

How firms can prepare for IR35 compliance under the new Off-payroll rules



We know for certain that the Off-payroll legislation will be extended into the private sector in April 2021. Whilst that may be many months away it is critical for firms engaging limited company contractors, as well as their advisors and accountants, to start some initial preparations now. This will help ensure smooth and proper implementation and ensure there are no damaging consequences of leaving things too late.

What is the Off-payroll legislation?

The legislation is billed as reform of the intermediaries legislation, despite the two being very separate statutes. The [original IR35 legislation](#), which will still apply to contract engagements with small companies, is found in Chapter 8 of the Income Taxes Earnings and Pensions Act (ITEPA) 2003 and was always referred to as IR35. It sets out the tax rules to be applied to limited company contractors who are considered “deemed employees”.

Since 2000, when IR35 came into effect, contractors have been required to assess the tax status of their own engagements and calculate the tax appropriately. Now, under [the new Off-payroll legislation](#), the onus lies on the hiring company, which is now also liable for extra employment taxes where an individual is deemed ‘employed for tax purposes’.

Assessing employment status is complex which is why off-payroll compliance needs expert assistance. HMRC can pursue companies for backdated tax sums when it believes an incorrect assessment has been made. Therefore, the importance of thorough compliance processes cannot be overstated.

It's critical for firms to understand that there are fundamental differences between the original legislation and the new legislation. Adopting an old approach to this fresh challenge is simply not going to be enough. The manner in which HMRC run IR35 cases is very different to over a decade ago, and the case law has moved on considerably. Any compliance strategy will need to be built around a solid understanding of how cases are now defended and argued in court.

The perils of non-compliance

Additional administration along with taking on the risk of tax liability has seen many businesses taking a blanket ban approach and ceasing to engage contractors via limited companies. We saw it happen in the public sector in 2017 and again in the build-up to the private sector rollout that was due to happen in April 2020 before Covid-19 brought about a pause.

The result to date has seen mass contractor walkouts which has had a damaging effect on projects as well as a dearth of skills for firms to access. However, with carefully planned compliance processes in place any risk can be mitigated and damaging repercussions to a firm's business halted.

Securing accurate status assessments

It is vital that compliance protocols are established now, well ahead of April 2021, and many companies will seek help from their accountants and advisers to help ensure a cohesive transition. Key to this is sourcing trustworthy compliance advice and accurate status assessments. HMRC encourages the use of its Check Employment Status for Tax (CEST) tool but [this has been widely discredited](#) because it does not align with the employment status case law and is considered to deliver biased results.

The tool often delivers an 'inside IR35' result when the facts of the engagement do not support this. HMRC has also been known to challenge CEST assessments which have resulted in substantial tax bills for public sector bodies.

One safe option is to enlist [IR35 legal expertise](#). However, organisations specialising in IR35 compliance are thin on the ground, and few will have the resources available to conduct contract reviews at the rate required of them by firms engaging large numbers of contractors.

It is unlikely that we will see more experts emerging anytime soon, given the specialist nature of IR35. Indeed, HMRC takes 3-5 years to train its status inspectors. Fortunately, alternative solutions are available online which will provide accurate assessments and tailored compliance advice.

Ensuring ongoing protection against HMRC

An accurate status assessment alone, however, is just the starting point of ensuring compliance for a particular contract, and on its own will not relieve a company of risk. IR35 status decisions made in court rely upon a critical examination of the actual day-to-day working practices and events that took place, together with a careful balancing of the evidence. Consequently, firms will need to gather the right type of evidence throughout an engagement to not only ensure that the working relationship continues to reflect the original status determination, but also to help shore up any future defence.

Some businesses may be discouraged by the perceived administrative burden. However, with HMRC permitted to retrospectively investigate a party's tax affairs by up to six years in some cases, the retention of such evidence is essential to protect against future risk. A strong defence file should prove enough to deter HMRC's advances, which should quickly help to close down an investigation dead in its tracks.

Insurance alone is not the silver bullet

Some may view insurance as an alternative to robust compliance processes, but this would be foolhardy. Insurance can obviously prove invaluable, and all businesses are advised to at least secure tax investigation insurance.

However, if a company or client views tax liability insurance as the silver bullet that will negate their compliance obligations, they should be reminded that insurance exists to compensate in the event of unforeseen circumstances, and not to recompense for ill-considered compliance decisions leading to non-payment of due tax.

Insurance companies will expect claimants to endeavour to arrive at the correct status determination and are unlikely to pay out if certain measures have not been taken. This will be explained in the small print of any insurance policy, to which close attention must be paid.

Put simply, an off-payroll defence must be founded on solid compliance-led processes and then optionally supplemented by insurance. Providing compliance obligations have been diligently fulfilled, firms should wind up in the enviable position of never having their reputation dragged through a tax tribunal, having a decision made against them, and then having to rely on making an insurance claim.

Act early to avoid any nasty surprises

Finally, it is important that firms get their houses in order well in advance of April 2021. If your company or client has failed to address the off-payroll legislation thus far, an exploratory discussion into their compliance plans could help prevent a nasty surprise.

Any contract that overlaps beyond 6 April 2021 is at risk of attracting unwanted attention from HMRC. If possible, companies are advised to issue shorter contracts in the interim while work is undertaken to establish effective compliance processes.

Want accurate status determinations?

[IR35 Shield for Business](#) is an outsourced SaaS solution available to hiring organisations. Companies can use IR35 Shield's Collaborative Assessments capabilities to pre-answer some questions on the assessment, ensuring accuracy, before inviting contractors to answer the remainder of the questionnaire.

[IR35 Shield for Contractors](#) provides unlimited IR35 assessments, helping you to stay compliant with IR35, combined with insurance to protect against HMRC investigations. Status Determination Statements can also be used as evidence to defend your status against unfair treatment.

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