

## An introduction to IR35 for expat and overseas contractors new to UK contracting

[IR35](#), also known as the 'Intermediaries legislation', is tax legislation aimed at [charging contractors more tax](#) if they are in reality 'disguised employees' of their client, rather than a bona fide contractor. It is extremely important for expatriate (expat) contractors to understand this legislation, because by doing so they can expect to enjoy a [much higher net income](#).

So why does a UK tax law matter to expat contractors? Because if they find that IR35 applies to one or more of their UK contracts, they could end up being taxed as if they were employed. That could mean paying significantly more in tax, up to 25% in some circumstances. To see what that means in practice, it could cost a contractor earning £40 per hour an additional £800 per month in tax.

### IR35 and expat contractors

Contractors, understandably, do not like IR35. It came into effect in 1999 and is generally recognised by the contracting sector and its industry body, the [Professional Contractors Group](#), as unfair. That's not only because of the additional tax liabilities suffered by contractors, but mainly because contractors [receive no employee rights](#) or other protection in exchange for paying tax like an employee.

Nevertheless, no one has yet proposed workable alternatives that satisfy the needs of the Government and other stakeholders, so it seems likely that IR35, in one form or another, is likely to apply to contractors for the foreseeable future.

### How does IR35 work?

IR35 applies to specific contractor contracts with an end-user client. So it is possible to have several contracts during a tax year, with some 'within' IR35 and others 'outside' IR35. The ideal is to [negotiate contracts](#) in such a way that they are always 'outside' IR35, but it is important to note that what counts is how the contractor works and the working relationship they have with their client.

The legislation is intended to identify 'disguised employees' who would be employees if they did not have an intermediary, such as the [contractor limited company](#), between them and the client. This is why IR35 is also referred to as the 'intermediaries legislation'.

If the IR35 enforcement agency, Her Majesty's Revenue & Customs ([HMRC](#)) judge a contractor to be an 'employee' in every other way but name, then their [contract is caught by IR35](#), they are working within IR35 and have to pay taxes as if they were employed.

### Employment 'tests'

HMRC apply a [number of tests](#) to a contractor to determine if they are actually a 'disguised employee', and these are based on UK employment law.

There is a long history of employment tests in the UK, because UK workers have generally been trying to prove they ARE employed, and can therefore claim potentially valuable employment rights from their 'employers'. IR35 is the reverse – contractors are trying to prove that they are NOT employees, and therefore do not have to pay tax as if they were.

As with all cases in UK law, each is judged on its individual merits and there is no absolute right or wrong answer. However, there are some broad indications of 'employment' that an expat contractor can apply to check whether they should [consult an IR35 expert](#).

The most commonly used tests of employment include:

- o [Control](#)
- o [Substitution](#)
- o [Mutuality of obligation](#)
- o [Part and parcel](#)
- o Provision of own equipment
- o [In business on own account](#)
- o Business/financial risk.

There are other factors taken into account, but the key tests are generally considered to be the first three in the list above – control, substitution and mutuality of obligation.

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## ‘Notional contracts’

If a contractor is being investigated by HMRC, the tax investigator will apply all the above tests to the contract in question to determine if the ‘notional contract’ is one of employment. If it is found to be so, the contractor is working within IR35 and has to pay tax accordingly.

A contractor should have a real contract in place signed by the agent or client. The notional contract, also known as the hypothetical contract, is constructed by HMRC and the courts, to show what the real situation is.

For example, the real contract signed by the contractor and client might say the contractor is allowed to provide a substitute, for example a fellow contractor, to do the work for them. But if other evidence, such as correspondence or evidence from the client, shows this not to be the case, then the notional contract would be deemed to have no right of substitution. In other words, the contract would be found to be ‘caught by’ or ‘within’ IR35.

## Professional IR35 advice for contractors

Contract law and employment law are highly complex areas of UK law, and ones that are constantly evolving, as new [case law](#) emerges on regular basis. If an expat contractor has concerns that a contract may be caught by IR35, they should [consult an IR35 expert](#), who will be a contract law and employment law expert.

With only a few exceptions, contractors should consult lawyers or specialist consultants who are experts in contractor employment law and contract law. Accountants are generally not as well placed to determine IR35 status as a legal specialist.

IR35 is hugely important and has an impact on every UK contractor. However, most contractors who seek advice manage IR35 effectively and enjoy long and profitable contracting careers without ever having to face the potentially [costly effects of IR35](#).

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