



How to navigate IR35 and retain
access to your contractors

Today's presenters



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Co-CEO, Sonovate



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What we're discussing

- IR35 overview
- What is changing in April
- Tips on how to prepare
- Sonovate's IR35 solutions
- Q&A



IR35:

Kevin Barrow



Proposed IR35 changes in April 2020

Sonovate

February 2020



Agenda

- 01 About Osborne Clarke

- 02 Context - growing Government action against contracting

- 03 IR35 detail

- 04 How the market is responding

- 05 What you need to do



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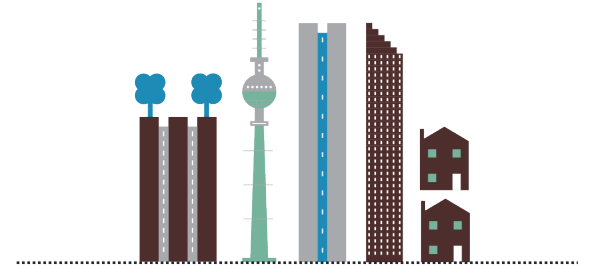
01

About Osborne Clarke



About Osborne Clarke

- International law firm
- Advice on consultancy/staffing programmes in 45 countries since 2012
- Have advised 180+ companies on IR35 in last three years
- All major HMRC, BEIS and Cabinet Office consultations 1999 -2019 including the original IR35
- Matthew Taylor meetings at OC



"The acknowledged experts
[in the world of contingent
workforces]"

Legal 500

02

Context - growing Government action against contracting



Context - growing Government action against contracting

Worldwide concerns about tax liabilities associated with Contingent Workers:

- "Worker misclassification" in the US
- German equivalents
- New Dutch tax legislation re self-employment
- Similar actions elsewhere... i.e. we are not alone
- ...and now a particularly topical issue in the UK following:
 - Media and Taylor Review focus on tax avoidance and self-employment
 - Increased HMRC enforcement of existing rules
 - Extension of IR35 in 2017 in public sector
 - Announcement and draft legislation in July re 2020 IR35 reforms



Context - growing Government action against contracting

- Historic risk profile for consultancies/end users in UK = relatively **low**
- **"Old" IR35 (2000)** was not a problem for end users and consultancies?
 - **Personal Service Company ("PSC")** is liable
 - HMRC rarely took action (except BBC etc)
 - For the time being, still the case where there are private sector end users
- [Regime re lower paid workers out of scope of this presentation]



Context - growing Government action against contracting

However UK tax risk has been increasing (1):

- HMRC is fed up
- HMRC November 2016 guidance to staffing co's and end users: "Use of labour providers"
 - check out supplier compliance – can't "turn a blind eye" re tax and NMW

<https://www.gov.uk/government/publications/use-of-labour-providers/use-of-labour-providers-advice-on-due-diligence>

Context - growing Government action against contracting

UK tax risk has been increasing (2):

Other recent legislation and claims

- HMRC Reg 80 assessments March 2017 under old rules re offshore and sole traders
- Loan Charge arrangements may involve end user risk
- MSC legislation enforcement against contractors and accountancy service providers (Christianuyi case Court of Appeal 2019)
- Criminal Finances Act 2017
- Enabling legislation 2017
- HMRC action at GSK etc re IR35 2019
- Taylor Report

03

IR35 detail



IR35 detail

- 22 November 2017 - statement in Autumn Budget
- Consultation closed in May 2019
- Research published in 2018 suggesting:
 - one third of private sector PSCs are “inside IR35”but only 10% of that one third are currently paying the right level of PAYE and NICs under existing IR35 regime
 - by 2022-23 this could lead to a £1.2 billion tax shortfall for the UK Treasury
- HMRC thinks the public sector IR35 regime "works" as a template
- HM Treasury needs to raise tax given spending promises



IR35 detail

- So...it looks like something is coming (with relatively little political opposition so far)
- Draft legislation published 11 July 2019 and 22 January 2020, with announcement 7 February 2020 – to come into effect on 6 April 2020
- Current Government review and House of Lords inquiry appear just to be a "look" – no major changes to the proposals likely



IR35 detail

But what is coming?

