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Off-payroll working rules from April 2020

Response by the Chartered Institute of Taxation

1 Introduction

1.1 The Chartered Institute of Taxation (CIOT) sets out below its response to the consultation on the implementation of the off-payroll working rules from April 2020.

1.2 The consultation asks for comments on how best to implement the extension of the off-payroll working rules from the public sector to the private sector.

1.3 As an educational charity, our primary purpose is to promote education in taxation. One of the key aims of the CIOT is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

1.4 Our stated objectives for the tax system include:

- A legislative process which translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
- Responsive and competent tax administration, with a minimum of bureaucracy.

2 Executive summary

2.1 The consultation document requests responses in respect of the implementation of reforms to the off-payroll rules from April 2020, rather than whether or not reforming the off-payroll rules and extending them to the

private sector is the right approach. We would, however, refer you to our response[1] of 7 August 2018 in which we set out a potentially better option. We remain of the view that this alternative approach would be more effective in tackling the estimated cost of non-compliance of £1.2bn a year by 2022/23. Our comments on reforming the off-payroll rules and extending them to the private sector should therefore be read in light of our view that the government's objectives can be met in a more effective way.

2.2 We would also make the broader point that, from a tax perspective, one of the reasons that business favours engaging via PSCs is that any NIC falls on the PSC not the business. Consequently, we think that in implementing '*The Good Work Plan*'[2] (which we refer to at 2.7 below) the IR35 issue, the taxation of the employed v self-employed and labour law should all be viewed through the same lens and considered together. This should be viewed as an opportunity to build a roadmap which provides clarity and consistency and also levels the playing field in terms of the amount of tax paid by, and benefits and rights afforded to, workers in similar situations.

2.3 We think a key aspect to a successful implementation of new off-payroll working rules will be how businesses, agencies, PSC/workers (and indeed HMRC) can confidently be assured that decisions on status can be relied upon. For most businesses this is likely to mean that they need to be able to rely on the output from HMRC's Check Employment Status for Tax (CEST) tool.

2.4 The complexity of IR35 has been noted in recent First Tier Tribunal decisions such as *Albatel*, *MDCM*, *Jensal Software* and *Atholl House Productions*[3]. These cases are examples of where HMRC's views as to employment status have not been upheld and highlight an important issue with CEST, which is that if the output from the tool does not reflect the decisions made by the courts (and, in particular, if CEST returns 'false positives' in such cases), this will not instil confidence to those relying on CEST to help with status decisions. And, ultimately, this will increase the number of cases where status is 'in dispute'.

2.5 This means that modifying and developing CEST so that it is better able to address a wider breadth of scenarios will be an important precursor to the implementation of new off-payroll working rules in April 2020. It also means that changes to CEST will need time to bed down before decisions have to be made as to the status of PSC/end client contracts.

2.6 In our view, an improved CEST tool needs to be available by October 2019 at the latest. HMRC guidance should also be available in good time (and, ideally, published at least in draft alongside the draft Finance Bill legislation).

2.7 Also, bearing in mind that the government announced in December 2018 that it intended to '*legislate to improve the clarity of the employment status tests*', we think that it will be important that the government indicate when these changes will be introduced as this will impact how (ie on what basis) IR35 status decisions are made and could materially affect the numbers caught by the IR35 rules. Indeed, depending on what other changes are made as a result of implementing *'The Good Work Plan'*, this could impact on whether the off-payroll working rules are needed at all, at least in their current (and proposed) form.

2.8 Another aspect that needs to be clarified is 'who is the end client?'. In particular, when has a business fully contracted-out a *service* to another business, as opposed being provided with *labour*, such that the off-payroll

[1] https://www.tax.org.uk/policy-technical/submissions/payroll-working-private-sector-ciot-comments.
[2] https://www.gov.uk/government/publications/good-work-plan.
[3] *Albatel Ltd* v *HMRC*, FTT [2019] UKFTT 195 (TC), TC07045, *MDCM Ltd* v *HMRC*, FTT [2018] UKFTT 147 (TC), TC06400, *Jensal Software Ltd* v *Revenue and Customs Commissioners,* FTT [2018] UKFTT 271 (TC) and *Atholl House Productions Ltd* v *HMRC*, FTT [2019] UKFTT 242 (TC), TC07088.

rules do not apply to the first business? We think it would be helpful for HMRC to publish guidance, with illustrative examples, to help businesses understand who the 'end client' is in these situations. This will build on the existing guidance for the public sector[4].

2.9 We welcome the government's decision to exclude small private sector entities from the off-payroll working rules, although we would suggest the government consider extending the exclusion to small public sector entities too, to ensure a level-playing field.

2.10 We agree with taking a simplified approach for bringing non-corporate entities in to the scope of the new off-payroll working rules and, on balance, we suggest that the preferred approach should be the second option proposed (ie that the new off-payroll working rules will only apply where an entity has both 50 or more employees and turnover in excess of £10.2 million).

2.11 This said, we think the government should consider how the number of employees test should be applied as a test based on a simple count of the total number of employees (even if averaged across the year) may discriminate against businesses with predominately part-time employees. This could, indeed, drive behaviour in some small businesses in order that they retain their 'small' status which would be unfortunate.

