

EMBRACING IR35



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You may have heard of 'IR35'...usually spoken of in hushed tones and panic-stricken voices. But IR35 doesn't need to be feared and it's certainly not a given that you should avoid IR35 contracts. Equipped with the right knowledge and advice, it's straightforward to handle contracts both inside and outside of IR35.

So, what do you need to know?



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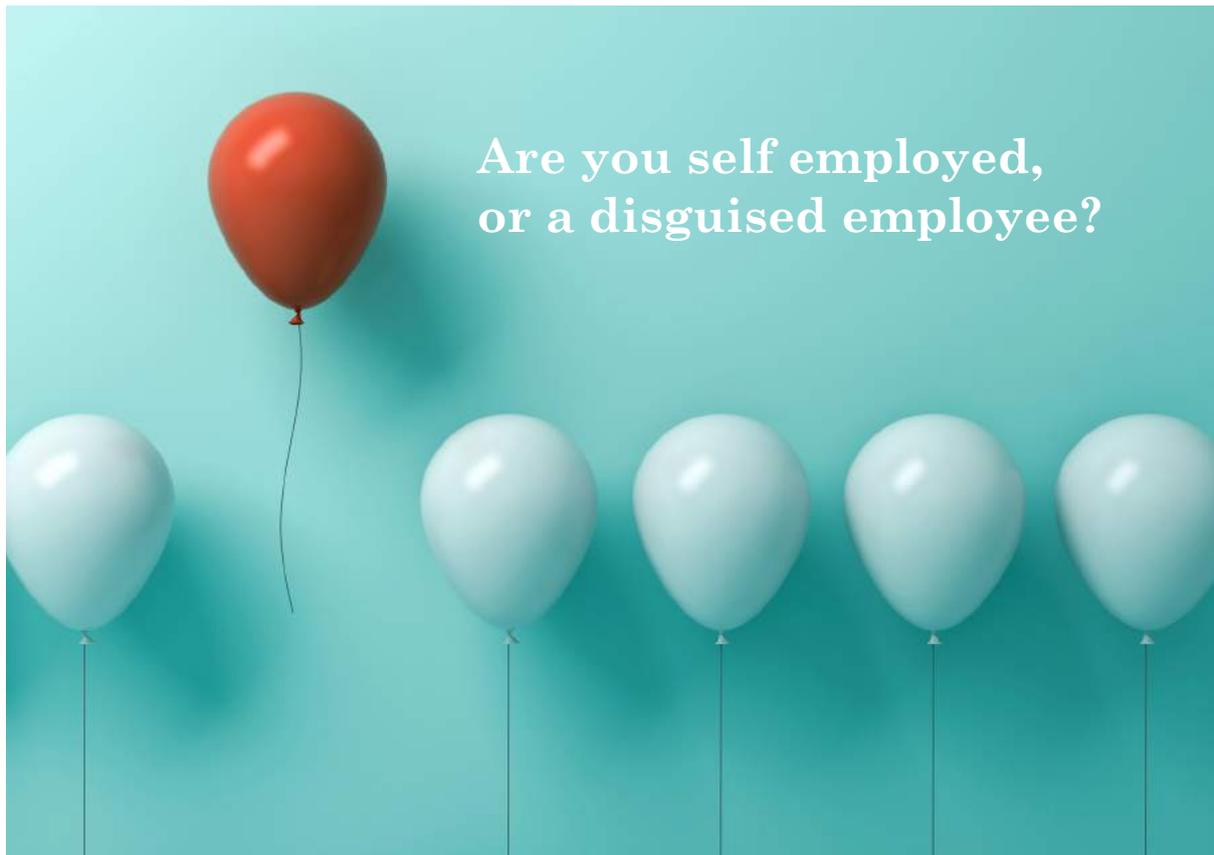
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WHAT IS IR35?

IR35 is the tax legislation which determines whether an individual is truly self employed, or is in fact working as a 'disguised employee' in permanent employment in order to take advantage of certain tax relief schemes which permanent employees cannot. If you are working 'inside' IR35 you are 'deemed employed' and will therefore be taxed as such.

IR35 applies to all business sectors and specialisms and your status can vary from contract to contract, depending on the nature of the work and details of the contract.