What we will try to cover:

- How the 2017 regime works in the public sector (and how it is likely to work in the private and public sector from 2020)
- How the market seems to have responded/may respond
- What HMRC seems to think



IR35 detail

4 steps determine when the IR35 liability arises in draft legislation:

1. Supply of labour
2. ...to the public sector or any non-small private company
3. ...involving a contractor who is a PSC
4. ...who "fails IR35"

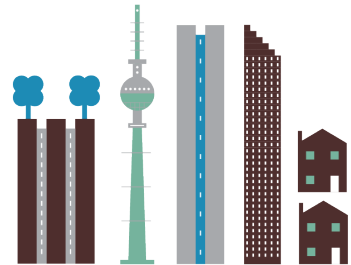
What does that mean?



IR35 detail

Step 1 - What is a supply of labour?

- "...personally performs or under an obligation personally to perform"
- what if hirer has no interest in who turns up?
- output-based contract with end user?



IR35 detail

Step 2 - What is: to the public sector or any non-small private company?

- FOIA definition of public sector – includes TfL, BBC, Channel 4, Network Rail, most Universities etc.
- Small company definition: two out of:
 - group t/o less than £10.2M,
 - balance sheet less than £5.1M, and
 - <50 employees



IR35 detail

Step 3 - What is a PSC?

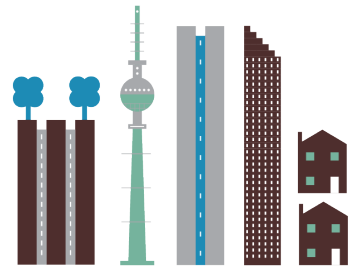
- Someone operating through their own corporate entity
 - not a staffing co's PAYE worker (normal PAYE and NICs rules apply)
 - not an umbrella company employee (umbrella liable under PAYE and NICs rules and new T&S rules)
 - not a sole trader (the 2014 Onshore Intermediaries legislation applies making Intermediary 1 liable unless no supervision direction or control – opposite end of the supply chain to IR35)



IR35 detail

Step 4 - who fails "IR35"?

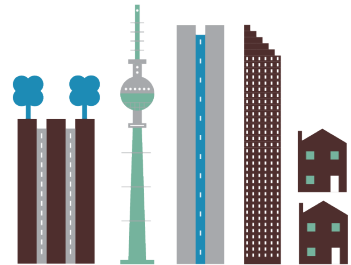
- same old multi-faceted test based on employment law
 - **Control** as to how the work is done (lack of control best evidenced by contracts being on an output rather than T&M basis)
 - Mutuality of obligation (n.b. HMRC do not seem to rate this an important test)
 - Personal service (n.b. note recent case law making substitution clauses less relevant)
 - Other factors such as whether the individual takes business risks, is integrated into the employer's business etc



IR35 detail

Online CEST tool

- No legal effect – not mentioned in the legislation
- HMRC bound in practice by it?
 - Only if answered correctly/honestly – and the questions are highly subjective
 - The tool usually says "don't know" in the more difficult situations
 - And it's a snapshot
 - HMRC £4.3M claim against NHS Digital following misuse of CEST
- Recent update does significantly improve reliability



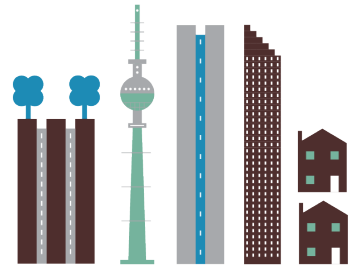
IR35 detail

Who is primarily liable?

- The "Fee Payer" i.e. the person who "makes" a "chain payment" to the PSC

Who is the Fee Payer?

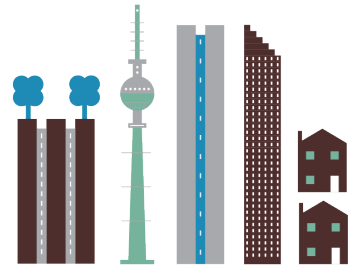
- If no chain (between public sector user and the PSC), then the end user is liable e.g. BBC and Jeremy Paxman etc.
- Otherwise the person in the chain who pays the PSC



IR35 detail

End user liable if:

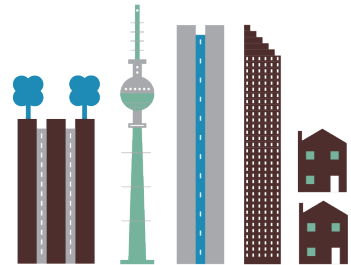
- worker is "inside IR35" but worker is paid gross and....
- end user
 - has **failed to communicate** a Status Determination Statement (SDS) to staffing co or worker or
 - has (i) issued an "outside" SDS and (ii) in doing so failed to take **reasonable care** or
 - has (i) issued an "outside" SDS and (ii) **has not given reasons/changed assessment when asked by worker/Fee Payer** (within [45] days) or
 - **directly engaged**