2.12 We also think that the government should reflect on when businesses should carry out the test for 'small' and, where a business ceases to be/becomes small, when the business starts/ceases to apply the off-payroll working rules. In particular, if the test is carried out at the accounting period end this may leave some businesses (eg with 31 March year ends) with only a few days until the end of the tax year to assess their size and, if appropriate, make status determinations to determine whether PAYE and NICs deductions are to commence. Our preferred approach, in order to provide the time required to assess size and, if appropriate, to make status determinations and notify relevant parties would be to base the timing of the test on the date by which the tax return in relation to an accounting period end/tax year is statutorily due to be filed and, where appropriate, for the off-payroll rules to apply/cease to apply from the following 6 April.

2.13 While we agree that a requirement for end clients to directly provide the PSC/worker with the status determination would make clear the end client's view, we think, on balance, it may be preferable if the end client is simply required to notify the decision to the party with whom the client contracts (and for there to be a requirement for that party to pass on the information until it reaches the fee-payer and PSC/worker). In particular, we note that where there are longer supply chains/IR35 does not bite the end client may not necessarily have direct contact with the fee-payer and/or the PSC/worker, so a requirement to pass the determination direct to the feepayer and PSC/worker may not be practical. That said, we think that doing so where feasible should be encouraged as best practice. In any event to facilitate the efficient flow of information we would suggest that HMRC works with industry representatives to produce, in guidance, a standard cascade template that could be used to pass information down the supply chain. This could include the reasons for reaching their status determination.

2.14 We agree with the proposal that where PAYE and NICs has not been correctly accounted for the liability should initially rest with the party that has failed to fulfil its obligations. We are, however, very concerned by the proposal to transfer liability back to the first agency in the supply chain – and ultimately, where HMRC is unable to recover the liability from the first agency, the end client – where HMRC is unable to collect an outstanding liability from the defaulting party.

2.15 Where the first agency/end client has used all reasonable endeavours to ensure the integrity of the supply chain but, for some reason, HMRC is unable to recover the PAYE and NICs it does not appear to us to be fair

[4] https://www.gov.uk/guidance/off-payroll-working-in-the-public-sector-reform-of-intermediaries-legislation#contracted-out-services.

and proportionate for the liability to be transferred to the first agency/end client. Indeed if the government were to adopt this approach it would create an uneven playing field relative to the provision of agency workers further to section 44, ITEPA 2003 (where liability is only transferred where a fraudulent document is provided). At the very least, a power to transfer liability should be tempered with a defence of reasonable care.

2.16 Also, while there is a need for due process to resolve a status disagreement we do not think that a statutory process is the answer. The costs and burdens associated with a statutory process are, in our view, likely to be significant and outweigh any benefits a formal process might have over and above the natural process of having to take reasonable care and reviewing determinations in the light of new facts, or where there has been a mistake made in the analysis. The public sector experience of the off-payroll working rules has generally seen a dialogue taking place between the parties and we think this the best approach. We suggest that this is supported by HMRC guidance (eg on best practice, how to fact-find and determine status/use CEST, etc), rather than statutory rules.

2.17 Our full response to the questions raised in the consultation document are set out below.

3 Defining the scope of the reform

3.1 ***Question 1 – Do you agree with taking a simplified approach for bringing non-corporate entities in to scope of the reform? If so which of the two simplified options would be preferable? If not, are there alternative tests for non-corporates that the government should consider? Could either of the two simplified approaches bring entities into scope, which should otherwise be excluded from the reform? Is it likely to apply consistently to the full range of entities and structures operating in the private sector? Please explain your answer.***

3.2 We understand that the government has decided that non-public sector small entities are to be excluded from operating the off-payroll rules and that the government intends to use the existing statutory definition within the Companies Act to determine whether or not a corporate entity is 'small', ie:

'*The qualifying conditions are met by a company in a year in which it satisfies two or more of the following requirements*-

1. *Annual Turnover – Not more than £10.2 million*
2. *Balance sheet total – Not more than £5.1 million*
3. *Number of employees – Not more than 50*.'

We note, and welcome, that the government recognises that the balance sheet test in this definition may not be suitable for non-corporate entities and therefore the government proposes two options for non-corporate entities which consider only the turnover test and the number of employees test. These two options are that the off-payroll working rules will only apply either when:

1. An entity has either 50 or more employees or turnover in excess of £10.2 million, or
2. An entity has both 50 or more employees and turnover in excess of £10.2 million.

3.3 We agree that taking a simplified approach to what constitutes a small entity for non-corporate entities is essential and will release such entities from the considerable burden of operating the off-payroll working rules. Omitting the balance sheet test is helpful, particularly as this may be more open to interpretation for non-corporates.

3.4 The question of which of the two proposed tests for non-corporate entities to apply the new rules to would seem to involve a trade-off between administrative burden and tax yield. In particular, the second option would result in fewer entities being brought into the off-payroll rules but the government will need to assess whether this approach is still consistent with the underlying policy objective of ensuring much greater compliance with the IR35 rules and protecting the associated tax yield.

3.5 In our view, and from an administrative burden on business point of view, the second option would be preferable. This is because it will mean that fewer non-corporate entities will be impacted. Also, the administrative requirements of implementing the off-payroll working rules should not be underestimated. It will require some quite detailed administration and entities with fewer than 50 employees may not have the resources to undertake this. Therefore, while 50 employees may be a good proxy for having an established payroll/HR department – so should be part of the test – the off-payroll rules should not apply to companies that are nevertheless 'small' notwithstanding that they may have 50 or more employees. Hence, we think there is a need for the test to be an 'and' test.

3.6 This said, we do have a number of concerns with the proposed 'qualifying as small' tests for both corporates and non-corporates.

