



Latest IR35 updates and developments



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What is happening?

- From 6th April 2020, responsibility for making IR35 decisions will fall onto the **client**, rather than the person providing the worker
- If IR35 applies, the liability to operate PAYE & NICs will fall onto the **fee-payer**, rather than the person providing the worker

(the **client** and the **fee-payer** are often, but not necessarily, the same person)

What is IR35?

- IR35 was the number of the press release which announced the introduction of anti-avoidance legislation back in April 2000
- It was introduced to counter the avoidance of tax & NICs by individuals providing their personal services via a limited company (or partnership)
- Personal Service Company (PSC) – where the majority of income derives from work performed personally by the shareholder(s)
- IR35 is a “look through” provision
- It asks a simple hypothetical question: “if the limited company did not exist, would the relationship between the end client and the worker be that of employer and employee?”

Client
Company

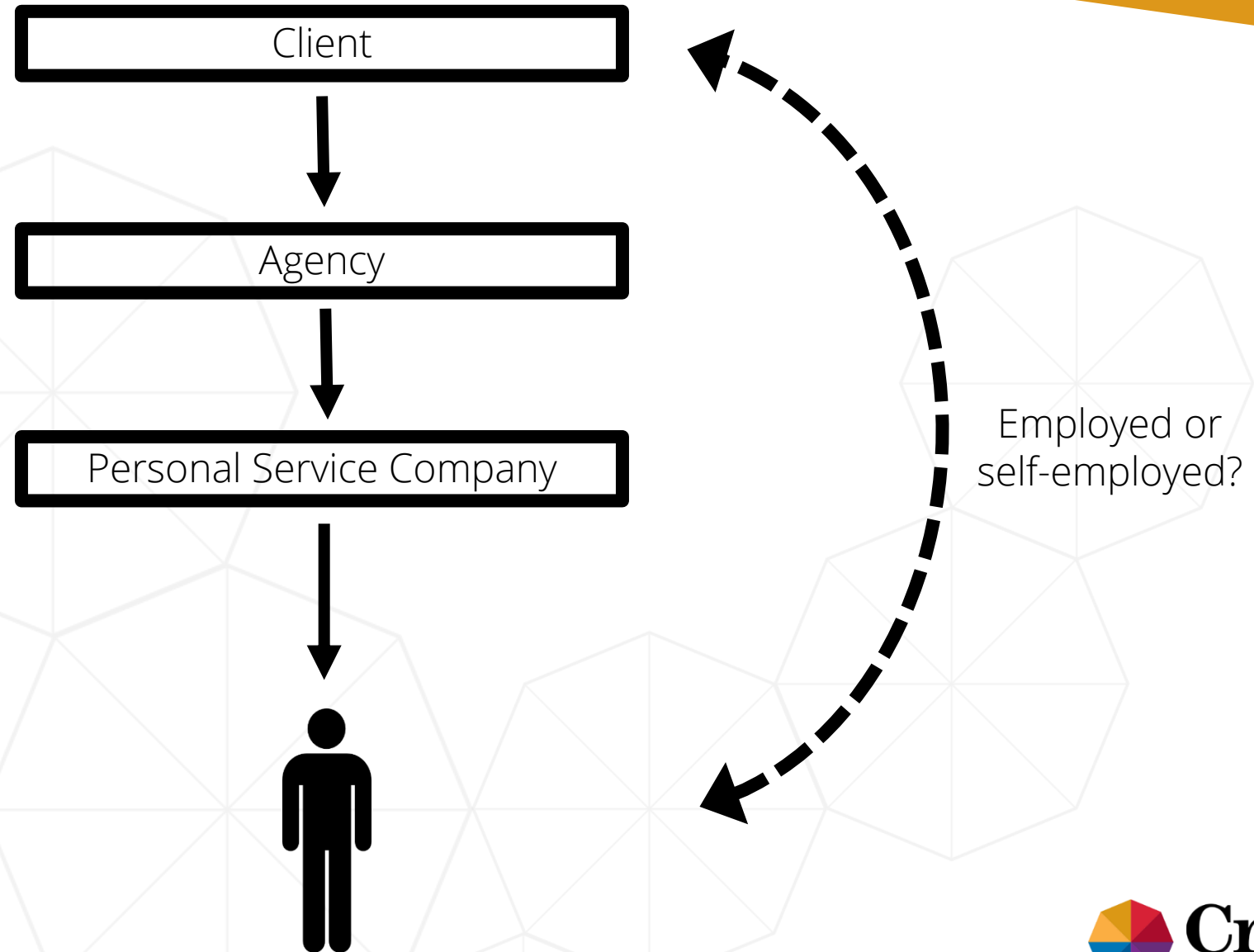


Personal
Service
Company



Employed or
self-employed?





