

IR35 & Off-Payroll Working: How does it affect your business?

IR35 is certainly a hot topic at the moment and the Off-Payroll Working Rules, which now apply across the public sector and to medium and large private sector organisations continue to create questions for clients and freelancers alike. Therefore, we have outlined below some of the most frequently asked questions regarding IR35 and hope that this gives you a baseline understanding of how to prepare.

Do grab a cuppa and have a good read through; whilst this piece is a bit lengthy, we hope that we have summarised the main points and can clear up some of the confusion.

How does this affect my business?

Firstly, it's important to say that this legislation currently exists and was introduced in 2000. It is essentially a way of HMRC assessing whether a freelancer is a 'disguised employee' and should, therefore, pay tax and National Insurance (NI) at normal PAYE rates instead of at reduced rates, or via dividends: In the case of a freelancer invoicing through their own LTD company/PSC (Personal Service Company).

This will mean that for a freelancer, if the end client has assessed that their assignment falls within the IR35 legislation, and unless the end client is prepared to increase the day rate being paid, to reflect the additional tax and NI (both employer and employee contributions), they will be taking home less pay.

As an end client, you may wish to either re-structure the way in which you utilise freelancers and how they work in your business, so that they fall outside of the IR35 Off Payroll legislation, or you may wish to consider paying a higher day rate to secure the freelancer so that they are not out of pocket. Either way, there are things you can do to be prepared.

What does 'disguised employee' mean?

A disguised employee is where a freelancer/contractor performs the same or a similar role to that of a company employee or acts as such and takes advantage of employer facilities and equipment.

This essentially indicates that the freelancer is not really performing the role of a self-employed contractor, in the eyes of HMRC, and therefore is subject to the same tax and NI, at PAYE rates.

Are there exceptions to this rule?

The Off-Payroll Working Rules apply to all public sector organisations and to medium and large private and voluntary sector organisations.

A private sector company will generally be considered small for the purposes of the current Off-Payroll Working Rules if it meets at least two of the following three criteria:

- **Annual turnover of £10.2 million or less**
- **Balance sheet total (assets) of £5.1 million or less**
- **50 or fewer employees on average**

Small private sector clients are not responsible for determining a contractor's employment status under the off-payroll working rules. Instead, responsibility remains with the contractor's intermediary.

The Government has increased the general small-company thresholds to £15 million turnover and £7.5 million balance-sheet assets for accounting periods beginning on or after 6 April 2025. However, HMRC has confirmed that these increased thresholds will not affect the Off-Payroll Working Rules until **6 April 2027 at the earliest**.

If a freelancer works for multiple clients, does that exclude them from IR35?

One of the biggest things that we are hearing from some clients is that the freelancers they employ also work for other clients and, therefore, they should be fine.

This is a myth! The IR35 ruling will apply to ALL freelancers for placements from one day to over 24 months!

It is the way in which you engage the freelancer (worker) that determines whether they fall inside or outside of IR35, and an assessment needs to be done for each engagement/booking.

What are the key Off-Payroll Working Rules?

Under the current Off-Payroll Working Rules, where a client determines that a freelance engagement falls within IR35, Income Tax and National Insurance contributions must be deducted through PAYE. This means that, unless rates are adjusted, contractors working inside IR35 may receive a lower net income than those working outside the legislation.

The end client is responsible for making these deductions before paying the freelancer, but this could equally be a recruitment business if they are paying the freelancer for the end client.

The alternative, and to maintain the current practice, is to change the way in which you are engaging that freelancer, if this is possible, resulting in them falling 'outside' IR35.

The key features of the current Off-Payroll Working Rules are:

1. A change in who is responsible for undertaking the IR35 status determination/assessments; The end client is now responsible for the assessment, each and every time they engage with a freelancer – currently, it is the freelancer.
2. Liability for incorrect status determinations is changing; Currently, the liability sits with the freelancer, who is liable for outstanding tax and NI, should an assessment be incorrect. Now, whoever pays the freelancer is liable. That could be the end-client if you engage the freelancer directly, or the recruitment business if we pay the freelancer for you.