3.7 Firstly, in regard to the number of employees test, we understand that the test applies to the average number of employees. What is not clear is whether this averaging is applied to a tax year or the period of account for the entity concerned. Also, while averaging may assist employers with seasonal fluctuations of employees, we understand that the test makes no distinction between full- and part-time employees, job-shares, etc. (ie there is no 'full-time equivalent' adjustment to counting the number of employees). This may therefore discourage some small businesses from engaging part-time employees. It may also mean that some businesses will prefer to engage workers via their Personal Service Companies (PSCs) rather than as employees in order to remain 'small'. We think the method of application of the number of employees test should be reviewed by government to ensure that it does not have any unintended consequences.

3.8 Secondly, we have concerns for entities whose turnover fluctuates year-on-year and who are near the cusp for exceeding/falling within the small entity threshold. We note that the consultation document proposes that where, for example, the annual turnover for an accounting period end exceeds the turnover test threshold and, as a result, the entity ceases to be small, the entity must commence applying the off-payroll rules from the following 6 April.

3.9 We are concerned that for many entities, it will be impractical to determine the annual turnover in sufficient time to decide whether the entity must apply the off-payroll rules (or cease to apply them) from the following 6 April. For example, where the accounting period end is 31 March (as is often the case for non-corporate entities in particular but also for many corporate entities too) this would leave only 5 days to the start of the following tax year in which to determine the annual turnover and, if appropriate, to assess whether any off-payroll workers are within the off-payroll rules.

3.10 We think it would be better for the tests to be applied at the time when an entity must file its tax return to HMRC (and based on annual turnover for the accounting period/tax year to which that return relates and the number of employees for the last tax year) and, where appropriate, for that entity to then start to apply/cease to apply (as appropriate) the off-payroll working rules from the following 6 April. We would also suggest that where an entity can show that, for example, exceeding the annual turnover test was a one-off and the entity will qualify as 'small' in the following accounting period (and has been small in previous accounting periods) then the entity should be able to apply to HMRC to be excepted from applying the off-payroll rules.

3.11 Guidance will also be needed where an entity is acquired/subsumed into a larger group, and how the tests are to be applied to UK branches of overseas entities.

3.12 Lastly, the government needs to consider how workers (and their PSCs) are to know whether or not an end client is 'small'. Will there be a statutory duty for small entities to notify workers and intermediaries/agencies that they are a small entity and therefore that the onus on assessing whether or not the IR35 rules apply rests with the PSC/worker? We certainly think it is important that all parties are clear on their responsibilities. Agencies and intermediaries will also need to know whether or not the end client is responsible for determining a worker's status and so that they are clear on whether or not they need to cascade the decision down the supply chain and, ultimately, whether or not the fee-payer needs to deduct PAYE and NICs.

4 Information requirements

4.1 ***Question 2 – Would a requirement for clients to provide a status determination directly to workers they engage, as well as the party they contract with, give off-payroll workers sufficient certainty over their tax position and their obligations under the off-payroll reform? Please explain your answer.***

4.2 We agree that information should be shared appropriately and promptly. In this regard, a requirement to provide the PSC/worker with the status determination would certainly make clear the end client's view and prima facie makes sense. However, we refer to this further at 4.3 below. We note that the government also envisages legislating to require the end client to provide the PSC/worker with the reasons for their determination. While we agree this should be useful there needs to be a balance struck in terms of the amount of detail required. In particular, tribunal decisions on employment status can run to many pages and a requirement to provide that kind of detail would clearly not be appropriate. The output from HMRC's Check Employment status for Tax (CEST) tool or an equivalent tool, or perhaps a succinct list of questions and yes/no answers on issues such as control, personal service, tools and equipment, financial risk, whether in business on own account, mutuality of obligation (MOO) etc. would be more reasonable.

4.3 We do have a concern that, in some circumstances (and particularly where there is a longer supply chain), the end client may not have direct engagement/communication with the PSC/worker, albeit in such cases IR35 would not generally bite. In this situation it would clearly be more difficult for the end client to notify their status decision direct to the PSC/worker. Therefore, given that it is essential there is always an efficient and timely flow of information down the supply chain we think that a requirement for the end client to provide the determination etc direct to the worker could sometimes be problematic. Accordingly, weighing up the situation in the round it may be preferable only to require the status determination to be supplied to the party with whom the end client contracts, albeit the end client could also supply it to the PSC/worker in 'supply chain' situations if it wished to do so and this could be encouraged as best practice where feasible. Please also see our comments at 4.11 and 4.16 below in answer to Questions 5 and 6.

4.4 ***Question 3 – Would a requirement on parties in the labour chain to pass on the client's determination (and reasons where provided) until it reaches the fee-payer give the fee-payer sufficient certainty over its tax position and its obligations under the off-payroll reform? Please explain your answer.***

4.5 In principle, yes, and provided that appropriate sanctions apply in cases of non-compliance so that instances of non-compliance are minimised.

4.6 As noted above, we think that it is essential that information flows promptly down the supply chain from the end client through any agencies and intermediaries in the chain to the fee-payer and from the fee-payer to

the PSC/worker. In this way both the fee-payer and the worker have certainty over the fee-payer's obligations under the off-payroll rules.

4.7 We would suggest that HMRC work with industry representatives to produce a standard cascade template that could be used to pass information down the chain. This would mean that everyone from end client to agency to PSC/worker has an identical view of the status determination and the reasoning behind it.

