

AML ALERT: Payroll Company Fraud

Extract from NCA Amber Alert – July 2020 (Reference 0618-NECC)

Overview

Payroll Company Fraud (PCF) is the outsourcing of labour and payroll responsibilities by active businesses to fraudulent entities, calling themselves 'payroll companies' and controlled by Organised Crime Groups (OCGs), who supply labour to the businesses but fail to remit all of the correct taxes owed to HMRC, including Income Tax, National Insurance Contributions (NICs) and Value Added Tax (VAT).

The active business may be unaware that the 'payroll company' is engaging in fraudulent activity. Also, the workforce may also be unaware that anything is wrong as they perform the same duties as they did prior to the involvement of the 'payroll company' for the same net pay.

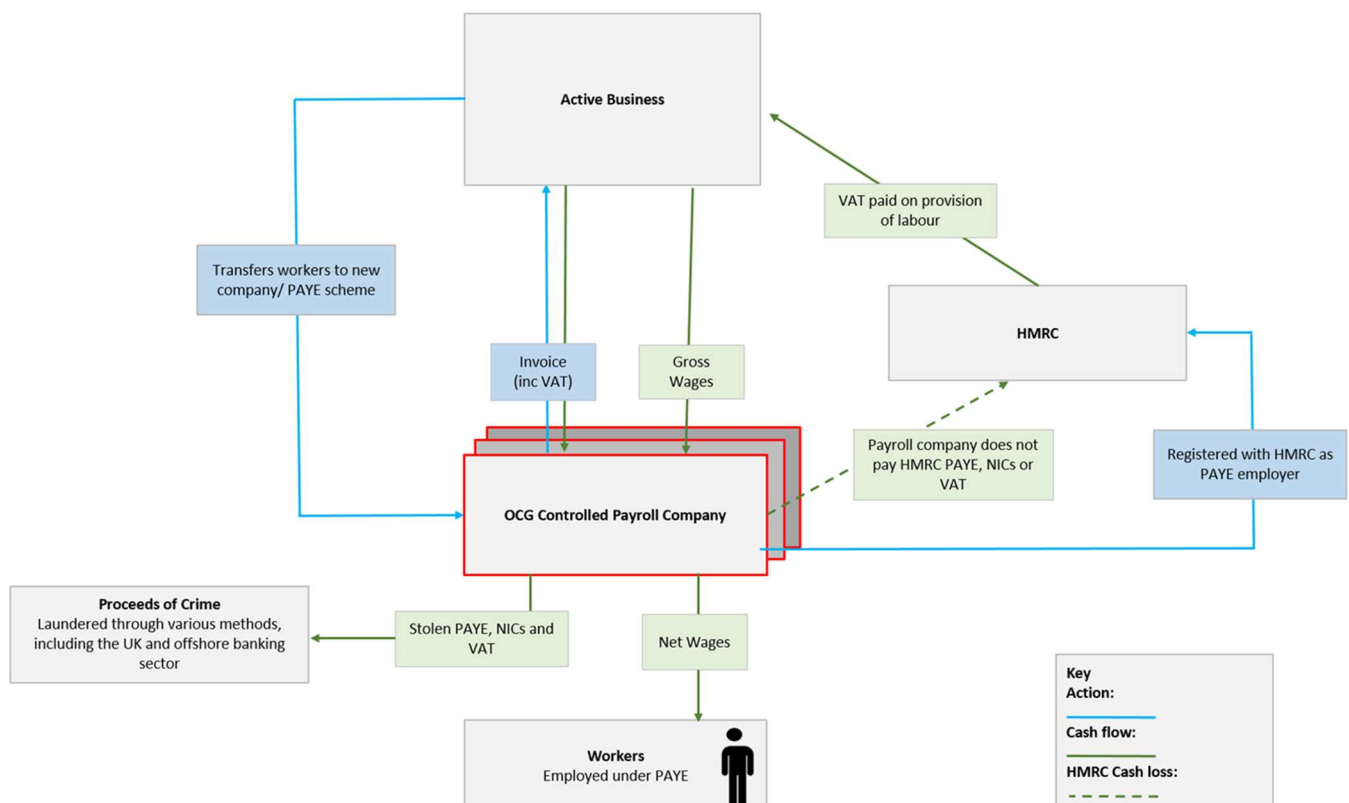
Tax loss is not the only consequence of PCF, there are other further effects on employees.

