

The 2026 UK umbrella regime



December 2025

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Why is the umbrella tax legislation being introduced?

The "umbrella company" tax legislation, published in the Finance Bill on 4 December 2025, will now form the new Chapter 11 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA). Those who use umbrella workers (clients), agencies, managed service providers (MSPs), and umbrellas have four months to plan and prepare before the new legislation comes into force on 6 April 2026.

Why is the umbrella tax legislation being introduced?

Tax non-compliance by certain umbrella companies is seen as one of the biggest risks within UK labour supply chains. The government has, therefore, introduced new tax legislation to try to ensure that umbrella workers are taxed as employees and to make it harder for unlawful tax avoidance and tax evasion schemes to operate.

What is not changing?

Umbrella companies will still be able to hold the employer's reference number which means that they will still be able to pay workers through their own PAYE payrolls.

What is changing?

The new umbrella legislation introduces joint and several liability between the umbrella company and either:

1. *the top agency* (that holds the contract with the client); or,
2. where there is no agency in the supply chain (or the agency is offshore or the agency and the umbrella company are connected) *the end client*,

for any tax that is not paid to HMRC by the umbrella company, for whatever reason.

Joint and several liability will be triggered where an umbrella operates a compliant payroll but fails to pay tax in full – this will be the case regardless of the reason for the tax default. So, regardless of whether the default is caused by non- or late payment by an agency, or a historic tax liability or general trading problems, joint and several liability will be triggered. It is important to note that none of these reasons would be uncovered by payslip or payroll compliance checks.

Liability will also pass where the top agency or end client, as the case may be, has carried out checks but been deceived by the umbrella about how the workers are paid. "Trying our best to check" or "hiring third parties to do market leading checks" are no defence under the new regime.

What is an 'umbrella company' under the new legislation?

The legislation applies to "umbrella company arrangements".

This term includes any arrangement whereby an individual is supplied to personally provide their services via an intermediary that employs them under a contract of employment or of service (an umbrella company), or which it is reasonable to suppose employs them (a "purported" umbrella company).

Who is caught – what is an 'umbrella company'?

Umbrella companies are broadly defined and will include:

- companies that identify as umbrella companies;
- employers of record (EOR);
- consultancies which employ the individuals under contracts of employment and second or deploy their services to end clients;
- agencies which employ or engage individuals on contracts of service;
- hire train-to-deploy suppliers which employ individuals they train and then deploy to clients; and
- any "purported umbrella company" – see more on this below.

What is *not* an umbrella company?

- Agency workers who are engaged under contracts for services (rather than a contract of service/employment) by the agency and paid on the agency's payroll will not be caught. The existing tax legislation under Chapter 7 sections 44-47 ITEPA, often referred to as the "agency tax regime", will continue to apply. The new umbrella legislation will not apply where the agency tax regime applies.
- Independent contractors who provide their services through a personal services company (PSC) are not caught. Most PSCs are excluded from the definition of umbrella company arrangements. The IR35 and off-payroll working regimes will continue to apply to these types of engagement. The exceptions to this are so-called mini umbrella companies and PSC arrangements which are caught by the "purported" umbrella provisions. For example: where an umbrella company tells agencies and/or end users that it employs and pays workers through its PAYE payroll but it, in fact, pays them gross via their PSC, that will be a purported umbrella arrangement and fall within the new umbrella regime.
- Construction Industry Scheme (CIS) subcontractors who engage workers via so-called "CIS umbrella" companies and engage those subcontractors on a self-employed basis are, similarly, not caught by the new legislation. However, "CIS umbrellas" will need to ensure that all parties in the supply chain know that CIS subcontractors are paid as self-employed and not via a PAYE payroll so as to avoid being caught as a purported umbrella company. As with agency payrolls, the agency tax regime (Chapter 7) will continue to apply to CIS umbrellas unless it can be shown the individuals are not subject to supervision, direction or control by anyone as to the way in which they work.

What is an 'umbrella company' under the new legislation?

Closer look at purported umbrellas

The final legislation sets out three cases where purported umbrella arrangements will be deemed to exist. These are broadly where an entity:

- Case 1 – holds itself out as or is assumed to be the employer of the worker but is not.
- Case 2 – engages and pays a worker to whom it has not provided work-finding services in relation to the role for which it is paid by the engaging entity.
- Case 3 – operates an arrangement in which the worker has a material interest but where the agency and/or client would assume that most of the amounts provided for the worker's services would be paid to the worker.

