

## **Response to HMRC Consultation on Off-payroll working in the public sector: reform of the intermediaries legislation**

from Crunch

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### **About Crunch**

[Crunch](#) is the UK's first and fastest-growing online accountant, helping over 9,000 micro-business owners easily control their finances. We also run [Chorus](#), a free-to-join membership association of 23,000 micro-businesses.

Since launch in 2009 Crunch has helped its clients invoice over £2 billion, and has been chosen by brands including Uber and B&Q to provide accountancy services for their contractors. Crunch serves freelancers, contractors, small business owners and sole traders with its uniquely integrated software and one-on-one client management. Crunch also offers Mortgages, Insurance and Collections services uniquely honed for the micro-business market.

### **Summary Position**

The proposals for IR35 set out in Budget 2016 and this consultation represent a very significant extension of how IR35 works in practical terms. We believe this presents significant logistical and policy challenges which will have negative impacts on public services, flexible workers and micro-business owners. We also fear this is just a staging post to similar expansion in the private sector which would similarly have major negative consequences for workers, their engagers and micro-businesses in general. The 'chilling effect' such broad new restrictions will have on micro-businesses and their potential clients should not be underestimated.

These proposals are likely to lead to a shortage of worker supply due to higher engagement costs, which will hence lead to higher prices for the public sector, thus overriding any benefits drawn from the hoped for boost in tax revenues.

While we agree that disguised employment is not desirable and can lead to unfair outcomes as well as possibly lower tax revenue, we believe that the solution lies in a more significant change to tax and welfare systems to reflect the nature of modern business practices.

### **Support principle of fairness**

We recognise the government's desire to ensure fairness in the tax system so that people doing equivalent work are paying broadly equivalent levels of tax. We also understand the desire to ensure that rules aren't unfairly exploited. However these proposals, if applied as set out, will lead to workers paying full National Insurance like an employee without having

any of the rights and protections an employee can benefit from. This doesn't feel like fairness to us.

### **Current rules too complex. We propose simple 3 tests**

The current IR35 rules are too complex forcing most businesses to seek professional advice just to understand if they may be falling under IR35. The proposals as they stand would result in making the situation more complex with significant practical differences for those with public sector clients.

A significant re-imagination of tax and welfare rules should be the primary goal to resolve tensions in the flexible workforce. Meanwhile, until such major work can be completed, we propose that the IR35 legislation should be amended to define a small number of clear tests. These tests should mirror the current case laws in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance 1968*.

We believe that these tests should be in plain english, avoiding jargon, so as to be unstandable for all readers. They should cover:

- Personal Service - Can someone else do the work?
- Control - Does the engager control how the work is done?
- Mutuality of obligation - Can either party walk away from the engagement?

### **Pushing liability on engagers will disadvantage micro-businesses in the market**

We are concerned with the suggestion of making the engager decide if IR35 applies. We believe such a change would result in engagers seeking to diminish their risk by preferring to hire larger firms to the detriment of one-person micro-businesses who will be considered a higher IR35 risk by potential engagers.

In our view simpler, clearer rules would be the best way to improve compliance, ease inspection and reduce uncertainty. Trying to push liability and responsibility onto engagers will result in behaviours which risk being highly detrimental to the significant numbers of creative, high skilled workers operating their own companies in the UK economy. They may choose to withhold from the public sector market as a result of these rules. Because why would someone work for the same effective pay as an employee without benefits like holiday and sick pay?

As government research has shown (e.g. [OTS Small Company Taxation Review](#) and [HMRC intermediaries legislation qualitative research](#)) the main reasons for incorporation are *not* tax minimisation, they are to limit their liability, to enhance their credibility and to provide a formalised structure. Hence tightening up IR35 is unlikely to shift a significant number of such workers to PAYE employment, which may be an underlying assumption behind these current proposals.

### **Responses to the consultation document**

We are responding to the document as published at <https://www.gov.uk/government/consultations/off-payroll-working-in-the-public-sector-reform-of-the-intermediaries-legislation>

*Question 1: Are there other easily understood definitions that work better than the FOI Act and the FOI (Scotland) Act?*

We believe this is a good basis on which to work.

*Question 2: Are there any public sector bodies which are not covered by the FOI acts which should be included in the definition for the proposed rules?*

No view.

*Question 3: Should private companies carrying out public functions for the state be included in this definition? Why?*

We don't believe these proposals should be implemented as proposed. However if they are, then we believe they can only be applied fairly if all public service providers, regardless of their organisational type, are covered. This will add complexity to the practical implementation which is one of the reasons we oppose the proposals. This will also result in additional costs of employment which will drive up overall cost to the Exchequer and reduce flexibilities - for instance in relation to agency staff working in the NHS.

We would like to see greater clarity on how umbrella companies would be treated in these proposals - would they be considered an agency or engager to which liability could fall?

*Question 4: Are there any public bodies caught by this definition who would face particular impacts which should be considered?*

At the high-end employment of highly skilled people may be affected. Highly skilled employees with unique and hard to access experience and skills currently working through personal service companies may be discouraged from taking on any public sector work due to the implications of these proposals. This is likely to affect public bodies with particularly specialist skills requirements.