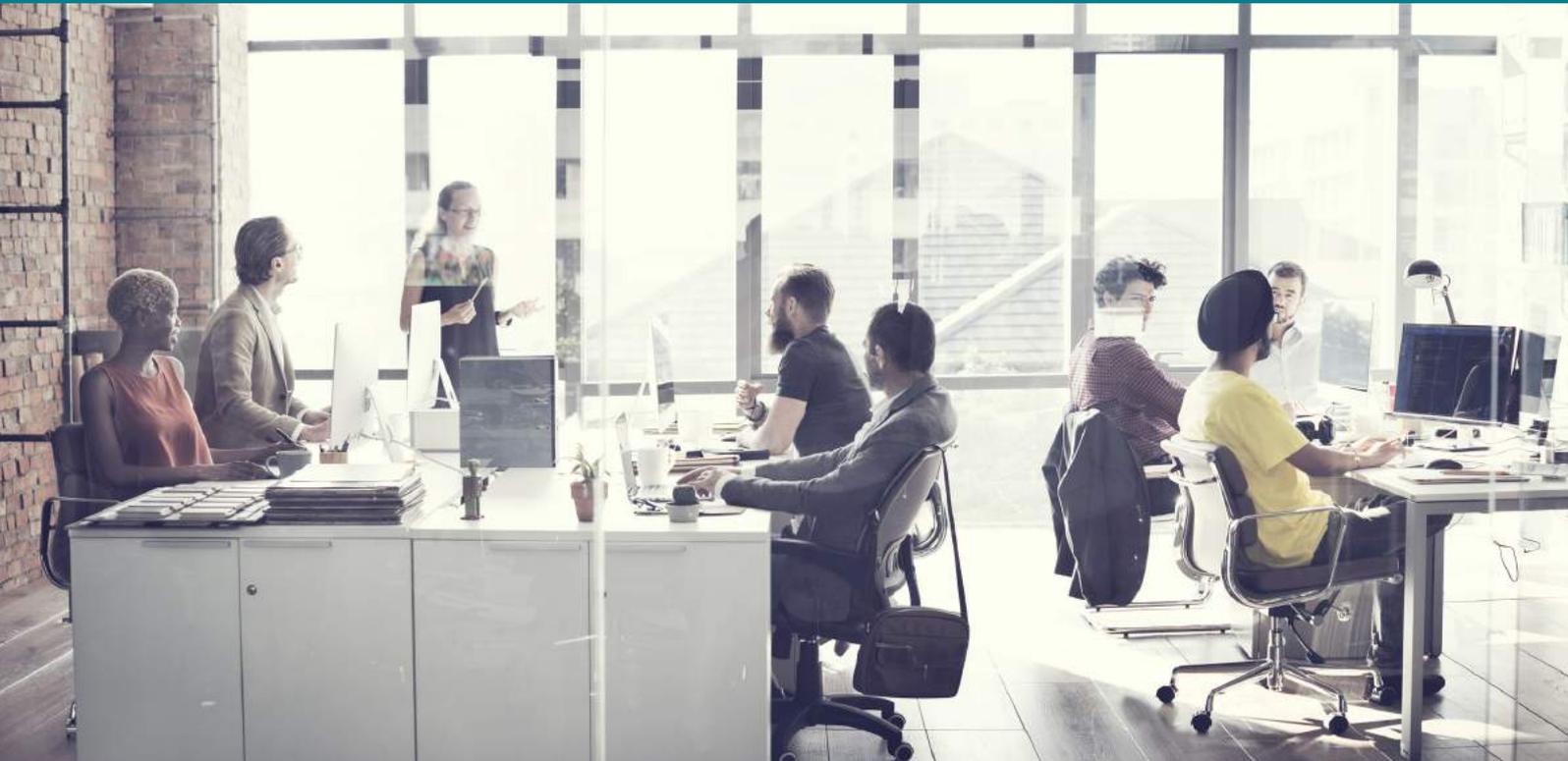


WHY IS IR35 IMPORTANT TO CONTRACTORS?

Your IR35 status determines your tax position with HMRC and as such can affect your take-home pay levels. Working as a contractor through a Limited Company 'outside' of IR35, you are able to split your income between a low salary and dividends in order to keep your Tax and National Insurance contributions to a minimum. You thereby achieve higher take-home pay than a full-time employee earning the same base pay. As a 'deemed employee' working on a contract 'inside' IR35, you are expected to pay the same amount of Tax and National Insurance contributions as a full-time employee, whether that's via your Limited Company, through your client's payroll, or via an Umbrella Company. Your take-home pay would therefore be lower than if your contract was 'outside' IR35.

Most contractors are at pains to avoid working 'inside' IR35 for these reasons.

HOW IS YOUR IR35 POSITION DETERMINED?



HMRC have a set of rules to determine if you are working inside or outside of the IR35 legislation. The rules relate to the way you work as well as the actual contract details, so you will need to consider IR35 for every new contract you undertake. The rules aim to identify whether you are actually working and behaving as you would if you were permanently employed doing the same job.

The basic rules are easy to understand, yet applying those rules and determining employment status can be far more complex. A specialist contractor accountant such as Intouch will be able to advise on a case by case basis, but the basic rules are based around the following areas:

1 Personal service/substitution

If your company has the right to provide someone other than yourself to deliver the services that it is contracted to provide then this would strongly indicate that you are operating outside of IR35.

2 Control

The level of control that your client has a right to exercise over your working practices impacts on whether you will be inside or outside of IR35. If you are in charge of when and where, but most importantly how you work, you are less likely to fall within IR35.