Case 1 involves arrangements where the purported umbrella holds itself out as or is assumed (by a party in the supply chain other than the purported umbrella or the worker, such as the client or the agency) to be employing the worker and paying the worker via a PAYE payroll but in reality is paying them via a PSC or, for example, as self-employed under the CIS scheme.

It is likely that Case 2 will apply where a client refers a worker to an MSP/agency or other entity to be paid on a "payroll-only" or reduced margin basis. This means that an MSP/consultancy/agency that payrolls workers which have been referred to it will either be an umbrella company (if it employs the workers) or a purported umbrella company (if it engages the workers on contracts for services or off payroll). It would appear that the purpose of this is to prevent parties in the supply chain seeking to create circumstances that sit outside the scope of the definition of umbrella company arrangements.

Given that a purported umbrella arrangement will pull agencies (and in some cases, clients) into joint and several liability, it will be important for all supply chain parties to know who is paying workers and on what basis. If there is any confusion (intended or not) about how workers are paid or expected to be paid, this could be enough to make the arrangement a purported umbrella company. Lack of knowledge of purported umbrella company arrangements will be no defence to joint and several liability.

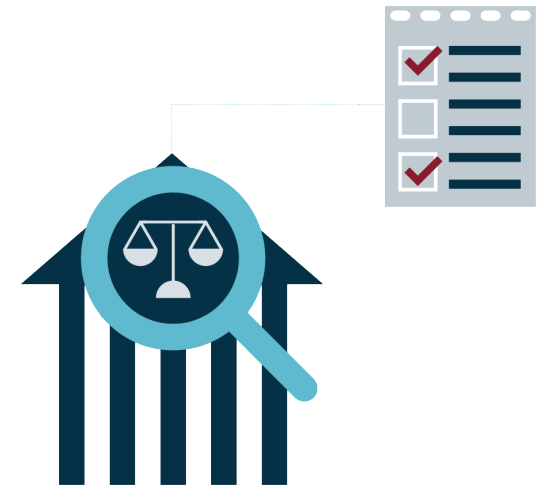
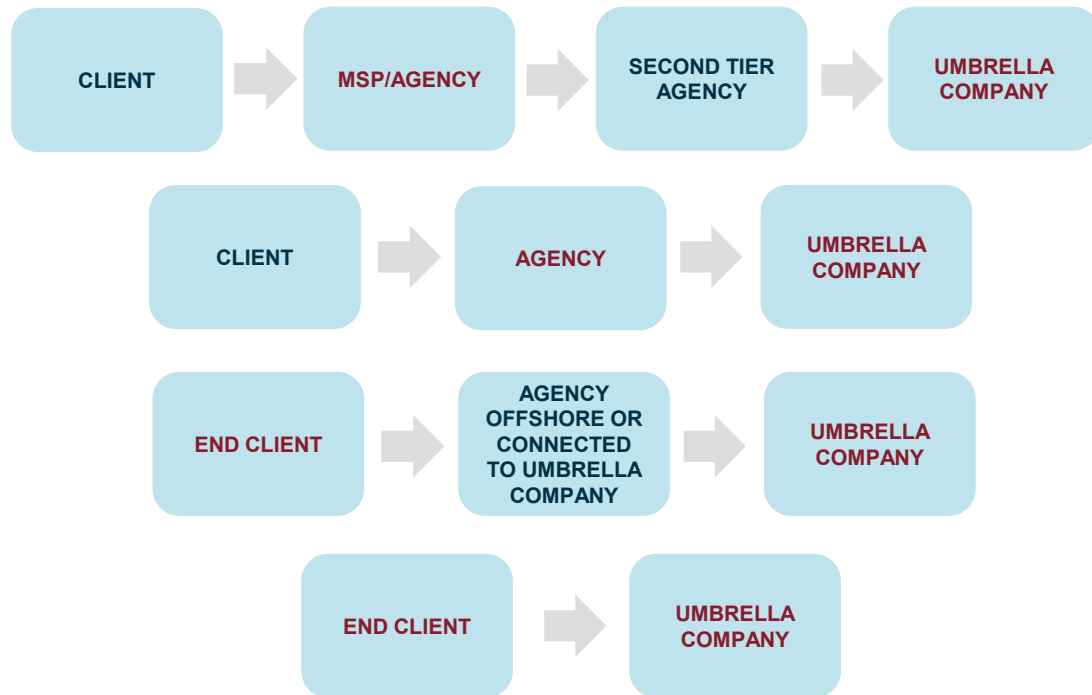
If they do not want the new regime to apply, clients, MSPs and agencies will want to check:

- that all parties in their supply chains, including clients, are aware of any arrangements that are not expected to be paid PAYE; and
- contracts and communications to ensure that there are no assumptions or requirements that workers are paid PAYE when in fact the expectation is that they will not (albeit they may then need to do checks required under whatever other tax regimes are applicable to the non-umbrella arrangements they expected to be in place).

Who will be jointly and severally liable?

The agency that holds the contract with the client will be the party that is jointly and severally liable with the umbrella company or purported umbrella company. This means that MSPs will be liable where the services of an umbrella worker who has been engaged via a second-tier supplier is "on-supplied" by the MSP to the client.

The flow diagram shows where liability in labour supply chains will now fall.



Who will be jointly and severally liable?

What does strict liability mean?

Joint and several liability under the new legislation is a strict liability regime. This means that if non-payment of PAYE or NICs triggers joint and several liability, there will be no defence regardless of fault, knowledge or wrongdoing. Even where the top agency (or client) has undertaken all reasonable tax compliance checks, they will still be liable if the umbrella company fails to meet its obligations.

So why carry out any due diligence at all?

Due diligence on umbrella suppliers will continue to be important. If conducted properly, targeted due diligence will still weed out many, if not all, intermediaries currently operating unlawful tax avoidance schemes.

Chapter 11 is not the only game in town

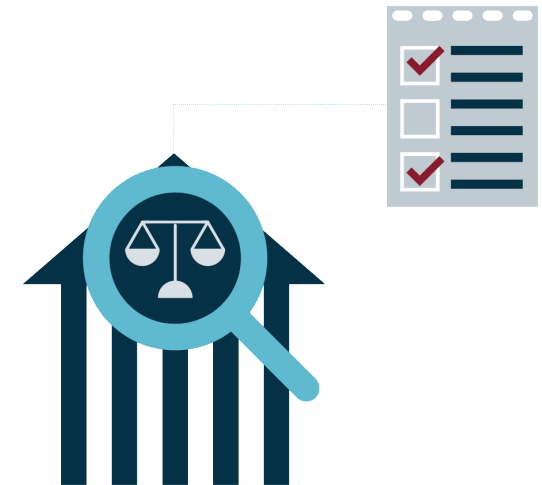
It is crucially important for businesses to show they have procedures in place to prevent the facilitation of tax evasion under the Criminal Finances Act (for large organisations), and the facilitation of fraud under the Economic Crime and Corporate Transparency Act 2023 (ECCTA), which came into effect on 1 September 2025. The defence to any offence of failing to prevent facilitation of tax evasion or fraud is undertaking reasonable checks and having reasonable procedures in place.

There are also other diligence issues to be looking out for, such as compliance with the national minimum wage, payment of expenses and the Modern Slavery Act 2017.

Even if an organisation thinks it has no umbrella companies in its supply chains, it will need to check that there are no purported umbrella companies.

Industry accreditations will be part of the due diligence approach, but should never preclude agencies and clients from carrying out their own due diligence. Some recent umbrella failures have involved umbrella companies with industry accreditations.

All entities that pay contingent workers should ensure they have an established trading history and sufficient balance sheet strength to cover their liabilities. Agencies will want to check that umbrella companies do not offer credit or extended payment terms to other agencies. In practice, this means that the larger, longer established umbrella companies are more likely to meet compliance and credit checking requirements.



Impact on MSP arrangements and agencies generally

MSPs may find the impact of this new legislation particularly challenging because they will be liable for umbrellas used by second-tier agencies. Some MSP models may change as they try to manage the risk, including by:

- taking the MSP out of the labour supply chain altogether: whereby the client has the same "managed service" without the MSP being in the contract chain between the client and second-tier agencies. While this approach has been difficult to sell in the past, it may be considered by some;
- requiring second-tier supplier agencies to be engaged on a margin-only basis (with the MSP paying the workers, or via mandated "approved" umbrellas direct); or
- requiring second-tier agencies to pay all agency workers via their own PAYE payroll or mandated "approved" umbrella companies.

