

Guide to IR35 Reforms

What you need to be aware of and
how we can help

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The Basics...

Historic background

IR35 is nothing new. Many people have only started hearing about it in the recent past due to the reforms but it actually dates back almost 20 years.

It was first introduced as part of the Finance Act in 2000 in response to a growing trend of tax and NIC (national insurance contributions) avoidance schemes through partnerships and limited companies. Employees were very easily changing their status to that of a limited company and thus decreasing the amount of tax they were paying. HMRC (then the Inland Revenue) saw these individuals as 'disguised employees'. Without a framework to help them investigate whether the worker was an employee or contractor, cases were complex and the Inland Revenue hypothesised that a considerable amount of tax went unpaid.

IR35 was introduced as a means of establishing the true employment status of the contractor.

What is IR35?

There are a vast number of pieces of legislation that affect the freelance market; it can feel quite daunting navigating this sphere for contractors, recruiters and end users alike. Firstly though, it is important to note that the IR35 legislation only affects contractors supplying their services through a limited company. Various other pieces of legislation cover employees, self-employed individuals and specific sectors, often many of them overlapping. Clipper Contracting Group can help explain these other complexities should you require it.

In very simple terms, IR35 was introduced to examine the relationship between the contractor and the end user to establish whether it was one of 'disguised employment' or a genuine business relationship.

In other words, would an individual be considered an employee for all intents and purposes were it not for the fact that they were providing their services and receiving remuneration, through their limited company?

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Inside or outside of IR35? How is status determined?

The status of a limited company is defined as either 'outside' IR35 or 'inside' IR35.

If you are considered 'outside' IR35, it is deemed that services are being provided as a genuine business.

If you are considered 'inside' IR35, then you are considered as an employee (a deemed employee). You may still be paid as a limited company but there are tax implications similar to those of being employed.

Determining the IR35 status of a limited company is complicated as there are so many factors to consider. We will explore a number of them below but this is by no means a comprehensive list. Anything associated with employment would push the determination towards that of disguised employment and inside of IR35.

- **Control** – there shouldn't be anything in the written contracts or how the contractor is engaged whereby the worker is controlled in any way. If the end-client can control the place of work, the times in which work is carried out or the scope of work being conducted, then this would suggest the contractor is inside IR35
- **Mutuality of obligation** – there should be no evidence that future work will be expected or offered at the end of the current assignment, by either party. The contractor is engaged for that specific contract only and there is the possibility this could be terminated early
- **Substitution** – a service should be provided, not a personal set of skills specific to the individual. If a substitute cannot be sent to complete the service, then substitution doesn't exist and the contractor is considered 'inside of IR35'
- **Taking financial risk** – a genuine business should be taking a financial risk. This would be in the form of owning and using their own equipment, perhaps having invested in a company office and being responsible for the financial implications of rectifying faulty work
- **Right of dismissal** - there should be the opportunity for immediate dismissal. A notice period suggests employment relationship
- **Employee benefits** - if working at a client's site, the contractor should not receive any benefits that a typical employee would. If the contractor attends the Christmas party, is provided with training or has any pension contributions, this would suggest an employment relationship

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IR35 Reform for the Private Sector

April 2021

Since IR35 was first introduced in 2000, it was the director of the limited company that was responsible for determining their IR35 status. If they considered themselves inside of IR35 for certain roles, the income from that assignment would be deemed as employed income and their accountant would treat this income differently.

This disguised employment arrangement was tricky for HMRC to police. On the one hand, very few company directors would declare themselves inside IR35 for a specific project; they wanted to take advantage of the more beneficial tax breaks. And on the other hand, if HMRC did want to challenge a limited company's self-determination, it was costly and time consuming going after one limited company, case by case.

Cue the reforms to IR35 that began in the public sector in 2017 and will be expanded to the private sector in 2021 after a delay due to Covid-19.

What are the reforms?

The reforms to IR35 are aimed at shifting this liability for determining IR35 up the contractual chain with a view that those entities will abide by the legislation more rigorously.