These are key responsibilities under the current Off-Payroll Working Rules and should be considered whenever engaging contractors through their own limited companies.

What is an HMRC status determination/assessment?

The Government has created a 'CEST' tool which can be found on the gov.uk website (<https://www.gov.uk/guidance/check-employment-status-for-tax>). You can use it to input information and determine the IR35 status of each freelancer.

How does HMRC determine whether the freelancer falls 'inside' or 'outside' IR35?

The information below is based on a document compiled by APSCo, a recruitment body that Beyond the Book are members of. APSCo has worked in conjunction with HMRC to assess this legislation (<https://www.gov.uk/guidance/check-employment-status-for-tax>). To determine whether a contractor will be caught by IR35, key criteria are reviewed to establish employment status. A decision is made about a hypothetical contract between the contractor and the end-client, and whether, if those two parties were contracting directly, there would be an employment relationship.

It is worthwhile working through HMRC's employment status for tax test and entering different responses to gain an understanding of the different outcomes. Essentially, if a contractor has similar working conditions, responsibilities, and control, as an employee of the client would have, then they are likely to be classed as "inside IR35" (i.e. the Off-Payroll working rules apply).

Case law is evolving constantly in the tax tribunals, courts and employment tribunals but the key factors that determine a contractor's IR35 status are as follows:

Substitution

A genuine right of substitution has long been deemed to be a very important factor when demonstrating that a contractor's assignment falls "outside IR35". For a substitution to be

considered valid, the right to supply a substitute must be a genuine one. This means that the client must agree to it in practice, the contractor must pay for the substitute, and it should be an unfettered right. An unfettered right of substitution means that a client must accept a substitute if the initial contractor is unavailable.

Control and Direction

In most cases where professional services are provided, it is important that a contractor can demonstrate a certain amount of autonomy in the way they undertake a project. Both the written contract and working practices must show that the client has no influence over how the contractor performs his/her services.

Control factors that may point towards an 'inside IR35' status include:

- Indicating that the contractor will be supervised, the client will be following the instructions and be directed by the client
- Including any "staff" benefits (including holiday or sick pay, a company email address)
- Including start/end/break times
- Contractual clauses that specify any rights of control or supervision over the contractor

The reality of the situation is that the individual is responsible for the delivery of the services. The individual will determine and control how and when they provide their services to the client, provided that they meet client-specific targets or project completion dates. It is worth noting that any clauses referring to control should be reflected in both the first tier (between recruitment business and client) and the second-tier contracts (between recruitment business and contractor).

Financial risk

The contractor may take on a level of financial risk in undertaking the engagement. Contractors who don't take any financial risk, for example, don't have to rectify poor quality services at their own cost, are more likely to be deemed 'employees' for tax purposes. Contractors taking financial risk would also be expected to maintain appropriate insurances.

Mutuality of Obligation (MOO)

This is a hotly disputed area of law, as the position of HMRC is different from that of many practitioners and case law. In essence, it is an obligation between the parties to provide and accept work. In an employer/employee relationship, mutuality of obligation is easy to establish, however, in client/contractor relationships, it is less clear. HMRC states that by having a contract agreeing to provide services, mutuality is established, but most experts consider the legal picture to be more complex.

Other factors include:

- Provision of equipment
- Any absence procedures
- Continuity of the engagement
- Termination agreements to Notice periods
- If the contractor has become “part and parcel” of the organisation

Every freelance engagement should be considered on its individual circumstances. HMRC looks at both the contractual terms and the actual working practices when determining employment status. Factors including control and direction, the requirement for personal service and right of substitution, financial risk, provision of equipment and how integrated the contractor is within the organisation can all contribute to the overall determination. No single factor should be considered in isolation.

We hope that this article has been useful and has helped to clarify some of the key considerations around IR35 and the Off-Payroll Working Rules.

Our freelance team has been on a number of training seminars and would be happy to discuss any element of the current legislation with you at your earliest convenience.

Should you wish to get in touch, please contact us at freelance@btbpeople.co.uk or call us on 01789 451510.