In some cases, agencies which are dependent on certain types of umbrella support may be forced off second-tier preferred supplier lists, with MSPs filling an increasing proportion of vacancies themselves.

Impact on clients

It may well be that having an agency in the supply chain will lull clients into thinking it is business as usual. However, clients should still be cautious. There are situations where even with an agency in the supply chain, the client could end up being the party with joint and several liability. For example, where an agency is offshore or is "connected" to the umbrella company. "Connected" would mean where the MSP/agency and umbrella are in the same group or are otherwise connected by ownership.

Clients will also need to check that they are not engaging with purported umbrella companies, including arrangements for paying client-referred candidates on a "payroll-only" basis.

For some, the risk of joint and several liability may be too great and lead to clients prohibiting the use of umbrella companies or to mandating a small list of umbrella companies they have checked and regard as low risk. In any event, there is likely to be a renegotiation of contracts to ensure that the client has rights to audit, warranties and indemnities.

Use contracts to manage the risk?

Given the potential for business-limiting amounts of tax liability, contractual indemnities should not be relied on to fully cover the risk, not least because contractual indemnities between agencies/clients and umbrella companies will only be as good as the umbrella company is creditworthy.

Nevertheless, most supply chain contracts will require amending to address new risk mitigation measures, including rights to audit compliance and any requirement involving the mandating of an umbrella preferred supplier list. Full transparency will be crucial so that every party is aware of what is going on below them in the supply chain.

Impact on MSP arrangements and agencies generally

Anti-avoidance provisions?

Except for the "purported umbrella" provisions – which address certain types of avoidance – there are no anti-avoidance provisions and no fraudulent document defence as in the agency tax legislation and the off-payroll regime. Therefore, the risk that an unscrupulous client in pursuit of low-cost workers will engage an agency that is willing to engage a "here today, gone tomorrow" umbrella that folds as soon as they come under HMRC's scrutiny does not go away.

This would be of particular concern to other agencies that dealt with the umbrella company because they would potentially be left sharing the tax liability. Given current economic pressures on businesses to reduce labour costs, it is not beyond the bounds of possibility that some staffing companies will continue to offer implausibly cheap labour and some clients will be prepared to turn a blind eye to the likelihood of tax avoidance. However, in the more extreme cases, HMRC would have other powers, including under criminal law, against organisations which fail to do reasonable checks on their supply chain or turn a blind eye, or worse.

What is the interplay with the new Employment Rights Bill?

Consultations on the regulations that will implement some of the detail, including changes intended to bring umbrella companies within the scope of the Employment Agencies Act 1973 and the Conduct of Employment Agencies and Employment Businesses Regulations 2003 are expected in coming months. These changes run parallel to, but are entirely separate from, the umbrella company tax reforms. It is possible that changes will be introduced to clarify that umbrella company work seekers will not be permitted to opt out of the conduct regulations.



Cashflow funding

Staffing supply chains that rely on umbrella companies to provide cashflow funding (under which the umbrella company pays the workers before being paid by the agency or client) may need to find other sources of funding. Invoice discounting arrangements are likely to be part of the solution for many. However, with joint and several liability in the background, it may well be that asset-based lenders will be nervous about providing funding to agencies and MSPs if there is a risk that they may become jointly and severally liable for umbrella company tax compliance.

Given the risk of joint and several liability, agencies will want to check that umbrellas are not extending credit or extended payment terms to other agencies. There have already been reports of umbrella companies going into administration, leaving behind sizeable tax liabilities, as a result of non-payment of invoices by agencies. Further umbrella administrations can be expected in the lead up to April 2026, as they seek to exit unsustainable credit arrangements with agencies.



What about accreditations and insurance?

New accreditation platforms are emerging that are capable of carrying out, in real time, checks into umbrella companies' tax treatment of umbrella workers' employment income and the corresponding payments of all sums due to HMRC, to help satisfy agencies and end clients using their services of their compliance with the legislation.

Such accreditations and checks may also be backed up by insurance policies, paid for by the umbrella companies, but which are intended to pay out to the agency or end client (whichever has the contract with the umbrella) in the event of PAYE tax default by the umbrella company. Some will regard this as preferable to an indemnity, which will only be as good as the umbrella is able to meet the liability. As with all insurance policies, the devil is in the detail: will the cover be sufficient and for the right things and what procedures will be needed to ensure it applies?

