



What is IR35?

IR35 is the name given to tax legislation in the Income Tax (Earnings and Pensions) Act 2003 (ITEPA), it applies to individuals supplying their services through an intermediary, usually a personal service company (PSC).

The IR35 legislation seeks to ensure that contractors working through their own PSCs pay employment taxes and NICs where, were it not for the PSC they work through, they would be employed by the client, commonly known as “inside IR35”.

If IR35 applies, then PAYE and National Insurance contributions are deducted from the rate. This prevents the contractor being paid a minimum salary, up to the limit of his/her tax-free allowance and leaving the rest in the company. If money is withdrawn from a company as a dividend, although tax is due at the dividend rate, there are no NICs payable.

When does IR35 apply?

IR35 applies where the worker operates through a UK limited company. If you engage and supply contractors who work via an intermediary (typically a PSC), where taxes and NICs are not deducted at source, then you are likely to be affected by IR35.

How is the employment status of a worker assessed?

HMRC provides an employment status tool to find out if you, or a worker on a specific engagement, should be classed as employed or self-employed for tax purposes: <https://www.gov.uk/guidance/check-employment-status-for-tax>

Further information can be found in the employment status manual <https://www.gov.uk/hmrc-internal-manuals/employment-status-manual/esm11000>.

Can I rely on the status determination produced by CEST?

HMRC have said that if the parties use the employment status tool and input information which is accurate and honest, and the answers remain accurate during the contract, then HMRC will stand by the outcome.

IR35 Criteria

Some of the factors considered when assessing employment status and whether or not an assignment would be inside or outside of IR35 are (this is not exhaustive):

- The contractor is not under supervision, direction or control of anyone in the supply chain as to the manner in which the services are provided. The contractor provides independent services, and the client does not treat them as if they are “part and parcel” of their organisation.
- The reality of the situation is that the contractor is responsible for the delivery of the services, and determines, and controls when and how they undertake the work they do for the client, as long as they meet client-specific targets or project completion dates.
- The contractor does not have to perform the work or services personally, and the client has to accept a substitute (subject to that substitute having the requisite skills and capabilities).
- The PSC maintains adequate business insurances.
- The PSC submits invoices for work completed or agrees to a self-billing arrangement.
- The PSC is responsible for paying the required taxes and statutory deductions on amounts paid in respect of the work undertaken. All amounts are treated as trading income.
- The contractor/PSC is only paid for services performed. There are no payments made for any time when the contractor is not available for work (including but not limited to holiday pay or sick pay). The client has no liability to pay for any periods during which the contractor is not providing their services.
- It is important to consider the factual reality of an assignment, not what the contract says.

The client has determined that the assignment is “inside IR35”, what are the options?

If an assignment is determined as “inside IR35”, there are various alternative engagement models to an off-payroll model:

PAYE payroll (agency workers) – Where a recruitment company contracts directly with the worker and operates tax and NICs under agency rules and provides the workers with worker rights, IR35 off-payroll rules do not apply.

Umbrella Company – Where an umbrella company employs the worker directly, the off-payroll working rules do not apply.

“Inside IR35” PSC – A contractor who is deemed “inside IR35” via their PSC, will be paid via a “deemed employment payment” using the RTI (Real Time Information) payroll system. The deemed employment pay rate is the income of the worker after deductions, including both employee and employer NICs and the Apprenticeship Levy. Neither worker rights nor stakeholder pension rights apply.

Statement of Work - A Statement of Work (SoW) is a document, typically used in project management, which defines a set of project-specific activities, deliverables and timelines for a contractor providing services to a client.

In an assignment where a contractor agrees to perform specific tasks or deliver certain outcomes for a set price and within an estimated delivery time, there is less likelihood of the client exerting control over the contractor. A SoW contract, if appropriately executed, is likely to be “outside IR35”, compared with the traditional time and materials-based contract on a set hourly or day rate.

If a contractor works for lots of different clients, does IR35 still apply?

The off-payroll working rules will still apply irrespective of how many clients and assignments a contractor is working on. Where a contractor is working on multiple projects for various clients, and is not financially dependent on any one client, then this is evidence that they are in business on their own account as an independent contractor, which supports an “outside IR35” assessment, forming part of the overall picture.

