Written evidence submitted by the Chartered Institute of Taxation New Clause 1 and New Schedule 1 Workers' services provided through intermediaries (FB31)

New Clause 1 and New Schedule 1
Workers' services provided through intermediaries

Executive Summary

This clause extends the Off-Payroll Working (OPW) rules from the public sector to the private sector and makes some changes as to how the rules are to be applied to both public and private sector bodies from April 2021.

Areas of significant concern include:

- **The recovery of PAYE from the client, or the agency with which the client contracts (first agency), where the deemed employer (fee payer) has, for some reason, not accounted for PAYE and NICs due. We think the liability should revert to the Personal Service Company in the same way as would have applied had the client been 'small' and the OPW rules not been applicable**
- **The omission of a requirement on the last agency in a contractual chain to confirm to the client that it is the deemed employer (fee payer) and will account for PAYE and NICs deductions**
- **The omission of an explicit requirement for the client to pass a Status Determination Statement (SDS) to the agency they contract with, and for the SDS to be passed down the supply chain until received by the deemed employer**
- **The omission of an explicit obligation for a client to issue a Status Determination Statement where it considers that the OPW rules do not apply**
- **Lack of clarity as to where liability for PAYE and NICs lies in a case where a client has incorrectly issued a Status Determination Statement stating that the OPW rules do not apply**
- **The omission of any specific requirement for a client to exercise reasonable care in considering any representations made by the worker (or deemed employer) following an appeal against the client's original status determination decision**

The CIOT is also calling for a wider review of employment status, looking at how to simplify status tests and how income from working should be taxed. It is unsatisfactory for the uncertainties and anomalies in the existing system to be addressed only in successive waves of complex anti-avoidance legislation.

Overview

This clause and schedule introduce Off-Payroll Working (OPW) rules to the private sector and amend the OPW rules currently applying to the public sector. These changes are now due to take effect from April 2021.

The extension of the OPW rules to the private sector (other than those private sector entities which are 'small') means that:

- Clients (i.e. private sector businesses and other entities, such as charities, and all public bodies engaging workers' services indirectly through intermediaries, typically a Personal Service Company (PSC)) will need to determine whether the IR35 rules apply rather than the worker and his/her intermediary vehicle.
- Clients will need to consider the status of existing workers before 6 April 2021 for all existing contracts extending beyond April 2021, in addition to considering the status of workers for contracts entered into or amended on or after 6 April 2021.
- Clients and agencies will need to account for PAYE and NIC where a worker is a 'deemed employee' for OPW purposes, including the potential transfer of the PAYE and NIC liability up the supply chain where there is non-compliance.
- Where the OPW rules apply, clients (including public sector bodies) will need to pass on a formal Status Determination Statement (SDS), explaining their reasoning, to the worker and to any agency they may contract with in relation to the worker's services (and that agency will need to pass on the SDS to any agency they contract with further down the supply chain).
- Clients (including public sector bodies) will have to establish an appeals process, so that workers can challenge the client's determination if they wish to do so, with a 45-day timescale in which they must respond.

CIOT comments

New Clause 1 (NC1) introduces New Schedule 1 (NS1), which makes provision for new OPW rules to take effect from 6 April 2021.

Our comments on NS1 are set out below.

UK presence and residence

Paragraphs 3(2)(b) & 3(5), 4(2)(za) and 5/Section 60I (When a person has a UK connection) –
Excluding persons (i.e. businesses, in this context) that do not have a UK connection from being required to operate the OPW rules is a sensible and practical change from the original proposal. Enforcing OPW rules against a business with no presence in the UK (even where that business is engaging a UK-based worker via a Personal Service Company (PSC)) would have been very difficult. The UK-based worker and their PSC will, of course, still be required to apply the existing IR35 rules.

Paragraphs 3(2)(b) & 3(5), 4(2)(za) and 5/Section 60I –
We assume that "*resident in the United Kingdom*" (section 60I(1)(a)) means resident under the UK tax code and that double tax treaty (DTA) non-residence does not count. For example, normally, where a company is dual resident and there is a DTA between the UK and the other country containing a residence tie-breaker for companies and, under that tie-breaker, residence is awarded to the other country, the company is 'treaty non-resident' and the tax consequences of non-residence apply in the normal way. We assume that the normal tax consequences of non-residence will not apply for OPW purposes where a company's non-residence is solely 'treaty non-residence' (i.e. they will be treated as UK-resident for the purposes of this legislation) but would welcome clarification on this point.