IR35 detail

Intermediary such as **MSP** liable if:

- worker is "inside IR35" but worker is paid gross and intermediary has **failed to pass end user assessment** down the line



IR35 detail

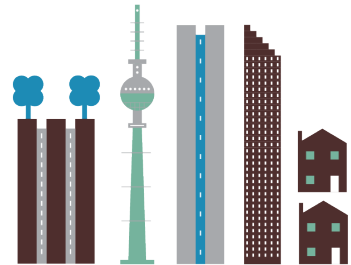
And

End user or MSP liable if:

- worker is "inside IR35" and HMRC considers there is no reasonable prospect of recovering the tax from the Fee Payer within a reasonable time (e.g. because of solvency issues)

This has spooked end users and MSPs

- if the Fee Payer fails to pay the tax the end user is liable - even if it has done everything it should i.e. assessed inside and communicated that to the Fee Payer



IR35 detail

- What if worker or Fee Payer (for example a consultancy/staffing company) disagrees with the end user "inside" SDS?
 - Right to challenge? NO.
 - Right to an explanation – and end user liable if it does not give reasons or change decision within the 45 day time limit - but no independent adjudication – **end user decision on appeal will be final**
 - Fee Payer could take a risk and (based on its own assessment of the “outside IR35” status of the PSC contractor) decide not to deduct PAYE and NICs on any payment to a PSC who has been assessed inside IR35 by an end user?
 - Uphill struggle for Fee Payer, **unless it has good evidence supporting its stance**, fighting any claim by HMRC



04

How the market is responding



How the market is responding

Blanket safety first "everyone is inside" SDSs or "no PSCs any more"?

- Lloyds/Barclays/HSBC etc
- **There is nothing in the draft legislation prohibiting private sector end users from doing this**
- Works in some cases/job types where PSC usage just not appropriate and workers do not have transferable skills (e.g. nurses)

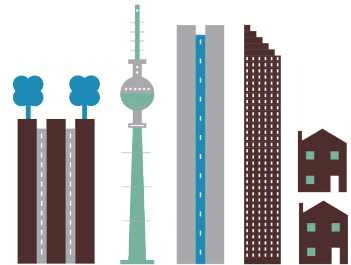
Move to

- employed option or
- various types of traditional umbrella/PAYE or
- to aggressive new umbrella schemes (**take care** - see later)



How the market is responding

- Significant reduction in the take home pay of some contractors (unless hirers agree to increase the rate, which has happened in some public sector cases)
- In other cases possible loss of good contractors leads to reassessment of blanket approach?
 - NHS experience with some doctors
 - TfL move from blanket inside SDSs to most outside
 - Will major banks allow exceptions to their policies?
 - Workers engaged via consultancies?
 - Indispensable contractors with transferable skills?



How the market is responding

Will there be lots of challenges from staffing co's to end user SDSs of "inside"?

- not really happened? Administrative challenges?

Some end users will not make SDSs, and intermediaries will just take a risk and rely on:

- the fact this leaves end users liable?but indemnities and reputational issues at key clients may stop most staffing companies doing this



How the market is responding

Alternative contracting models which manage/avoid risks (1):

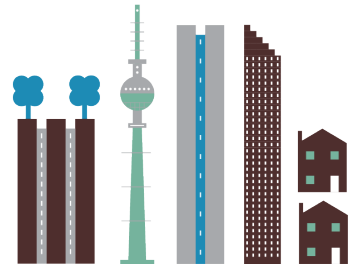
- Third party checkers re status, combined with insurance?
 - MSC risk to be managed - your directors' personal liability if you use checkers who also advise or influence the PSCs
 - Avoid using checkers who do not carry out in depth checks or over-fixate on a "simple" get out like mutuality of obligation
 - Check insurance details



How the market is responding

Alternative contracting models which manage/avoid risks (2):

- UK growth in "genuine" SOW/output based contracts (as in other countries) outside IR35?
- Intermediary becomes "end user" to the extent IR35 applies – gets away from end user blanket over-cautious SDSs
- Increased margin?
- BUT it requires a completely different approach:
 - Not enough just to put a different name on the contract or just to have a new type of contract
 - Are you and your contractors happy not to be paid if the output is unsatisfactory?
 - Will your clients and contractors co-operate with you to define the deliverable and work out a fair fixed price?



