Preparing for the new IR35 Off Payroll Rules
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IR35 Explained

Background

IR35 isn’t new – it’s a piece of anti-avoidance tax legislation that was introduced in April 2000.
It only applies to contractors who supply their services through a limited company (also referred to as a ‘Personal Service Company’ or ‘PSC’). It doesn’t affect workers engaged via Umbrella or PAYE models.

IR35 requires the PSC contractor to pay the same employment tax and national insurance on fees paid to its PSC as directly engaged employees - if the reality of the work done is akin to employment (aka “disguised employment”).

Historically, it was the responsibility of the PSC to determine whether the PSC contractor was working inside or outside IR35 and (if inside IR35) to pay the appropriate taxes and national insurance contributions (NIC) due. This meant that the legislation was relatively ineffective as HMRC didn’t have the resources to pursue all incorrect assessments made by PSCs.

To combat this, HMRC started with the public sector – reforming the IR35 legislation in 2017 with the introduction of the off-payroll rules. The key changes were:
- The responsibility for deciding if the PSC contractor was inside or outside IR35 moved from the PSC contractor to the end user client.
- Where the end user client determined that the PSC contractor was inside IR35 - the responsibility for making income tax and NIC deductions from the PSC contractor’s fees shifted to the “fee payer” (typically the end user client or recruitment business).

Private Sector Reform – What is Changing?

In April 2020, the Government intends to extend the off-payroll rules into the private sector for all medium and large companies that engage with PSCs. Small businesses will be exempt.

Draft legislation was published in July 2019 (to be finalised later this year) becoming law on 6th April 2020. Consultation is due to continue in the run up to April 2020 to fine tune how the new rules will apply in practice.

As with the public sector IR35 regime, end user clients will be required to assess whether there would be a deemed employment relationship where services are provided to it by a PSC. Once the end user client has carried out its assessment it must issue a Status Determination Statement (SDS) to the PSC contractor and the party it contracts with confirming its finding of inside or outside IR35 status. Each subsequent party in the supply chain will be required to pass the SDS on until it has reached the fee payer (typically the recruitment business).

End user clients are expected to use “reasonable care” in making an assessment and PSC contractors will have the right to appeal an inside IR35 assessment if they feel it is incorrect. When this happens, the end user client must provide a response to the appeal within 45 days confirming why it believes the assignment is inside IR35 or withdrawing the SDS and issuing a new one.

Where a PSC contractor is assessed as inside IR35 - then liability for making PAYE deductions, NICs and the Apprenticeship Levy will shift to the fee-payer (e.g. the recruitment business).

Practical points for end users:
- For any assignments with PSC contractors that are likely to continue past March 2020 – assess IR35 status now.
- Develop your IR35 assessment process and train those will implement it.
Tools available for assessing IR35 status?

Checking employment status is fact specific and in some cases there is no clear outcome. Some options for assessing the assignment are:

**HMRC’s Check Employment Status for Tax (CEST) Tool**
- HMRC’s on-line tool for assessing employment status.
- Widely criticised by industry professionals for producing inaccurate and inconclusive results in difficult or borderline cases.
- It has no legal effect and while the outcome is binding on HMRC – HMRC can still challenge it if the (subjective) questions have been answered incorrectly.
- HMRC is due to release an updated version of CEST prior to April 2020 but it is unclear how substantive the changes will be.

**Other on-line tools**
- A number of other on-line tools have come to market recently that claim to provide a more comprehensive approach to determining status.
- As with CEST, whether these tests will be effective will depend on the reliability of the information that goes into them and the suitability of the questions used to carry out the assessment.

**Outsource to a professional IR35 advisor**
- There are a number of SRA regulated law firms with significant experience and expertise in IR35.
- In cases where IR35 status is potentially unclear, such firms can advise on the “grey areas” and discuss the possibility that aspects of the working practices might be changed in order to move a PSC contractor/role outside IR35.
- Depending on the quality of the provider - this can be a very practical solution.