However, IR35 status is assessed on an assignment basis.

The client is making blanket determinations for all contractors, can I accept this?

One of the biggest issues to arise from the public sector reform in April 2017 was blanket “inside IR35” determinations. This resulted in a large number of contractors being moved into umbrella arrangements. It became clear that such a blanket assessment would not meet the statutory obligation to take reasonable care when making an IR35 status determination. Clients can take a role-based approach if they have a number of contractors working on the same contract on similar terms and conditions.

Clients choosing not to engage with PSCs in their supply chains is not the same as making a blanket determination.

How will payrates be affected by the new rules?

If an assignment falls “inside IR35”, the take-home pay for the contractor will be less as there is a statutory duty to deduct the appropriate tax and NICs.

Are “inside IR35” contractors entitled to employment rights?

Should a contractor choose to continue operating via their PSC although the assignment is “inside IR35”, they will not benefit from any “employee rights” such as holiday pay, sick pay, pension contributions, dismissal rights etc. Contractors receive these benefits through their employment in their PSC.

Off-payroll Working Rules – Delayed Until 2021 Revised Draft Legislation Published

Following the announcement on 17 March 2020 that the Government was to delay the reform to off-payroll working rules in the private sector to 06 April 2021, the latest version of the amendments to Chapters 8 and 10 of Part 2 of ITEPA 2003 were published in the Finance Bill on 18 May and can be

found https://publications.parliament.uk/pa/bills/cbill/58-01/0114/amend/finance_rm_pbc_1805.1-4.html and the accompanying notes <https://www.gov.uk/government/publications/finance-bill-2020-public-bill-committee>.

Following agreement by both Houses on the text of the bill, the Finance Act 2020 received Royal Assent on 22 July 2020 (<https://www.legislation.gov.uk/ukpga/2020/14/contents/enacted/data.htm>).

The reforms apply to people contracting their services through intermediaries, most usually a personal service company (PSC) to the public sector and large or medium-sized private sector organisations with a UK connection.

Changes in Finance Act 2020 (compared to the 2019 Finance Bill) arising from 2020 Review of Implementation

Non-UK Clients: Limiting the rules to UK resident clients and clients with a UK permanent establishment immediately before the beginning of the relevant tax year (Clause 60I). Existing rules

- Deeming some non-UK clients to be UK resident are repealed (paragraph 15 of the Finance Bill). UK residency and permanent establishment are legally complex. The legislation on permanent establishment for a company can be found <https://www.legislation.gov.uk/ukpga/2010/4/part/24/chapter/2> and guidance <https://www.gov.uk/hmrc-internal-manuals/international-manual/intm153060>.
- **Status Determination Statements (SDS):** Ensuring changes apply only to services provided on or after 06 April 2021, with payments for assignments straddling the implementation date having “just and reasonable” apportionment being made. SDS and disagreement process representations may be made earlier but clients are deemed to receive disagreement process representations only on commencement, namely 06 April 2021.
- **Status Disagreement Process:** Representations that the status is incorrect can be made by the worker or deemed employer any time up to the final chain payment being made for an engagement (61T (1)). The client must give a statement to the worker or the deemed employer (depending on who made the representation) that either the SDS is correct with reasons or give a new SDS, stating the date from which the client considers that the conclusion in the new SDS became correct and stating that the previous SDS is withdrawn. The deemed employer is deemed to have received the reply from the person above it in the chain of supply.

The client has 45 days beginning with the date the client receives the representations to respond. If it fails to meet that deadline then from that date on it carries fee payer liability until it complies.

- **Size of Client:** Requirement for clients to state, in their opinion, if asked, whether it qualifies as small in a tax year (60H). The “client’s agent” (the agency/recruiter with whom the client has a contract) or the worker can make the request if the meet the following conditions:
- The worker personally performs, or is under an obligation to perform services for the client;
- The client is not a public authority; and o the services are provided under arrangements involving a third party (‘the intermediary’) and not under a contract directly between the client and the worker.

The client must respond to size-related information requests for the relevant tax year within the later of 45 days of receipt and if they fail to do so within the time limit the party can apply to court for an injunction (Scotland) or specific performance under the Court of Session Act 1988 (England and Wales).

