

IR35 roundup – Part II

(Lecture B1084 – 21.55 minutes)

Deemed salary calculation

If caught by IR35, the following calculation is used to calculate the deemed salary as follows.

	£
Income <u>received</u> from relevant engagements in tax year	A
Less: 5% automatic deduction	<u>(B)</u>
	C
Less: Expenses paid by employer allowable as deductions from earnings if paid by an employee	(D)
Less: Employer pension contributions	(E)
Less: Employers NIC on workers actual pay	(F)
Less: Actual salaries and benefits paid	<u>(G)</u>
Gross deemed payment	H
Less: Employers NIC ($H \times 13.8/113.8$)	<u>(I)</u>
Net deemed payment (= Gross pay process through payroll)	I

Compliance

The net deemed payment must be processed through the personal service company's payroll with the tax and NIC paid over to HMRC no later than 22nd April where payment is made electronically.

Remember, the £3,000 employers NIC allowance is never available to deduct from the secondary Class 1 NICs due in respect of a deemed payment.

Corporation tax relief

Under IR35, dividends are effectively reclassified as salary.

The income received from relevant engagements will form part of the intermediary's profits that means that the salary plus employers NIC is tax deductible in the accounting period that includes 5 April. It is not possible to make an accrual in respect of the deemed payment and related national insurance contributions

Dividend repayment

Dividends will only be taxed as dividends to the extent that they exceed the deemed salary payment. If the worker draws a dividend and is also treated as receiving a deemed payment then the same income is being taxed twice! The intermediary company will make a claim for relief to remove this anomaly by setting the deemed employment payment against the dividend.

The relief applies to dividends paid in the same year as the deemed employment payment

Off payroll workers in public sector

From April 2017, any public body engaging a Personal Service Company must decide whether IR35 applies to your client and if so, put the individual on their payroll!.

The system works as follows:

- Personal Service Company invoices £6,000 plus VAT of £1,200;
- Tax and Employees NIC of £1,613 is deducted by public body;
- Public body then pays the Personal Service Company £5,587 (6,000 - 1,613 + 1,200);
- A number of public bodies have started to reduce day rates to account for the fact that they will need to pay the Employers NIC;
- The net pay will be paid to the Personal Service Company and not to the 'employee' worker.
- Output VAT of £1,200 is paid over to HMRC in the normal way:
 - Box 1 £1,200
 - Box 6 £6,000
 - Even if on cash accounting which need to be overridden

In the personal Service Company's accounts, the original entries will be:

DR Debtors	£7,200
CR Turnover	£6,000
CR VAT Liability	£1,200

Turnover will then be reduced by the income tax and Employees NIC of £1,613 deducted at source:

DR Turnover £1,613 (or salary might be more appropriate)

CR Debtors £1,613

The owner then extracts £4,387 as salary); this would be posted to salary as well. Salary would now be showing as £6,000 (1,613 + 4,387).

Do not include the extracted £4,387 on the director's self-assessment return as the director has a payslip from the public authority and a P60 that will show the £6,000 gross amount reported. This is the amount to include on the tax return with the tax deducted.

How has it been going?

Research has confirmed that reform has raised £410m in first ten months of operation. Around 58,000 more public sector contractors are paying tax and NIC. Some contractors did walkout but were replaced with "compliant" contractors. There was no evidence of contractors reverting to self-employed. Public bodies reported experiencing difficulty in filling vacancies due to staff shortages rather than these new IR35 rules.

Public bodies said the rules were easy to administer.

Extending the rules to the private sector

HMRC are very keen on the off payroll rules. With no input from HMRC needed, they get an extra £410m in 10 months. Just how much would they get in the private sector if the same rules were introduced?

There is a consultation on extending the rules to the private sector that runs until 10 August 2018. Under the proposals, the end client would deduct PAYE from the personal service company invoice. This will be a significant change and one that we should assume will happen and it could be in place from April 2019.

What should we be doing now?

Is this a fee opportunity for us? We should certainly be discussing the issues with our Personal Service Companies and explaining recent issues and what is round the corner. Perhaps, we should consider a short, punchy letter to grab their attention.

Could we offer a contract review service for a fixed fee? This could be done using information learnt from the recent First Tier Tribunal decisions. We should look to ensure that good substitution clauses are in place, no mutuality and limited control all feature clearly in the contracts with end users. Consider suggesting shorter contracts to promote no mutuality and while contracts may be renewed ensure that there is no obligation to do so.

Additionally, ensure that the contract's financial terms are clearly stated "excluding all taxes" as who pays the employers NIC has been a problem in the public sector;

By taking these steps, when the private sector use HMRC's online employment indicator tool, the results should be favourable to our clients and they can stay away from payroll.

There is no doubt that Personal Service Company clients will be getting more attention going forward. Contract reviews, making sure your clients know what is happening and what they should be doing will provide a valuable service to clients.