When does IR35 apply?

The hypothetical question is applied to each contract separately:

- If the hypothetical relationship between the end client and the worker would be that of employer and employee, then IR35 applies to that contract
- If the hypothetical relationship between the end client and the worker would be that of self-employment, then IR35 does not apply to that contract

How does IR35 work right now?

In the private sector, the Personal Services Company (PSC) decides for itself whether IR35 applies

- If IR35 applies, the PSC is responsible for applying PAYE & NICs to the 'deemed direct payments' received under the contract - including the liability for employer's NICs
- The 'deemed direct payment' is effectively a minimum salary that must be processed by the PSC – which prevents the shareholder extracting the money in the form of dividends

Why the need for change?

Off Payroll Working in the Private Sector – the initial consultation ran from May 2018 to August 2018

- “We have estimated that only 10% of individuals working in this way apply the rules properly, costing the Exchequer hundreds of millions of pounds in lost tax revenues every year.”

Off Payroll Working rules from April 2020 – further consultation ran from March 2019 to May 2019

- “Non-compliance with the off-payroll working rules in the private sector has been growing... expected to reach £1.3 billion a year by 2023/24”

What is happening?

- From 6th April 2020, responsibility for making IR35 decisions will fall onto the private sector **client**, rather than the PSC providing the worker
 - Unless the client is 'small'
- If IR35 applies, the liability to operate PAYE & NICs will fall onto the **fee-payer**, rather than the PSC providing the worker

(remember that the **client** and the **fee-payer** are often, but not necessarily the same)

How does the fee-payer apply PAYE & NICs?

- PAYE/NICs are applied to the 'deemed payment' *as if* the worker was a direct employee of the Fee-Payer
- s61Q ITEPA 2003
 - Take the payment, net of VAT
 - Deduct any direct cost of materials
 - Deduct any *allowable* expenses, as if the worker was an employee (optional)
 - s339A ITEPA2003, see EIM32135

How does the fee-payer apply PAYE & NICs?

- PAYE/NICs are applied to the 'deemed payment' *as if* the worker was a direct employee of the Fee-Payer
 - No entitlement to SSP/SMP/SPP/SHPP etc
 - No deduction for Student Loans will apply
 - RTI returns should show the 'Off Payroll Worker' marker
- The Fee-Payer is liable for the employer's NICs
- Payment of the net amount is made to the PSC
- Full VAT is also paid to the PSC
- At the end of the year/contract a P60/P45 should subsequently be issued in the worker's name

Deemed direct payment

- s61 Q ITEPA 2003
 - Take the payment, net of VAT
 - Deduct any direct cost of materials
 - Deduct any *allowable* expenses, as if the worker was an employee (optional)
 - s339A ITEPA2003, see EIM32135

How does the client decide whether IR35 applies?

- *"if the intermediate company (or companies) did not exist, would the relationship between the end client and the worker be that of employer and employee?"*
- Apply the normal Employment Status Tests to the hypothetical relationship..

Employment Status

- Employment Law has 3 possible status outcomes:
 - Self Employed
 - Worker*
 - Employed
- Tax & NICs (IR35) has only 2 possible status outcomes:
 - Self Employed
 - Employed

* 'Worker' status conveys employment rights such as holidays & NMW etc but *not* necessarily PAYE/NICs for HMRC purposes

Employment Status Factors

- Control
- Personal service
- Mutuality of obligations
- Integration
- Economic reality

Employment Status Factors

- Ready Mixed Concrete (South East) Limited v Minister of Pensions and National Insurance [\[1968\] 2 QB 497](#)
- 'A contract of service exists if these three conditions are fulfilled:
 1. "The servant agrees that, in consideration of a wage or other remuneration, he will provide his own work and skill in the performance of some service for his master."
 - Personal service
 2. He agrees, expressly or impliedly, that in the performance of that service he will be subject to the other's control in sufficient degree to make that other master."
 - Control
 3. The other provisions of the contract are not inconsistent with its being a contract of service."
 - Other tests

Control

What?

- Time, task or project based?

Where?

- Place of work? Client's office, home, and who chooses?

When?