Those supplying and using the services of umbrella workers will likely want to make inquiries of their suppliers as soon as possible to understand which industry accreditations and insurances they hold or are working towards holding in the near future.

It is also important to remember that no due diligence or accreditation tool will be perfect, and users of umbrella company services must also put their own additional measures in place. Compliance teams checking accreditation and audit reports will need to understand what payslip checks do and do not reveal and when results require further investigation – in some cases checking what is not disclosed by the report will be just as important as what is.

Anyone relying on third party accreditations will need to consider whether they also provide a reasonable procedures defence for Criminal Finances Act purposes, and all will need to ensure that the information sharing those checking services will involve do not breach the General Data Protection Regulation and that the accreditation bodies have robust cyber security systems in place, backed by appropriate cyber insurance.



Osborne Clarke comment

Many UK staffing supply chains rely on the use of umbrella companies, to a greater or lesser extent. Early indications are that agencies using umbrella companies already are increasing, or will increase, their due diligence into umbrella companies, in many cases using third party auditors and accreditations to help manage risk.

All involved will want to understand how, when and to what extent the new legislation will apply and will need to start thinking about what changes need to be implemented before April 2026 – four months is not much time to restructure engagement and payment models, especially where changes need to be implemented through multiple supply chain parties.

More sophisticated and well-established umbrellas should be able to set up processes that are transparent, in terms of how they pay workers in a way that agencies and end clients can have confidence in, and many are already well on that journey. MSPs and agencies are already reducing or are likely to reduce the size of their umbrella company panels, relying on the bigger and well established players or those that can satisfy agencies of their quality and compliance and leading to a natural decline in less compliant umbrellas.

There may be other cases where MSPs look hard at the risk they are prepared to carry in their supply chain, seek to consolidate supplier lists and choose not to use agencies who rely on certain types, or any type, of umbrella. Staffing companies affected by this, and not able to run their own payroll, will need another way of working and may look to use umbrella companies solely as payroll administrators or payroll agents, or the like.

Staffing companies (and clients), who have hitherto benefited from implausibly cheap labour supplies from certain umbrellas in sub-sectors such as healthcare and logistics, may, if they do not want to be landed with large tax bills, find their staff costs going up significantly. Some may no longer be able to operate competitively in their chosen markets. Regular timesheet-based payments from umbrellas back to staffing companies are also likely to be curtailed, with some staffing companies who have historically relied on such payments to remain profitable facing insolvency.

Many clients, MSPs, agencies and more sophisticated umbrellas will seek to move to demonstrably compliant arrangements (whether to "approved" umbrellas or in-house payroll).

Care should be taken before requiring or forcing umbrella workers to cease using one umbrella company in favour of another. Undoing legacy arrangements may not be straightforward and there is case law to suggest that if umbrella workers are treated as chattels to be moved around at the whim of agencies or end clients, then they were never "really" employees of the umbrella company, but were "really" employed by the agency or end client. If so, this could raise some complex questions around who is liable as the employer for any historic tax or employment rights purposes.

Some outgoing umbrella companies may try to argue that the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) applies to transfer employment liabilities, such as holiday pay, to the new, preferred umbrella companies. Whether or not TUPE applies is a matter of law, not choice or contract: in most cases involving umbrella workers, it will not apply.

We may see a move away from umbrella arrangements towards self-employed engagements where the circumstances allow. A shift to self-employed models should be considered only where the arrangements are genuinely outside IR35 or capable of being supplied as a deliverable rather than a person's time. Perceived lack of enforcement of IR35 in the private sector may lead some to believe that the use of PSCs is a lower-risk option.

We also expect to see renewed interest on statements of work or provision of output-based services as a way of moving supplies away from the supply of staff to supply of services. Anyone looking to rely on statements of work to remove the umbrella company risk will want to ensure that the arrangement is not a purported umbrella company or one that could give rise to liability under the off-payroll working rules (IR35).

Key Contacts



Frances Lewis

Consultant
United Kingdom

+44 207 105 7032
frances.lewis@osborneclarke.com



Kevin Barrow

Partner
United Kingdom

T +44 207 105 7030
kevin.barrow@osborneclarke.com



Shaziya Kurmani

Associate Director
United Kingdom

T +44 207 105 7588
shaziya.kurmani@osborneclarke.com



Belinda Brooke

Associate Director
United Kingdom

+44 207 105 7963
belinda.brooke@osborneclarke.com

