

Contractor HMRC inspections: do you have your IR35 life raft ready?

HMRC have various options for detecting contractors according to Carl Whittaker of [Qdos Consulting](#), which specialises in [IR35](#) and [legal matters for contractors](#) throughout the UK, and every [limited company contractor](#) is a potential investigation target.

"It is not difficult for HMRC inspectors to identify contractors," he says, going on to warn: "But contractors who have not prepared their 'IR35 life raft' will face treacherous waters in the event that they are investigated."

So, how come contractors are so easy to find?

Just to give an example, during a review of the end-user client's accounts an inspector would notice if there were a large number of small limited company suppliers and then the inspector would ask for more information, such as copies of invoices.

Although contractors' costs are variously described and under all sorts of headings in the accounts of different client organisations, an experienced HMRC inspector would discover if a large number of [personal services companies](#) are being used.

Copies of the contractors' invoices or details of the contractor's company name and addresses would be requested from the end-user client. This information would enable an appropriate inspector to issue Employer Compliance Review notices to all the contractors, an indication that the contractors' lives are about to become very uncomfortable.

HMRC has access to tax records and accounts

HMRC's databases contain a huge amount of data about every individual and organisation in the UK, as all the information submitted by contractors on their tax returns, P35s and P11Ds is kept on file by HMRC.

And contractors can be identified by HMRC for a number of reasons with specific patterns that will alert an inspector that they are looking at a contractor who might fall within IR35. Some of the more obvious features of a contractor limited company include:

- o Directors receiving an extremely large [dividend](#) and
- o No employee salaries, or only very low employee salaries to, for example, a spouse.

These features of a company's finances strongly indicate to HMRC that the business is a personal service company. Plus, of course, contractors who ticked 'yes' to the question in their P35 confirming they are a service company are easily identified, which is HMRC's intention by including this question in the employer's annual return.

Can contractors avoid tax inspections?

The short answer, Whittaker says is no, there is not a lot that can be done to keep a company below HMRC's radar if an inspector looks hard enough: "Contractors would be wise to accept the inevitable. I advise my clients that they could be investigated at any time, and I help them to prepare an 'IR35 life raft' should the worst happen."

According to Whittaker, essential IR35 survival aids include:

- o Ensuring all [contracts are reviewed](#) by an [IR35 specialist](#)
- o Where possible have a [statement of working practices](#) signed by both the end user and the contractor. This statement should include agreement to a genuine [right to substitution](#) and also that the contractor [controls](#) the how and when he provides his services
- o Take out [IR35 investigation insurance](#) to cover the cost of professional guidance and advice through the investigation process.

Contractors targeted by HMRC can find investigations highly stressful, time consuming and ultimately very costly. Time away from work, funding professional advisers for a defence, plus paying any back taxes, interest and penalties if you lose, can all add up to a considerable sum.

"With the right precautions in place," concludes Whittaker, "contractors should be able to go about their legitimate business secure in the knowledge that if in the event they are investigated, they will come through the inspection with no nasty surprises."

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Carl Whittaker, Qdos Consulting

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