

IR35 off-payroll working legislation:
what does the new IR35 legislation
mean for contractors?

grant



what is IR35?

The IR35 legislation was introduced in April 2000, its purpose was to determine whether a contractor working through their own limited company (often known as a Personal Service Company or "PSC") is a disguised employee of the hirer (inside IR35) or is in business on their own account (outside IR35). The answer has a material impact on the contractor's net pay. Under the former, the contractors pay from their limited company should all be taxed as salary, and under the latter they can pay themselves by a combination of salary, expenses and dividends which saves the contractor £000's in tax and employers national insurance each year. Each individual assignment undertaken by the PSC should be assessed for its IR35 status and the income from that assignment taxed accordingly.



The more a contractor can differentiate themselves from a permanent employee, the more likely they are to find themselves outside of IR35 and able to benefit from the significant tax advantages. The decision on IR35 status and tax liability for getting this wrong (only relevant with an outside IR35 determination) has until recently always fallen on the contractor, however, due to mass non-compliance, the government implemented reforms in the public sector in April 2017 which put the decision and risk in the hands of the end hirer and fee payer (the party that pays the PSC without deduction of taxes). These reforms known as Off-payroll working will be implemented, with a few changes, in the private sector this coming April 2021.



what are the IR35 reforms (also known as off-payroll working)?

In April 2017, Off-payroll working legislation was brought into the public sector making public body hirers responsible, and not the contractors, for making the IR35 status decision. The logic being that the hirer should know whether the contractor is working independently and not under their control or conversely, whether the contractor was working in a similar way to an employee. The overwhelming majority of decisions by hirers were that contractors were caught in scope of IR35. As a result, HMRC deemed the new legislation a great success.



HMRC believes that 9 out of 10 outside decisions in the private sector are incorrect, losing the government millions in tax revenue each year (estimated at around £1.3 billion by 2023/24) hence, they will be rolling out the private sector reforms from April 2021. Any amendments will also be effective for public bodies. The hirer's IR35 decision and reasoning (status determination statement) will be passed down to the party it contracts with and the contractor. Each party must pass the status determination statement on to the next party in the contract chain. Failure to do so will make that party liable for any potential unpaid tax during the period they do not pass on the statement.



There will be an appeals process (to be used where an inside IR35 decision is made), but in our opinion this will have a limited effect on a hirers decision as there is no mediator in the process or penalties on the hirer if they don't change their mind despite presented evidence, and is therefore, ineffective and only relevant for those initially caught when the legislation is first implemented. After April 2021, certain roles will be advertised with their IR35 status known upfront. Small and medium sized hirers meeting two of the following three criteria will be exempt from this legislation: turnover less than £10.2m; balance- sheet total less than £5.1 million; number of employees less than 50.

If the hirer is considered small, contractors will continue as they do today and will be responsible for making the IR35 decision and will carry any subsequent liabilities for the tax. It is important that you check with your hirer to see if they meet these criteria as there is no onus on the hirer to tell others of their exempt status!



what are the key factors for deciding an IR35 status?

The main areas looked at to make a status determination include:

- control - examples of what HMRC might look at include; whether you report into someone, use your own equipment to do the job, dictate your own working hours, make your own decisions on how you carry out the work. The more you are controlled by the hirer the more likely you will fall inside of IR35
- mutuality of obligation (moo) - as a genuine contractor (outside IR35) you should not be obliged to accept further work from a client at the end of your assignment and they should not be obliged to find you alternative work therefore ongoing, rolling contracts are not favorable



- substitution - as a genuine business you should have the “unfettered right” to substitute yourself for someone else within your business with equal skills and ability
- financial risk – most genuine businesses take on an element of financial risk, for example a PSC might quote for a job and take on the financial burden if it is not able to complete the work within timescales and budget IR35 is a complex piece of legislation and passing or failing on one point does not automatically mean an assignment is definitely inside or outside of scope, in fact you are unlikely to be 100% sure unless investigated by HMRC! Courts would look at both the contract and the actual working practices. Specifically defined, project based work and contractual agreements that pay based on meeting set deliverables and not based on hours/ labour are favorable to getting an outside IR35 status decision.



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