Off-payroll working in the public sector: reform of the intermediaries legislation

Employment Tax

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The government proposes changes to the IR35 rules for public sector workers. The ATT and CIOT have responded, raising concerns about the burdens the proposed policy would place on engagers, workers and the latter's PSCs.

In response to HMRC's consultation on reforming the tax treatment of off-payroll workers in the public sector, the ATT and CIOT have indicated that imposing a requirement to account for income tax and NICs through the PAYE system (in circumstances where the IR35 rules appear to apply) on the payer of a worker's own limited company (PSC) would cause significant burdens for the payer, the PSC, the worker and the Revenue.

As a result of HMRC's decision, as announced at Budget 2016, to reform the intermediaries legislation (commonly referred to as IR35) for off-payroll engagements of workers who operate through an intermediary, such as their own limited company, in the public sector, a formal consultation was launched on 23 May 2016 and closed on 18 August 2016.

The condoc proposed that, from April 2017, the responsibility for considering whether the IR35 rules apply will move from the worker's PSC to the public sector body, agency or other third-party body (known as the engager) paying it. The engager will then be liable for any associated income tax and NIC if the engager assesses that IR35 applies.

The ATT and CIOT submitted responses to this consultation which, as a Stage 2 consultation, sought only views on the impact of the proposed change and the detailed design of the policy, which includes a new process to determine whether an

intermediary is in scope of the rules.

The CIOT noted that some public sector bodies already had to determine the employment status of off-payroll workers (who are engaged for more than six months and paid more than £220 a day) and must seek assurances from them that the correct taxes are accounted for (see Procurement Policy Note 08/15: tax arrangements of public appointees. We suggested that extending this requirement to all off-payroll workers engaged by public bodies and introducing a reporting regime for those bodies to report the status of such workers to HMRC would have been the simplest method of improving the current 'widespread non-compliance with the legislation' noted in the condoc. The CIOT repeated its view, made in response to last year's Intermediaries Legislation (IR35): discussion document, published on 17 July 2015, that two better options were possible: a form of reporting obligation on the part of the engager; or simply bar public bodies from engaging workers through PSCs that provide labour-only services.

The ATT noted that most of its members would be concerned primarily with the impact of these new rules on the PSC in terms of the personal tax and corporation tax implications, including those for cash flow. However, the condoc was notably silent on these particular aspects and instead focused on the impact on the engager.

The ATT also highlighted three main problem areas with the new rules. First, when agencies are considered to be the engager responsibility will be placed on them to make decisions for which they will have insufficient information about the exact nature of the engagement passing down from the public sector body. We suggested that HMRC would have to implement statutory obligations on the body to provide relevant information to agencies. The CIOT also raised this point and thought that these obligations would inevitably need to be underpinned by a penalty regime. This would ensure that all parties provided accurate and timely information for a proper assessment to be made on whether IR35 applies.

Second, the ATT noted that potential financial liabilities would be placed on agencies that are then likely to make decisions on the basis of protecting their own interests. This could lead to the new rules being implemented across the board and businesses genuinely not within the new rules will be wrongly subjected to them. The CIOT added that the government would also need to consider whether an engager could adopt a 'default position' in particular circumstances, – say, if information is not forthcoming and what this would mean for the engager, the PSC and HMRC should a

dispute follow. The CIOT also asked whether, if an engager decided not to deduct, the PSC could rely on this in determining its own position for IR35 purposes.

Third, the ATT noted that the government appeared to be placing significant emphasis on the proposed new online tool intended to enable users to determine the relevance of the IR35 rules to particular engagements. The tool has to be capable of determining whether IR35 applies, not simply in ‘black and white’ cases, but all the ‘grey areas’ in between. It is, however, difficult to see how a simple online tool could direct users to the correct conclusion when there remains significant uncertainty over the IR35 rules some 16 years after they were introduced. The CIOT also noted that the online tool was a crucial element to the new rules and thought that, unless the tool is up to the job, the administration of the new rules would move from ‘difficult’ to ‘impossible’.

The government proposes to introduce these new rules from April 2017. The CIOT thought that, even assuming that HMRC’s online tool could be built by then, it would impose significant pressures on public sector bodies, agencies and software companies to develop and test IT systems and related procedures to capture the information required to assess whether IR35 applies (for example, whether the proposed gateway tests are passed and, if so, whether HMRC’s proposed online tool indicates that there is a deemed employment status for the worker) and, where appropriate, deduct PAYE and NIC and then report this to the Revenue.

The CIOT added that time must be built into the framework for introducing any changes for HMRC to develop, test, evaluate and pilot its proposed online tool. We thought, however, that in reality there would be insufficient time between now and April 2017 to do this properly. As a result, the CIOT recommended that, if it is decided to proceed with the current proposals, the new rules should not be introduced until IT systems (HMRC’s and third parties’) are proven to be ready. Even then we suggested it would be better to adopt a staged introduction.

Finally, in the CIOT’s opinion, the proposed new rules will cause commercial uncertainty, particularly in regard to employer NICs and whether and where this cost is borne (that is, although the liability may rest with the engager, it may well be the worker that ultimately bears the cost). We added that the proposed change would require existing contracts (that may extend beyond the start date) to be renegotiated and a new basis to be established for future ones (for example, with clauses to deal with who bears the cost of any employer NIC liability). We also

thought that the change would have an effect on commercial rates charged by PSCs and lead to a disparity between public and private sector rates, which could lead to two systems developing for the public and private sectors where the former is put at a disadvantage in competing for resources.

Read the ATT response on the ATT website.

Read the CIOT response on the CIOT website.