all fingers on the IR35 pulse.

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human forward.

preparing yourself

for IR35.

Come April 2021, IR35 legislation that was launched in the public sector in 2017 is being introduced into the private sector.

This legislation is set to crackdown on personal service contractor tax avoidance. The onus for determining whether IR35 applies sets to shift from contractors (temporary or shift workers) to clients, bringing with it increased workload and risk. The positive news is that private workers and clients within the care, education and student support sectors continues to show their resilience and, with the right preparation, it's a challenge that public services industries can absolutely overcome.

We've created this helpful guide to best support our private sector clients in the months ahead, whilst offering a reminder and overview to our public sector clients.

When it comes to IR35, there is a lot of important detail and we always urge businesses to secure independent legal advice. If you're one of many who are pushed for time or feel overwhelmed by the legislation, skip through to our snapshot features and top tips. These can be digested in minutes and will enable you to eliminate any nasty surprises come April 2021

One word of warning. It's crucial to remember that the IR35 consultation only closed at the end of May 2019. There's still ample opportunity for parliament to amend the scope and rules. It's a reminder that, whilst preparation must start now, businesses need to remain agile in order to successfully future-proof IR35 plans.

In the meantime, we have an expert IR35 team ready to support you as and when required.

Victoria Short
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keeping it simple.

No one wants to be bamboozled when it comes to tax legislation.

You'll see these terms referenced frequently when covering IR35 so here's our jargon-free summary to get the ball rolling.

what is IR35?

The common name for legislation contained in the Finance Act 2000, which requires individuals providing services via a PSC to assess their employment status for tax (and make appropriate deductions based on that assessment).

PSC - personal services company or contractor?

When referring to contracting, a limited company normally consists of a sole shareholder and director through which services are provided. Although IR35 applies to services provided through any intermediary that is not an agency, the most common model is via a limited company. We will refer to this as a PSC throughout this guide.

who is the end user?

The organisation benefitting from the services provided by the PSC.

who is the fee payer?

The organisation paying the PSC for the services. This may be the same organisation as the end user or another party - such as an employment business.

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IR35 in a snapshot.

New legislation will be introduced in April 2021 designed to combat tax avoidance. It targets individuals providing their services via an intermediary, most commonly a limited company.

Under current rules, these individuals assess each contract and determine whether IR35 applies. When it does, income received from that contract should be treated as employment income. This means it's subject to tax deductions and national insurance contributions.

From April 2021, the responsibility for making this determination will fall to the end user of the services. The organisation paying for the services will be responsible for making the relevant deductions.

IR35 in detail.

The 1990s saw significant growth in contracting in the IT sector.

It was common for employees to leave the office on a Friday and return on the Monday as an independent contractor. This growth led to concerns that tax liabilities were being avoided and that individuals providing their services as PSCs were in fact disguised employees.

In 1999, the government announced that legislation would be introduced to combat this issue. The Finance Act 2000 made provision for individuals providing their services via PSCs to assess their own status for tax in respect of each engagement. If that assessment resulted in a determination that the engagement was more like employment than a business-to-business relationship, the PSC had to account for PAYE income tax and national insurance contributions.

In April 2017, the government introduced rules within the public sector which moved the responsibility for making the assessment to the end user of the PSC. Under the off-payroll rules, the end user is responsible for determining the status of the PSC and communicating that status to the fee payer. The fee payer must then operate deductions for tax and national insurance on the payments to the PSC.

The implementation and effect of the changes in the public sector was considered a success and the government announced that similar changes would take effect in the private sector, eventually confirming April 2021 as the effective date.

are you in scope?

making the determination: snapshot.

With many small businesses in operation in your sector, it's important to check whether you're in scope. IR35 rules do not apply to small companies.

To be "small", a company must meet at least two of the following three requirements:

- under 50 employees
- turnover under £10.2m
- balance sheet value under £5.1m

If you're a small company, you're exempt and the PSC will remain responsible for making their own status determination (and account for their tax accordingly).

The legislation currently proposes that the size of a company is assessed annually.

We predict that this will be the most challenging part of the legislation for clients as determining employment status for tax is a highly specialised area.

HMRC's employment status manual is the authoritative source for how HMRC makes its own determinations.

HMRC have also developed the Check Employment Status for Tax tool to assist in making determinations. There are also several third-party organisations that offer assessments.

However, the determination is made, the responsibility is on the end user to use reasonable care in making the determination and communicating that to the fee payer.

are you in scope?

making the determination: detail.

Most assessment tools work by taking organisations through a series of questions designed to understand the nature of the work being undertaken by the PSC. Whilst there are a number of factors that make up the picture, it's really useful to know that there are three primary factors.

1. mutuality of obligation.

Mutuality of obligation is linked with two other factors. Firstly, is the individual obliged to provide their own skill and expertise or can the PSC supply a substitute to undertake the work? Secondly, is the end user obliged to pay for work carried out or does the PSC take some financial risk in the arrangement?

Even where a worker is obliged to provide their own skill and be paid, it does not necessarily follow that IR35 applies. An element of control must be present in the relationship, please see below.

2. control.

