

Key Points

- Draft legislation published on 11 July 2019
- Off-payroll reform in the private sector takes effect from April 2020
- Prepare for the changes
- Understand the alternative engagement models
- Communicate with the supply chain – the agency and the end client
- Challenge any status determinations you do not agree with

CONTRACTOR GUIDANCE ON IR35 OFF-PAYROLL REFORM IN THE PRIVATE SECTOR - WHAT TO DO NEXT

BACKGROUND

The Chancellor announced at Budget on 29th October 2018 that the government will reform the off-payroll working rules (known as IR35) in the private sector. This follows *consultation* and the roll-out of reform in the *public sector*. The responsibility for operating the off-payroll working rules will move from individual contractors to the organisation, recruitment business or other third party contracting with and paying the contractor (the “feepayer”). Small client organisations are exempt. The new rules are scheduled to come into force in April 2020.

The Government consultation closed on 28 May 2019, and on 11 July 2019 the *draft legislation, explanatory note and summary response document* was published. Following this, in August the Government also published new and updated guidance on the new rules including a guide on the *April 2020 changes to off-payroll working for intermediaries*.

WHEN THE OFF-PAYROLL WORKING RULES (“IR35”) APPLY

The off-payroll rules apply if a worker provides their services to a client through an intermediary (your personal service company (PSC)) but would be classed as an employee if they were contracted directly with the client. Before 6 April 2020, if your client is in the private sector, it's your limited company's responsibility to decide your own employment status for each assignment.

From 6 April 2020, how the rules are applied will change. All public sector authorities and medium and large-sized private sector clients will be responsible for determining whether or not the rules apply – i.e. are you “inside IR35” or “outside IR35”? Where the private sector client is considered “small”, your limited company will remain responsible for deciding the contractor's employment status and whether IR35 applies.

Where IR35 is applicable and the client makes the status determination, the contractor's fees will be subject to tax and National Insurance contributions. These deductions will be levied by the “fee-payer” which is the entity who holds the contract with your limited company, typically this is the recruitment business.

SMALL COMPANY EXEMPTION

The new off-payroll rules will only affect medium and large private sector organisations, so “small” end clients are set to be exempt - the definition of which is based on the Companies Act 2006 definitions. The government anticipates the changes will not apply to the smallest 1.5 million businesses, which may need flexible resource.

The existing off-payroll working rules will continue to apply for assignments if you are providing services to a client classed as a “small” company, meaning that the responsibility for making the status determination remains with the PSC.

Under section 382 of Companies Act 2006, a client qualifies as “small” if two of the following conditions apply:

- 1. Annual turnover** **Not more than £10.2 million**
- 2. Balance sheet total** **Not more than £5.1 million**
- 3. Number of employees** **Not more than 50 employees**

Please note that the small company exemption applies to the end client, not the fee-payer or the PSC. The recruitment business should inform you if the client is a small entity, however there is no statutory obligation to do so. Therefore, you must make enquiries when discussing the assignment details, as you will have the responsibility and liability to apply the off-payroll working rules when the client is a “small” company.

MAKING THE STATUS DETERMINATION - “INSIDE IR35” OR “OUTSIDE IR35”

From 6 April 2020, it will be the client’s responsibility to determine whether the off-payroll working rules apply,

i.e. is this assignment “inside IR35”? You can refer to the [*HMRC guidance and the employment status for tax \(CEST\) tool*](#). Although much criticised, the CEST tool does give you a good steer of the approach taken by HMRC and the indicators that they are looking for. HMRC have confirmed that they are making enhancement to the CEST tool, these changes are expected to be delivered before the end of 2019.

Assignments “Outside IR35”

When the client makes the status determination that an assignment is “outside IR35”, they must ensure that “reasonable care” was taken during the decision-making and that the decision itself is reasonable. If the client does not exercise reasonable care, the status determination statement will not be valid, and the client will be liable for the unpaid taxes. HMRC have confirmed that it will issue detailed guidance in late 2019, which will include further details on “reasonable care”.