Exemption for small businesses

Paragraph 5 (When a person qualifies as small for a tax year) –
The carve-out exempting small private sector entities (e.g. companies, partnerships, LLPs, joint ventures, etc) from the OPW rules is welcome, although we think it would have been better to have excepted small public sector bodies, such as academy schools, from having to operate the OPW rules as well.

Paragraph 5 (Section 60A) (When a company qualifies as small for a tax year) –
This sets out the basic conditions for when a private sector company qualifies as small and is exempt from the OPW rules for a tax year. Section 60A(2) provides that a company will always be small for its first financial year and section 60A(3) adds that a company is small if the '*small companies regime applies to the company for its last financial year that is relevant to the tax year*'. While we understand this phrase to mean that the definition of 'small' in the Companies Act 2006 (CA06) applies to determine whether a company is small, we think it would be better if the legislation specifically signposted the relevant CA06 definitions.

Paragraph 5 (Section 60G) (Sections 60A to 60F: connected persons) –
The application of the CA06 turnover test in determining whether a company is small for OPW purposes requires that account be taken of any business which is 'connected' to that company. That includes any business run by a 'connected person' such as a close family member. This said, the business of a connected person may in no way be related to the company, this being because the definition of connected person is very wide. For example, a company controlled by one family member (which may be very small) can be treated as connected with a (perhaps very large) business controlled by another family member even where the businesses are quite separate. So, this approach will mean that some businesses that might *prima facie* look to be small will in fact not qualify for exception from the OPW rules.

Paragraph 5 (Section 60H) (Duty on client to state whether it qualifies as small for a tax year) –
The inclusion of an obligation on a client to state whether it qualifies as small for a tax year, if requested to do so by the client's agent or the worker, is welcome.

Deemed employer

Paragraph 12 –
We think it would be desirable to add a requirement that, if the OPW rules apply and PAYE and NIC must be accounted for, then any agency with whom the client contracts (the first agency) should confirm to the client whether they are the deemed employer (fee payer), or if not who is. If the first agency isn't the deemed employer, then it will also be necessary to require that there is suitable messaging up the agency supply chain for the first agency to comply with this requirement. We think this will improve compliance within the supply chain and also provide the client with assurance that PAYE/NIC deductions are being duly accounted for (see below for a brief explanation of supply chain integrity).

Status Determination Statements

Paragraph 12 (Amendments to Section 61N) (Worker treated as receiving earnings from employment) –
The legislation (section 61N(5)) only refers to a client giving a Status Determination Statement (SDS) to the worker and not, where relevant, to the client also giving a SDS to their agency (nor that agency passing the SDS down the supply chain where it extends beyond the first agency). We accept that new section 61N(8)(za) means that if an agency in the chain has not received an SDS from the agency immediately above them in the chain, then they are not a 'qualifying person' for the purposes of the OPW rules – meaning that the client (or the last agency to receive the SDS) remains liable for PAYE/NICs where the OPW rules apply, apparently regardless of whether anyone else does so. Nevertheless, we think there should be an explicit requirement for the client to pass the SDS to the agency they contract with, and for the SDS to be passed down the supply chain until received by the deemed employer (fee payer). An explicit requirement to pass on the SDS will, among other things, provide assurance that the client (and agency) is not in breach of data protection laws when conveying details of the worker's status determination.

Paragraph 13 (Section 61NA) (Meaning of status determination statement) –

This provides that a SDS issued by the client must state the client's decision as to whether an engagement falls within the OPW and must also include the reasons for reaching that decision. The legislation requires the client "*to take reasonable care*" in reaching its decision. The legislation is not specific as to the form the Status Determination Statement (SDS) should take and we would suggest that the legislation prescribes that the SDS be in writing (to include electronic notification).