- Hours of work? Same as employees?

How?

- Line management oversight?

Why?

- Rate of pay? Who determines?

Personal service

Who?

- Right of substitution?
- Note that this is about the right – it may not necessarily have happened (though very compelling evidence if it has)
- Fettered?
- Substitution must be made by the PSC – i.e. the substitute must be paid by the PSC, not the client

Mutuality of obligations

- Ongoing expectation on behalf of each party, that:
 - The engager will offer work
 - The worker will accept and supply the service
- Exclusive arrangements
- Typically a relationship built over time

Integration

- The worker is 'part and parcel' of the organisation, for example:
 - Given a title
 - Given office space
 - Appears on telephone/email extension lists
 - Performs work of similar nature to other employed workers

Economic reality

- Is there evidence that the individual is in business on their own account, for example:
 - Premises
 - Supply of major tools & equipment
 - Element of risk
 - The capacity to make profits and incur losses
 - Existence of other customers

Making the decision

- The factors will seldom all point in the same direction
- Decisions are made 'on balance of probability'
- HMRCs Check Employment Status for Tax (CEST)
 - Erratic results
 - Not detailed enough to properly consider all factors
- Independent Review

Making the decision

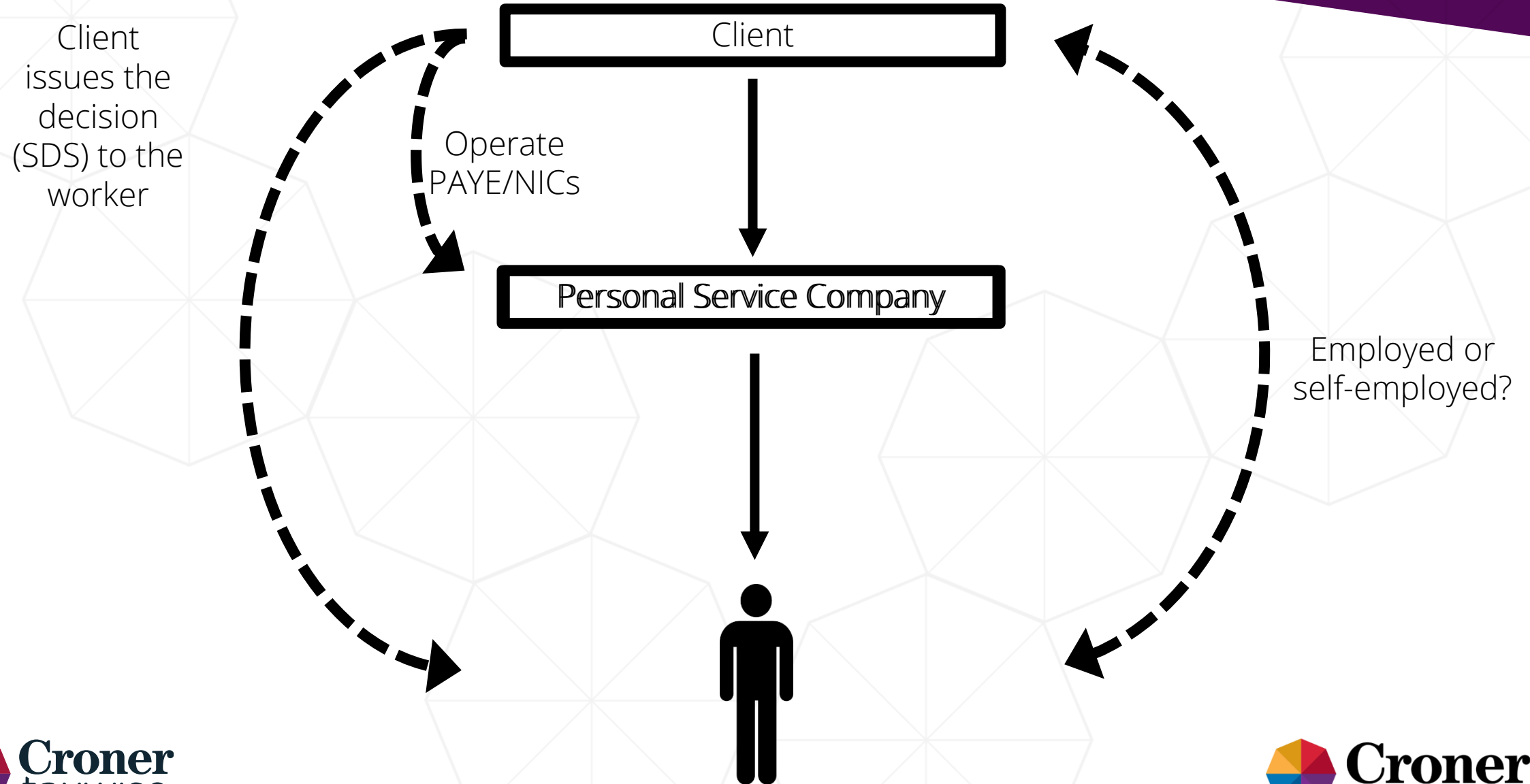
- The Client must issue a 'Status Determination Statement' - if IR35 applies
 - HMRC have confirmed that under the current draft of the legislation there is no requirement to issue a statement if IR35 *does not* apply, but suggest it is good practice
- The Client is liable for any underpaid PAYE & NICs until the SDS is issued *or* if it gets the decision wrong – unless it is provided with false information

