

A guide to off-payroll working rules for contractors

Although off-payroll working rules aren't new, recent adjustments to the rules have resulted in major changes for contractors. This guide offers a concise overview of the rules and how they apply.

What are the off-payroll rules?

The off-payroll rules were first introduced in 2012 following a review of the tax arrangements of public appointees. They were incorporated into all new contracts issued by government departments after 23rd August 2012.

The off-payroll working rules were put in place to make sure that, where an individual would have been an employee if they were providing their services directly, rather than through an intermediary, they pay broadly the same tax and National Insurance contributions (NICs) as an employee.

Up until April 2017, contractors earning a rate of £220 per day or more or on contracts of more than six months have had to provide assurances to the relevant public sector body that they are outside of IR35. However, new rules were introduced in April 2017 that removed this obligation and placed the responsibility to determine the IR35 status with the public authority.

In the 2018 autumn budget it was announced that these reforms would also apply to private sector businesses from April 2020. Confirmation of this also came in the spring budget 2020. However, less than one month before the reforms were due to be implemented, the [government announced that they would be delayed until April 2021 because of the coronavirus outbreak](#).

Who do the off-payroll rules apply to?

Workers providing their services through an intermediary to a public sector authority will be subject to the legislation.

- **An intermediary** can be a limited company or personal service company (PSC), a partnership or another individual. Most intermediaries providing workers will be PSCs.
- **A public authority** is as defined by the Freedom of Information Act 2000 and Freedom of Information (Scotland) Act 2002. This covers companies owned and controlled by the public sector, local authorities, the NHS, educational establishments including universities and academies.

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What are the new off-payroll rules?

As from 6th April 2017, the responsibility for assessing a worker's employment status will transfer to the public authority, agency or third party paying the intermediary. They will also be responsible for deducting and paying over any PAYE tax and NIC (including employers' NIC) to HMRC.

At the start of a contract, the engager will use [HMRC's online employment status tool](#) to determine whether the rules apply. The tool attempts to determine the worker's employment status with questions relating to their working practice while engaged on a contract. These questions broadly relate to the key concepts of Control, Substitution and Mutuality of Obligation:

- **Supervision, Direction and Control (SDC):** Does the worker exercise control over when, where and how the work is carried out?
- **Personal Service and Substitution:** Is the working arrangement a personal one, or does the contractor have the right to provide a substitution?
- **Mutuality of Obligation (MoO):** Is there an obligation from the client to provide consistent and paid work, along with an obligation from the worker to personally carry out this work?

What happens when the off-payroll rules apply?

If the engager decides the new rules apply, then they will deduct tax and NIC from the contractors' VAT exclusive fee before payment is made and the worker is treated as receiving a deemed employment payment.

The public sector client must inform the intermediary, agency or third party with whom they have a contract whether or not the contract falls within the off-payroll rules. Where the public sector body fails to provide such notification, then a request may be made in writing that the information is made available, together with the reasons supporting their conclusion. Failure to respond to such a request within 31 days of receipt will result in the public sector body becoming responsible for accounting for PAYE.

To enable the "fee payer" to deduct the correct amount of PAYE tax and NICs, the worker will be legally required to provide their National Insurance number, tax code and identity details.

For tax and NICs purposes, the worker is treated as having an employment with the fee payer, so once the contract ends they will be given a P45 form. The relevant pay and tax details will then be entered on the contractors' employment supplementary pages of their self-assessment tax return.

Further details on paying an intermediary can be found [here](#).

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Exceptions and variations to the new off-payroll rules

The off-payroll rules do not apply to small companies, those which meet two or more of the following criteria:

Less than £10.2m turnover

- Less than £5.1m balance sheet total
- 50 employees or less
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The rules don't apply where a public sector authority has fully contracted out services to a third party (like an outsourcing company) and the workers don't personally provide their services to the public authority.

[Slightly different rules apply](#) if the person paying the intermediary is outside of the UK.

If the contractor chooses to work through an umbrella company, the umbrella company becomes the contractor's employer for the purposes of tax. They will deduct PAYE tax and National Insurance contributions at source. Therefore the responsibility for applying IR35 is removed from any other party.

Expenses and pension contributions under the off-payroll rules

A Personal Services Company (PSC) will still be able to make pension contributions on behalf of the contractor with relief being obtained through the company.

Whilst the 5% allowance to cover unspecified expenses has been removed in the public sector for contracts that are inside IR35, the PSC can still claim tax-allowable business expenses that could be claimed by an employee working directly for a public sector organisation. The allowance will also be removed in the private sector after April 2021 where IR35 applies.

Travel and subsistence claims referring to the expenses claimed in relation to travel costs such as train tickets, food or accommodation cannot be claimed where a contract is inside IR35.

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Impact summary of the new off-payroll rules

The introduction of the new rules has been problematic, with many public sector organisations adopting a safety first policy and treating all workers as being inside IR35 so as to avoid liability. As a result many contractors have turned their backs on the public sector, resulting in worker shortages in organisations such as the NHS.

Despite tax experts advising that the new rules are not suitable for application in the private sector, not least because of the confusion surrounding CEST, HMRC has pressed ahead. In the Autumn Budget 2018, it was announced that the public sector off-payroll rules would be extended to the private sector in 2020.

This resulted in similarly non-compliant measures being taken in the private sector. Many large scale companies including Barclays, HSBC and Lloyds adopted a ban on PSCs, forcing contractors out of their limited companies and onto the payroll. The measures met with outrage from contractors who found themselves taxed as employees, yet denied the right to employment benefits. Many were also left paying travel expenses out of their own pocket, as these can't be claimed inside IR35.

[Such was the public outcry against the reforms](#) that the government promised to conduct an Off-Payroll Review following its reelection in December. Concluding in February 2020 after just six weeks, the review stated that the reforms were necessary. The review was widely derided as a sham for refusing to address the serious issues arising from the reforms, and instead insisting that compliancy has improved in the public sector.

[In February 2020, a House of Lords Inquiry was launched to look into the impact of the reforms as part of the Finance Bill.](#) The hearings produced convincing evidence that the reforms have been detrimental, and that the increase in revenue to the exchequer is likely to be a result of forcing contractors onto the payroll, rather than of the increased compliancy claimed by Treasury.

Many stakeholders hope that the years' delay in response to the covid-19 outbreak will provide the government with an opportunity to reevaluate the reforms. Although a welcome reprieve, the suspension presents both businesses and contractors with the difficult decision of whether to proceed with any preparations they have made, or to reverse them.

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