**In-House**
- Depending on the size of your business, you may have an in-house tax or appropriately skilled HR team that can take on the task of carrying out assessments.
The employment status tests
What do you need to look at?

When you assess whether a PSC contractor is genuinely operating outside IR35, employment status tests must be applied. The tests haven’t been codified, there is no set list, but the key factors that determine a PSC contractor’s IR35 status are set out below:

**Control**

- To fall outside IR35, the PSC contractor should have a high degree of expertise and knowledge and shouldn’t be subject to control in terms of how, where and when the work is to be carried out.
- However, “control” shouldn’t be confused with monitoring the progress or quality of the work being undertaken - which is a reasonable approach adopted by end users to ensure that the services are progressing according to the overall project plan.

**Substitution**

- The contractor agreement shouldn’t place any obligation on the PSC contractor to provide a personal service to the end user, as personal service is a strong indicator of employment.
- The PSC should have the right to provide a substitute and ideally should have actually done this on past occasions or on the assignment.
- The contract between the first-tier (recruitment business and client) and second tier (recruitment business and contractor) should reflect this where it applies.

**Mutuality of obligation**

- If the PSC contractor is obliged to be present every day at the end user’s offices and the end user is obliged to provide the PSC contractor with work - it can show that there is a “mutuality of obligation” between the parties. This is also the case where you have long assignments with mutual notice periods. All of which can indicate employment.
- In a genuine contractor relationship there is no obligation on the client to provide ongoing work and no obligation on the contractor to accept it.

**Financial risk**

- The PSC should incur financial impact/hardship for any failure arising in the delivery of the services e.g. having to rectify poor quality services at their own cost.
- The PSC should be accountable and responsible and carry the risk of non-payment by the end user as well as having appropriate insurances.

**Other relevant questions to ask**

- Does the PSC contractor invest in their own business?
- Is the PSC contractor integrated into the business of the end user – e.g. managing permanent staff and presented internally as part of the team?
- Does the PSC contractor provide their own equipment and training?
- Does the PSC contractor receive holiday/sick/ maternity pay or any other employment or worker type perks from the end user?

You must look at the reality of the entire arrangement – not just what the contract says. It can be difficult to reach a concrete conclusion in every case.
Barclay Simpson is pleased to announce we are partnering with the leading IR35 law firm in the UK - Brookson Legal to help our clients get prepared.

https://www.brooksonlegal.co.uk/who-we-are/about-us/

Brookson Legal has advised hirers, agencies and contractors on IR35 since its introduction in April 2000 - carrying out thousands of employment status assessments each year.

Through this partnership, Brookson Legal will be able to offer clients the following services:

**Education**
- Bespoke education packages (delivered through presentations, seminars and webinar) to explain the new rules to key stakeholders in the business, so that they know and understand the challenge they have ahead of April 2020 and, where necessary, begin to change the way in which they work with contractors.

**IR35 Audit**
- IR35 audit of existing contractor populations – to identify roles that are clearly inside or outside of IR35 and where you might consider changes to working practices.

**Development and implementation of compliant processes**
- Taking the output from the IR35 audit - new policies, processes and structures can be put in place so that we can work together compliantly and with the least impact upon resourcing and cost.

**On-going Support**
- Brookson Legal provide an IR35 helpline, manned by IR35 experts, with queries answered quickly and constructively.
- They can also carry out a periodic audit so that our clients are in a position to demonstrate to HMRC that they have applied the new rules with "reasonable care" as required by the law.
To put it simply, a Statement of Work or “SoW” is a legally binding, commercial agreement which is used to define and measure the delivery of a piece of work – the project or outcome.

A SoW contract is only suitable for assignments involving contracted out services i.e. where there is no requirement for personal service by particular contractors. SoW contracts are genuinely outcome or delivery based and independent. A SoW contract would list all the work that a supplier will carry out during a project - usually with payments made on successful completion of milestones - as opposed to payments made on a time and materials basis.

