

# THE REC IR35 GUIDE FOR CLIENTS



## Extension of the off-payroll rules into the private sector

**NOTE:** The REC has written this factsheet for members to share with clients in preparation for the IR35 reforms in April 2020. We have written it based on the draft legislation produced in July 2019 – we will update this document when the legislation has been finalised.

### WHAT IS HAPPENING AND WHEN?

**What:** The Government is extending the off-payroll rules, which have applied in the public sector since April 2017, into the private sector. The new rules will apply to work done by contractors working through intermediaries such as personal service companies. Importantly, the tests for IR35 status are not changing but the responsibilities for making the IR35 status decision and related deductions are.

**When:** The new rules will apply to all payments made to personal service companies on or after 6 April 2020.

**What's the difference?** From 6 April 2020, the client, and not the contractor, will be responsible for assessing IR35 status. For inside IR35 assignments, the fee-payer will have to make tax and national insurance deductions before paying the personal service company.

The off-payroll rules which currently apply in the public sector will be extended into the private sector from 6 April 2020, albeit with some changes. This means that a client will need to know how a contractor is engaged e.g. whether PAYE'd by an agency, or whether paid via an intermediary such as a personal services company or an umbrella company (the rules will apply even where clients engage contractors directly rather than through an agency). The key issue is that where the off-payroll rules apply, **the client will be responsible for assessing the contractor's status for tax purposes**. So which clients will the off-payroll rules apply to and what will the client need to do?

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**Small companies exemption** – small companies will be exempt from the changes. A small company is one which meets two or more of the following criteria (a) annual turnover of not more than £10.2 million, (b) balance sheet total of not more than £5.1 million or (c) no more than 50 employees. Companies in groups and joint ventures will be exempt provided all of the group companies or joint venture partners are small. Unincorporated organisations with a turnover of less than £10.2 million will also be exempt. Where organisations are exempt, the existing IR35 rules (where the intermediary is responsible for applying the rules) will continue to apply.

When an organisation becomes or ceases to be small in an accounting period, for the purposes of the off-payroll rules that change will apply from the start of the tax year following the end of that accounting period, irrespective of whether the organisation is incorporated or unincorporated. There will be anti-avoidance rules to prevent organisations restructuring so as to avoid the rules.

**From 6 April 2020 the off-payroll rules will apply to all public authorities, medium and large companies and organisations with a turnover of more than £10.2 million.**

**Making the tax status decision** – the client will have to understand the IR35 rules and use an appropriate assessment tool to reach an accurate IR35 status decision (called a status determination statement (SDS)). In 2017 the Government introduced the [Check employment status for tax](#) (CEST) which is an online tool. CEST has come in for significant criticism and the Government has been working to enhance the tool. HMRC have said that they will stand by CEST outcomes provided the information inputted is accurate. Importantly, CEST is not mandatory and clients can use any assessment method they wish – however at all times the client must use 'reasonable care' in making its tax status assessment. So, clients should not make blanket decisions such as 'all contractors are inside IR35' or 'all contractors are outside IR35'. If a client does not take reasonable care in making its decision it will be liable for unpaid tax and national insurance.

**Agencies should make not tax status decisions for the clients.** If a client does not have internal expertise to make these decisions, they could use an established IR35 external reviewer to help them.

## TOP TIP

Be wary of contract reviewers who say they can “get an assignment outside IR35” simply by adding an unrestricted substitution clause to a contract. Courts look at the reality of the engagement rather than just the contractual documentation. An ability to substitute by itself will not get an assignment outside IR35 if all other circumstances point to inside IR35.

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**Passing status decisions through the supply chain** – having made the tax status decision, the client will have to pass that decision, together with the reasons for that decision to both the party they contract with (usually the recruitment business) and the contractor (including where the client does not have a contract with the contractor). Each party has to pass the decision down until it reaches the fee-payer i.e. the party next to the intermediary in the supply chain.

**Resolving disagreements over status** – the end user client must set up a client-led status disagreement process to help resolve disagreements about the status decision reached. The client must respond within 45 days of receiving a query and must:

- (a) confirm that it has considered the representations made and decided that its SDS is correct, and give the reasons for that decision; or
- (b) give a new SDS containing a different conclusion and state that the previous SDS is withdrawn.

If the client does not respond within 45 days it will become the fee-payer.

**REC advises its agency members not to substitute its own or a contractor's view on status where this conflicts with the client's decision.**

**Liability** – we are still waiting for draft transfer of liability legislation. In the meantime the proposals are that where the fee-payer is off-shore its responsibilities move up the supply chain to the next UK based entity. It is also proposed that liability should rest with a party that has failed to fulfil its obligations until such time as it does meet its obligations at which point liability moves down the chain. However if HMRC are unable to collect the outstanding tax liability from a party, the consultation proposes that the liability should transfer back to the first party or agency in the chain, and if that fails, then HMRC will pursue the client. It is not appropriate for a client to ask an agency to indemnify it if the client does not do what it is required to do under the legislation.

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## NEXT STEPS

REC has responded to the technical consultation on the [draft legislation](#) – we are waiting for the outcome of that as well as some legislation regarding the transfer of liability. Meanwhile HMRC has produced some [initial guidance](#), though more should follow by the end of 2019. **Clients should start to prepare now** for what is a fundamental change in the tax rules affecting how they engage with contractors. Clients should:

1. Assess whether they will be affected or exempt from the off-payroll rules, because they are a small company (or not) and should record this assessment. If exempt, tell their agencies, explaining why.
2. Assess who amongst their contractor population might be affected by these changes and why. REC recommends that clients assess all roles filled by contractors, and not just those it identifies are filled on a given day by contractors working through their own personal services companies.
3. Identify who within their organisation can make IR35 status decisions and ensure that those individuals understand how to assess status and have the appropriate tools to do so. If there isn't an internal person to do IR35 status decisions, then engage a well-established external reviewer.
4. Put processes in place to pass down the status decision and the reasons for that decision.
5. Work with agencies who will have their own processes to implement.
6. Agree with agencies how the increased employer costs will be met – agencies will not be able to simply absorb these costs and pay contractors the same rates.

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**Recruitment & Employment Confederation**

Dorset House  
First Floor  
27–45 Stamford Street  
London SE1 9NT

Tel: 020 7009 2100  
Fax: 020 7935 4112  
Email: [info@rec.uk.com](mailto:info@rec.uk.com)  
Twitter: @RECpress  
Web: [www.rec.uk.com](http://www.rec.uk.com)

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