4.8 ***Question 5 – What circumstances might result in a breakdown in the information being cascaded to the fee-payer? What circumstances may result in a party in a contractual chain making a payment for the off-payroll worker's services but prevent them from passing on a status determination?***

4.9 Provided that the matter is given appropriate attention by each party in the supply chain and processes and systems are hardwired to require that determinations are conveyed on or before payments are made then there should be no breakdown in information flows. However, this is a big proviso in that it will require close co-ordination between finance and HR/procurement teams in many organisations. Consequently, in our view, breakdowns in information flow will inevitably occur from time-to-time (for example, because the relevant staff are absent, or because the supply chain is long and complex, or involves off-shore entities, or there is a misunderstanding as to whether or not an end client is small, etc.) but it should be possible to minimise these.

4.10 ***Question 5 – What circumstances would benefit from a simplified information flow? Are there commercial reasons why a labour supply chain would have more than two entities between the worker's PSC and the client? Does the contract between the fee-payer and the client present any issues for those or other parties in the labour supply chain? Please explain your answer.***

4.11 While in an ideal supply chain the end client and fee-payer will be known to each other (or be the same party) so that information flows could be 'short-circuited' by the end client sending information direct to the fee-payer, the reality is the end client may not necessarily know who the fee-payer is, particularly where there is a long supply chain. For example, where a national company engages with a national agency to provide workers but a local office of that national company requires a specialised worker, the supply chain may involve the local office making a request to head office for a worker, head office contracting with the national agency, the national agency contracting with a local agency, that local agency then contracting with a sector specific agency, that sector specific agency then contracting with a specialised agency which finally then contracts with the PSC/worker. In such circumstances the end client is unlikely to be aware of who the fee-payer is.

4.12 Consequently, we do not think a 'short-circuit' approach to information flows is realistic.

4.13 As noted above there may well be commercial reasons why a supply chain would have more than two entities between the PSC/worker and the end client. Single agencies often cannot supply all the workers required by an end client. Clients may need workers across the whole spectrum of specialisms and in many different regions. An end client will therefore contract with a provider who in turn will sub-contract to another provider and so on until the specific tasks and locations become much more self-contained and specialist and ending with a worker being supplied (either direct or via his/her PSC). Consequently, longer supply chain are inevitable and the end client will not have direct contact with the fee-payer in these situations.

4.14 ***Question 6 – How might the client be able to easily identify the fee-payer? Would that approach impose a significant burden on the client? If so, how might this burden be mitigated? Please explain your answer.***

4.15 As noted above we think it would be difficult for the end client to identify the fee-payer in many cases. Many end clients have a managed outsourcing relationship with an agency and would rely on them to identify the

fee-payer. Furthermore, for commercial reasons, an agency may not want an end client to have direct contact with intermediaries further down the supply chain, including the fee-payer.

4.16 We also do not think that there is any easy approach to end clients being able to identify the fee-payer in all cases. A requirement for the end client to identify the fee-payer is likely to result in significant administrative burdens arising. Consequently, we think that imposing such a requirement would be a mistake. A better option is to require information to flow down the supply chain and enforce this requirement through appropriate sanctions for non-compliance.

4.17 ***Question 7 – Are there any potential unintended consequences or impacts of placing a requirement for the worker's PSC to consider whether Chapter 8, Part 2 ITEPA 2003 should be applied to an engagement where they have not received a determination from a public sector or medium/large-sized client organisation taking such a n approach? Please explain your answer.***

4.18 Provided that all end clients, except small entities, are required to provide determinations to the PSC/worker (or that PSC/worker receives them via the fee-payer where there is no direct contract with the end client) then (all else being equal) not receiving a determination should logically mean that the PSC/worker will then need to self-assess. This is unless something has gone awry and the flow of information down the supply chain has been disrupted. To cater for this eventuality we can see that the PSC/worker may wish to double-check the position before self-assessing.

4.19 Accordingly, we think it would be helpful if the PSC/worker is able to confirm whether or not they are working for a small entity. For example, by the introduction of a proforma notification that the PSC/worker could request certifying that the end client is small, and which would then trigger the need for the PSC to self-assess under Chapter 8. Alternatively, might there be a central register of small entities which PSCs could access to determine this information?

4.20 But we would query what happens in the situation where a determination is made by the end client that IR35 does apply and, for some reason, the fee-payer does not make a deduction: are we right in thinking that the fee-payer remains liable and the PSC is not required to apply Chapter 8? Also, is the PSC required to notify HMRC of a failure to deduct in such circumstances?

4.21 ***Question 8 – On average, how many parties are in a typical supply chain that you use or are part of? What role do each of the parties in the chain fulfil? In which sectors do you typically operate? Are there specific types of roles or industries that you would typically require off-payroll workers for? If so, what are they?***

4.22 This question is not specifically relevant to the CIOT. We are responding to the consultation as a professional body and have commented above in response to Question 5 on the general question of length of supply chains and sectors.

4.23 ***Question 9 – We expect that agencies at the top of the supply chain will assure the compliance of other parties, further down the labour supply chain, if they are ultimately liable for the tax loss to HMRC that arises as a result of non-compliance. Does this approach achieve that result?***

4.24 We note that the government proposes that where PAYE and NICs have not been correctly accounted for the liability will initially rest with the party that has failed to fulfil its obligations.

4.25 We agree that this is a sensible approach, whether the liability arises as a result of (i) not conveying information on status determinations, or (ii) in the fee-payer not deducting PAYE and NICs when required to do so, or (iii) in the fee-payer failing to pay to HMRC the taxes it has deducted. In all these circumstances we

consider that the basic position should always be that the responsibility should rest with the party that has failed to comply.

