

## IR35 and contracting bonuses – how to manage bonus payments to avoid IR35

Contractors receiving bonus payments can find themselves pitched straight into **IR35**, as HMRC is likely to see such bonuses as being evidence of the contractor actually being a **disguised employee**. But contractors can legitimately receive 'bonuses' and **remain outside IR35** if they pay attention to detail, says **Andy Vessey** of **Qdos Consulting**.

The IR35 expert warns that something as simple as the wrong word on a document could tip the balance against a contractor in an **IR35 investigation**. So the first lesson is, never to call a bonus a 'bonus', because that is associated with employment. In fact, that simple word on a contract may be sufficient to spark a full-blown IR35 enquiry, Vessey says.

"So contractors offered a bonus during contract negotiations should ensure that the contract and surrounding 'paperwork' never refers to the payment as a 'bonus'," he explains. "The wording should always be amended to say 'incentive' or 'completion payment'."

### Expert contract reviews are essential

Whilst the contract is only one piece of the jigsaw used by HMRC to determine a contractor's employment status, having it **professionally reviewed for IR35 status** is a vital step in identifying and correcting inappropriately worded clauses, such as those for incentive payments.

"In addition to correcting the terminology, a contract review will also confirm that the incentive payments are specifically related to a project and will only be paid on completion of milestones, or once the project has been successfully completed and the specifications met."

To accept a contract that includes automatic payment of a 'bonus' would place the contractor on dangerous IR35 ground. That's because the implication would be that the contractor is 'owed' the bonus, as an employee might be entitled to one.

### Tests of employment

As Vessey explains, although the bonus issue can be a tipping point in a borderline case, the key tests of employment will take precedence – things like **control, substitution** and **mutuality of obligation**.

"Mutuality of obligation can be an issue with an incentive scheme if the contractor is locked in for a period of time," Vessey says, "because the contractor is therefore under an obligation to perform work in exchange for the incentive payment."

“**Mutuality of obligation can be an issue with an incentive scheme if the contractor is locked in for a period of time**”  
Andy Vessey, Qdos Consulting

And, although mutuality of obligation is considered by some IR35 experts to be of less importance in IR35 cases than substitution and control, Vessey reminds contractors that the courts have increasingly been siding with HMRC's simplistic view of mutuality in status decisions.

### Taking shares as a performance bonus

Vessey warns contractors about the dangers of accepting shares in the client company as part-payment for services, or as part of an incentive payment: "Most share schemes are specifically employee share schemes and designed to award shares or share options to employees."

"So contractors participating in such a scheme are likely to be viewed as effectively working on the same terms as employees. They are clearly becoming integrated into the client's organisation and could be inside IR35 as a result. It is possible to create paperwork that awards the shares in such a way as to circumvent this issue, but this requires expert drafting."

In addition to identifying issues such as inappropriate or unhelpful contractual clauses, seeking a professional contract review can also assist contractors with demonstrating they have taken due care with the tax affairs. This is helpful as failing in this duty of care can result in steep penalties.



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Andy is a Senior Tax professional at Qdos and has a wealth of experience in IR35 and status matters which he guides the firm on.

Qdos Consulting is a leading expert in status and IR35. The company also consults in taxation and employment law and provides low cost business insurance for contractors. [Read Full Profile...](#)

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"Contractors should not be discouraged from working on a performance-related basis, as that's precisely how many businesses operate," says Vessey. "But it's clear this area is an IR35 minefield and so expert contract and contract renewal reviews are essential."

Published: Tuesday, August 10, 2010

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