Where an end user client buys a SoW style service, it will not have the obligation to assess the IR35 status of the PSC contractor(s) involved in providing the services. This will be the responsibility of the provider of the SoW service.

When used correctly, the SoW model will ensure outside IR35 compliance for all PSC contractors provided as part of the service but, merely labelling an assignment as a SoW will not be enough - the SoW must be legitimate.

In addition, the following requirements in a SoW arrangement must also be met:-

- Zero Direction, Control or Supervision on the activity being undertaken by the PSC – achieving the deliverables is the responsibility of the supplier.
- The PSC has the freedom to deploy, as they deem appropriate, any suitable replacement contractor (right of substitution) or possibly add more people to the project/outcome – at the PSC’s cost.
- Financial impact/hardship for any failure in the delivery of any outcome for which they are accountable & responsible.

Taking all of the above elements, detailing and documenting them well and in-turn defining payments that are based on performance will all help to ensure any contractor/PSC are operating outside of IR35.

Talk to us about whether a particular assignment may be suitable for SoW and we can help manage and document the process.
The end user client must produce the IR35 status determination and the supporting reasons and communicate this down the supply chain to the PSC contractor and fee payer (e.g. the recruitment business who pays the PSC). In addition, the end user client must also facilitate a status disagreement process and respond to any status challenge by a PSC contractor within 45 days.

Where a PSC contractor is assessed as inside IR35 - provided that the end user client carries out these responsibilities properly - liability for making PAYE deductions, NICs and the Apprenticeship Levy will shift to the fee-payer (e.g. the recruitment business). Liability will remain with the end user client if it directly engages the PSC contractor (i.e. not by a recruitment business) or if it fails to:

- issue an SDS and pass this on to the PSC contractor and/or next party in the supply chain;
- use "reasonable care" in making a status determination and has incorrectly assessed as outside IR35;
- respond to an appeal by a PSC contractor within 45 days of the request.

It is also critical that end user clients take care to ensure compliance in their supply chain – working with reputable recruitment service providers. This is because they may still be on the hook for PAYE, NICs and the Apprenticeship Levy if the fee payer fails to make appropriate deductions and HMRC cannot settle the liability – as set out in the HMRC example below.
Steps to take now to prepare

**Step 1: Identify where you have temporary workers operating via a PSC in your supply chain**
- Check all your arrangements where workers are provided by agencies/other third parties i.e. through PSCs/partnerships or any other individual.
- Establish what they are doing.
- You can ignore temps working through a recruitment business as PAYE or umbrella workers as the recruitment business or the umbrella are already deducting full tax and NICs.

**Step 2: Make employment status determinations**
- An employment status determination should be carried out for each of your current off-payroll contractors where the assignment is likely to continue past March 2020.
- For any temporary resourcing needs from April 2020 onwards – you should assess the role and whether it would likely be inside or outside IR35 or suitable for SoW - and communicate with your recruitment service providers.
- We can assist you in this process and arrange input from Brookson Legal.

**Step 3: Analyse the results and communicate your findings**
- Role definitely "inside" – decide whether the role is critical and what rate would need to be paid on an inside IR35 basis. Terminate the current assignment before March 2020 and negotiate a change of pay structure and rates via the recruitment business to take effect post March 2020.
- Role definitely "outside" – potentially no action needed except future periodic monitoring.
- Borderline role – consider possibility of changes to working practices to strengthen "outside" IR35 status.

**Step 4: Educate your team about status determinations and set up a process**
- Set up a process for assessing status of new temp roles post April 2020 – talk to us and Brookson Legal for assistance in this area.
- Set up a process for status determination challenges.
- Educate all your people who will be involved in the process.

**Step 5: Future proof contracts with agencies**
- Update contracts with your recruitment providers to confirm the responsibilities of the parties post April 2020.