4.26 The challenge is then developing a fair and proportionate approach whereby a liability that initially rests with one party might then move to another party in the chain in particular circumstances. But any transfer of liability provisions must factor in the consequences and commercial impact of the entity to which the liability is transferred, especially where that entity has acted responsibly and complied with all the legislative requirements of the off-payroll working rules.

4.27 In this regard we note that the government proposes to transfer liability back to the first agency in the supply chain where HMRC is unable to collect the outstanding liability from another agency that has defaulted on their obligations. And if the first agency cannot pay the proposal is for HMRC to recover the liability from the end client.

4.28 However, we would question why, for example, if a fee-payer ceases to exist having not accounted for PAYE and NICs the first party in the supply chain should automatically be responsible? If that party has used all reasonable endeavours to ensure the integrity of the supply chain but, for example, for some reason, the fee-payer goes insolvent and HMRC is unable to recover the PAYE and NICs this does not appear to us to be a fair and proportionate response. Similarly, where the first agency cannot pay, we do not see why the end client should become liable where the end client has done its best to ensure compliance.

4.29 We consider that, as a minimum the first agency and the end client should be able to offer a defence of having taken reasonable care in these circumstances.

4.30 There is also the point that HMRC receives regular information under Real Time Information (RTI) on amounts of PAYE/NICs due on or before payments are made and so can readily see when payments of PAYE/NICs are late and take prompt recovery action accordingly in such situations. It also has the power to require security deposits where there is a risk that PAYE/NICs will not be accounted for and to transfer liability to directors in certain circumstances. In the present circumstances consideration could be given to adding a power under the off-payroll rules so that in extremis, ie where there is wilful default, the directors of the defaulting entity could become liable for the PAYE and NICs. And in any event, we note that the government is presently consulting on making HMRC a preferred secondary creditor for PAYE and employee NICs. Accordingly, we consider that HMRC should explore these avenues before thoughts turn to transferring liability to a non-defaulting party in the supply chain.

4.31 The consultation document suggests that the first agency/end client should indemnify themselves as a precaution to cater for this outcome, but we query from whom they would seek indemnities because the very party from whom they could seek recovery no longer exists. Accordingly, the effect on the business of the first agency/end client could be materially detrimental and we would therefore urge the government to reflect carefully before adopting this approach.

4.32 We note that transfer of liability to the end client is not the approach taken in the agency workers legislation, except in circumstances where the end client provides the agency with a fraudulent document stating that there is no supervision, direction or control when this is not correct (see ITEPA 2003, section 44(4)). It is true that ITEPA 2003, section 689(1B) – which addresses employees of a non-UK employer, agencies, etc – provides that where an agency is onshore but sub-contracts to an agency offshore for the supply of employees to the end client, the onshore agency is responsible for accounting for any PAYE/NICs. However, this is different because the onshore entity knows this upfront and can comply accordingly.

4.33 Accordingly, in our view if the government adopts an approach under the off-payroll rules whereby ultimate liability may pass to the first agency or end client when (i) they have not been obliged to withhold PAYE/NICs in the first instance, and (ii) they have provided accurate information on a timely basis, this will create an uneven playing field relative to labour provided via an agency. Hence, as noted above, we consider that any transfer of liability should be tempered with, at the very least, a defence of reasonable care.

4.34 ***Question 10 – Are there any unintended consequences or impacts of collecting the tax and NICs liability from the first agency in the chain in this way? Please explain your answer.***

4.35 Please refer to our response to Question 9. In particular, we consider that the proposed collection of PAYE and NICs from the first agency or end client fails to consider the consequences to, and commercial impact on, a party that has complied with its obligations.

4.36 ***Question 11 – Would liability for any unpaid income tax and NICs due falling to the engager (if it could not be recovered from the first agency in the chain), encourage clients to take steps to assure the compliance of other parties in the labour supply chain?***

4.37 Yes, but if the end client has indeed taken such steps and yet there is a default by the fee-payer or first agency it would be disproportionate for the engager to have to account for the PAYE and NICs liability. As noted above, the end client should at the very least be permitted a defence of having taken reasonable care. Also, again as noted above, this would create an uneven playing field with the supply of agency workers further to ITEPA 2003, Section 44.

4.38 ***Questions 12 – Are there any potential unintended consequences or impacts of taking such an approach? Please explain your answer.***

4.39 Please refer to our responses to Questions 9 and 10. An unfettered power to transfer liability to the end client could, for example, cause a material adverse impact on the end client's business, ie potentially putting jobs at risk even though the end client had done its best to ensure the compliance of the supply chain.

5 Helping organisations to make the correct status determination and ensuring reasonable care

5.1 ***Question 13 – Would a requirement for clients to provide the reasons for their status determination directly to the off-payroll worker and/or the fee-payer on request where those reasons do not form part of their determination impose a significant burden on the client? If so, how might this burden be mitigated? Please explain your answer.***

5.2 Please refer to our responses to Questions 2 and 3. We agree that information should be shared appropriately and promptly. We also agree a requirement to provide the PSC/worker with the status determination would make the end client's view clear. This said, weighing up the situation in the round, we think the least burdensome process would be to require the information to flow down the supply chain until it is received by the PSC/worker. A requirement for end clients to provide status determinations direct to each individual worker, in addition to having to provide the first agency with appropriate information, would present significant extra burdens in terms of time and cost. Also, this requirement cannot be viewed as a one-time exercise (or cost/burden). A 'new' status determination is required anytime the nature of the contractual arrangement changes and, for ongoing contracts, it is likely that most end clients will put a process in place to review the contract at least annually to ensure the situation has not changed. A requirement to provide

status determinations direct to PSCs/workers in all such cases would mean significant additional costs being incurred by the end client (both in terms of staff and technology).

