

IR35 & THE OFF-PAYROLL RULES

(they have not gone away!)

What are they?

As a piece of legislation, IR35 has been around since 2000. In simple terms it says that if a contractor considers that he is inside of scope of IR35 he is technically employed, and his intermediary/PSC must pay his employment taxes (PAYE) and National Insurance contributions (NICs) to HM Revenue and Customs (HMRC). If the contractor considers that he is outside of scope of IR35 he is self-employed, and he does not have to pay PAYE or NICs to HMRC.

In a large part this has become a financial decision that the contractor has been making, based on the information he knows about the role, as remaining outside of IR35 nets a larger income. That is because the relevant rates of taxation for a PSC that pays its director/contractor a dividend income, is lower than paying PAYE and NICs.

In 2017 the legislation was altered in the public sector by the Intermediaries Legislation (AKA the Off-Payroll Rules). The change meant that responsibility for deciding if the contractor's assignment was inside or outside of scope of IR35 moved from its current assessor (the contractor's PSC) to the end-user/Client; and liability for paying any PAYE or NICs arising from that decision was passed to the recruitment business, or other third party paying the intermediary e.g.: an Umbrella Company. If the end-user/Client decides that the contractor is technically employed and inside IR35, whoever pays him is also liable to pay HMRC the relevant PAYE and NICs.

It also means that if the decision that the contractor is outside of IR35 is the wrong decision, the recruitment business (or other third party who pays the contractor) could end up liable to pay PAYE and NICs to HMRC without any facility to pass that additional cost on, or claw it back from anyone.

In 2021 (unless it is postponed again) the 2017 legislation change in the public sector will be extended to the private sector in the same way. And as in the public sector the potentially tricky part for the recruitment business is that the decision about the contractor's employment status comes from the client, who has little or no financial liability if the decision is wrong. That liability will rest, for the most part, on the recruitment business.

With effect from 2021 the client will be legally obliged to issue a Status Determination Statement to both the recruitment business and the contractor, determining the contractor's deemed employment status. From the recruitment business will know whether the role is inside or outside of scope of IR35 and therefore whether or not to deduct PAYE and NICs.

So what?

From a contractor's perspective being inside IR35 will reduce the value of an assignment by around 25 – 30% & potentially increase the costs of running a limited company business, without giving the contractor any of the employment rights enjoyed by an employee paying PAYE and NICs. They do not become an agency worker and reap the benefits of the Agency Worker Regulations if they are inside scope of IR35.

From a client's perspective, a contractor being inside IR35 could increase the costs of engagement by around 25%, unless the recruitment business is going to swallow that increase (unlikely), leading to a higher turnover of contractors which might delay or disrupt a project. Consequently, a client may prefer not to use a contractor at all.

From a recruitment business' perspective, unless they can pass the increased cost on to the client or the contractor, a contractor being inside IR35 could wipe out its profit margin and/or leave it with a liability to HMRC for unpaid PAYE & NICs.

How can I deal with this?

1. Audit all on-going roles if they are likely to run over into April 2021. Address the 3 primary areas used to determine whether a role is inside or outside of scope or IR35, and work with the client and contractor to establish where a role will sit.

It is likely that some roles will definitely be outside of scope, some will definitely be inside of scope, and some will be on the cusp. Those that will definitely be outside must remain that way. Those that will definitely be inside can be terminated and/or re-negotiated. But it is the either way roles that need to be more closely examined in order to determine whether to conclude them or change them.

2. Amend all recruitment business' agency contracts to reflect the impending changes in order to protect the business going forward. Client contracts need to be amended to outline the client's responsibilities when assessing whether a role is inside or outside scope, and to give the recruitment business the facility to increase its charges if necessary. Contractor contracts need to be amended to strengthen the contractor's responsibility for ensuring a role remains outside or inside scope, and to give the recruitment business the facility to decrease the rates payable if necessary.
3. Assimilate & train internally to ensure all the recruitment business' consultants understand the implications of a role being inside or outside of scope of IR35. That way they can more easily determine whether a role is inside or outside, guide a client or contractor accordingly, and help safeguard the recruitment business' margins.

If you think your recruitment business will be affected, please get in touch for an informal chat about how we can help. You can call us on 0333 400 4499 or email Lucy Tarrant at lucy.tarrant@cognitivelaw.co.uk.