- **Debt Recovery from Client or Agency 1:** The legislation is now clearer on when an unpaid PAYE debt payable by a deemed employer (the fee payer) can be recovered from others (relevant persons) (Schedule 1, Part 3, Paragraph 19 of the Finance Act 2020 amendment to S688AA ITEPA 2003). If an HMRC officer considers there is “no realistic prospect of recovering from the deemed employer within a reasonable period” then HMRC can recover from the highest person in the chain or the second highest person in that chain, where that agency is also resident in the UK.

Impact

These amendments are made following announcements by the Government after its review of IR35 implementation earlier this year, so do not come as a surprise.

Supply chains in the private sector can continue as normal for now, with contractors responsible and liable for their IR35 status. SDS's issued by clients have no legal standing although they are evidence of how the client views the assignment and should be taken into consideration by the contractor when making their decision on status. The contractor must take actual working practices into account in making their decision and keep that decision under review during an assignment.

Contractors must have regard to the fact that under the existing rules they have always been legally responsible for making the status determination on IR35 status by assignment and should continue to use HMRC's employment status for tax tool (CEST) or take the advice of a third-party specialist to make the decision.

Public sector clients must continue to follow the 2017 Off Payroll rules as of present.

Some clients particularly in the finance sector have issued variations stating that no PSC contractors can be supplied to them and all contractors must be on payroll. We do not anticipate immediate reversals of these decisions. Again, clients will be focusing on mitigating the impact of the Coronavirus.

Annex – Detailed list of changes to the legislation

1. Review

Section 60H sets out the requirement for clients to confirm whether they qualify as small for a tax year, if they receive a request from the worker or party they contract with. Clients have 45 days to provide confirmation.

- Numerous sections are amended to give effect to the change regarding the treatment of overseas clients:
 - Paragraph 2 amends the heading of Chapter 8 of Part 2 of ITEPA 2003 so it reflects the new scope of the Chapter, which now only covers workers providing services through an intermediary to small clients and clients without a UK connection outside the public sector.
 - Paragraph 3 adds the phrase “or does not have a UK connection for a tax year” to the scope of to whom Chapter 8 of Part 2 ITEPA 2003 applies.
- Paragraph 4 amends section 50 of ITEPA 2003, which treats the worker as having received earnings from employment if certain conditions are met. Sub-paragraph 4(2) inserts new section 50(1) (za) which introduces a new condition which requires

the client to qualify as “small” or have no UK connection in order to treat payments, arising from these engagements, as earnings from employment.

- Paragraph 5 introduces new sections 60A to 60I, into ITEPA 2003. These sections set out the conditions under which a client will qualify as “small” for the purposes of Chapter 8, as well as the duty on a client to confirm in response to requests from the worker or party the client contracts with, whether they qualify as “small”. The sections also set out when a person is treated as having a UK connection.
- New section 60I outlines when a person has a UK connection for the purposes of Chapter 8 of Part 2 of ITEPA 2003.
- Paragraph 9 amends section 61K of ITEPA 2003, to widen the scope of Chapter 10 of Part 2 of ITEPA 2003 to bring into scope all public authorities and any client that has a UK connection in accordance with new section 60I and does not qualify as “small” as provided for in new sections 60A to 60G.
- Subparagraph 11(2) expands the definition of a client to include public authorities and medium or large clients with a UK connection.
- Subparagraph 12(5) amends new section 61NA to include “or does not have a UK connection”.
- Paragraph 15 removes subsection (7) of section 61R, which sets out the circumstances in which a public sector client not resident in the UK would be treated as being resident in the UK for the purposes of Chapter 10 of Part 2 of ITEPA 2003.
- Paragraph 30 sets out the transitional provision whereby the rules in Chapter 10 of Part 2 of ITEPA 2003 will not apply to chain payments made on or after 6 April 2021 in respect of services performed by the worker before 06 April 2021. This transitional provision does not apply to public authorities within the scope of Chapter 10 prior to the amendments made by paragraph 10 of Schedule 1.