The hirer (end-client) will now be responsible for determining the IR35 status of the contractor. If they are found to be inside IR35, then the fee-payer (entity that pays the limited company) will be responsible for deducting employment costs such as Employer's NI and tax and national insurance from the limited company. The fee-payer could be the end-client (if they engage a limited company directly) or a recruitment agency should they have introduced the contractor. It is important to remember that it is the fee-payer that will be liable for not applying an 'inside IR35' determination if it was deemed so by the end-client.

This is already the case in the public sector and has been since 2017. These rules will be extended to the private sector in April 2021.

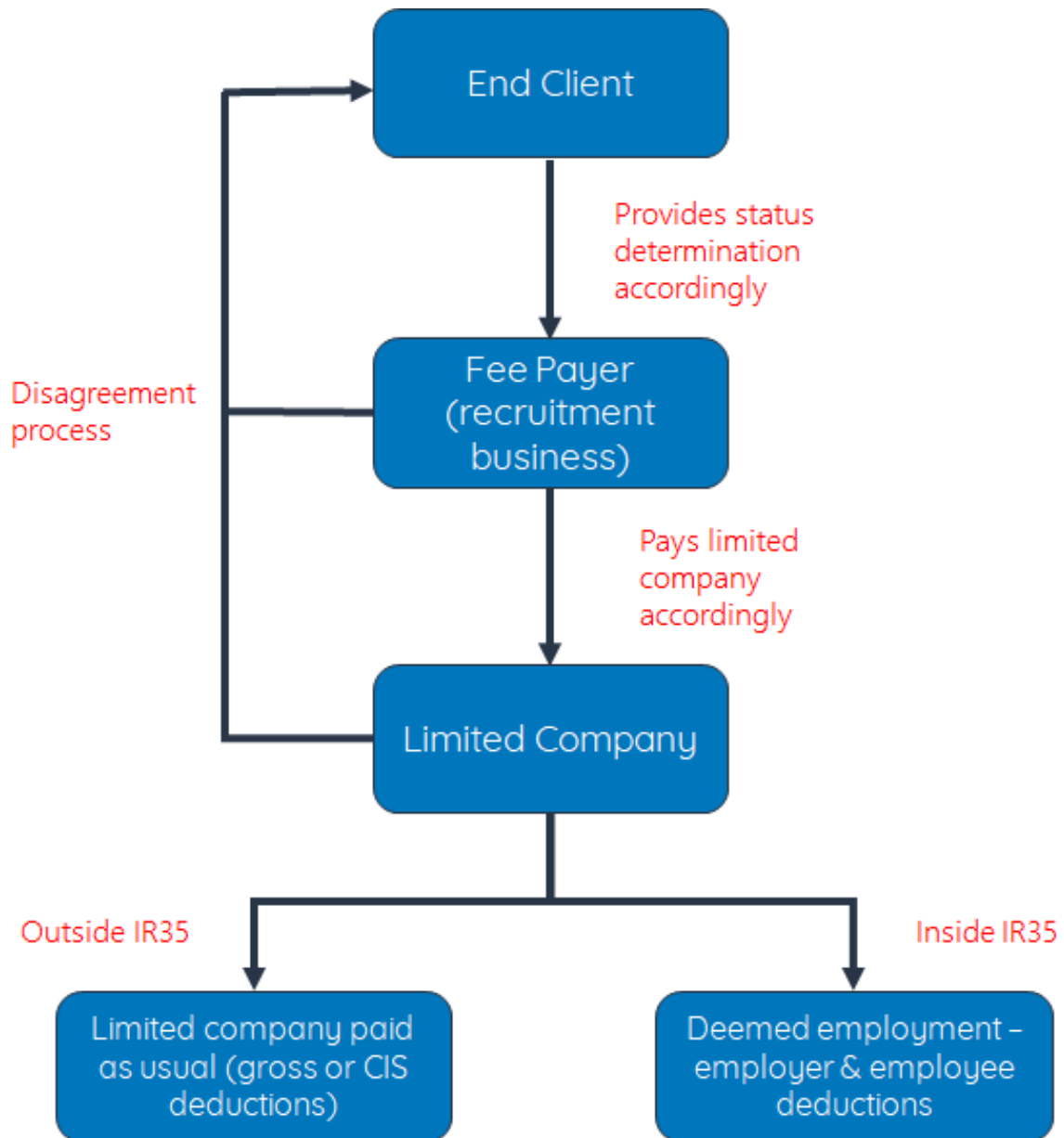
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Where the responsibility will fall from April 2021



Do the reforms apply to all businesses?

