

## Off-payroll working – Important changes (Lecture B1247 – 24.49 minutes)

### *Introduction*

For individuals providing services through their own company from 6 April 2021, the 'off-payroll' working rules (which have previously only affected work for public sector engagers) are being extended to include a lot of private sector clients too. Whether private sector clients are affected depends on their size, as discussed below.

These changes are a further attempt to extend the reach of payroll taxes (PAYE, employer and employee National Insurance Contributions (NIC)) to those contracting with clients via their 'personal service company' (PSC).

Note that the rules can apply:

- even if an agency is the fee-payer rather than the end-client; and
- if the worker uses a different form of intermediary vehicle to a PSC, such as a partnership, to contract for their services (although in this article we will only consider the impact on PSCs).

### *The April 2017 changes*

After years of HMRC struggling to enforce compliance with IR35, on 6 April 2017 new rules came in for PSCs contracting with public sector engagers, referred to as the "off-payroll working" rules. The IR35 rules have always put the onus on the PSC to determine whether there is an underlying employment relationship with the client and to then self-assess tax accordingly. In contrast, the public sector off-payroll working rules make the client (such as an NHS trust or the BBC) determine whether there is an underlying employment relationship with the worker. If it determines that there is, then the public sector body (or, if appropriate, an intermediary such as an employment agency) must register the worker for PAYE and deduct the worker's payroll taxes when paying the fees that the PSC has billed (even though the worker is employed by the PSC, not the public sector body, and does not themselves contract directly with the client or agency).

The deemed employment payment is the VAT-exclusive amount due to be paid to the PSC, less the direct cost of materials included in the invoice. The fee-payer may, at their discretion, also exclude from the deemed payment any expenses met by the PSC that, had they been incurred directly by the worker, would have been allowable against earnings if the worker were an employee.

This complicates both the tax position of the PSC and the way the worker can tax-efficiently withdraw funds from their company. However, the good news is that responsibility for compliance rests with the engager rather than the PSC, so that the worker does not have the risk of an IR35 enquiry on their company.

The government regards these off-payroll working rules as having been so successful that they are extending them to many private sector clients of PSCs from 6 April 2021, having previously delayed this twice. Those PSCs that do not contract with public sector engagers will therefore be meeting the rules for the first time.

### *Extension of off-payroll working rules to the private sector for 2021/22*

From 6 April 2021, the off-payroll working rules will also apply to private sector work done via a PSC, unless the client is 'small' (see below). To fall within the new rules, the work must be performed and the payment for the work made after 5 April 2021.

The legislation largely rolls out the current rules applicable to public sector clients to medium or large (i.e. non-small) private sector clients that receive services from PSCs. 'Small' for companies or limited liability partnerships (LLPs) means that they must meet two of the following three tests:

- Turnover  $\leq$  £10.2m;
- Assets  $\leq$  £5.1m;
- Employees  $\leq$  50.

For other clients (e.g. an unincorporated partnership), only the turnover test is used.

Businesses will be legally required to provide information regarding the size of the business to agencies and contractors, upon request, within 45 days. Remember that, where the PSC's client is **small**, they continue to pay the invoices received in full and the PSC must decide if IR35 applies to the contract.

### *Exclusion for overseas clients*

Where a large or medium-sized private sector client is based wholly overseas and has no UK connection, the off-payroll rules do not apply. The worker's PSC will remain responsible for deciding the contractor's employment status for tax purposes and self-assessing whether IR35 applies. "No UK connection" means that the client is neither UK resident nor has a 'permanent establishment' (broadly, a fixed place of business) in the UK.

### *Contractors operating under Construction Industry Scheme (CIS) rules*

The off-payroll working rules take precedence over the CIS rules. Thus, if they apply, the fee-payer would not need to consider applying the CIS rules (which may also necessitate withholding of tax) to payments made.

If the party receiving the worker's services is a small private company, the worker's PSC would be responsible for considering whether IR35 applies and self-assessing accordingly. Any deductions made by the client under the CIS when paying the PSC would be a separate matter dealt with under normal CIS rules.

### *Status Determination Statement*

The end-client must provide a Status Determination Statement (SDS) to the contractor and all relevant parties (e.g. a recruitment agency) in the contractual chain, at the time the contract starts or before the off-payroll worker starts work. All such businesses using contractors must therefore make sure that they have the appropriate processes in place to produce and pass on the SDS to all relevant parties. In the absence of this, the PSC's end-client will take on the responsibilities of the fee payer (if they are not the fee-payer) to operate PAYE and NIC, where applicable.

If the client decides that off-payroll working rules apply, the client (or any agency responsible for paying fees to the PSC for the worker's services) must create a payroll record for the worker. This means that they must:

- obtain the National Insurance Number (NINO) from that worker;
- withhold PAYE and employee's NIC when paying invoices of the PSC;
- account for employer's NIC; and
- send the worker a P60 if still engaged at tax year-end, or a P45 if the engagement has ceased.

Although they must treat the worker as if they are an employee for payroll tax purposes, the worker has no employment rights at all from the client, which also does not make student loan deductions.