*Question 5: Are rules needed to ensure that engagers have the information they need to make the decision? If so, what should they be?*

We believe engagers are going to be risk averse, hence likely to say the worker is under the scope of new rules. This will result in the a lower daily fee as the engager won't want to pay employer's national insurance out of their own pocket. Thus we believe it makes sense for the worker to complete the HMRC tool and then the engager has to accept the result of this regardless. A record of this result will need to be retained by the engager.

*Question 6: How would accounting for the 5% allowance work in practice?*

How will a worker's invoice be dealt with for corporation tax? Will the 5% expenses deduction be subject to corporation tax? Also we have a concern that agencies will attempt to retain the 5% for their own costs and not pass it on to the worker's PSC.

Will a new tax code need to be issued for each engagement? RTI will need to be updated to allow for the 5% deduction to be flagged and allowed.

How will a tax overpayment be handled? Will each engagement be a separate entry on the employment pages of a self assessment return? We would propose that by 31st May of each year a worker should be given a standard form summarising tax and NI deducted for the year. This would then be input onto the self assessment as a tax credit amount. We believe it is important that the worker could get a refund for any overpaid tax compared to what has been paid PAYE.

*Question 7: Are there business costs specific to PSCs that are covered by the 5% that aren't covered under the usual business expense rules?*

We would expect existing rules to continue so that allowable expenses that an equivalent employee could claim (e.g. travel to temporary work place) would continue to be excluded from NI and PAYE and so passed on to the PSC gross.

*Question 8: Does the first part of the test work to quickly rule out engagements that are clearly out of scope?*

Yes, with the exception of agency workers where essentially the test pushes the questions on to the agency or intermediary.

*Question 9: Are these the right questions in the right order of priority?*

Yes.

*Question 10: Are the questions simple to understand and use?*

Yes.

*Question 11: Do the two parts of the test give engagers certainty on day one of the hire?*

Part two is still sufficiently vague that doubt will arise when considering these questions. The detail of contracts and case law will likely need to be considered before a final determination can be made.

What if there are differences between an engager and PSC over how they actually work? We believe there will be situations where one engager believes a firm passes the tests and

another engager won't. We know that some engagements change in nature over time, how will they be handled?

We also believe clarification will be needed on how to deal with existing contracts continuing past the point at which these changes are proposed to become active. Will contracts being extended or renewed all need to be reviewed as if new, thereby adding to transaction costs?

Take Examples 3 and 4 on page 14. We suspect that contracts would be shifted or adapted in example 3 to be more similar to example 4 so as to avoid liability so that PSCs wouldn't need to be added to payroll.

The implication of example 4 is that PSC workers serving a PFI hospital project which includes provision of building and services would not be caught by these proposals. Would that be HMRC's view?

*Question 12: How can the organisation completing the tests ensure they have the information to answer the questions?*

They will need access to the procurement process documentation, contracts, working practices at a minimum before determining the status of a worker. As the nature and type of work can evolve over the period of engagement this may need further information and review.

*Question 13: How could the new online tool be designed to be simple and straightforward to use?*

With minimal jargon, questions which have clear yes/no answers that gives an unequivocal result that is easy for users to action.

We have concerns that there is a very short timeframe for HMRC to deliver this tool in time for proposed timescale of these rules becoming active.

*Question 14: Where should the liability for tax and National Insurance (and penalties and interest where appropriate) fall when the rules haven't been applied correctly?*

Jointly the engager and with the ultimate end client (public sector body). This will ensure public sector bodies do supervise the conduct of the agencies and providers they engage.

*Question 15: Should the liability move to the PSC where the PSC has given false information to the engager?*

Yes, however this needs to be carefully scoped: If a PSC, in good faith, gave information they thought to be correct then there should be an element of protection. A PSC alone is not in full control nor awareness of how an engager will actually seek to use their services. It is important to note that a PSC and engager will be completing a test before work has begun, thus making it hard to know how it will proceed in reality.

We would want to ensure that engagers could not disclaim liability through weasel words in a questionnaire or contract.

*Question 16: What one-off and ongoing costs and burdens do you anticipate will arise as a result of this reform?*

Additional costs of administering systems will be ongoing on already stretched public sector back office functions, or be borne as additional costs that agencies pass on to public agencies or deduct from PSC payments reducing their income. There will be an immediate need to invest in new software and ICT systems to administer this process. Purchase order, procurement and payroll systems will need to be brought together, or at least be accessible at the same time by those undertaking tests and processing payments for those who fall within scope.

It will be logistically challenging to keep track of those workers in scope and how they should be paid across payroll and invoice payment systems. Smaller firms already find it challenging to get paid in a timely fashion by the public sector, these proposals risk exacerbating this situation.

### **Further points**

“Departments are also asked to provide HMRC with the personal details of any workers where the engagement has either been terminated, ended as a result of assurance, or ended before the assurance process has been concluded.” -- Why is this proposed?

Appeals: Will the appellant have to pay HMRC the assessed amount of tax then await Tribunal? In other words will HMRC issue notices with liability immediately then appeals much later?

Ends.