The reforms don't apply to all private businesses equally. As per the definitions within the Companies Act of 2006, 'small businesses' will be exempt from the reforms and they will only apply to 'medium' and 'large' businesses.

A small business is defined as:

- Annual turnover of no more than £10.2 million
- Balance sheet total no more than £5.1 million
- No more than 50 employees

Where two of three of the above are met, the reforms for IR35 will not apply. The responsibility for determining the IR35 status will remain with the director of the limited company.

Receiving a status determination

As mentioned already, the end-client will be responsible for determining the IR35 status of the contractor. In the case of a recruitment company supplying this contractor, this status determination would be provided to the recruitment agency (the fee-payer).

Whilst there are currently no specific rules about what this should look like, it is likely to be a written statement. It will need to outline the reasons behind a decision (both inside or outside IR35) and have been written with a reasonable amount of care.

The draft legislation hasn't specified what reasonable care is yet. Even looking at HMRC's 'reasonable care' approach in other areas doesn't help much but it is likely to centre on whether there was a careless error or the information supplied is false or deliberately withheld.

The final publication of the legislation should provide further guidance.

The client disagreement process

The draft legislation published in the summer also identified that there would be a disagreement process. Details are still hard to come by on what this will look like in theory but the facts as they stand are that there will be a 45 day period to lodge a disagreement with an inside IR35 status determination.

The end-client will have this period of time to respond, with reasoning, whether the original decision stands or whether there has been a change in determination. End-clients will have to have a process to manage this as failure to do so will render them the fee-payer. However, once this process has been completed and if the outcome is unchanged, contractors will have no further recourse.

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What are the options?

The options for contractors vary widely depending on a great number of factors. Here we explore the options depending on an inside or outside IR35 determination and also look at options should contractors decide that they want to shut their limited company and engage in another manner.

Outside IR35

If the assignment is determined as outside of IR35 then nothing need change. The fee-payer can continue to pay the limited company gross (or with CIS deduction if within construction)

Inside IR35

If a determination is returned that the contractor falls inside of IR35 (deemed employment), then the options are:

- Continue being paid as a limited company but with employer and employee deductions
- Choose to engage as an employee and be paid PAYE through an umbrella company or by the recruitment agency or end-client directly
- Engage as a permanent employee of the end-client

Shutting down your limited company

Some contractors may decide that the assault on the freelance market has reached tipping point and that the recent changes in dividend tax, the costs of running a limited company and now the additional hurdles with IR35, will leave them little choice but to shut down their limited companies.

There are a number ways of engaging on a freelance basis that could be considered:

- Being paid as an employee of an umbrella company – the worker receives a full suite of employment rights and may be able to claim expenses each week to better their net pay
- Engage on a self-employed basis – whether CIS or as a sole trader, as long as there has been no inside IR35 determination done for that assignment, a worker may be able to engage on a personal self-employed basis through an umbrella company
- Go permanent – again, a viable alternative for some people that comes with the advantage of additional job security

