

Written evidence submitted by Dave Chaplin, tax expert in the freelance sector (FB12)

Finance (No.2) Bill: Call for evidence on 16 Jan 2026.

Capacity in which made: Personal.

Re: Clause 24: Umbrella Companies

Purpose:

There is a sensible refinement needed: expand the conditions under which "the client" can become a relevant party.

Background:

Clause 24 is designed to address the tax issues with non-regulated umbrella companies: These are:

- a) workers are being **forced to use umbrella companies**.
- b) Umbrella companies are pickpocketing workers' pay.
- c) workers being **overcharged to be payrolled**.
- d) Umbrellas are going bust, having **borrowed treasury money** to provide lending.
- e) Treasury is **losing circa £1bn per year** due to **tax avoidance/evasion**.

In my view, clause 24, which inserts a new Chapter 11 ITEPA 2003, requires two refinements to:

- 1. Give the "client" skin in the game (they become a relevant party) if they promote or influence the use of umbrellas by agencies.
- 2. Prevent clients and agencies from "forcing" a worker to use an umbrella who does not want to.

Reality on the ground

Employment businesses (recruiters) currently **force** the use of umbrella companies because they **turn internal payroll costs into profit via kickback commissions from umbrella companies**.

The combination of forcing & commission kickbacks **ignites the "race to the bottom"**. It **fuels aggressive tax avoidance/evasion** – the more money the umbrella can **take from the workers' wages (or not pay to the Treasury)**, the **higher the kickback paid to the employment business**, encouraging more workers to be sent their way.

Umbrellas are unregulated, and some rely on cash flow generated by stalled tax payments to **effectively provide unlicensed lending to agencies**. When agencies are unable to pay, **the umbrella goes bust**, with no consequences and the owners just phoenix and start again.

That's the racket.

The purpose of Chapter 11

The underlying principles of Chapter 11 are to make the employment business and, in some cases, their customer (the "client") liable for the unpaid tax bills of those below, without any defence available, thereby producing a behavioural effect where the clients and agencies police the market and prevent bad actors from entering the supply chain.

"Relevant parties" take on joint and several liability for the tax owed.

Current design

A "relevant party" (61Z) will be jointly and severally liable with the umbrella (61Y(2)).

Where there are multiple agencies in the supply chain between the client and the umbrella, the top agency is held accountable (61Z(1)).

If there is no agency, the client is on the hook 61Z(2)(a).

If there is an agency on the hook which is "connected" to the umbrella company, then the client is also on the hook (61Z(2)(b)(i)).

All the above is good, but **it's not enough**.

Problem with the current draft of Chapter 11

Amendment #1

Employment Businesses are at the mercy of their clients. It is not uncommon for clients to dictate to their agencies which umbrellas must be used.

However, under the new Chapter 11 rules, if the client dictates to the agency and the agency uses an unconnected umbrella that goes wrong, the client is not on the hook for the lost tax. They should be, because they dictated the umbrella(s) used.

An update to 61Z can resolve this.

After 61Z(2)(b) Insert clause 2(c):

61Z Relevant parties

- (1) If the contract referred to in subsection (4)(a) of section 61Y is between the umbrella company and a person other than the client, the person referred to in subsection (4)(c)(i) of that section is a relevant party.
- (2) The client is a relevant party if—
 - (a) the contract referred to in subsection (4)(a) of that section is between the umbrella company and the client, or
 - (b) the person referred to in subsection (4)(c)(i) of that section—
 - (i) is connected with the umbrella company, or
 - (ii) is non-UK resident.
 - (c) the client promotes, influences or facilitates the use of any umbrella company to either the another person in subsection (4)(a)(ii), or the person the in subsection (4)(c)(i).

Amendment #2

The "race to the bottom" mechanism, in which an umbrella pays kickbacks to agencies, promotes the race to the bottom.

Clients need to police this by giving them an incentive. If it occurs, then the client must be a relevant party.

A further clause can be added to 61Z(2) as follows:

- (2) The client is a relevant party if—
 - ...
 - (d) either the another person in subsection (4)(a)(ii), or the person the in subsection (4)(c)(i), directly or indirectly receives any fee (or monies worth) from the umbrella company in consequence of the worker being employed by the umbrella company, or receives monies or money's worth for promoting, introducing, or arranging the purchase of services by the worker from the umbrella company.

The proposed new 61Z(2)(d) is intended to eliminate the practice of an umbrella company paying or providing another form of financial benefit to an employment business so that the employment business can make the provision of work conditional upon the worker using such a service.

Payments, or the provision of benefits for money's worth, by umbrella companies to employment businesses, increase the likelihood of bad behaviour. It is recommended that payments or provision of financial benefits by any umbrella company, whether or not owned by an employment business, should then trigger the client becoming a "relevant party."

Effect

The two new amendments should achieve:

- Preventing umbrella kickbacks to employment businesses and **curbing the financial motivation for allowing tax avoidance/evasion.**
- **Preventing the client from dictating the use of a specific umbrella company without being liable** for any tax loss as a result of the umbrella company not paying the correct tax.

It is envisaged that employment businesses will provide workers with the choice of either:

- (1) processing payroll internally (as per Chapter 7 of Part 2 of the Income Tax (Earnings and Pensions) Act 2003)
- (2) using an external payroll provider, or
- (3) continue to use umbrellas, but pay the taxes directly to HMRC

Clients will then police the agencies to ensure they do not become a "relevant party", thereby eliminating the "race to the bottom" behaviour fuelled by umbrella kickbacks.

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