2. Incidental changes and corrections to ensure the legislation applies as intended

- Paragraph 13 (rather than 12(6)) now introduces section 61NA.
- Paragraph 14 substitutes new paragraph 61O(1)(b) to expand the conditions where an intermediary is a company to include where a worker has received a chain payment from the intermediary or where the worker is entitled to receive a chain payment from the intermediary.
- Paragraph 16 (rather than 13) now introduces sections 61T and 61TA.
- Section 61T (3) rather than (2) requires the client to respond to representations from a worker that the Status Determination Statement is incorrect within 45 days.
- Section 61T (3) rather than (5) provides that the client will be treated as the fee-payer if it fails to fulfil its obligations under section 61T.
- Paragraph 17 amends section 61W to apply to ‘the client’ rather than a public authority.
- Paragraph 18 (rather than 14) amends section 61D and introduces subsections 4A to 4C into section 61D.
- Paragraph 19 (rather than 15) introduces section 688AA, which has now been amended to specify the parties in the labour supply chain from which HMRC can seek to recover unpaid tax using the recovery from other persons power. These parties are limited to the first agency in the labour supply chain and the client.

- Paragraph 20 (rather than 16) inserts subsections 3A, 3B and 3C into section 60 of the Finance Act 2004.
- Paragraphs 21 and 22 make consequential amendments to the cross heading before section 141A of the Corporation Tax Act (CTA) 2009 and the heading of section 141A to take into account the changes made to the new scope of Chapter 10, of Part 2 of ITEPA 2003.
- Paragraph 23 makes consequential amendments to Part 13 of CTA 2009 to ensure that claimant companies can continue to claim the same amount of relief for expenditure on research and development in light of the new rules for intermediaries.
- Sub-paragraph 23(2) inserts a new subsection (4A) into section 1129 and sub-paragraph 23(3) inserts a new subsection (3) into section 1131 of Part 13 of CTA 2009, which cover the situation where the company claiming the research and development tax relief makes payments to HMRC under section 61S of ITEPA 2003 and primary Class 1 National Insurance contributions under regulation 19 of Social Security Contributions (Intermediaries) Regulations 2000, or regulation 19 of Social Security Contributions (Intermediaries) (Northern Ireland) Regulations 2000.
- Sub-paragraph 23(4) inserts a new section 1131A of Part 13 of CTA 2009, which covers the situation where the company claiming the research and development tax relief makes payments to HMRC in respect of secondary Class 1 National Insurance contributions as a result of making use of externally provided workers.

3. Commencement

- Paragraph 24 sets out that the amendments made in Part 1 will have effect for tax year 2021-22 and subsequent years.
- Paragraph 25 sets out that the amendments made in Part 2 will only have effect in relation to deemed payments made on or after 6 April 2021.
- Paragraph 26 sets out that the amendment made by paragraph 18 has effect where payment or benefit is received on or after 6 Apr 2021.
- Paragraph 27 sets out that the amendments made by paragraph 20 of Schedule 1 will have effect in relation to payments made under a construction contract on or after 6 April 2021.
- Paragraph 28 sets out that the amendments made by paragraph 23 of Schedule 1 will have effect in relation to expenditure incurred on or after 6 April 2021.
- Paragraph 29 sets out that interest under sections 101 to 103 of Finance Act 2009 come into force on 6 April 2021 in relation to amounts payable or paid to HMRC in respect of a PAYE debt.
- Paragraph 31 states that where a qualifying chain payment was made to the worker's intermediary on or after 6 April 2021 in respect of services performed by the worker before 6 April 2021, Chapter 8 of Part 2 of ITEPA 2003 will apply to that chain payment.
- Paragraph 32 sets out that where a chain payment is made in respect of services provided over a period that begins before and ends on, or after, 6 April 2021, the payment shall be treated as two separate chain payments apportioned on a just and reasonable basis.
- Paragraph 33 sets out that sections 61N(5), (5A)(a) and (8)(za) of ITEPA 2003 will apply from 6 April 2021 even if a status determination statement is given before that date.

- Paragraph 34 sets out that it does not matter for the purposes of new section 61T of ITEPA 2003 if the client receives representations before 6 April 2021 as the 45 days for responding will start from 6 April 2021.