- Non-payment of employee NICs, which can affect their right to pensions and benefits
- Non-payment of employee pension
- Links to illegal working, modern slavery, shadow workforces and national minimum wage issues

The following models illustrate examples where the proceeds of crime can be syphoned off at any point in the chain.

Model 1 – Simple Start-up Model

As the chart below demonstrates, OCGs use a small number of companies running in succession to perform the entirety of the payroll duties for the active business.² The fraudulent company registers as the workforce's new employer with HMRC and the workers are transferred to their PAYE scheme. The 'payroll company' invoices the active business for the supply of labour. The value of the invoice is usually equivalent to the workers' gross wages plus a small fee plus VAT. The active business pays the fraudulent company who pay the workers their net wages. However, the Income Tax, NICs or output VAT are not fully remitted to HMRC.

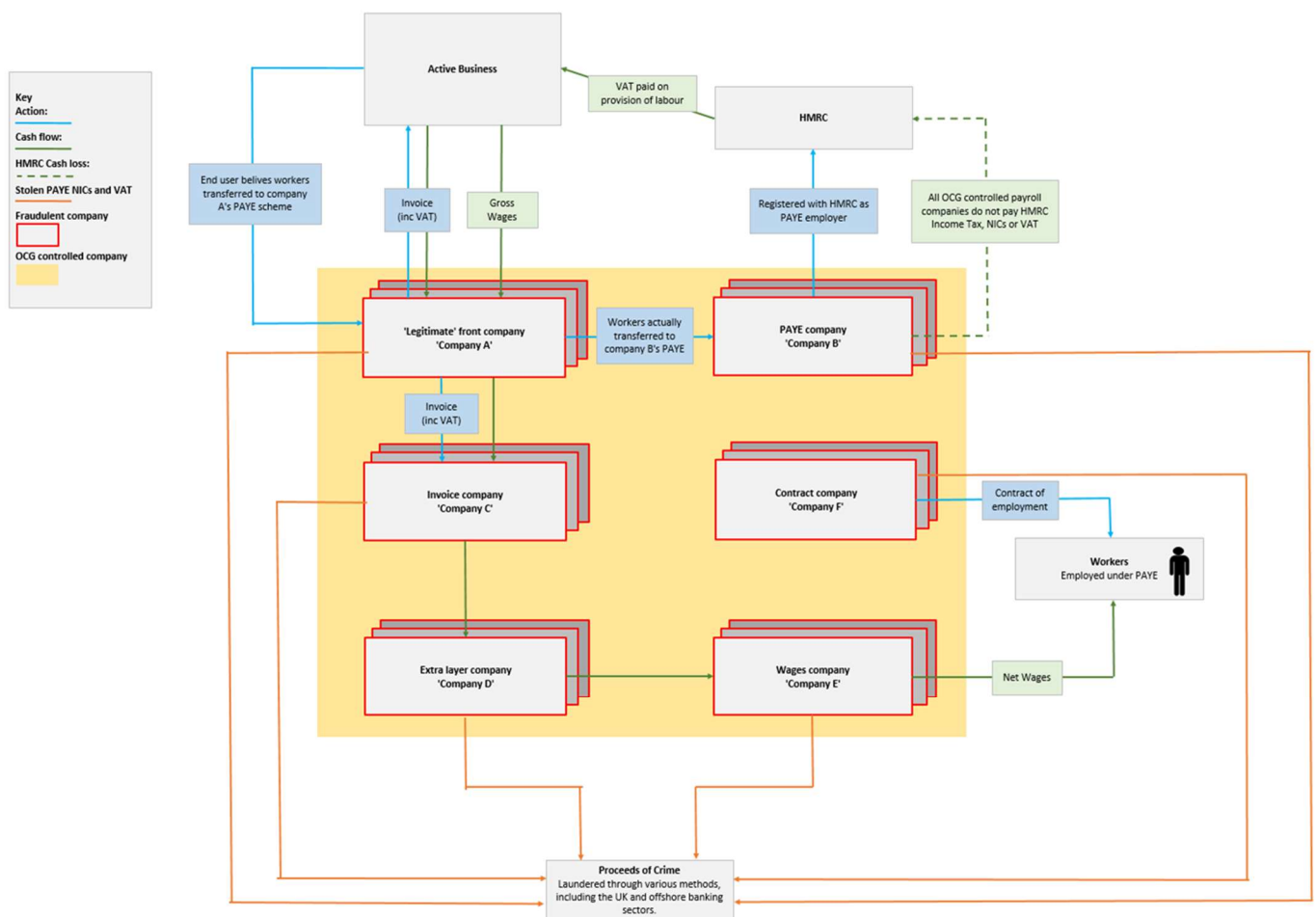


Model 2 – Established PCF Model

In model 2 OCGs use a larger number of companies to perform the function of one payroll company, creating a longer and more complex supply chain in an attempt to conceal which company is actually liable for the unpaid taxes.

The number of companies and the structure may vary considerably in more complex structures. In the model below, provided for illustration, the companies perform the following functions:

- 'Legitimate' front company – engages with the customer and is the professional face of the business.
- PAYE company – runs the payroll and engages with HMRC.
- Invoice company – creates invoices for the supply of staff. May invoice the front company for onward invoicing or may invoice the customer direct using a similar name as the front company.
- Extra layer company – provides no function other than as a buffer.
- Wages company -
- Contract company – the 'employer of record' for the workforce.



Indicators of PCF

As with all indicators, a combination is a better indication of wrongdoing and it is unlikely that one indicator, alone, is indicative of misconduct. Therefore, we recommend you use this list of indicators alongside existing business processes and procedures. The lists below are not exhaustive.

- Registered Office address is not reflective of trading activity.
- A Director's past employment and/or business history suggests they lack the experience required to run a Payroll Company.