3 Mutuality of obligation

As an employee you are obliged to go to work at certain times and days of the week, and there is an obligation to pay you, even if the work dries up. If this describes you, then you could be 'deemed employed'. A higher level of obligation implies that IR35 might apply.

WHO DECIDES WHETHER YOUR CONTRACT IS WITHIN IR35?

It's all very well having these rules and tests, but whose responsibility is it to apply them on a day to day basis in order to determine the IR35 status of your contracts? Well, that depends...

IR35 in the Private Sector

If your contract is with a Private Sector client then it is your responsibility to determine your status under IR35 and you bear the tax risk if you get it wrong.

If you have determined that your contract is outside of IR35 but the authorities decide that you are 'deemed employed', there will be more tax to pay, and potentially other penalties as well. The extra tax can be charged retrospectively, potentially for as long as the engagement took place, even if that means several years.

This is why it is useful for you to take professional advice to determine your status. Working with a specialist contractor accountant offering unlimited IR35 reviews included in their fee really pays off.

The scary stories of contractors closing their companies because of IR35 usually occur where the contractor has ignored IR35 for some time and is faced with a large bill from HMRC. All of this can be avoided by having an IR35 review early in the assignment and continuing to have regular reviews to ensure things have not changed.

IR35 In the Public Sector

When working in the Public Sector, the end client is responsible for assessing your IR35 status, and bears the tax risk if they get it wrong. Some Public Sector bodies initially imposed blanket bans on Limited Company contractors, insisting on Umbrellas for everyone. Thankfully, the majority of these have since been relaxed, with IR35 decisions now being carried out on a case-by-case basis (as mandated by HMRC). However, decisions on IR35 are still more likely to be risk averse and some contractors remain wary of Public Sector assignments for this reason.

Just remember that although some contractors remain wary of Public Sector assignments, they don't mean you'll automatically be working inside IR35.

SHOULD I REFUSE IR35 CONTRACTS?

There's no getting away from the fact that contracts inside IR35 will impact on your take-home pay compared with one on the same day rate that is outside. But there's more to life than money, right? So if the project looks great, the timing works for you, the experience is going to look cracking on your CV, and there's no negotiating over terms or the IR35 status, then ask yourself if the money really is a deal-breaker.

Before turning down a contract based purely on IR35 status, take the time to consider what the project means for you and whether the other benefits make it worth taking.

IF MY CONTRACT IS INSIDE IR35, SHOULD I USE AN UMBRELLA COMPANY?

IR35 is really nothing more than a different basis used to calculate tax when certain conditions apply. Unquestionably the tax liabilities under IR35 are higher than those outside IR35; but they are also less than the tax liabilities incurred as an Umbrella Company.

So if you are 'deemed employed', and therefore inside IR35, you will still be better off trading through a Limited Company than an Umbrella (and it's worth pushing back with any agency or client trying to push you down the Umbrella route for their own convenience). You will pay the Tax and National Insurance contributions required based on your 'deemed salary'; your accountant can help you with this.

And there are other benefits to sticking with Limited too:



Stay Limited

- Claim more expenses than an Umbrella**
- Benefit from the Flat Rate VAT Scheme**
- Claim the cost of computers or capital equipment**

WHAT IS MY TAKE HOME PAY INSIDE IR35?

If you are involved in a contract that falls inside of IR35 then a calculation is made each year to determine the 'deemed salary'. Your contractor accountant can do this for you. An IR35 deemed salary is simply a calculation of the Income Tax and National Insurance due. You do not have to actually pay yourself the deemed salary, but you do have to pay the calculated PAYE and National Insurance contributions to HMRC.

If a Public Sector body has confirmed that you are inside IR35, then the fee payer (usually the agency) will deduct the NI and tax, and pay the Limited Company the net income after tax. This can be taken straight out of the company, with no additional tax implications.

IR35 deemed salary calculations follow the tax year (6th April to 5th April) rather than your company year. Contractors with contracts within IR35 may choose to pay a small salary throughout the year or request their contractor accountant to estimate what their deemed salary will be and pay a monthly salary in line with that. The benefit is that deemed taxes due will be spread evenly throughout the year, and you will have a smaller balancing payment each April.

How do I stay IR35 safe?

An IR35 investigation by the HMRC can be stressful, time-consuming and costly, so where the responsibility is on you to make the assessment, it's important to get it right.

However, we'll likely soon see the Public Sector application applied to the Private Sector, taking the decision on IR35 out of the contractor's hands. The main issue with this will remain a lack of understanding and experience of those making the assessments.

A specialist contractor accountant such as Intouch can review and comment on your contracts, advise you on all aspects of IR35 and equip you with the knowledge you'll need to successfully discuss and negotiate with your client or agent.

HOW INTOUCH CAN HELP

Looking for a specialist Contractor Accountant to give you IR35 advice? At Intouch, our monthly service includes unlimited IR35 advice, risk assessments and fee protection. You'll have a direct line to your own Personal Accountant who will help you understand your options, make the right decisions for your business and stay compliant. Get in touch today for more information.



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