

IR35 changes in the public sector

Likely impact on the flexible workforce – Survey results

Introduction and Background

The Government [announced proposals in the March 2016 Budget](#) to introduce legislative changes to IR35 in the public sector from April 2017.

A Government [consultation was released on 26th May 2016](#) detailing that clients, recruitment businesses or other third parties such as consultancies will become responsible for determining the IR35 status of contractors trading via their own limited company who are working on public sector contracts.

Expert commentators have expressed concern at the HMRC proposals, both in their objectives and workability. ContractorCalculator CEO Dave Chaplin, who has been following the flexible workforce for two decades, has stated that a [simple binary tool that assesses status cannot be achieved](#) and that [HMRC is attempting the impossible with its proposed online IR35 tool](#).

This survey of c500 contractors sought to understand the likely behavioural effects of the proposals on contractors, together with the resulting impact on the public sector and Treasury tax collection figures.

Summary of findings

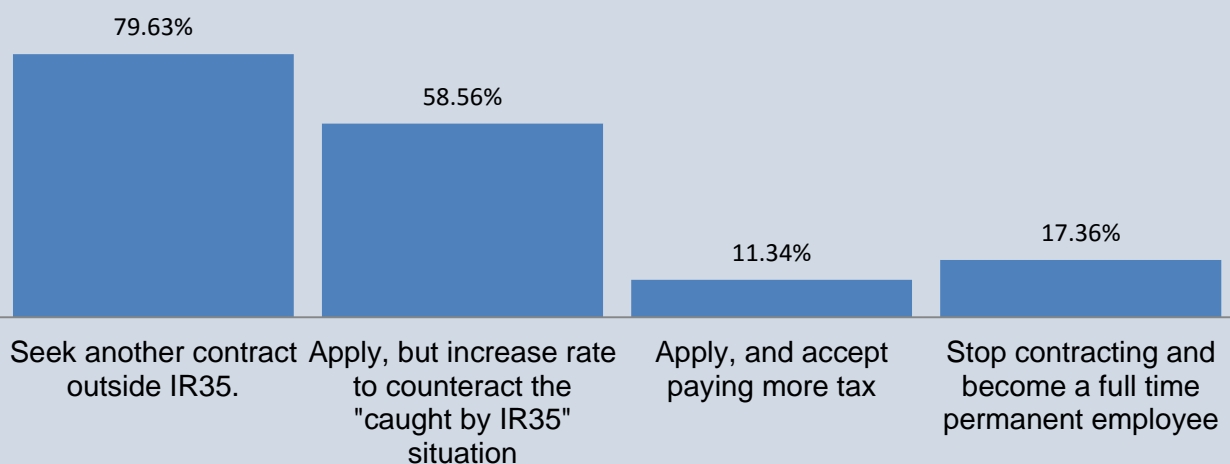
- Four out of five contractors say they will quit working for the public sector if the new rules come in.
- 89% of contractors say they earn the same or more than permanent employees.
- Forcing contractors into employment is a tax reduction exercise and could lose the Treasury £115m.
- Reforms could see a rise in Government spending of £610m to keep projects running.

Contractors will leave the Public Sector

Contractors were adamant that they were not prepared to accept contracts where they were taxed like employees:

- Four out of five contractors (79.63%) say that they will seek an alternative contract if the public sector contract is advertised as being caught by IR35.
- Three out of five (58.56%) say they will stay working for the public sector, but only if their rate is increased to compensate for the extra tax they will need to pay.
- Only one in ten contractors (11.34%) say they will stay working in the public sector under the new rules on their current rates.
- Almost a fifth (17.36%) of the flexible workforce in the public sector say they will stop contracting and instead seek permanent employment.