- An unusually high rate of changes in directors and/or Registered Office addresses.
- Directors have a history of phoenixing companies.
- Directors are foreign nationals.
- The Payroll Company's prices are too good to be true.
- Multiple iterations of one company, with similar names.
- A lack of online presence, often preferring social media advertising to a company website.
- There is not specific Trade Classification Number (TCN) for payroll companies. There are common TCNs which are used. However, as mis-classification often occurs, nothing should be discounted.

Suspicious Activity Reporting

If you know/suspect ML or terrorist financing activity you should make a SAR and include the reference **0618-NECC** within the text *in addition* to the ongoing use of the Glossary of Terms.

Guidance on reporting is available at: www.nationalcrimeagency.gov.uk.

Data Protection Considerations

Please consider your obligations under the relevant data protection regulations and where necessary remove any related personal data from your systems securely and within a satisfactory timeframe.

Glossary

- *Phoenixism*: a company is liquidated or discarded and subsequently its business is carried on under the same or broadly the same ownership via a new entity. Companies used to perpetrate PCF tend to trade for 12 – 18 months before phoenixing to another company.
- *Construction Industry Scheme (CIS)* is a UK government scheme that regulates and monitors the tax of individuals and companies in the construction industry, involving tax deducted at source by contractors from payments made to their subcontractors relating to construction work. More information can be found here: <https://www.gov.uk/what-is-the-construction-industry-scheme>.
- *Gross Payment Status (GPS)* is a UK Government initiative that enables contractors and subcontractors working in the construction sector to receive payments without CIS deductions at source. Companies will still be required to pay all of their tax liabilities but the initiative helps improve a business's cash flow and subcontractor reputation. More information can be found here: <https://www.gov.uk/what-you-must-do-as-a-cis-subcontractor/gross-payment-status>.

Useful resources

Businesses can find out more information about the general risks posed by PCF via the following link: <https://www.gov.uk/government/publications/use-of-labour-providers>.

Disclaimer

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