34 for details.</td>
</tr>
<tr>
<td><strong>Standard Rate</strong></td>
<td>The rate of deduction from matched (registered with HMRC) Sub-contractors who are liable to deduction</td>
</tr>
<tr>
<td><strong>Sub-contractor</strong></td>
<td>A Sub-contractor is a person or body that has agreed to carry out construction operations for a contractor on a self-employed basis. See CIS 340 paragraph 2.24 for details.</td>
</tr>
<tr>
<td><strong>Sub-contractor Statement</strong></td>
<td>Monthly statement produced by the contractor detailing all payments made to all Sub-contractors for the previous Tax Month – nil returns not required</td>
</tr>
<tr>
<td><strong>Tax Month</strong></td>
<td>A HMRC designated period for taxation purposes spanning from 6th of one month to the 5th of the next month</td>
</tr>
<tr>
<td><strong>TTQT</strong></td>
<td>Tax Treatment Qualification Test – the test by which HMRC determines the tax status of the Sub-contractor (Gross or Net).</td>
</tr>
<tr>
<td><strong>Tax Year</strong></td>
<td>HMRC Tax year runs from 6th April to the 5th April the following year.</td>
</tr>
<tr>
<td><strong>UTR</strong></td>
<td>Unique Taxpayer Reference. The contractor and Sub-contractor will each have a UTR which needs to be recorded within the contractor’s records. This will be a ten digit number.</td>
</tr>
<tr>
<td><strong>Verification</strong></td>
<td>Verification is the process whereby a contractor checks the tax status of a Sub-contractor with HMRC. If the Sub-contractor details are matched, this will result in the contractor being informed that payments should be made either gross or net of deductions at the standard rate. If the details are unmatched the contractor will be given a unique verification number for the Sub-contractor under which payments must be made at the higher rate of deduction. See also matching.</td>
</tr>
<tr>
<td><strong>XML</strong></td>
<td>eXtensible Markup Language – the open standard for the exchange of data over the Internet. This is an optional standard to be used for communication with HMRC.</td>
</tr>
</tbody>
</table>
Useful Contacts:

CIS Helpline – 0845 366 7899
CIS website – www.hmrc.gov.uk/new-cis/
BASDA CIS Knowledgebase – www.basda.org/CIS

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<td>01206 322575</td>
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</tbody>
</table>