Assignments “Inside IR35”

If the client determines that an assignment is “inside IR35”, you need to understand what options are available in terms of an alternative to an off-payroll model. The options are:

- **PAYE payroll (agency workers)** - Where a recruitment business contracts directly with the worker and operates tax and NICs under agency rules and provides the workers with worker rights - the offpayroll working 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** - Should you wish to continue to engage as a contractor via your PSC who is deemed “inside IR35”, your recruiter will need to calculate 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. No expenses allowance applies.

Incorrect determination

If the off-payroll proposals are legislated in their current form, where HMRC disagrees with the determination made, it can investigate and insist on back payment of tax, as well as fines for late payment from the feepayer.

FREQUENTLY ASKED QUESTIONS

I work for lots of 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. There is the argument that if you are working on multiple projects for various clients, this will demonstrate that you are in business on your own account as an independent contractor, and therefore fall “outside IR35”. However, your IR35 status is assessed on an assignment basis - working for multiple clients is not a significant indicator of being in business on your own account; the IR35 status for each assignment is judged on its own merit.

The client does not understand/will not apply the new IR35 rules, do I need to worry?

From April 2020, all public sector authorities and medium and large-sized private sector clients will be responsible for deciding whether IR35 applies. If the client either 1) fails to make a status determination, 2) fails to pass the status determination down the supply chain, or 3) fails to take reasonable care when making the status determination; the client may be liable for the tax and NICs as the deemed “fee-payer”.

Contractors are advised to engage with their agencies and clients regarding the new rules to help to ensure that all parties are prepared for April 2020. It is important that clients exercise reasonable care when making a status determination, given the issues that arose from the public sector reform in April 2017 as a result of blanket “inside IR35” determinations.

If you are providing services to a small private sector client, they will be exempt, and they are not required to follow the new IR35 rules. Your PSC will remain responsible for determining your IR35 status and making the appropriate tax deductions and NICs.

Can I be involved in the client’s status determination?

It is expected that you will be involved to some degree in the client’s status determination process, as there are some questions in the HMRC CEST tool which require the contractor’s input - for example questions on how you run your business. However, there is no statutory right for a contractor to be consulted during the status determination process.

I do not agree with the client’s status determination, can I appeal it?

The draft legislation imposes an obligation on the client to provide a “client-led status disagreement process”, either the recruiter or the contractor may disagree and follow the process. The client must respond to a request to review the status determination

statement within 45 days. The client must either confirm the determination is correct, with reasons, or provide a new status determination statement reaching a different conclusion and withdraw the previous one.

If you disagree with the client's determination, you will need to write to the client and give reasons why. You need to ensure you keep records of status determinations and any corresponding disagreements. During the dispute process the client's determination stands.

Will my rate be affected by the new rules?

If your assignment falls "inside IR35", the take-home pay will be less as the recruiter has a statutory duty to deduct the appropriate tax and NICs. Be aware that historically, PAYE rates have always been lower than PSC rates so you may find that in future pay rates offered are lower.

Can I be forced to pay for employer's NICs?

Recruitment businesses cannot lawfully deduct secondary NICs from an agreed fee, but recruitment businesses may adjust the contractor's pay rate to factor in the additional costs of supply which include employers' NICs. Depending on your contractual terms, there may be scope for the rate to be negotiated accordingly.

Do I get employment rights if I am "inside IR35"?

Should you wish to continue operating as an "inside IR35" contractor, you will not benefit from any "employee rights" such as holiday pay, sick pay, pension contributions, dismissal rights etc. You may receive these benefits through your employment in your PSC.

If your assignment falls "inside IR35", it is likely that you are no longer in business on your own account and could be within scope of the Agency Worker Regulations (AWR). Under AWR, you are entitled to comparable pay to a permanent employee on the client site. If you opt to engage via an umbrella company, you are an employee of the umbrella company and therefore you will benefit from employment rights and AWR will apply.

My assignment is for 2 years - is it automatically "inside IR35"?

The 24-month rule is in reference to claiming travel expenses. This rule has no bearing on the IR35 status of an assignment.