The greater the level of control placed upon the PSC, the more likely that IR35 applies. This can range from control as to where the work needs to be performed and at what times - right through to detailed instructions on how the work needs to be done.

3. substitution.

If the PSC can supply a different person to do the work, it is less likely that IR35 applies. IR35 is about identification of an underlying employment relationship and employment is inherently personal. If the worker can be substituted for another then that element of personal service would not exist.

In addition to these three core factors, making a determination should also consider the following:

- does the worker use their own equipment to provide the services?
- are they 'part and parcel' of the client's organisation or can they be distinguished from other employees?
- are they engaged to work on a discrete project that requires specialist knowledge or are they working on 'business as usual' matters?
- are they paid at a rate that indicates a level of specialism?
- is the contract for a fixed period without the likelihood of renewal?

The government consulted on granting PSCs a right to ask for reasons why the end user reached a particular conclusion so it is important to ensure the assessments are done diligently.

https://www.gov.uk/hmrc-internal-manuals/employment-status-manual/esm8000

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

communication is key.

Once the determination has been made, it must be communicated to the fee payer who must then pay the PSC in accordance with the assessment status.

Where there is a contractual chain between the end user and fee payer, each party in the chain is responsible for passing the determination to the next.

where does the liability sit?

The government consulted on how liability should be apportioned and in certain circumstances is proposing that liability be transferred up the supply chain to the end user. It is therefore critical that supply chains are properly managed to ensure the ability of all parties to comply with their obligations under the legislation.

prepare like a pro.

There are three steps to effective preparation.

step one: due diligence

It is vital that you identify how many PSCs you have engaged within your organisation and how they are procured. Why not create a simple spreadsheet tracking the PSC name, what they do, how much they are paid, how long they have been/will be engaged for and the source of the PSC e.g. agency, direct etc. Once this information has been collated, you can define some rules of thumb for IR35. Of course, this will depend very much on your organisational risk appetite.

You may decide, for example, that PSCs on contracts of under 6 months and paid more than £250/day are not caught by the rules. These rules of thumb will leave you with three pools of contractors: not caught by IR35, caught by IR35 and undetermined.

You can now move on to the criticality assessment.

step two: criticality

For PSCs to which the rules apply and those that are undetermined, you must understand their importance to your organisation. Operating under IR35 will lead to a significant reduction in take-home pay. This may lead to those PSCs asking for increased rates to cover the tax liability. To be able to make these decisions, you need to know how critical the PSC is to your organisation. Can their work be concluded before April 2020? Is there an alternative solution to using their services?

After this step, you will have a list of critical PSCs whose status means that IR35 will or might apply. For those PSCs whose status is undetermined, you will need to put them through a more structured assessment.

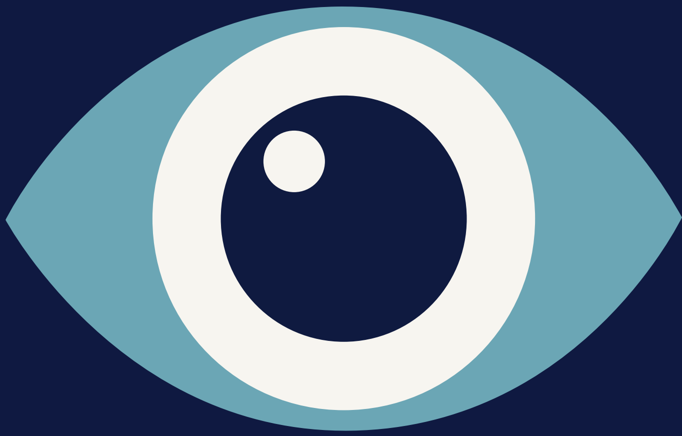
You will finally have a list of PSCs who are critical and who will be affected by IR35. This is likely to result in commercial negotiations with each of them to ensure their retention.

step three: technical capability

Where you engage PSCs directly, you will need to ensure that your payroll system is capable of making the correct deductions and accounting to HMRC for the tax and national insurance contributions. If PSCs are paid through your accounts payable on an invoice, this may mean significant internal work to ensure that the rules can be operated in a compliant manner by April 2021.

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

in the eyes of a PSC.



From our work in the public sector, we know that IR35 can effectively push up rates. Workers who are in scope are increasing their fees to ensure their take-home pay is not impacted by the newly enforced deductions.

It's important to work closely with any recruitment partners to help limit the impact of IR35 on your organisation. This may include ensuring you budget for increased contractor costs in 2020 and beyond and/or discussing opportunities to explore permanent hires.

7 tips for IR35 success:

- Don't waste time. Check your organisation is in scope as small businesses are exempt.
- Familiarise yourself now with the HMRC's IR35 determination tool and the factors that influence whether a PSC is in or out of scope.
- Preparation is key and you should have conducted your internal PSC audit by October 2019.
- Work with a recruitment partner who has experience of IR35 within the public sector so you can learn from their experience.
- Remember that, at the time of going to print, the legislation is only at draft stage.
- Ensure your preparation and processes factor in some flexibility to allow for change.
- Put robust processes in place to ensure you are logging and communicating your determinations with the relevant employees and/or partners within your recruitment supply chain.

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