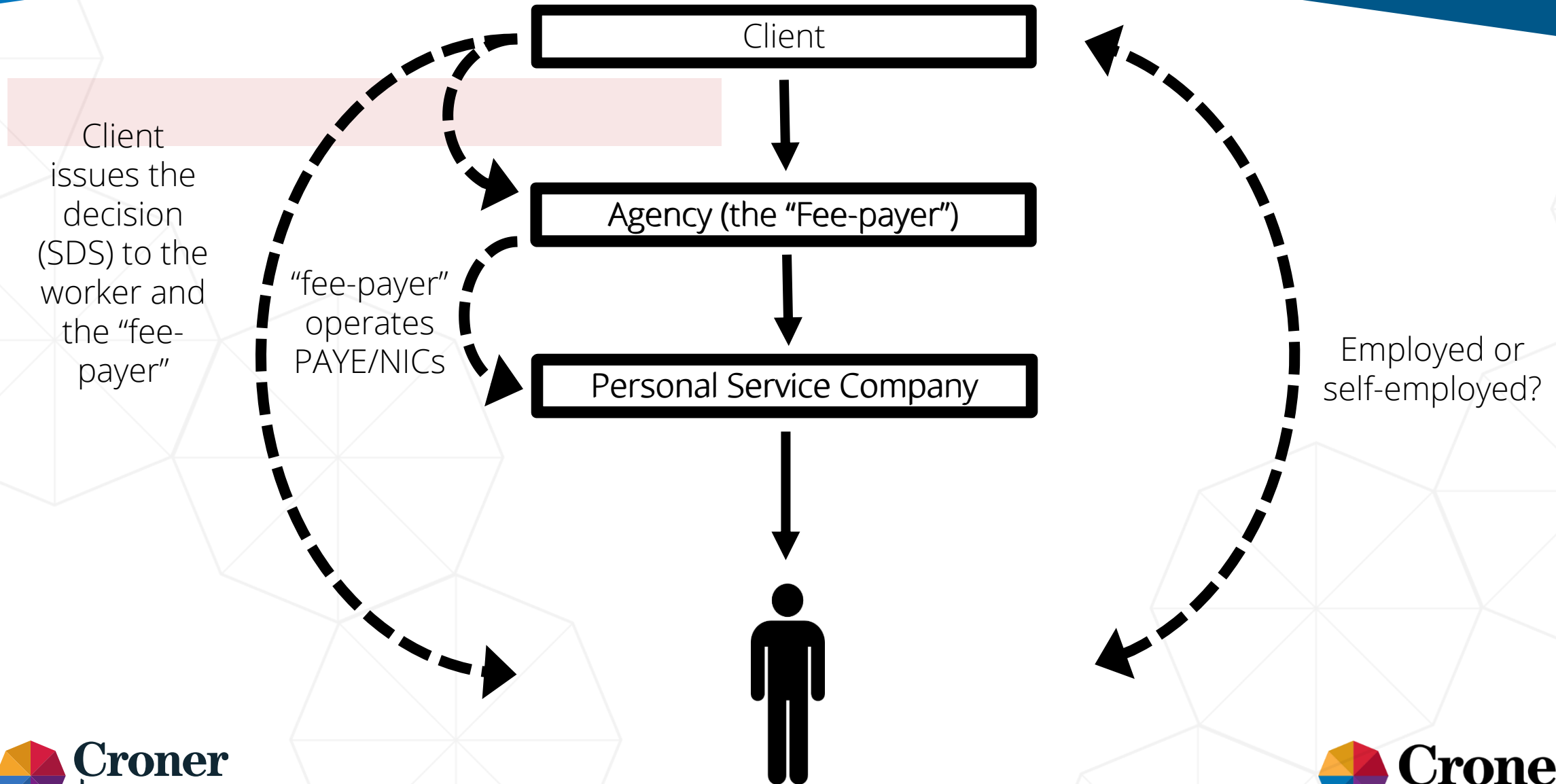
Status Determination Statement

- The 'Status Determination Statement' (SDS) must be issued:
 - to the worker – s. 61N(5) ITEPA 2003; and
 - to the intermediary with whom the client contracts - s.61N(8)(za) ITEPA 2003
- Each intermediary must then pass the SDS to the next intermediary below them in the chain, down to the 'fee-payer'
 - failure to pass on the SDS renders that intermediary liable for PAYE/NICs – s. 61N(7) ITEPA 2003

Status Determination Statement

- Must give reasons for the conclusion – whether IR35 does (or does not) apply
- Must take reasonable care in coming to the conclusion – otherwise is not a valid SDS
- Client-led Status Disagreement process
 - Either the worker or the fee-payer may object to the decision (but no right of appeal to HMRC)
 - Client has a 45 day time limit for considering the case
 - Client must give reasons for its conclusion or issue a revised SDS to the worker and the fee-payer





What is a 'small' company?

- The qualifying conditions are met in a year in which it satisfies **two** or more of the following —
 - Annual turnover - not more than £10.2 million
 - Balance sheet total - not more than £5.1 million
 - Number of employees - not more than 50 (monthly average)
- Apply these tests to the last financial year which ended before the tax year starts
- For new entities, the first financial year is disregarded if it does not end before the tax year starts, so it will automatically be regarded as small

What is a 'Small' group?

- Parents, Subsidiaries & Joint Ventures
 - Apply the Companies Act 2006 'small group' test - even if the parent is not a company but is another form of undertaking (s60C ITEPA 2003)
- The qualifying conditions are met in a year in which it satisfies **two** or more of the following —
 - Aggregate annual turnover - not more than £10.2 million net (or £12.2m gross)
 - Aggregate balance sheet total - not more than £5.1 million net (or £6.1m gross)
 - Aggregate number of employees - not more than 50 (average per month)

"net" means excluding group transactions

"gross" means including group transactions

What is a 'Small' relevant undertaking?

- Not necessarily a UK registered company at all...
- "Relevant undertakings" are also treated as companies (s60D ITEPA 2003)