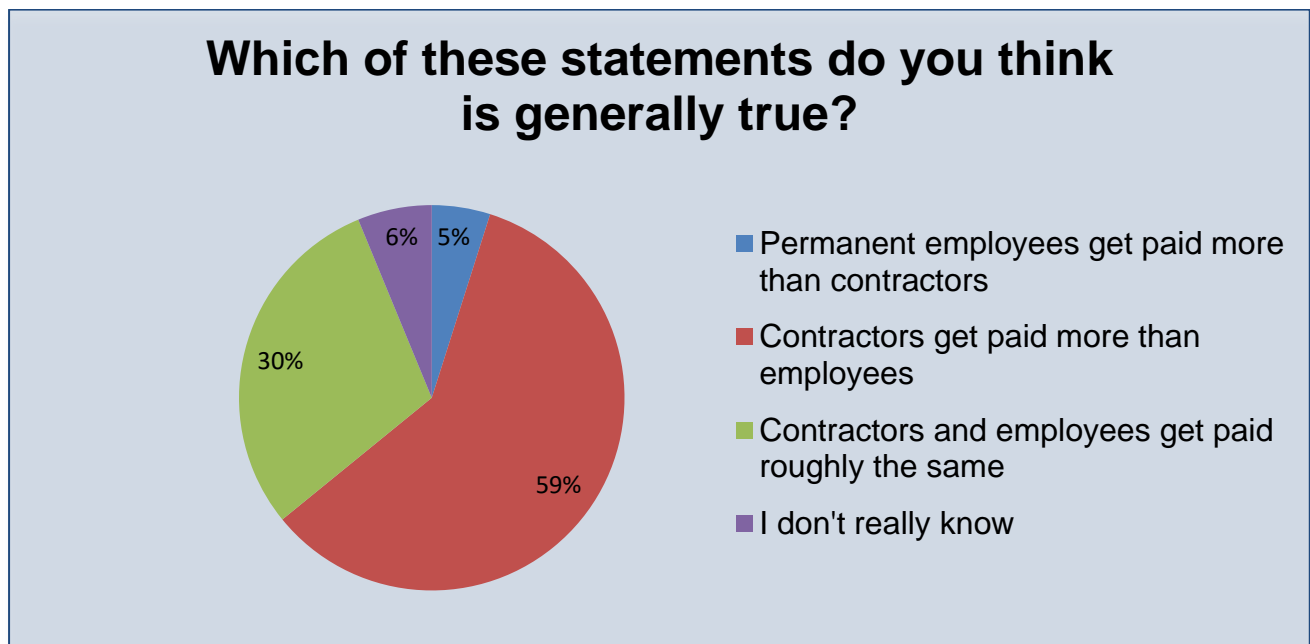
If a contract you were interested in was advertised as "caught within IR35" then what would you do? (Tick all that apply)



How contractors earnings compare to employees

The responses from contractors indicate that HMRC is wrong to assume that contractors earn the same in gross fees compared to their permanent employee counterparts.

- 59% of all contractors said they earned more contracting than they would if they were a permanent employee.
- 30% said they earn roughly the same.
- Only 5% said that employees earn more than contractors.

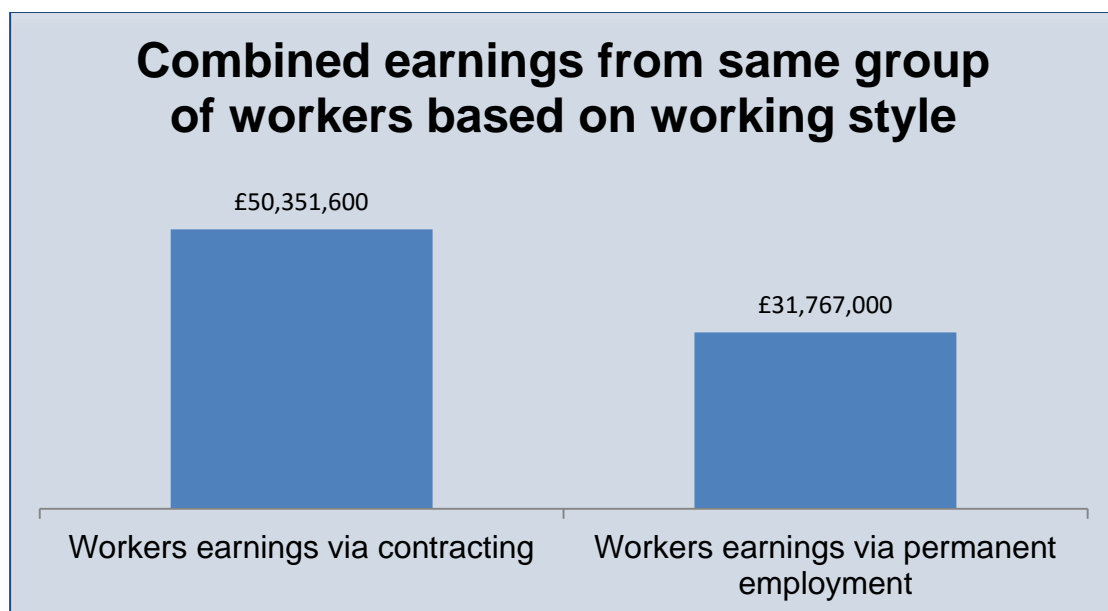


Forcing contract workers onto payroll reduces GDP by £750m

All respondents reported their daily contract rates and how much they would be expected to earn as employees.

We then calculated and summed the combined annual contract fees, combined annual salaries and combined taxes via both working styles for the whole group.

If the contract workers moved to employment they would expect to earn combined total salaries of £31.8m. But as contractors their combined gross fees are considerably more at £50.4m, an increase of 58.5%.



