

Construction industry scheme: landlord payments to tenants for tenants works

General Features

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The CIOT has written to HMRC on the business and administrative burdens of operating the Construction Industry Scheme on landlord contributions to tenant's works.

The Construction Industry Scheme (CIS) requires a contractor to withhold tax from payments to subcontractors for certain construction work. The scope of CIS means that it extends (or it may extend) to landlords making payments to tenants where tenants have contracted to carry out construction works, unless the payments fall within the definition of reverse premiums.

Landlord payments to tenants for landlord works (Cat A) and landlord contributions to tenants for tenants' works (Cat B), or a combination of both, are becoming more common as landlords work more closely with tenants to assist them in obtaining early possession and/or to model space to suit their needs, instead of tenants having to remodel the building.

Although the reverse premium exclusion provides an exemption for landlord to tenant payments for tenants' fit-out works, it is of limited and sometimes uncertain application. To fall within that exception, the relevant payment must be a pure 'inducement' in connection with a transaction being entered into by that person or a connected person, for example in connection with a tenant entering into a lease. A common problem area is where the tenant's works are not clearly identifiable as basic tenant fit-out works.

Where these issues arise, the question of the application of CIS may not be identified until a fairly late stage, if at all.

If the reverse premium exemption does not apply, it will be necessary to undertake detailed investigations to ascertain whether the landlord is or could be a deemed contractor and to identify the nature of works. Accordingly, landlords are forced into adopting an overly-cautious approach and apply CIS by default, at the expense of tenants because incorrect classification results in disputes with tenants and potentially significant tax liabilities and penalties.

For tenants who are, or could be, affected, obtaining a gross payment registration can take some time and is often impossible to achieve within the transactional timetable. Administratively, registering as a sub-contractor is a significant burden on tenants outside the construction industry in totally unrelated industries. Additionally, obtaining gross status is far more difficult if tenants are setting up business or expanding into the UK as they will not have a trading history.

CIS also applies if one company in the group acts as developer under a development management agreement providing services to another group member. The company providing the services to another group member will have to register as a sub-contractor as above but additionally act as a deemed/mainstream contractor in respect of the contracts it operates with 'genuine' third party contractors.

The CIOT's submission suggests that given the wider policy intent of the scheme, consideration should be given to a wider exclusion to remove from CIS all contribution payments made by landlords to tenants in connection with the grant, variation or assignment of a lease whether for tenant's fit out or for landlord's works. In addition, consideration might be given to removing the administrative burden of operating CIS in a group context where one company in the group acts as developer under a development management agreement providing services to another group member.

The full CIOT submission can be found on the [CIOT website](#).