### *Disputing a decision*

If contractors disagree with the decision made by their client on their employment status for tax purposes, they will be able to raise concerns through a client's status disagreement process. All clients are required to introduce a process, from 6 April 2021, to allow contractors to disagree with the decision.

Under the Finance Act 2020, the client has 45 days to respond to representations by a worker who has received an SDS. During this time, the client (or other fee-payer) should continue to apply the rules in line with the original determination. HMRC will not get involved in any disputes.

After completing the client's status disagreement process, if the contractor believes that they have paid too much income tax and NIC, they can follow existing Self Assessment and National Insurance processes to seek a repayment.

### *The client's responsibility*

A client must take reasonable care when making a determination.

HMRC guidance cites various examples of what does not constitute "reasonable care", including:

- determining that every worker who provides their services through an intermediary is caught by the off-payroll working rules without giving any consideration to the specific facts of each individual case;
- failing to reconsider determinations where there has been a material change in circumstances;
- inputting inaccurate information into CEST.

Failure to take reasonable care means that the issuer becomes the deemed employer (if they are not already) and is responsible for applying PAYE to the worker's PSC invoice. There is no financial sanction.

### *FB 2021 changes*

The substantive rules were included in FA2020, but these are now amended so that they work as intended, with additional provisions introduced to tighten up the impact of the rules. All these provisions are within Clause 21 and take effect from 6 April 2021.

### *Definition of intermediary*

For the off-payrolling rules to apply, there has to be an intermediary, which is most commonly a PSC. To come within the provisions, the PSC has to meet certain conditions. The intermediary is caught if the worker either has a material interest in that company or is receiving income from the intermediary that represents payment for services rendered but is not taxable as employment income. This latter provision prevents avoidance by diluting shareholdings below the material interest figure. These conditions have been in place for IR35 since it was introduced in 2000.

The FA 2020 rules updated these conditions, so that the company could be caught where the worker has a non-material interest in the intermediary but receives payment for services from anyone within the supply chain (such as where they get direct payment from the end-client), but the wording was such that it applied in all cases where a worker was getting a payment from elsewhere in the supply chain. The legislation is being amended, so it now makes reference to situations where a worker receives payments that are not already wholly taxed as employment income.

The definition of 'non-material interest' is having:

- 5% or less of the ordinary share capital;
- Having entitlement to receive 5% or less of any distributions that may be made by the company; or
- Where the company is a close company, having entitlement to receive 5% or less of the assets available for distribution on a winding up.

### *Information provisions*

Another change relates to provision of information within the supply chain. There is currently a requirement for the worker to provide information to the potential deemed employer regarding the application of the off-payroll working rules. This basically requires the worker to notify the potential deemed employer that the basic structure is such that these rules might apply (e.g. the worker has a material interest).

This is amended so that the intermediary will have a requirement to provide the necessary confirmation, where the worker does not do so. The changes will bring the intermediary into the process of confirming whether a worker is potentially caught by the off-payroll working rules. If no confirmation is given by the worker or intermediary, it can be assumed by the end-client that the rules apply.

### *Fraudulent provision of information*

There are specific provisions where fraudulent information is provided, so that the person providing that information becomes liable for any taxes which arise by virtue of their actions. This currently only applies to the worker or anyone connected with the worker but will be extended to cover any UK-based party in the supply chain.

### *Targeted Anti-Avoidance Rule*

Finally, there is a new TAAR, which will apply where at least one relevant person within the supply chain is involved in a 'relevant avoidance arrangement'. These are arrangements where the main

purpose (or one of the main purposes) is to gain a tax advantage by circumventing the conditions of the provisions, such that the off-payrolling rules do not apply.

If these conditions apply, the person who has entered into the arrangements will be treated as the deemed employer and will become liable for the taxes due on payments to the worker. Where more than one relevant person participates in the avoidance arrangements, HMRC will treat the higher person in the supply chain (assuming there is a realistic prospect of recovering the tax) as the deemed employer. This could be the worker or intermediary if other members of the supply chain no longer exist.

#### *Impact of new rules on pre- 6 April 2021 years*

HMRC has said that it will not normally open a new compliance enquiry into a contractor's tax return for tax years before 6 April 2021 in circumstances where:

- a client decides that a contract is within the off-payroll working rules from 6 April 2021;
- a contractor changes the way they work from providing and invoicing services through a PSC to being employed directly by the client; or
- a contractor ends a contract because they disagree with a client's decision on status.

HMRC will only open an enquiry using information acquired through the changes to off-payroll working rules if it suspects fraud or criminal behaviour.

#### *'Light touch' on penalties*

HMRC has confirmed it will adopt a light touch approach to penalties. Consequently, there will be no penalties for inaccuracies relating to the off-payroll working rules in the first 12 months, unless there is evidence of deliberate non-compliance. However, where HMRC believe contractors are adopting artificial, contrived arrangements claiming to avoid the application of the off-payroll working rules or result in customers paying less tax than should be the case, HMRC will take action.

*Contributed by Kevin Read*