05

What you need to do –
some tips

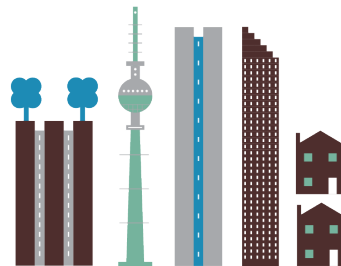


What you need to do – some tips

Talk to line managers at end users

If they are planning blanket ban, or to assess some or all inside IR35

- Help them assess likely cost increase/migration relating to the most "hard to find" contractors - "blanket" assessments not safe?
- Test appetite for finding extra budget to gross up
- Test appetite for alternative contract models outside IR35
- Make sure you have a PAYE option
- Terminate those "inside" before end of March and issue new contracts at new rates after employers NICs deduction
- Need to be aware of disgruntlement among contractors found "inside", and set up processes for handling contractor distress and challenges
- Find more flexible clients where you can place disgruntled contractors "outside"?



What you need to do – some tips

Talk to line managers at end users

If they are planning some or all **outside** IR35

- Information will be needed by you as Fee Payer from end users/MSPs – start asking how they are planning to assess and make sure you trust their assessment
 - Fee Payers have primary liability and will need a lot of reassurance before they are prepared to pay "outside".
- Terminate and re-engage on new terms before 6 April 2020 under which end users and contractors confirm they agree with the outside assessment.

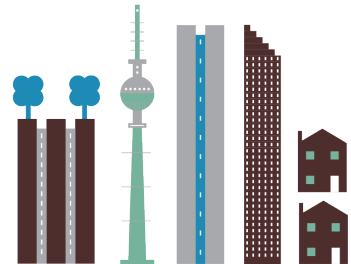


What you need to do – some tips

Talk to end users and contractors

Put them off use of staffing companies using aggressive umbrella schemes e.g. loan schemes and small umbrella company (suc) schemes.

- Loan schemes simply unlawful, and April 2019 loan charge (HMRC spotlight 45 August 2018).
- HMRC spotlight 24 etc. *"this [suc] scheme simply does not work [in terms of small co NICs allowance]HMRC is investigating cases where people have used this scheme and will challenge every case it sees....a promoter for such a scheme who has not notified it under the DOTAS rules could be liable for a fine of up to £1million"*.
- Risk for you? Some have closed down, and there is criminal liability risk for end users and staffing companies – CFA.
- **Some major end users are prohibiting use of umbrellas by their staffing companies – wise to have an in-house PAYE option going forward.**



06

Conclusion



Conclusion

- There are options
- Some contractors will be caught – so go PAYE?
- Others can use output based SOW or other models to stay outside but...
"Fee Payer" will be primarily liable so can't take risks - only pay outside IR35 if really sure
- Some end users will initially respond with blanket assessments inside/"no PSC" policy, even for more independent contractors - they need to think through the cost/talent loss implications of this
- Watch out for pedlars of dodgy umbrella schemes!



Final word

- The UK has been a relatively benign environment for use of contingent workers.
- That is changing
- Staffing companies will need to adopt new processes and new contract models, and issue new contracts in March



Sonovate's IR35 solutions

Kirsty Brice



Creating the solutions

- Consulted our customers
- Engaged with legal experts
- Designed solutions to feed into tech strategy



Our solutions

Inside	Outside
PAYE	Statement of Work (SOW)
PSC Deductions	Time & Materials
Time & Materials Umbrella	



Our IR35 solutions: features

- 100% advance funding on all temporary assignments
- Online timesheets and invoicing for all time and materials based assignments
- Online invoicing for deliverables based Statement of Work (SOW) assignments
- Payroll for inside or outside IR35 PSC assignments including VAT, Employee's Tax & NI and Employer's NI
- Payroll for inside IR35 PAYE temporary workers





Questions

Kevin Barrow

- *"If a UK based contractor works for a non UK- based client, would they fall under IR35 legislation?"*
- *"Does a MSA/SOW delivery model solve the problem? If so, what do I need to do to prepare for this?"*
- *"Is Sonovate the fee-payer?"*
- *"As the legislation comes into force on 6th April, does this mean that all payments to non-compliant IR35 contractors need to be made before this date?"*
- *"Will contracts need to be revised and reissued? if so, who to?"*
- *"What about employment claims by contractors caught inside?"*

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Thanks for joining us today

- We'll email a copy of the recording and the questions we didn't have time to answer.
- We'll continue to engage with our customers and Osborne Clarke leading up to the implementation of the changes.
- If people would like specific legal advice, please contact Osborne Clarke.
- Similarly, to find our more about Sonovate's products, please get in touch at hello@sonovate.com

