

## Structural problems remain with IR35, says Public Accounts Committee

House of Commons



Committee of Public Accounts

# Lessons from implementing IR35 reforms

A report published today by the Public Accounts Committee says “widespread non-compliance” with IR35 tax reforms in central government departments is “not acceptable” after HMRC “rushed implementation of the reforms, provided poor guidance, and public bodies struggled with its tool to assess status.”

The Committee also says “government bodies should be best placed to understand the rules”, which now also affect the private and third sectors, but in 2020-21 it became clear that many central government departments had struggled to comply with the reforms and owed or expected to owe HM Revenue & Customs (HMRC) £263 million in back-taxes.

Dame Meg Hillier MP, Chair of the Public Accounts Committee, said: “While workers in the gig economy have challenged their work and tax status in the courts, there is no recourse for workers deemed subject to IR35 tax rules despite the confusion and non-compliance that persist even in central government itself.

Dave Chaplin, CEO of IR35 Shield, who provided evidence for the review, said: “The Public Accounts Committee is spot on with its observations and recommendations, demonstrating that it was ill-conceived to extend the legislation to the private sector from April 2021.”

### Blanket bans & structural problems

The Public Accounts Committee found that many public bodies reported that the reforms caused problems for them in recruiting contractors. Some contractors report that, to avoid perceived risks of failing to comply, their clients are changing hiring practices - such as no longer engaging workers through personal service companies.

The report criticised the design of the legislation, acknowledging that while the reforms appear to be bringing in more tax revenue, it is “clear that structural problems remain with the way IR35 operates”, in particular, drawing attention to three key areas:

- Hiring organisations unable to properly assess a worker’s status
- No appeals process means it’s too difficult for workers to challenge incorrect determinations
- A lack of good data and legislative provisions has seen HMRC taxing the same income twice: a particular concern in the public sector where government can end up subsidising private-sector contractors for all of their tax

The Committee were also concerned that HMRC has “done little to understand the wider impact of the reforms on workers or labour markets”

or particular sectors and “underestimated the additional costs of implementing the reforms to hiring organisations”. It claims to be unconvinced by such evidence but has not conducted its own research, making it “difficult to disaggregate the direct impact of the reforms from the effects of EU Exit and the COVID-19 pandemic”.

## Key observations and findings

The PAC report main five damning observations:

- High levels of non-compliance in central government reflect poor implementation by HMRC and other government bodies
- Concerns that it is too difficult for workers to challenge incorrect status determinations.
- HMRC is not doing enough to understand the impact of the reforms on workers and labour markets
- PAC are not confident that HMRC works proactively to establish whether any sectors have been affected disproportionately by the reforms and why
- HMRC has not made a robust assessment of the additional costs of implementing the reforms

Chaplin says: “Firms are struggling to get status determinations right, and CEST is proving to be dangerous for firms – a hindrance, not a help. The disproportionate tax risk and double taxation issue has still not been resolved, and neither is there any independent appeals process for contractors who are not being treated fairly.”

## Recommendations by the Committee

The Committee made considerable recommendations, including:

“HMRC should develop robust estimates of non-compliance for the public sector as a whole and use this to identify areas where it can reduce the inherent challenge of complying with the reforms, for example by improving its guidance and tools. It should adopt a similar approach for the private sector as the reforms bed.

“HMRC should ensure there is a fast and independent process for contractors to resolve disputes over status determinations. As part of this, it should assess the extent to which workers are using existing appeals routes, and how well they are working.

“HMRC should conduct and publish specific research into the impacts of the IR35 reforms on contractors and labour markets, to check it is being applied as intended and not adversely affecting employment opportunities.

“HMRC should proactively identify and work with sectors that have been particularly affected to understand the challenges, establish how to address them and make it easier to comply.

“In light of actual experience, HMRC should produce and present to Parliament a cost-benefit analysis of the reforms that reflects the actual costs of compliance to HMRC itself, hiring organisations, workers, and others in the supply chain.

“HMRC should review how the system is working and whether it can be made more efficient and effective. In particular, it should develop solutions to address problems with how the IR35 rules work in practice, including ensuring that HMRC has the data it needs to accurately reflect each worker’s tax position in cases of non-compliance; and HMRC does not end up taxing the same income twice, or unwittingly contributing to workers not paying their fair share in tax”

## The future of off-payroll

HMRC have been tasked by the Public Accounts Committee to conduct more detailed research and to report back to them in six months time.

PAC are clearly unimpressed with the handling of the off-payroll implementation. Hillier said: “After years of fiddling with these reforms and with central government spending hundreds of millions of pounds to cover tax for individuals wrongly assessed as self-employed, the fundamental problems underlying UK taxation of work remain. It is now up to HMRC to demonstrate that the system can work fairly in the real world; to prove that it is correctly claiming revenues under the system and that the additional revenues raised are worth the costs and unintended consequences in the labour market.”

Chaplin says: “Over the last 20+ years, there has been considerable misjudged and damaging legislation heaped on the contracting sector and the sensible option would be to go back to the drawing board and design a fair tax system that works fairly for everybody.”

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