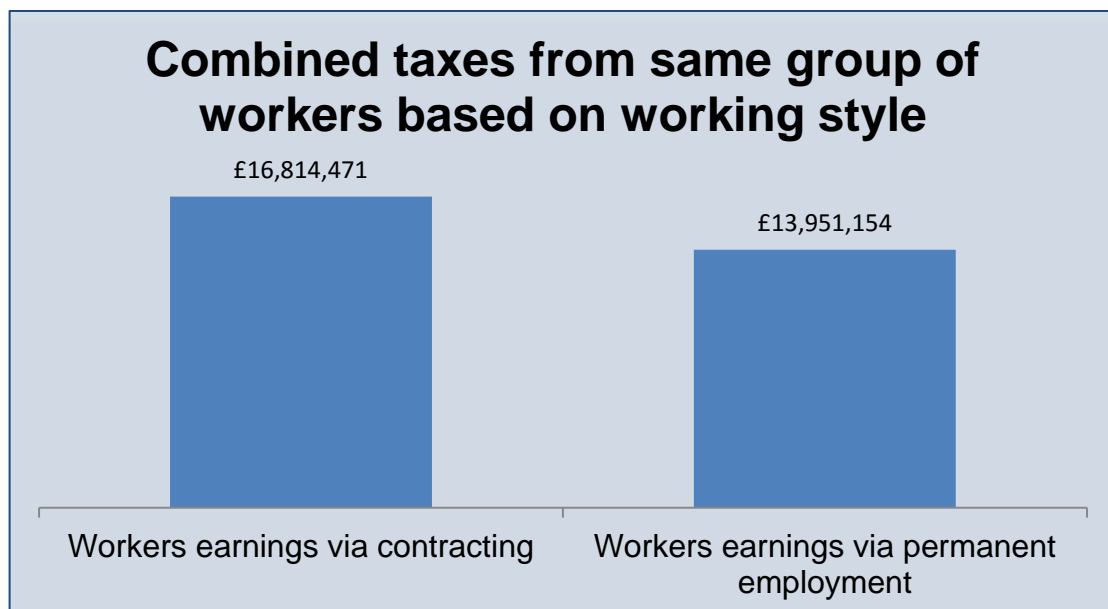
If this sample size is extrapolated to the 20,000 workers that HMRC claims will be affected then the total reduction in taxable earnings will be £750m.

Forcing contract workers onto payroll reduces tax collection by £115m

We calculated the taxes for each individual in the group, both as a contractor and as a permanent employee on the salary they said they could command.

From the contractors combined earnings of £50.3m, working via personal service companies the combined amount of tax paid (including all corporation tax, salary taxes and dividend taxes) would be £16.8m, 33% of the gross fees.

If they moved to permanent employment on the lower salaries, from the combined salaries of £31.7m the combined total amount of tax paid (including all income tax and NICs (both employers and employees NI)) would be £13.9m – a 17% reduction.



If this sample size is extrapolated to the 20,000 workers that HMRC claims will be affected, the total tax loss to the Treasury will be £115m, contrary to the £400m HMRC claims it will raise with this measure.

Keeping Government projects running could cost up to £610m

The vast majority of contractors have indicated they would only continue to work in the public sector if they were paid more to compensate for the extra taxes due.

To earn the same income after taxes from contracting after being caught by IR35, a typical contractor will need to increase their fees by 30%.

£ 610,000,000

If this sample size is extrapolated to the 20,000 workers that HMRC claims will be affected, the increased fees required to keep contractors working for the public sector would be £610m.

Further Resources

Budget 2016: public sector contractors face tax avoidance crackdown from 2017 [16/Mar/2016]
http://www.contractorcalculator.co.uk/public_sector_contractors_tax_avoidance_crackdown_519010_news.aspx

IR35 public sector consultation released [27/May/2016]
http://www.contractorcalculator.co.uk/ir35_public_sector_consultation_released_524410_news.aspx

HMRC: Off-payroll working in the public sector: reform of the intermediaries legislation [26/May/2016]
<https://www.gov.uk/government/consultations/off-payroll-working-in-the-public-sector-reform-of-the-intermediaries-legislation>

HMRC's planned IR35 tool is impossible, claims expert [12/July/2016]
http://www.contractorcalculator.co.uk/hmrCs_planned_ir35_tool_impossible_claims_expert_527410_news.aspx

Devising a simple statutory employment status test is impossible [14th Jan 2015]
http://www.contractorcalculator.co.uk/simple_statutory_employment_status_test_impossible_484410_news.aspx

How contractors pay more tax than employees [8th September 2015]
http://www.contractorcalculator.co.uk/how_contractors_pay_more_tax_than_employees_502010_news.aspx

ContractorCalculator HMRC consultation submission [29th September 2015]
<http://www.contractorcalculator.co.uk/docs/IR35ReformResponseByContractorCalculator.pdf>

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