5.3 Also, in our view, a requirement for the end client to provide the information direct to the fee-payer is not practical as the end client will not necessarily know who this is (please refer to our response to Question 5 in this respect).

5.4 While we agree that the reasons for the end client reaching their status determination should be provided with the status determination, we also consider that the content and format of such information must be succinct. In particular, we suggest that it might follow a standard cascade template, or indeed perhaps the output from HMRC's CEST if the end client decides to use this tool. This is something that should be covered in HMRC guidance and examples.

5.5 ***Question 14 – Is it desirable for a client-led process for resolving status disagreements to be put in place to allow off-payroll workers and fee-payers to challenge status determinations? Please explain your answer.***

5.6 While we agree that there is a need for due process to resolve a status disagreement, we do not think that statutory rules with prescribed requirements imposed on the end client, the PSC/worker, etc. is the right approach. When there has been disagreement on status in the public sector this has generally seen a dialogue taking place between the end client and the PSC/worker (or their tax advisers). So, to this extent a process naturally exists, and the question is what, if any, further requirements might be imposed in connection with that process.

5.7 In our view there are a few key points to bear in mind in considering an appropriate process for PSCs/workers and fee-payers to challenge end client status determinations. Firstly, such a process cannot be unduly lengthy. In particular, it is unrealistic to think that it could replicate the deliberations of a tribunal in documenting its decisions in a lengthy 'judgment' in each case. Secondly, the end client should already have made the initial decision using reasonable care and based on what they understand to be the full facts and, of course, they will be accountable if they get the decision wrong. For example, if they determine that IR35 does not apply when it should. Thirdly, where the end client has, for whatever reason, not taken into account the full facts and/or misjudged the position and so inadvertently arrived at an unreasonable/untenable view then one would expect that the determination should be able to be challenged and changed if appropriate. But we think this is something best left to HMRC guidance than legislation.

5.8 More generally, we are hearing that numbers of end clients intend to advertise roles/work as within or outside IR35 so that the applicant knows upfront where he/she (and their PSC) stand and can decide accordingly whether they wish to apply or accept that work on that basis.

5.9 ***Question 15 – Would setting up and administering such a process impose significant burdens on clients? Please explain your answer.***

5.10 Please refer to our response to Question 14. An informal process would be expected to apply naturally and we think that a statutory process would risk imposing significant burdens so care should be taken before deciding to go down this route. Of course, one way that a status disagreement between the end client and PSC/worker could be resolved is through the intervention of an independent party who would reassess the determination. However, the costs and burdens associated with such an intervention are likely to be significant, and the 'cost' to the working relationship between the end client, agency and worker should not be ignored either.

5.11 In summary, what we think would be preferable is clear HMRC guidance around best practice on how to determine status, coupled with an upgraded CEST tool (although we do not underestimate the challenge in

the latter respect). We also think it should be possible to discuss the position with HMRC in more difficult cases (for example, where CEST is unable to determine status).

5.12 ***Question 16 – Does the requirement on the client to provide the off-payroll worker with the determination, giving the off-payroll worker and the fee-payer the right to request the reasons for that determination and to review that determination in light of any representations made by the off-payroll worker or the fee-payer, go far enough to incentivise clients to take reasonable care when making a status determinations?***

5.13 Yes, we think it does. This said, in our experience, end clients would be expected to take reasonable care in making status determinations in any event. Of course, the reality of human behaviour is that if in any doubt the end client is very likely to take a prudent path and determine that IR35 applies, and it is possible that the worker/PSC/fee-payer may disagree. This means that either the worker/PSC will subsequently choose to work elsewhere, or the case will make its way in due course to HMRC and possibly thence to the First Tier Tribunal.

5.14 The problem, as we see it, is that if there is an abundance of caution by end clients (as may well be the case) and disputed cases become numerous then for those PSCs/workers who nevertheless continue to work for the end client (albeit subject to IR35) then these disputes could overwhelm the courts. This is not an easy problem to solve as recent cases like *Albatel*, *MDCM*, *Jensal Software* and *Atholl House Productions*[5] show that one party can genuinely take one view whilst another disagrees, and the matter may be decided on relatively fine points. Indeed, as was said in *Atholl House Productions* (at paragraph 130(b)), '*… each case involves a value judgement and … it is inevitable that different people may come to different conclusions on the same facts*'.

6 Other matters

6.1 ***Question 17 – How likely is an off-payroll worker to make pension contributions through their fee-payer in this way? How likely is a fee-payer to offer an option to make pension contributions in this way? What administrative burdens might fee-payers face which would reduce the likelihood of them making contributions to the off-payroll worker's pension?***

6.2 We agree that consideration should be given to replicating the position whereby PSCs make pension contributions to the worker's pension plan, particularly in view of the savings in employer's NIC that can apply in this situation (as they do for regular employers where the employer makes pension contributions). However, we do not think that fee-payers would want to adopt an approach whereby they are required to give tax relief (and NICs relief in the case of employer contributions by the PSC) by making the deduction for each worker/PSC and paying this over to their particular pension scheme.

6.3 The fee-payer will often be dealing with many individuals who may be making pension contributions to many different schemes. Accordingly, we think that the burden on fee-payers in administering pension contributions on behalf of each worker/PSC would be excessive.

