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TAX ADVISORY

IR35: Key Concerns Ahead of 6 April 2021

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IR35 off payroll rules[1] were introduced in 2000 to stop workers from reducing income tax and employer's and employee's NICs by supplying their services through an intermediary, such as a personal services company (PSC), and paying themselves in dividends from that company.

The changes for medium- and large-sized business were originally to apply from 6 April 2020. However, the changes are now to come into effect on 6 April 2021 due to the COVID-19 pandemic. HM Revenue and Customs (HMRC) have been at pains to stress that 'the delay to the introduction of the changes is not a cancellation'. Clients have, therefore, been presented with an extra year in which to ensure that they are prepared for the changes.

Medium- and large-sized businesses will be under an obligation to assess the status of workers who contract with them through a PSC. If a worker is then found to have an employment relationship with the client, the client must account for Pay As You Earn (PAYE) income tax and National Insurance contributions (NICs) to HMRC in respect of the payments it makes to the PSC.

What Are Businesses' Main Concerns Around the Changes to IR35?

Following the publication of draft legislation in July 2019 by HMRC, amending the existing IR35 regime to extend to medium- and large-sized private businesses. Concerns were voiced by the business community as to the efficacy of the incoming changes. The most serious issues included:

- the potential liability of end clients for the actions (or inaction) of intermediaries further down the 'supply chain', over which the end clients could exercise no control;
- the suitability and subtlety of HMRC's 'check employment status for tax' (CEST) tool, especially with regards to the CEST tool's ability to ascertain mutuality of obligation;
- how to exercise 'reasonable care' in determining employment status; and
- the mechanics of a client-led status determination status, which HMRC will not intervene in.

How has HMRC Addressed These Concerns?

On 27 February, HMRC published its response to a public consultation process into incoming changes. Several notable amendments have to the incoming changes have arisen out of the Government's consultation process.

- A lenient transition period has been introduced, where penalties will not be levied for errors made in applying the incoming changes in the first year following implementation, except in cases of deliberate non-compliance.
- HMRC confirmed that there will be no new investigations of PSCs for tax years prior to 6 April 2020 arising out of information resulting from the incoming changes, unless there is reason to suspect fraud or criminal behaviour.
- The incoming changes will now apply only to payments made for services provided on or after 6 April 2021. Prior to this alteration, the incoming changes would have applied by any payment made on or after 6 April 2021, regardless of whether the services themselves were provided prior to that date.

[2] Social Security Contributions (Intermediaries) Regulations 2000 (SI 2000/727) and Chapter 8 of Part 2 of ITEPA 2003

- The CEST tool was upgraded earlier in November 2019 to provide clarity as to the questions it asked of users. The guidance provided alongside the CEST tool has also been updated.
- HMRC state that the legislation 'will be made clearer' regarding the client-led status disagreement process.
- The legislation will be amended so that companies without any UK presence will be excluded.
- Finally, the legislation will be amended to impose a requirement on end clients to respond to enquiries as to their size (and thus whether the rules apply) within 45 days.

General 'communication resources' have also been published by HMRC, aiming to simplify the process of end clients informing intermediaries and individuals about the incoming changes. The 2020 Budget indicated that the changes to the existing IR35 regime would be legislated for in the Finance Bill 2020 — however, due to the ongoing COVID-19 pandemic, the changes did not appear in the Finance Bill 2020 and instead we expect to see them in a later Finance Bill.

HMRC have clearly listened to industry concerns to some extent. However, practitioners should be aware that question marks around at least three issues with the incoming regime remain. Firstly, the accuracy of the CEST tool determinations remains relatively unknown, and concerns remain around the ability of the CEST tool to provide the appropriate level of nuance required. It is hoped that case law and HMRC manual guidance will shed light on the CEST tool as time passes. Secondly, the liability of end clients for failures by intermediaries in the contractual supply chain remains worrying. Finally, there remains an inevitable tension between businesses which may wish to ensure compliance with the incoming by treating individuals for whom arguments could be made either way as to their employment status as employees, and the individuals themselves, who may wish to continue benefitting from favourable tax treatment offered by supplying their services through a PSC.

What Should a Client Led Status Determination Process Involve?

While entering into a dispute resolution process at the beginning of a business relationship may not seem like a fortuitous start, it is something that may be necessary from 6 April 2021 if an individual does not agree with the determination of the end client.

As a result of the incoming rules, end clients will have to provide individuals who contract with them through a PSC with a determination as to their employment status. Where an individual decides to challenge the accuracy of the status determination, HMRC will not intervene or adjudicate in any way — it is up to the client to work through a "Client-Led Status Disagreement Process" with the individual within a prescribed timescale. The disagreement process must meet minimum criteria set by the government.

If a worker contests the findings of a status determination statement, then they may make representations, either verbally or in writing. Representations should include the workers reasons as to why they disagree to ensure the client has sufficient information.

The client must respond to the worker within 45 days of the date the representations were received (not when the status determination statement was issued). If a client fails to respond to a worker within 45 days, then they may be treated as a fee-payer liable to pay income tax and NICs.

If the client finds that their original determination was reasonable, they must confirm that they have considered the workers representations and provide reasons for their conclusion. If the client concludes that their original determination was incorrect, they would need to issue a new Status Determination Statement and ensure that it contains reasons for reaching the conclusion. Clients should also bear in mind that corrections may need to be made through payroll.

This means that if a client believes its status determination is correct at the end of the process, it will stand regardless of the opinion of the worker. A worker would have to follow the exiting Self-Assessment and National Insurance processes if they want to take this further.

If the client has not issued a status determination statement, the worker can still make representations. However, the normal 45-day time limit would not apply. The client should still consider any representations received, however, as they will be responsible for any deductions of tax and NICs if the engagement is one to which the rules apply.

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