

Off-Payroll: Lords report urges overhaul of flawed and exploitative tax framework



The House of Lords Finance Bill Sub-Committee has implored HMRC and Government to scrap the fundamentally flawed Off-Payroll rules in favour of a fairer and more holistic approach in a report that delivers a scathing review of the now postponed proposals.

Published this morning, '[Off-payroll working: treating people fairly](#)' describes the Off-Payroll rules as the result of a Government that considers the issue of taxation of the self-employed too narrowly, and one that has failed to consider fully the many concerns raised by stakeholders, adding:

'It has severely underestimated the costs to business of implementing the changes... And it did not analyse sufficiently the unintended behavioural consequences of the proposed reforms or their wider potential impact on the labour market, and on the gig economy in particular.'

Government urged to rethink framework for tackling tax avoidance

With HMRC's failings and the resulting burden and injustice imposed upon UK business and contingent workers highlighted throughout, the report urges Government to take the opportunity afforded by the [Off-Payroll postponement](#) to rethink its framework for tackling tax avoidance. The report notes numerous ways in which Government can use this time effectively:

- Commissioning an independent review of the impact of the legislation in the public sector
- Undertaking an analysis of how a private sector rollout would affect the labour market
- Tackling the ongoing deficiencies with HMRC's Check Employment Status for Tax (CEST) tool and the status determination process
- Revisiting Government's highly questionable assessment of Off-Payroll's cost to business

The report adds: *'The extra time should also be used to consider alternatives to the off-payroll rules that are fairer and less risky, and which do not treat individuals as employees for tax purposes when they do not enjoy the rights of employees.'*

'Government is privatising tax compliance' through Off-Payroll

Many recommendations made within the report are borne out of an ill-considered and unheeding approach by Government. In making hiring firms and agencies responsible for enforcing compliance, the report notes: *'Effectively, the Government is privatising tax compliance.'*

The decision to pass the compliance burden for legislation that HMRC has admittedly been unable to effectively enforce for 20 years seems odd. Given the complexity of the underlying employment status test, the Lords also deem the legislation an unfair burden to impose upon clients and agencies, and one which isn't effectively mitigated by the support offered by Government.

This includes CEST, which the Lords argue offers *'limited assistance to businesses, which need to spend considerable time and money clarifying the status of their contractors as a result'*. As a by-product of this, the report argues that HMRC's estimate that the Off-Payroll rules will result in a one-off administrative cost to business of £14.4m has been *'severely underestimated'*, adding:

'Given that the off-payroll rules do not change the substance of the IR35 status determination requirement, we conclude that HMRC is imposing a heavy burden on businesses by requiring them to determine status using a complex, fact-specific test. We agree with our witnesses that the support offered by HMRC in determining status - and the CEST tool in particular - falls well short of what is required.'

Lords warn Government against repeating Off-Payroll mistakes

As much as anything else, the report takes aim at the application of the proposals, highlighting that HMRC and Government appear intent on repeating the same mistakes made during the public sector rollout.

Whereas the HMRC-commissioned study into the public sector impact portrayed the reform as a success, the Lords acknowledge that its witnesses painted a less rosy picture, citing issues amongst end-clients such as difficulty applying the legislation, recruitment challenges, and significantly heightened overhead costs.

The report concludes that concerns regarding HMRC challenges to status determinations have caused many clients to undertake blanket assessments, leading to the *'mis-categorisation of contractors as within the off-payroll rules'*.

Despite a wealth of evidence, this is an issue that HMRC has consistently denied, and one that wasn't addressed in its study, which came in for heavy criticism, ultimately prompting the Lords to conclude:

'We are not convinced that the Government has learnt lessons from the application of IR35 in the public sector. If the Government continues with its plan to introduce the off-payroll reforms in April 2021, we recommend that the Government undertake an independent review of the implementation of the off-payroll rules in the public sector and an analysis of the impact of those rules on the labour market.'

Action required to address Off-Payroll's inherent injustice

The threat of tax risk and substantial compliance costs for end-clients are a recipe for non-compliance and risk-averse behaviour, of which contractors ultimately bear the brunt.

The report condemns HMRC's failure to address non-compliant blanket assessments by clients. However, it also acknowledges that the legislation itself enables the exploitation of self-employed, highlighting the creation of a new class of workers that are deemed employed for tax purposes but without the rights that employees can expect.

Adopting the term coined by the [Stop the Off-Payroll Tax](#) campaign, the report argues: *'It is unfair that contractors within the rules are treated as employees for tax purposes but do not qualify for employment rights, thus creating a class of "zero-rights employees". The Government is replacing one unfairness with another.'*

During the inquiry, many witnesses advocated the alignment of employment status for tax and employment rights purposes to counter this inherent unfairness, alluding to the Government-commissioned Taylor review of modern working practices.

With Government yet to act on its 16-month-old promise to legislate to improve the clarity of the employment status tests, and to develop detailed proposals on how to align the employment and tax frameworks, the report offers a timely reminder:

'It is concerning that the Government has pressed ahead with the off-payroll working rules at a time when the Taylor Review, which it commissioned, recommended a more holistic solution than these rules can offer.'

Don't let Off-Payroll compound COVID damage, urge Lords

A failure by Government to address this brazen imbalance threatens damage to the economy that the report notes the UK can scarcely afford given the current climate.

Offshoring of work and the movement of contractors themselves overseas were both identified as likely results of the Off-Payroll rules, posing problems for firms dealing with heightened costs caused by Off-Payroll compliance and increased contract rates from affected, in-demand

contingent workers.

All of these factors will compound existing damage to the labour market resulting from the COVID-19 pandemic, described by the Lords as *'the greatest shock that the UK's economy has experienced since the Second World War'*.

The report implores Government to thoroughly consider the damage that the Off-Payroll rules threaten the labour market and the broader economy, before issuing a stark warning against the legislation's possible inclusion in the Finance Bill:

'Even if the economy were to begin to recover in the next 12 months, the severity of the economic impact of COVID-19 is so great that it would be completely wrong for the Government to impose a new burden on businesses in the form of the existing off-payroll proposals. Business is likely to need considerably longer than a year to recover from the disruption caused by the COVID-19 pandemic.'

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