



IR35

Understanding the new off-payroll regulation

Off-payroll working rules for clients, workers
(contractors) and their intermediaries.

Project Start Recruitment Solutions
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IR35 HISTORY

1999 – When it all started

The HMRC originally issued IR35 in March 1999. This tax status regulator was created to monitor the one-person limited company offering client services, where an individual was acting as a traditional 'employee', while enjoying more favourable tax benefits afforded them by a corporate structure.



Despite many appeals and court cases to overrule the unfairness of this regulation by the contractor market, the high courts have continued to support the Inland Revenue in the implementation of IR35 which has now been in place for more than 20 years.

2001 – High Court Case

They ruled in favour of the Inland Revenue that the regime was not unfair to the one-person limited company, and the contractors' group lost its appeal in December 2001.

2011 – The IR35 had an overhaul of the regime

George Osborne and the OTS (Office of Tax Simplification) requests a review of improvements to IR35.

And these were...

- **Creating a dedicated helpline staffed by specialists.**
- **Publishing clear guidelines and scenarios to help individuals determine their IR35 status more easily.**
- **Restricting IR35 reviews to high-risk cases.**
- **Creating a new IR35 Forum to monitor HMRC's improved enforcement of IR35.**

2015 – 32 more recommendations were raised

In Jan 2015, HMRC released a series of 32 recommendations on how to improve IR35.

The HMRC today, believe that IR35 is ineffective and that "non-compliance with the legislation is widespread". In fact, the Government stated that non-compliance may cost the Exchequer £430m per year.

2016 – Off - Payroll working

On Budget Day - March 16th, the Government announced that there would be a clampdown on so-called 'off-payroll working' within public sector organisations.

2017 – New IR35 Test

In March 2017 – a new IR35 Employment Status Test (ESS) was launched in early March 2017 – to help workers, clients and agents determine whether or not someone is caught by IR35. This tool evolved into the CEST tool that is in use today.

2018 – Off-Payroll extension to the private sector

2020 – The latest IR35 review

In April 2020, the private sector implementation was delayed to April 2021.

As a result of the COVID-19 outbreak, the Government deferred the implementation date of 6th April 2021 and the private sector off-payroll implementation is going ahead.



The implementation of IR35

So, what has changed?

The new HMRC CEST tool will assess if a one-person limited company operates inside or outside of IR35.

If the CEST tool determines that you are inside IR35, then contractors will need to pay the same income tax and NICs as if they were employed. However, they still won't get any employment benefits, like paid holiday or sick leave, from the managing business.



Genuine contractors' that represent such an important part of the UK economy, should be able to carry on working outside IR35 after April 2021, but the HMRC will now look for the payment of taxes, fines and penalties from the contractor and end client, should an assignment be deemed incorrectly outside IR35.

So, what do you need to do as a client to make sure your decision is accurate?

You will need to complete the online CEST process for each worker by giving accurate answers. This will then provide you with a decision if the contractor is deemed to be operating inside or outside IR35.

Before you start, please make sure you have the following information:

- Details of the contract
- The worker's responsibilities
- Who decides what work needs doing
- Who decides when, where and how the work is done
- How the worker will be paid
- If the engagement includes any corporate benefits or reimbursement for expenses

Please copy and paste the link below to be directed to the Government CEST tool page:-

<https://www.gov.uk/guidance/check-employment-status-for-tax>

So, what should you be aware of as a one-person limited company?

You can still work as a limited company inside IR35. Yes, there are more tax benefits if you are working outside IR35, but just because a specific contract is inside IR35, doesn't mean you should immediately turn to other solutions.

There are still benefits to operating inside IR35 and working through a limited company, rather than using an umbrella company.

Here are a few benefits

Take-home pay should be slightly higher via a limited company due to extra income gained from the Flat Rate VAT Scheme, which can often add thousands to your annual income - on a £100,000 contract it would add £1,400 extra income. You will not benefit from the flat rate scheme if you use an umbrella company.

In the private sector, until April 2021, you only pay tax on 95% of your income rather than 100% via an umbrella company. HMRC provides a 5% allowance, which is intended to help with the running costs of your company. This allowance will still be available where you retain the responsibility for administering the rules, i.e. working for a small end client.

Just because this contract is inside IR35, it doesn't necessarily mean other contracts that run concurrently and after, won't be outside and you will have everything in place to engage this was with other companies.



If you wish to discuss anything in this brochure in more detail, please contact our office on **01454 529009** and ask to speak to our Compliance Manager.

Please visit our website for more information on our services.

www.projectstart.co.uk

How has CEST been transferred?

Who determines the Employment Status for Tax of a limited company?

The HMRC has confirmed that it cannot effectively enforce IR35, and its responsibility for assessment of status and payment of relevant taxes on a one-person limited company.

It transferred this liability to the client in the Public Sector some years ago and this has now transferred to private companies also on 6th April 2021.

The end client will take responsibility of assessing the nature of their contractor relationships and, if necessary, take steps to ensure they are genuine business to business relationships that would fall outside of IR35. This now involves a full contractual review and completion of the CEST tool process to determine if they fall outside or inside IR35.

What does CEST cover?

The client will assess the following areas for each contractor and complete an online HMRC CEST form. The decision is made up of the following: -

- **Control and Supervision**
- **Equipment**
- **Working arrangements**
- **Substitution**
- **Mutuality of obligation**
- **Financial risk and opportunity to profit**

We have explained each of the 6 points in more detail for clarity.



Control & Supervision

One of the most important determinants of IR35 status revolves around the extent to which a client controls where, when and how an individual performs his work.