6.4 An alternative approach would be for the payment of pension contributions by the PSC to qualify for a commensurate rebate of PAYE and NICs to the PSC, ie to the extent that PAYE and NICs has previously been accounted for by the fee-payer to HMRC. In principle, this could extend to secondary NIC as well as primary NIC and PAYE.

[5] *Albatel Ltd* v *HMRC*, FTT [2019] UKFTT 195 (TC), TC07045, *MDCM Ltd* v *HMRC*, FTT [2018] UKFTT 147 (TC), TC06400, *Jensal Software Ltd* v *Revenue and Customs Commissioners,* FTT [2018] UKFTT 271 (TC) and *Atholl House Productions Ltd* v *HMRC*, FTT [2019] UKFTT 242 (TC), TC07088.

6.5 ***Question 18 – Are there any other issues that you believe the government needs to consider when implementing the reform? Please provide details***

6.6 *Interaction of the off-payroll and IR35 rules with the agency workers legislation (ITEPA 2003, Section 44)*

We think the interaction of IR35 rules with the agency workers rules can be complicated and difficult for end clients, agencies and workers to appreciate. It would be helpful for HMRC to publish guidance to explain which rules apply and in what circumstances (including illustrative examples). An important point here is that different tests apply to trigger PAYE and NICs for agency workers and under IR35, ie supervision, direction or control for agency workers but the broader employment status tests in the case of IR35. Situations where end clients engage with non-UK PSCs (being non-UK resident employers under ITEPA 2003, section 689) and when the end client is a host employer also need to be explained.

6.7 *Personal service or outsourced/contracted-out service*

Deciding who is the end client in a supply chain can prove problematic. There is a material difference between (i) a client engaging business-to-business with a supplier of, for example, construction services who in turn engages business-to-business with a sub-contractor that finally engages with a PSC, and (ii) a supply of a PSC/worker along a long chain through to the end client. In (i) the chain for IR35 purposes would only include entities between whom labour is provided and so would terminate with the sub-contractor. In (ii) labour would be delivered from one entity to another along the chain right up to the end client.

6.8 For example, Utility PLC enters into a contract with Contractor Ltd to replace a section of piping/cabling. Contractor Ltd undertakes to carry out all work to fulfil the contract (eg dig hole, lay pipe/cable, fill in hole) and is liable for any delays or defects etc. Contractor Ltd engages workers via their PSC and through an agency to complete the contract. In our view, the end client is not Utility PLC as it has fully out-sourced the service it requires to Contractor Ltd. Instead, Contractor Ltd is the end client for the purposes of the off-payroll rules and would be responsible for determining the status of the workers and notifying the agency and PSC/worker accordingly.

6.9 We think it would be helpful for HMRC to publish guidance, with illustrative examples, to help clients, agencies and workers understand who the 'end client' is for the purposes of the off-payroll working rules. This should build on the existing guidance published for the public sector[6].

6.10 *CEST*

We think a key issue to implementing the off-payroll rules in the private sector is how the CEST tool is developed and modified to ensure that it is better able to address the breadth of scenarios that arise in the private sector.

6.11 It is key that not only is CEST improved but that the new-improved CEST is made available sufficiently ahead of the introduction of the new off-payroll rules in April 2020 to enable end clients to review existing and new contracts by April 2020. It is important that modifications to CEST are made in good time and not just before go-live, which is what happened in the case of the public sector changes. In our view the latest that an improved CEST tool should be available is October 2019. The new CEST also needs to be fully tested ahead of going live and capable of producing accurate results in at least 95% of cases. Similarly, HMRC guidance should

[6] https://www.gov.uk/guidance/off-payroll-working-in-the-public-sector-reform-of-intermediaries-legislation#contracted-out-services.

also be available in good time. We would suggest that draft guidance should be published alongside the draft legislation that is due to be published this summer.

6.12 We would refer HMRC to our response[7] of 7 August 2018 further to the previous consultation on extending the off-payroll rules to the private sector in regard to a number of our concerns with the CEST tool, which have yet to be addressed. We understand that HMRC research indicates that in about 15% of cases the CEST tool is unable to determine employment status. Factoring in recent decisions where the First Tier Tribunal has decided that IR35 does not apply (eg *Albatel*, *MDCM*, *Jensal Software* and *Atholl House Productions*[8]), it is evident that CEST does need to be improved if organisations are to have confidence that they can rely on its output. As noted above, we think the gap in 'unable to determine' outputs from CEST needs to be closed from 15% to less than 5%.

6.13 We believe that CEST should take proper account of mutuality or obligation, multiple engagements, contractual benefits (including holiday pay, maternity/paternity pay, etc) and whether someone is in business on their own account.

6.14 We illustrate in the attached Appendix how variations on a particular situation or theme can make it difficult to reach a binary Yes/No answer as to whether IR35 applies. Our example is based on a 'web designer' with the basic fact pattern varied to illustrate how 'grey' rather than 'black and white' status decisions can be. It is the nuances that distinguish one situation from another that make it very difficult to conclude definitely whether or not IR35 should apply.

6.15 *Off-payroll working and small public sector entities*

The changes to the off-payroll rules are to apply to the public sector as well as the private sector from April 2020 with the notable exception of the small entity exemption. There are many entities that are deemed to be public sector bodies, for example, academy schools, that are 'small', and which provide services that are no different to services provided by private sector entities. It seems to us that the government should consider extending the 'small' entity exception to all small entities and not just those in the private sector.

6.16 *The Good Work Plan*

In December 2018 the government announced that it intended to '*legislate to improve the clarity of the employment status tests, reflecting the reality of modern working relationships*'. Furthermore, the government endorsed the Taylor Report's recommendation that '*there should be more emphasis on control and less on the notional right – rarely in practice exercised – to send a substitute, reflecting new business models*' and indicated they would legislate accordingly.

