

HMRC ESS tool has no legal authority, says IR35 legal expert



HMRC's Employment Status Service (ESS) tool is not legally binding and use of it cannot be seen to be taking 'reasonable care' when determining a contractor's IR35 status.

This is according to Martyn Valentine of [The Law Place](#), a firm that specialises in employment status law, who stresses that the [shortcomings of the ESS tool present serious risks to clients and agencies](#).

- The ESS has no legal authority
- The only way 100% certainty can be provided is in court
- The ESS doesn't constitute 'reasonable care' being taken
- Using the ESS could put agencies and clients at risk of incurring tax liability

"Relying on the error-prone ESS could be tantamount to negligence unless it is radically overhauled," warns Valentine. "It is likely a far more reliable defence to an accusation of failure to exercise reasonable care to establish tax status would be provided by a reasoned opinion based on the terms of the contract and the working practices."

Why doesn't HMRC's ESS tool amount to 'reasonable care'?

The standout change to the IR35 public sector rules was the confirmation in the [Finance \(No. 2\) Bill 2017](#) that tax liability will be borne by the client if they are unable to prove 'reasonable care' was taken when determining a contractor's status.

"In the context of a contractor facing an IR35 inquiry, taking reasonable care constitutes acquiring independent legal advice," Valentine explains. "So you would assume that the same is implied in this instance for the public sector client."

"The ESS tool doesn't go into enough detail to be viewed as equivalent to legal advice. As it stands, it's merely a simple question and answer tool. It looks like a 1980's adventure book where you flick through the pages and answer multiple choice questions until you get to the end."

HMRC's ESS tool – the risk to agencies and clients

Beyond its oversimplification of determining IR35 status, Valentine points out further issues which mean the ESS falls short of meeting legal requirements:

- The ESS gives results that are inconsistent with case law
- Whilst it examines the contract, it doesn't fully assess the ongoing working practices

No tool can be legally binding. It can only be advisory at best. But Valentine would be highly reluctant to encourage parties in the supply chain to even use the ESS to inform their decision:

"It's clear that [the ESS doesn't produce results which align with case law judgments](#) and cannot be safely relied upon in the event of an inquiry and possibly an appeal to the First-tier Tribunal.

"HMRC may have suggested that it will stand by the outcome decided by the ESS, but agencies and clients who base IR35 status decisions purely on what the tool says will not be acting reasonably and so leave themselves at risk.

"In the same way, HMRC has no legal authority to stand by the outcome given by the ESS. The only way 100% certainty is provided is in court, and until a judgment is given, everything is speculative."

Finance Bill 2017 - what constitutes 'reasonable care'?

[Contracting stakeholders have reacted positively](#) to the news that public sector clients will be liable for outstanding tax if reasonable care cannot be proven. But agencies still face significant risks.

The Finance Bill states that the client is required to inform the agency of its IR35 status decision prior to the beginning of the contract. The agency may send a written request to the client, requesting reasons for the status decision, to which the client has 31 days to respond.

The fact that the client is encouraged to take 'reasonable care', or else risk assuming tax liability, provides a measure of comfort for agencies. But because there is no guidance on what constitutes reasonable care, there is always an element of uncertainty and risk for agencies and clients.

Could agencies face retrospective action from HMRC?

Whilst sending a written request an agency can be seen to be conducting its due diligence, the worry is that subsequent adjustments to working conditions which impact IR35 status could place them in trouble further down the line.

"What might happen in practice is you have a contractor that a client decides is outside IR35 at the beginning of the contract, after taking reasonable care," notes Valentine. "If the ongoing working practices differ from this, HMRC may decide at a later date that the contractor was inside IR35 and take the public sector parties to tribunal."

Finance Bill leaves contractors without appeal procedure

One glaring omission from the Finance Bill is the absence of provisions for an appeal should a contractor wish to challenge an IR35 status decision. Valentine explains that contractors are left somewhat short of options when contending their status, adding that in order to overturn a decision they may be required to:

- Obtain an independent review of the proposed contract before the start date
- Persuade the client that the public sector rules don't apply to their engagement
- Indemnify the public sector client and possibly agency in respect of any additional tax

IR35Testing.co.uk – simple IR35 assurance for agencies

A simpler way for agencies to process contractors as outside IR35 whilst mitigating their risk is to conduct IR35 status tests themselves, and take out insurance against the process. There are numerous providers of tax liability insurance, including [contractor insurance provider Kingsbridge](#).

If a contractor has received a pass having [acquired an IR35 review using IR35Testing.co.uk](#), Kingsbridge will insure the contractor's risk based on that result.

Adopting IR35Testing.co.uk as your IR35 compliance solution means contractors can continue to work outside IR35 whilst eliminating tax liability risk for your organisation.

Published: Wednesday, March 22, 2017

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