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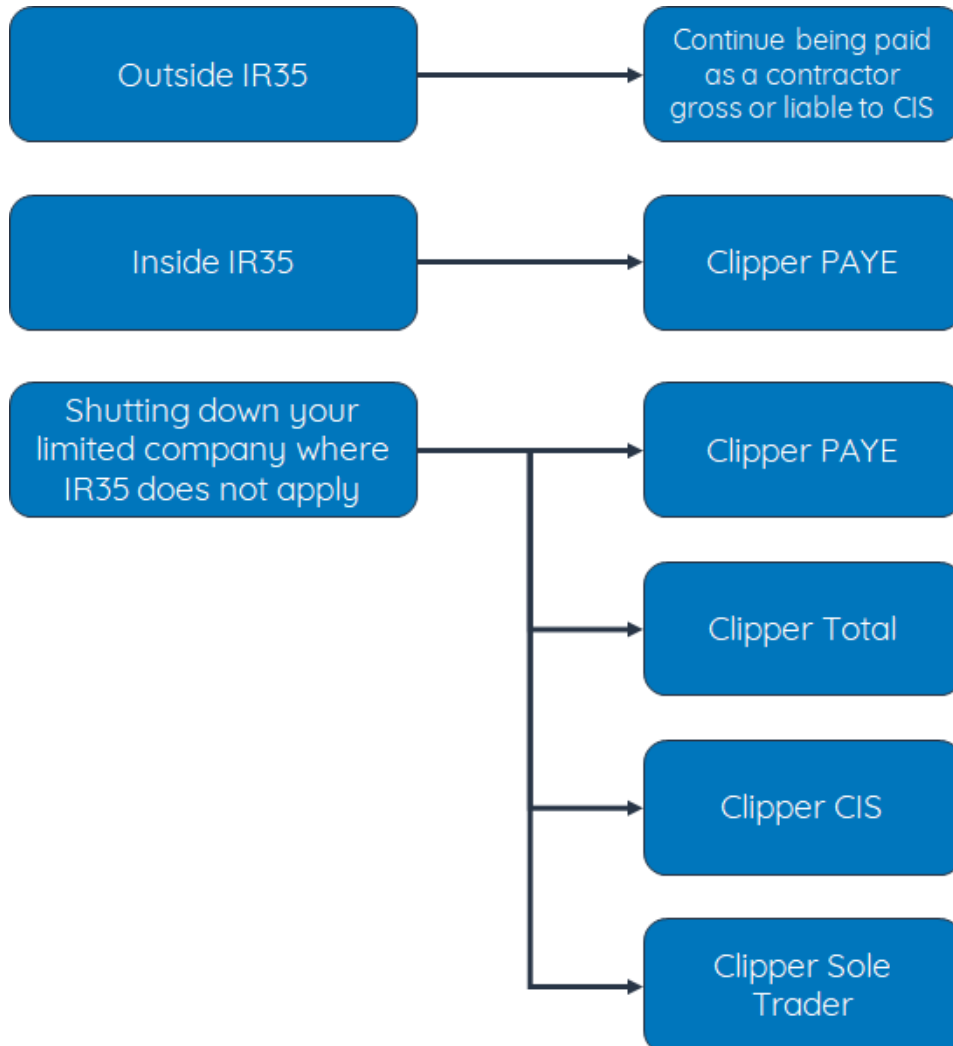
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How can Clipper Contracting help?

We have several solutions that may help your individual requirements. There is no one size fits all approach with IR35 so please call us on 01305 233170 so we may best assist you.



Clipper PAYE

- Full suite of employment rights as opposed to deemed employment through a limited company
- Holiday pay, pension, SSP, SMP/SPP
- Employed by Clipper Contracting; ease of being paid through one employer for multiple assignments
- Full suite of insurance offered including personal accident insurance

Clipper Total (where no inside IR35 determination for that assignment)

- Full suite of employment rights as opposed to deemed employment through a limited company
- In addition, your employer Clipper Contracting Group may be able to pay certain expenses to you for the assignment your are carrying out
- Holiday pay, pension, SSP, SMP/SPP
- Employed by Clipper Contracting; ease of being paid through one employer for multiple assignments
- Full suite of insurance offered including personal accident insurance

Clipper CIS (where no inside IR35 determination for that assignment)

- Recruitment agency dependent, may be able to engage on a self-employed basis, avoiding the expensive costs associated with running your own limited company
- 20% (or 30%) CIS deduction paid to HMRC towards future tax liabilities
- All invoicing and remittance issuing administration taken care of

Clipper Sole Trader (where no inside IR35 determination for that assignment)

- Recruitment agency dependent, may be able to engage on a self-employed basis, avoiding the expensive costs associated with running your own limited company
- Tax must be put to one side to cover future tax liabilities through self-assessment
- All invoicing and remittance issuing administration taken care of

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