Are you under the direct control of your client?

In most cases where professional services are provided, it is important that a contractor can demonstrate a certain amount of autonomy in the way they undertake a project.

Employees are typically under the direct supervision and control of their employers, however the truly self-employed will have more influence over how they complete the work they have been hired to do.

In the case of IT contractors and consultants, the client is likely to provide a fairly detailed specification outlining the tasks it requires the contractor to complete. However, for IR35 to not be an issue, the contractor should be presented with specific milestones or tasks to achieve, rather than being provided with an open-ended pile of work.

For a contractor to successfully demonstrate that they are not under the direct supervision and control of the client, both the written contract and working practices must show that the client has no influence over how the contractor performs his services, nor the manner in which they are performed.

Control – things to look out for

The HMRC has confirmed that it cannot effectively enforce IR35, and its responsibility for assessment of status and payment of relevant taxes on a one-person limited company.

Contractual pointers towards a classic ‘employment scenario’ include:

- Indicating that the contractor will be supervised by a line manager or similar company employee.
- Including work start and end times, and even break times in the contract.
- Including any ‘staff’ perks, including provisions for holidays or sickness.
- Any clauses that specify any rights of control or supervision over the contractor.

It is worth noting that any clauses related to control must be mirrored in both the upper-tier contract (between agent and client) and the lower tier contract (between contractor and agent).

Provision of Equipment

Does the individual use equipment provided by the client, or do they use their own? Receiving company assets to fulfil the contract, may result in you being deemed as a traditional employee.

Substitution

The right to provide a substitute in a contractual agreement has long been deemed to be an important factor when demonstrating that a contract assignment falls outside the scope of IR35.

An employee provides his/her personal services to an employer (client), whereas a business would provide its services to a client, rather than the exclusive services of an individual.

As a result, all professionally drawn-up 'IR35 friendly' contracts will include a substitution clause.

The right of substitution – important points

The right to supply a substitute must be a genuine one, otherwise, HMRC may conclude that the clause is a 'sham'. You should be able to show how a substitute could be used in practice, however employment status experts say that simply having the right to provide a substitute is a strong pointer to being outside IR35, even if the right is never exercised.

An 'unfettered' right of substitution means that a client must accept a substitute if the contracted worker is unavailable. This is a strong pointer towards self-employment, but rarely available given the nature of IT contracting.

Clearly, if a substitute has actually been used during the course of an assignment, this is another strong pointer towards self-employment.

Your company should always pay for any costs relating to providing a substitute worker, should the need ever arise. Your company should also provide any training, and make all arrangements for bringing the substitute on site.

In the real world, end clients will often maintain a veto to accepting a substitute, on reasonable grounds – for example, if the substitute does not have sufficient qualifications to perform the job

If you do not have a right of substitution in place (i.e. your contract is one that requires personal service), this does not automatically mean that you will be caught by IR35, as many other factors are also taken into account.

Working arrangements

- Does the individual work for just one client, and have their contracts been renewed many times?
- The self-employed typically work for a number of clients at once. Do you have your own business website and company email address?
- Do you have company stationery, letterheads, a logo, and customised invoices?
- Is your company registered for Value Added Tax (VAT)?
- Has your company ever employed anyone else or used sub-contractors?
- Do you have business liability and professional indemnity insurance in place?

- Has your company invested in training, or improving its marketability in any other way?
- Does your contracting business ever advertise its services, either on its own website or on freelancer-type portals?
- Do you have dedicated office space in which you have carried out any contract-related work?
- Do you regularly tender for contract work, or apply for contract positions, or have you had multiple renewals for the same client?
- Is your company registered under the Data Protection Act (for dealing with client's data)?

Mutuality of Obligation

A mutuality of obligation exists when an employer expects a worker to undertake work when asked to do so, and the worker expects to be given work on a constant basis. For self-employed people, they would expect a client to hire them to undertake a specific task, with no expectation of further work being provided after the initial task expires.

For a contract of service to exist at all, there must be what is known as an 'irreducible minimum of mutual obligation' – that the engager is obliged to remunerate the worker, and the worker is obliged to provide his/her skills. As this irreducible minimum could exist in both a contract for services AND a contract of personal service, this is not sufficient to determine the true nature of a contract.

The mutuality of obligation question arises not during the course of the initial contract, but what happens when this contract expires.

Useful links:-

<https://www.contractorcalculator.co.uk/ir35.aspx>

<https://www.totaljobs.com/advice/ir35-explained>

<https://www.ukfinance.org.uk/news-and-insight/blogs/ir35-explained>

It is possible that, by having an IT contract renewed many times, then this could be a pointer towards 'employment'.

In **ESM0543**, HMRC argues that “*where work is regularly offered and accepted over a period of time a continuous contract of employment may be created.*”

Things to consider

As a result of the different ways in which HMRC and outside experts interpret case law, employment status specialists tend to focus more on demonstrating that non-mutuality exists in a contractor for services, rather than trying to show that mutuality of obligation does not exist.

Problems may arise if, for example, an end client cannot issue terminate a contract for services immediately, but instead has to provide notice. Again, if a contractor has a 'rolling' contract with a client, rather than a fixed-length contract, this could also indicate that a mutuality of obligation exists at the end of the initial contract period.

Financial Risk

How much financial risk does the individual undertake in their work? If all the risk lies with the client, then this is an indicator of 'employment' rather than 'self-employment'.

The regularity of payment may have some influence on IR35 status. Self-employed people are often paid by the job, rather than a fixed hourly/daily rate.

Does your company have any income from non-contracting sources (e.g. designing websites in your spare time)?