




Guide to IR35

Managing the
new compliance
requirements

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Is your business ready for changes to IR35 from 6 April 2021?

Organisations need to be considering the IR35 changes and how they are going to manage these new compliance requirements. Our easy to use guide outlines the steps you should be taking and what the change means.



IR35



IR35 Steps to Compliance

January 2021 or sooner:

Meet with HR, finance, and operations to identify consultants and form a preliminary view on risks. Identify types of contracts and prioritise consultants that are engaged most frequently

Early February 2021:

Communicate with consultants and ask for any relevant information to assess IR35.

February 2021:

Carry out individual assessments of consultants to determine status. Complete CEST tool but be aware of limitations.

Late February 2021:

'Sense check' the CEST tool results against professional advice.
Advise consultants of results directly.

Late February/Early March 2021:

Issue Status Determination Statement (SDS) to consultants.

Post Late February/Early March 2021:

Allow for 45 day disagreement/appeal process.

March 2021:

Implement changes to status where required and update contracts to include appropriate clauses

Record

Keep records of your assessments and information relied on to demonstrate compliance



Changes from 6 April 2021

What is IR35?

Broadly speaking, there are three categories of employment status – employee, worker, and self-employed. The self-employed include sole traders and those working under a limited company or Personal Services Company. However, these definitions are not the same in employment law as they are in tax law. Unlike employment law, tax law only recognises two categories – employed and self-employed. Employment status is not a choice, it is determined based on the contract terms and crucially how these operate in practice.

IR35 is aimed at targeting contractors engaged through intermediaries, normally limited companies, where an individual is supplied to the client through a limited company and there is no direct contact between an individual and a client, although the individual may act similarly to an employee. At particular risk of IR35 are limited companies which have been set up to provide the services of a single contractor (usually the sole shareholder/director) which are known as Personal Service Companies (PSCs). These individuals are also commonly referred to as “off payroll workers”.

Background to IR35

PSCs became increasingly popular in the 1990s as they allowed individuals to structure their working affairs in such a way that resulted in individuals paying less tax and national insurance, as they could be classed as self employed. In 2000, the Government introduced IR35 legislation to recover some of these amounts where the structure was seen as ‘disguised employment’. However, HMRC struggled to enforce this as the burden was on the PSC or intermediary to determine whether there was ‘disguised employment’ and therefore HMRC had to enforce this against each individual PSC.

To address this from April 2017 Public Sector Bodies (PSBs) have been required to determine if IR35 applies to their ‘off-payroll’ workers. This change saw an increase in tax revenue as HMRC was able to enforce larger amounts against the end client. Due to this success the new IR35 rules were introduced. They were originally due to apply within the private sector from 6 April 2020 but this was postponed to 6 April 2021 given the impact of the Covid-19 pandemic.

What are businesses required to do from April 2021?

From 6 April 2021 medium and large sized private bodies which engage individual contractors or consultants through intermediaries or PSCs will be required to determine their status. We have set out further details below, but this test essentially comes down to whether the worker would be regarded as an employee of the client if the services had been provided under a contract agreed directly between the worker and the client.

It is ultimately the client who has responsibility for determining status regardless of how many other bodies are between the worker and the client. If there are agencies in between then they will be advised of the status of the off-payroll worker by their client and will need to make the subsequent administrative adjustments to pay.

From 6 April 2021, the liability for tax and NICs will pass down the labour supply chain.

Clients at the top of the supply chain will need to be particularly diligent to ensure that the proper payments are being made as they may be liable where payments cannot be recovered from other parties. This will occur in situations where HMRC considers there has been tax avoidance rather than a mistake made.

How do I determine a contractor’s status?

This is a legal test which looks at whether, if the individual’s company didn’t sit in the middle of the individual and the end client, the individual would be regarded as employed by the client. To determine this, a hypothetical contract is constructed taking into consideration any current written contracts and other circumstances/factors. In practice, this is likely to prove a tricky task, particularly with work relationships that have factors which both point to and point away from, IR35. The new rules require that ‘reasonable care’ will need to be taken in considering whether IR35 applies to each entity.



HMRC have created an online tool known as CEST (Check Employment Status for Tax) which business can use as a starting point. It goes through a series of questions and then gives HMRC's view of employment status, based on the information provided. Most businesses will need to request further information from the contractor before they are in a position to use the tool.

Crucially whilst HMRC confirms that it will stand by the outcome of the CEST tool, this does not apply where the information provided is inaccurate or the tool has not been used in accordance with HMRC's guidance. There are also limitations to the CEST tool and it doesn't take into account all factors. The outcome of the CEST tool can also unhelpfully be "unable to determine."

What information do businesses need to provide contractors?

Once an assessment has been made the client business must provide each contractor with a 'Status Determination Statement' (SDS). If a contractor is found to be outside the scope of IR35, it should record reasons stating why the end user considers that in addition to confirmation of the decision.

'Reasonable care' can be demonstrated by end users through showing processes are in place to obtain and consider additional information provided by individuals, having a paper trail recording matters considered, and seeking professional advice.

Statements need to be provided upon request within 45 days.

As IR35 is implemented and advisors start taking decisions about tax status, we can expect to see an increase in the number of people being taxed more, with clients and fee-payers who engage contractors making deductions for NICs and PAYE.

Do businesses need to amend their contracts with contractors?

There are several changes that businesses can make to help to protect their position under the new IR35 changes. Contracts should be updated to include obligations for contractors to update the business should any information change which may affect their status. Businesses may also want to include positive confirmation from the contractors that the information they have provided to the business is accurate. To assist in future reviews clauses can also be added confirming that the contractor will agree to amend the contractual terms should this be needed due to a change in status.

Of course if the outcome of a status determination is that they fall within IR35 the consultant may simply accept this and accept that the client will make the necessary deductions, or may discuss with the client about becoming a direct employee. Alternatively, they may decide to review the nature of their engagement to vary their working practice to bring it outside the scope of IR35, If this is the case they may wish to seek professional advice.

Who won't be affected by the changes?

Small companies will not be affected by the changes. The definition of a small company is one in which two of the following three criteria are met:

- A turnover of not more than £10.2m
- A balance sheet total of not more than £5.1m
- No more than 50 employees

This exemption will not apply if the company is a subsidiary company with a parent undertaking that is not small. Nor will it continue to apply to companies which fail to meet the criteria over two consecutive years. Agencies and compliant umbrella companies are also unlikely to be affected as they pay workers net of tax and NICs.

Jargon buster

Personal Services Company

A limited company which has been set up to provide the services of a single contractor (usually the sole shareholder/director).

Mutuality of Obligation

The obligation of the employee to personally undertake work and the employer to provide and pay for work.

Off-Payroll Worker

Workers not on PAYE payroll including contractors, freelancers, and consultants.

Intermediary

An entity that the contractor operates through, such as a PSC.

Client

A party that receives services from the worker through the intermediary.

End User

The final client in the labour supply chain.

Liability Transfer Rules

Rules to allow HMRC to transfer liabilities which may arise as a result of non-compliance down the labour supply chain to an entity at the top of the labour supply chain (such as the end client).

Status Determination Statement

A Statement declaring a contractor's deemed employment status and reasons for the status following an IR35 assessment.

Fee Payer

The party immediately above the worker's intermediary (or PSC) paying for their services.

Engagers

The party which requires the worker's services.



Speak to an expert

You can speak to any of of our team for further help or advice on IR35



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