

Off-Payroll audit guide: How to avoid IR35 compliance risks in the supply chain



For hiring firms and their recruitment suppliers, IR35 status assessments and the tax treatment of contract income aren't the only issues to consider regarding Off-Payroll compliance.

Due to HMRC's inclusion of debt transfer provisions within the [private sector Off-Payroll draft legislation](#), both are now expected to ensure compliance amongst other parties in the supply chain, or else assume tax liability risk.

The provisions have prompted considerable criticism from the industry, with HMRC accused of having introduced them simply to ease its tax collecting task when non-compliant parties prove difficult to locate. Many have highlighted the inequity of an arrangement where a company's tax risk is based on decisions made by other parties that are beyond its control.

Nonetheless, this will undoubtedly place a premium on compliance for end-clients seeking recruitment partners. Now, both must work together to avoid exposing themselves to unnecessary risk.

How do the debt transfer provisions work?

The debt transfer provisions permit the taxman to pursue parties at the top of the supply chain for outstanding tax liabilities caused by non-compliance by another party further down.

Should HMRC fail to recoup the liability from the non-compliant party, it can target the agency at the top of the chain for the sum due, bypassing any other agencies that may exist in between. Finally, the debt will transfer to the client should HMRC be unable to retrieve the money owed from the agency.

There are three prominent instances of non-compliance from an intermediary which could result in tax liability being passed up the supply chain:

1. Where an intermediary has failed to share the client's IR35 [Status Determination Statement \(SDS\)](#) with the party below it in the supply chain
2. Where the hiring firm making the determination has failed to take reasonable care in reaching its determination
3. Where a fee-payer ignores the client's status determination and provides the contractor with a higher rate of take-home pay

HMRC has attempted to justify the move by arguing that agency number one – or the client's recruitment partner - has enough visibility of the labour supply chain to influence compliance. However, industry experts have countered that policing the compliance of other parties, particularly in long and convoluted supply chains, is a far more difficult task than HMRC acknowledges.

Is proliferation of public sector tax avoidance schemes to blame?

The debt transfer provisions are believed to have been created in response to the [prominence of tax avoidance schemes](#) and their uptake following the public sector Off-Payroll reform.

Adoption of the loan-based schemes was reported to have been particularly [prevalent amongst NHS locum nurses](#). Having suffered an effective overnight pay cut of 20% as a result of being deemed within scope of IR35, many were attracted by the more favourable rates of take-home pay on offer from these intermediaries.

These schemes would typically operate under the guise of an umbrella company and many would appear credible to the layman. Often registered to dominions overseas, they can also prove rather tricky for the taxman to track down. Unfortunately, for firms and recruitment partners in the private sector, this is now your problem.

How to operate a compliant supply chain

The solution for clients and their recruitment partners is easy to identify; prevent non-compliant intermediaries from entering the supply chain. Ensuring this may prove more difficult. But the first step towards doing so is firms to risk profile all of the payroll service providers.

A solid indicator of a low-risk service provider is accreditation from a recognised industry body. Accreditations show that a service provider has demonstrated that it is operating in accordance with the highest industry compliance standards.

When vetting a service provider, accreditations from the likes of [Professional Passport](#) - who helped build the Shield Passport Process - are positive indicators. Professional Passport is the only insured accreditation available, meaning firms can make a claim for tax loss of up to £5m if they engage an accredited umbrella company involved in non-compliance. You can access Professional Passport's list of [approved providers here](#).

A medium-risk service provider would demonstrate no evidence of non-compliance, yet at the same time they will have no accreditation, effectively making them 'unknowns'. If you find that you are currently engaging a medium-risk provider, we suggest that you ask contractors to move to a low-risk provider when their contract is next up for renewal.

Dealing with high-risk service providers

Finally, high-risk providers are the subject of intelligence in the market suggesting that they aren't what they claim to be, or that they are undertaking dodgy practices. It goes without saying not to deal with these companies.

If you already have a high-risk provider in your supply chain, you would be advised to insist that all contractors involved move immediately to an accredited supplier. It is important to ensure that the provider isn't considered for any future contracts offered.

If a high-risk supplier was introduced to the supply chain via another intermediary, you may also wish to consider whether to continue relationships with this intermediary, as their approach to compliance could pose a risk going forward.

With the introduction of the debt transfer provisions, service providers will be expected to secure accreditation as firms exercise more caution over who they engage. More than ever, this means that a lack of endorsement from an industry body should serve as a positive indicator to steer clear.

Client and recruiter cooperation key to Off-Payroll compliance

The contractor supply chain is a potential minefield. But it's also just one of many issues that hiring organisations and recruiters will need to navigate with caution – and its best that they do so together.

With April 2020 just months away, firms and their recruitment partners should now be putting into place plans to overcome the multiple hurdles to Off-Payroll compliance. For those who have yet to act, the [Shield Passport Process \(SPP\)](#) provides a structured approach to Off-Payroll compliance in a comprehensive compliance workshop.

Hosted by compliance experts [IR35 Shield](#) and [Professional Passport](#), this workshop is available for agencies to book before inviting their clients to attend, to ensure that compliance practices are aligned throughout the supply chain and that Off-Payroll is tackled together. If you would like an SPP workshop to be held at your organisation, then [please get in touch](#).

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