6.17 We think that it is important that government signal when these changes will be introduced as this could materially impact the baseline IR35 status determinations that businesses are, and will be, undertaking ahead of April 2020 for contingent labour engaged via PSCs.

6.18 Similarly, if the government were to decide to introduce employment rights in respect of those engaged by clients via PSCs, ie rights to be applied directly between the worker and the end client, this would likely materially affect whether or not clients continue to engage labour via PSCs.

[7] https://www.tax.org.uk/policy-technical/submissions/payroll-working-private-sector-ciot-comments.

[8] *Albatel Ltd* v *HMRC*, FTT [2019] UKFTT 195 (TC), TC07045, *MDCM Ltd* v *HMRC*, FTT [2018] UKFTT 147 (TC), TC06400, *Jensal Software Ltd* v *Revenue and Customs Commissioners,* FTT [2018] UKFTT 271 (TC) and *Atholl House Productions Ltd* v *HMRC*, FTT [2019] UKFTT 242 (TC), TC07088.

6.19 *Post-implementation review*

We recommend that a review is undertaken by HMRC in, say, mid-2022, after a full tax year (2020/21) of operating the new off-payroll rules and with the submission deadline (31 January 2022) for SA returns for that year having passed. This would provide the opportunity to assess what is working well, what is working less well and to assess whether or not changes are needed to ensure that the process works as effectively and efficiently as it can for PSCs/workers, agencies, clients and HMRC.

7 Acknowledgement of submission

7.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

8 The Chartered Institute of Taxation

8.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 18,500 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation

28 May 2019

APPENDIX

An illustration of the potential difficulties of determining employment status for IR35 purposes

This example is based on a 'web designer' with the basic fact pattern varied to illustrate how 'grey' rather than 'black and white' status decisions can be.

Consider an individual with a PSC jointly owned by his/her spouse. The PSC is engaged to design a website for a retailer. Assume the retailer does not qualify as 'small' for the purposes of the April 2020 changes to IR35. To determine whether or not a hypothetical employment contract exists between the individual and the retailer assume that in the PSC/retailer contract there are terms covering the areas listed below:

- what is to be done,
- by whom (whether substation permitted),
- with whom,
- degree of autonomy,
- when/timing,
- location,
- basis of fees,
- benefits,
- exclusivity,
- mistakes,
- insurance and
- equipment.

Scenario 1 – The PSC/worker is engaged to:

(1) Design and build a website for the retailer,
(2) Personal service is required,
(3) The worker will work alongside the existing ITE team,
(4) The worker reports daily to the head of IT,
(5) The worker works 5 days a week, 9-5, for 8 weeks,
(6) The worker works at the retailer's site,
(7) The worker is paid on a daily rate,
(8) No benefits are provided save for the use of the staff canteen,
(9) The worker is not permitted to work for anyone else,
(10) Mistakes have to be rectified but at the daily rate,
(11) No insurance is required, and
(12) The design and build is carried out on the retailer's equipment.

In this scenario the hypothetical retailer/worker contract would in our view pretty clearly be one of employment.

Scenario 2 – The PSC/worker is engaged to:

(1) Design and build a website for the retailer,
(2) The worker could involve another specialist, subject to the approval of the retailer,
(3) The work is mostly done independent of the existing IT team,
(4) The worker reports weekly to the head of IT,
(5) Delivery of the website is required in 8 weeks, the hours are up to the worker,
(6) The location of the work is up to the worker as long as he/she is contactable,

(7) The fee is based on 8 weeks at the worker's daily rate,
(8) No benefits are provided,
(9) The worker is permitted to work for others concurrently if time allows (and does so),
(10) Mistakes have to be rectified in the worker's own time,
(11) Insurance is required, and
(12) The design and build is undertaken on the worker's/PSC's own equipment (with installation following user-testing).

In this scenario we think a hypothetical retailer/PSC contract would pretty clearly be one of self-employment.

Having taken these two 'black and white' situations and tested whether IR35 applies, can a clear view be reached if the facts are further varied? In particular, we can mix and match terms 1-12 in scenarios 1 and 2 in many different permutations so that the question of employment or self-employment becomes 'grey' and reflects the multitude of circumstances that arise in real life. For example:

Scenario 3 – The PSC/worker is engaged to:

(1) Design and build a website for the retailer,
(2) The worker could involve another specialist, subject to the approval of the retailer,
(3) The work is mostly done independently of the existing IT team,
(4) The worker reports daily to the head of IT,
(5) Delivery of the website is required in 8 weeks, the hours are up to the worker,
(6) The worker works at the retailer's site,
(7) The worker is paid on a daily rate,
(8) No benefits are received save for the use of the staff canteen,
(9) The worker is permitted to work for others if time allows (and does so),
(10) Mistakes have to be rectified in the worker's own time,
(11) No insurance is required, and
(12) The design and build is carried out on the retailer's equipment.

In this scenario there are pointers to both employment and self-employment in considering a hypothetical PSC/retailer contract. In our view it's less than clear cut for the retailer whether or not to apply IR35. Given the downside in getting the decision 'wrong' the retailer may well decide that IR35 does apply and so to account for PAYE and NICs, albeit the worker/PSC may not be happy with this. In any event a key question is whether HMRC's modified CEST will be able to form a view in situations like this or will there still be a significant number of circumstances where it will register 'cannot determine'?