 - LLPs
 - Unregistered companies
 - Overseas companies
- Apply tests to the last financial year to end before the tax year starts
- For new entities, the first financial year is disregarded if it does not end before the tax year starts, so it will automatically be regarded as small

What is a 'Small' other undertaking?

- "Other undertakings" (neither a company nor a relevant undertaking) have a slightly different test - s60E ITEPA 2003
- "undertaking" means - s1161 Companies Act 2006:
 - a body corporate or partnership, or an unincorporated association carrying on a trade or business (with or without a view to profit)
- Apply test to the last financial year to end at least 9 months before the tax year starts
- For new entities, the first financial year is disregarded if it does not end 9 months before the tax year starts so it will automatically be regarded as small
- The qualifying condition is met in a year in which -
 - Annual turnover - not more than £10.2 million

What is a 'Small' other person?

- "Other Persons" that are not a Company, a Relevant Undertaking or Other Undertaking (this generally means sole traders) have a slightly different test - s60F ITEPA 2003
- Apply test to the last *calendar* year to end before the tax year starts
- The qualifying condition is met in a year in which -
 - Annual turnover - not more than £10.2 million

What is 'Small'?

- Connected persons
 - s60G ITEPA 2003
 - If connected at the *end* of the assessment year (ie the financial year or calendar year depending if an undertaking or other person)
- Include the turnover of the connected persons from their respective relevant financial or calendar years
 - If the connected person is a member of a group, don't include turnover from other members of that group unless they are also connected persons in their own right

Private Sector Client ceases to be medium or large

- s61TA ITEPA 2003
- Must issue a statement before start of the next tax year:
 - To the worker (and also to the “fee-payer” if they had previously been issued with an SDS)
 - Informing that no longer medium or large
 - Withdrawing the SDS from start of next tax year
- IR35 liability reverts to the PSC
- Failure to issue renders the Client liable



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