

**ARE YOU IR35-READY?**

**HERE'S WHAT TO DO**

**IR35**



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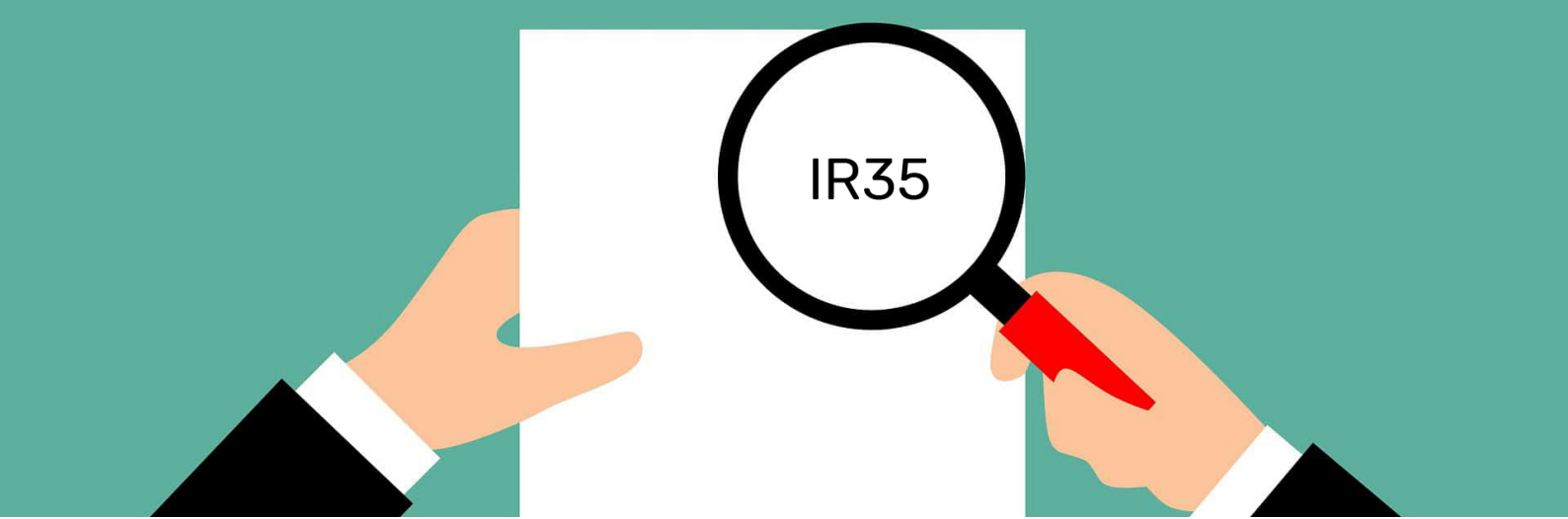
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## What is IR35?

IR35 is the UK legislation to prevent “disguised employment” tax avoidance. Introduced in 1999, it’s set to change on 6th April 2021.

“Disguised employment” involves contractors who are effectively employees but avoid paying income tax like employees by operating through an intermediary, like a personal services company (PSC), which allows them to take advantage of the lower rate of income tax for corporates.

## Who’s “outside IR35”?

Genuine independent contractors count as “outside IR35”, and you can pay their PSC gross, with no deductions for tax or National Insurance, because the relationship between you, the worker and the PSC employing them is a service supply relationship.

But who counts as a “genuine independent contractor”? That’s a difficult question – so difficult that a whole industry has sprung up to try to answer it for contractors. HMRC has created the “CEST” (Check Employment Status for Tax) test, but even its creators admit that it’s often inconclusive.

Nevertheless, here are four key factors to look for that will hopefully make it clear.

### 1. Mutuality of obligation

If you’re obliged to provide work, and your contractor is obliged to accept it, you have a mutuality of obligation. If so, they probably count as an employee (inside IR35).

### 2. Substitution

Can the contractor send a substitute, at their own cost, if they’re sick or can’t make it for some other reason? (You or an agency finding someone else doesn’t count.) If not, they could be inside IR35.

### 3. Supervision and control

Of course, managing a contractor isn’t the same as employing them. But if you have an agreement with them that dictates their working hours or how they perform their work from day to day, they’re likely to be inside IR35.

