

## IR35 and Off-Payroll Working

As a provider of services through your own limited company you will no doubt be aware of the IR35 or off-payroll regulations. In principle, the IR35 regulations need to be considered if an individual provides services via their own limited company to third parties (possibly but not necessarily via an agency). The IR35 regulations, which basically prevent companies distributing profits tax efficiently via dividends, apply where the relationship between the individual director/shareholder and the ultimate recipient of that director/shareholder's services would be an employment relationship if the intermediary company and (if appropriate) agency were ignored. In other words, are you really an employee "disguised" behind your limited company?

There is no straightforward way to determine whether IR35 should apply to a worker as there is no statutory distinction between a contract of service (employment relationship) and a contract for services (self-employed relationship) so we need to rely on past court judgements to establish the relevant factors.

The tests to establish a person's employment status have largely remained unchanged since the early case of *Ready Mix Concrete (South East) Ltd v Minister of Pensions and National Insurance* (1968), which established that three factors had to be present in order to create a contract of employment. These three factors, control, personal service and mutuality of obligations, are still considered to be the irreducible minimum in establishing employment relationships. The following issues are of only limited relevance:-

- The intention of the parties
- Provision of small items of equipment by the contractor
- Attendance of the contractor at social functions
- Training arrangements for the contractor
- Sick pay and holiday arrangements
- Payment by the contractor of minor expenses

Although these factors will be considered in any IR35 enquiry, they are incidental to the main three which are **control, personal service and mutuality of obligations**. If any of the main three are not present, then there simply cannot be an employment relationship.

### **(1) Control**

We need to establish whether the end client is controlling the work, or whether you as a contractor have a reasonable degree of autonomy over the performance of the services. This will be determined by how, where, when and what is to be performed. If a contractor wants to be seen as being independent, then they will need to have a strong degree of influence over most of these. Strong levels of control exercised over a contractor would point to an employment relationship.

### **(2) Personal Service**

The key question here is whether the contractor is entitled to send a substitute of his/her choosing to undertake the services in question. If such a situation is genuinely the case, and indeed ideally if a substitute has been used, then it is almost impossible for an employment relationship to exist and consequently very difficult for HMRC to impose the IR35 regulations.



### **(3) Mutuality of Obligations**

Here the issue is whether the end Client (or the agency) is obliged to offer you more work and if it is offered whether you are obliged to accept it. If the answer to both of these is “No”, then there is no mutuality of obligation. Compare this with an employment contract where your employer must continue to pay you even if there is no work, or make you redundant and compensate you.

### **Why is IR35 so important?**

If any contract falls within IR35 then the legislation seeks to tax the worker as if they were an employee. Whereas if the contract falls outside of IR35 the director/shareholder can organise their affairs so that they receive their income as a combination of salary and dividends which makes it much more tax efficient. 2<sup>nd</sup> shareholders can also be brought into the company making the distributions even more tax efficient.

### **Who Assesses IR35/Employment Status?**

When IR35 was introduced in 2000, it was the responsibility of the worker (as the director of their limited company) to make a suitable judgement as to whether any of their contracts fell within IR35 or outside of IR35. However, in April 2017 this changed for any contractors working for a public sector body and the responsibility for the assessment then moved to that public sector body.

From April 2021, these rules have been further extended to the private sector. (This extension had initially been postponed from April 2020 because of COVID-19.) This means that for most contracts it is the end client who has the responsibility of making a correct assessment. So, if your end client deems your contract is caught by IR35 then your fee-payer is required to deduct tax and national insurance from their payment to you (excluding vat) and pay these deductions over to HMRC.

There are, however, some exceptions to this, the main ones being in relation to the size of your end client and whether or not they are based overseas.

#### **(1) Size of End Client**

The new legislation does not apply to any end clients who meet the criteria of being a small company. If your end client is defined as being small the responsibility will remain with you.

A client is deemed as small if it meets any 2 of the 3 following conditions:

- Annual turnover is not more than £10.2m
- Balance sheet total is not more than £5.1m
- Average number of employees is not more than 50

#### **(2) Overseas Clients**

If your end client has no connection with the UK and operates wholly overseas immediately before the beginning of the tax year, then the responsibility for assessing the contract will remain with yourself. However, if you, as the worker are also outside the scope of UK tax, then the legislation simply will not apply.

### **CEST**

HMRC has an online tool called CEST (Check Employment Status for Tax) which you can use to determine whether the IR35/off-payroll rules apply. Whilst this tool has been much improved since it was first launched, you should note that the absence of the consideration of MOO (mutuality of obligations) remains a concern and the determinations reached when using this tool may not necessarily agree with decisions that would be reached by a court or tribunal. However, HMRC has



said that it does stand by determinations arrived at by CEST, provided the details input “are accurate and in line with HMRC guidance”.

Our advice is to use the CEST tool and answer the questions honestly. If you get a determination that falls outside of IR35, then please keep a copy of it and send a copy to us. If you get a determination that states you are caught by IR35 then you should probably seek another opinion from elsewhere.

<https://www.gov.uk/guidance/check-employment-status-for-tax>

### **Status Determinations**

Unless your client falls under one of the exemptions outlined above, then from 6 April 2021 they are required to give you a status determination which sets out their decision as to whether your contract is caught by IR35. Note that if you operate via an agency, it is the job of your end-client and not your agency to provide these.

If you disagree with the status determination then you, as the worker, or your agency, as your fee payer, has the right to appeal against it and your end client must respond within 45 days with reasons for its reconsidered decision. Any disagreements are dealt with between yourselves and there is no involvement of HMRC.

If you would like a professional independent review of your contract, then we are recommending that you get in touch with Vantage who are underwriting our tax investigations service this year. Their fees are very reasonable, and their review is very detailed. They will give you practical feedback and if appropriate will even suggest alternative phrasing to any parts of the contract which may bring you inside of IR35. Some of our clients have already used this service and have been able to re-negotiate their position with their client to put them in a much stronger position. Please ask for further details if you would like to pursue this.

ABM also has a tax investigations scheme which we offer to all our clients. This service is designed to cover our fees for dealing with any enquiry from HMRC and covers all the major taxes. For more information on this or on IR35/-off-payroll working, please contact Loraine Sullivan.



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