### 4. Part and parcel

Is your contractor part and parcel of the company structure? Are they acting as a line manager for your employees, for example? If so, again, they’re probably inside IR35.

## What's changing?

Despite the press furore, the substance of IR35 will remain the same: everyone who's genuinely outside IR35 will still be outside.

The changes closely follow similar rules introduced in the public sector in 2017, despite criticism at the time that they were rushed and ill-considered.

In the private sector, contractors currently self-report whether they're inside or outside IR35, and if they get it wrong, they're liable for any unpaid tax and NICs. HMRC believes many contractors are abusing the system, but recovering unpaid taxes one individual at a time is difficult and costly, so they're moving the assessment and the tax liability up the supply chain to employers.

Here's what you can expect from 6th April 2021:

- The IR35 changes have already been delayed for a year because of COVID-19. It is extremely unlikely they will be delayed again.
- Small companies are exempt from the new rules and can carry on as normal. Companies count as small in their first financial year or if they satisfy two of the following: an annual turnover of no more than £10.2m, a balance sheet total of no more than £5.1m, and/or no more than 50 employees on average for the financial year.
- Unless you're a small company, you'll be responsible for determining whether your contractors are inside or outside IR35. If they're inside, they'll be taxed as employees.
- You can use HMRC's Check Employment Status for Tax (CEST) tool to check your contractors' status, but CEST has been widely criticised, and alternatives are available.
- The fee payer is responsible for accounting for tax, NICs, employer's NICs and the apprenticeship levy. The fee payer is whoever pays the PSC, whether that's you or an agency.
- If the fee payer is an agency, you could still be liable for tax and NICs if you failed to take "reasonable care" when making the decision or if the agency is unable to pay (e.g., because of insolvency).
- Once made, the decision must be passed on to the supply chain and the contractor.
- The contractor has 45 days to appeal the decision. If they do, you must respond in writing within 45 days, giving your reasons for the decision.

## Mistakes to avoid in your contractor audit

Learn from the public sector's mistakes: back in 2017, when they faced similar changes, many public sector organisations took an oversimplified approach to assessing their contractors. Some even categorised all of them as inside IR35 and put genuine independent contractors on PAYE contracts. This not only drove up costs for the organisations, but also drove many contractors to the private sector.

And cost isn't the only concern if you're overzealous about complying with the new regulations. Because contractors can appeal if they don't agree with your decision to place them inside IR35, you could face a major administrative burden if you take a blanket approach.

Another learning from the public sector: there's likely to be temporary disruption in the contracting market as everyone adjusts.



## Your options

Once you've audited your contractors, you have a choice between four options:

### Remain outside IR35

Nothing changes here: your genuine independent contractors stay outside IR35. If you're worried about the risk of making a wrong determination, consider insurance to cover it.

### Pay as you earn (PAYE)

Reclassifying a contractor as a PAYE worker inside IR35 is an option, but they won't be happy: not only will they be liable for more tax, it'll also make HMRC suspicious that their self-assessment was fraudulent. You run the risk that the contractor will quit.

Also, if they've worked for you for two years or more continuously, they can claim security of employment tenure, which is grounds for a claim of unfair dismissal. They might also try to claim under Agency Worker regulations.

### Umbrella

If a lot of your contractors will be inside IR35, you could offer them the services of an umbrella company that will withhold necessary taxes but will also offer them PAYE benefits like a pension, loyalty schemes, and healthcare.

### Deemed model

Under the deemed model, the contractor is still a contractor and the director of their PSC, but is "deemed" inside IR35 for this specific assignment, and their agency has to withhold the relevant taxes. This may be helpful if a contractor works on several assignments with different statuses, but is generally considered too complicated and risky to be a useful alternative to PAYE and umbrella in the private sector.

### Statement of Work (SOW)

A more viable solution, as long as the work can genuinely be done through deliverable and milestone-based outcomes, an SOW makes the agency the "end user" instead of you, passing the buck of IR35 decisions to the agency.

However, if the work doesn't constitute a genuine service provision relationship, you could be liable for unpaid tax and employer's NICs on the basis that you didn't take reasonable care over the decision (since you didn't make it at all). This puts you in a worse position than if you'd made a decision with reasonable care and got it wrong. Fake SOWs are also likely to be early targets for enforcement.

Even if it doesn't cause you legal trouble, an SOW can be more administrative trouble than it's worth, as you need to manage, describe and measure all the deliverables properly, leading to time and money costs.

## Employed consultant

Employed Consultancy is an increasingly popular model. If your contractor is willing to be categorised as a permanent employee, they can be employed by a service provider to provide their services to you, usually on the traditional basis of T&M (Time and Materials), and billed either through timesheets or under an SOW agreement.

Since the contractor is employed by another company, this puts you at less risk (although still not zero) and means you only pay for days worked. However, unlike a true SOW, it leaves you with little accountability for the project, so it's not a complete answer to IR35 – it'll only be useful in specific cases.



## Risks to be aware of

While HMRC doesn't have the resources to hound everyone who makes a suspicious IR35 decision, it will be enforcing the legislation, and might even make an example of a high-profile company if it doesn't see the industry policing itself adequately.

The changes could also affect work permit status. For example, if someone with a Tier 1 Entrepreneurial Worker Permit is switched to PAYE status, they're likely to be unable to keep working unless either you or the agency sponsor them as a fixed-term employee. Neither will be easy, especially for short-term assignments.

It's also possible that the Government will take the recommendations of the Good Work Plan on board and adopt a 12-month tenure limit for contractors, which will cause headaches for ongoing projects.

Educate yourself on IR35, and don't wait till April to get a sense of whether your contractors are likely to be inside or outside.



### **Your next steps**

1. Start communicating with your contract workforce and their managers about what's happening, and keep them in the loop throughout.
2. If you made plans for IR35 in March 2020, take a second look at them, especially at the "Part & Parcel" and "Control" aspects, which may have been impacted by COVID-19.
3. Provide all relevant staff with refresher training on IR35.
4. If you audited your contractors in March, do it again, as your contractor population will have changed.
5. If you made any IR35 decisions for March, make them again and share them.
6. Make IR35 decisions for any new contractors who've joined you since then.
7. Choose and get familiar with the right determination tool and process for your organisation. If you were using CEST before, consider alternatives.
8. Make sure your appeals process is ready.
9. Reinstate your internal policies, communication processes and FAQs around IR35.
10. Update your IR35 timelines, especially pay and invoicing dates.

## IR35 actions and timelines



Review working practices



Review legislation and technology



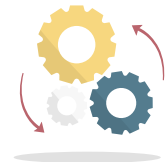
Audit contractors



Start commercial negotiations



Make turnover plan



Re-establish appeals process



Set up new working processes



Amend contracts



Communicate with contractors and staff

## How can MANE help?

Mane are proud to be offering a comprehensive IR35 solution that manages the entire process, from status assessment to process consultation, so you can confidently and compliantly maintain your flexible workforce outside IR35.



## The Status Tool

The Status Tool provides:

- Fast, efficient and accurate IR35 assessments
- Access to real time reporting
- IR35 specialists on-hand to assess indeterminate status result
- Interaction with the whole supply chain, including unique circumstances
- The ability to request a manual review irrespective of the result produced by the tool

The Status Tool takes a best-of-both approach, allying a custom-designed automated process with expert consultancy to provide the quickest, most accurate IR35 status result available.

If it is a clear-cut case, the tool then generates an instant determination, as well as a comprehensive report that pulls through the notable positives or negatives of a given engagement, as well as an official Status Determination Statement (SDS). If it is a borderline result, the answers given are passed over to external IR35 specialists for further manual review.

### **Our IR35 protect offering covers the contractors and supply chain against any tribunal costs and tax liability**

If a role is successfully outside of IR35, it is important to back the assessment with IR35 insurance.

We have a partnership with a provider, underwritten by Zurich, to offer an IR35 insurance policy that protects the whole supply chain for up to £100k legal defence costs and £100k tax liability, as well as providing a legal expenses policy.

Not only does this insurance protect the contractor in the run up to April 2021, it's also designed to flex come the reform deadline to cover the fee-payer as well. This means that the entire supply chain is protected against the potentially crippling costs of an IR35 enquiry and any tax debts found owing - peace of mind for the contractor, and a safe bet for the fee payer.

To find out more, contact us today.

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