Paragraph 13 (Section 61NA) –
The legislation only explicitly requires a Status Determination Statement (SDS) to be issued where the client thinks the OPW rules apply. The issuing of a SDS in such circumstances, assuming reasonable care is taken in reaching the decision and that the SDS is notified to the client's agency (where relevant), absolves the client from the liability for PAYE and NICs. This said, there is no explicit obligation for a client to issue a SDS where it considers that the OPW rules do not apply. Albeit there is an incentive to do so in that, assuming reasonable care was taken in reaching the decision that the OPW rules do not apply, this provides the client with protection from liability to PAYE and NICs if the SDS subsequently proves to be incorrect. However, it is unclear where liability for PAYE/NICs lies in a case where a client has incorrectly issued a SDS stating that the OPW rules do not apply but has taken reasonable care in doing so. We think this point needs clarification.

Paragraph 14 (Amendments to section 61O) (Conditions where intermediary is a company) –
This amendment applies where the worker's intermediary is a company (i.e. a Personal Service Company (PSC)) and introduces two new conditions (at section 61O(1)(b)(ii) and (iii)) on when the worker is to be treated as receiving earnings from employment under section 61N. These new conditions concern receipt of (or entitlement to receive) a 'chain payment' by the worker from the worker's intermediary. This seems strange as our understanding is that the chain payment rules in section 61N are aimed at the flow of deemed employment income from the client to the worker's PSC, not from the PSC to worker. In any event, it is unclear to us why these new conditions are necessary. Furthermore, we are not sure whether a dividend payment from the PSC to the worker (as shareholder) (or entitlement to such a payment) is to be regarded as a 'chain payment' for this purpose? It would be helpful if the government could set out what the purpose of this part of the legislation is.

Paragraph 16 (Section 61T) (Client-led status disagreement process) –
This clause introduces a new obligation on clients (businesses engaging off-payroll workers) to reconsider their status determinations if asked to by the worker or the deemed employer (fee payer). It permits a worker or the deemed employer (fee payer) to dispute the client's Status Determination Statement (SDS) (typically where the client has determined that the OPW rules apply but the worker disagrees).

The addition of a requirement for representations to the client to have to have been made before the final chain payment is made to the worker's intermediary is welcome. While an obligation to initiate a dispute within, say, 30 days of receiving an SDS might be preferable, the approach provided for in the legislation will allow the worker (or deemed employer) to query his/her status at any point during the contract (for example, in the event of a change in how services are provided which may require the position to be reviewed).

That said, the legislation requires that the process must be initiated "*before a final chain payment is made*". We assume this refers to the final payment from the deemed employer to the worker's intermediary, but given the new section 60O(1) requirements (see above) if the worker pays him/herself more salary or dividend does this then extend the time limit? Again, clarification would be appreciated.

Paragraph 16 (Section 61T) –
Where a client originally decides the OPW rules apply and issues a Status Determination Statement (SDS) accordingly and subsequently, on appeal, changes their mind, then under section 61T(2)(b) they are to issue a "new SDS". But section 61NA, which defines an SDS, does not appear to provide

for an SDS which correctly says the OPW rules do not apply. It only provides for an SDS to "*incorrectly*" say that the OPW rules do not apply. So, we are unclear what "new SDS" section 61T(2)(b) is referring to. Again, this is a point which needs clarification from government.

Paragraph 16 (Section 61T) –
Section 61T does not provide for what should happen while the client is considering the worker's appeal. For example, the original Status Determination Statement (SDS) will have been notified to an agency who will have passed it down the supply chain. Is that original SDS still valid while the appeal is determined (HMRC's draft guidance implies that it is and that the deemed employer (fee payer) remains responsible for deducting PAYE/NICs during the disagreement process)? If this is so, we consider that the legislation should specifically say that the deemed employer (fee payer) must continue to apply the originally notified SDS to any payments made in the intervening period and until notified otherwise, i.e. even if they are aware that the SDS has been appealed.

Paragraph 16 (Section 61T) –
Where the client decides its original decision was incorrect section 61T(2)(b) requires a new Status Determination Statement (SDS) to be issued and for that SDS to state when the new SDS conclusion became "*correct*". If this results in a worker's status falling outside of the OPW rules from that point – which could well be from when the work first commenced – but PAYE/NIC has already been deducted from payments to the worker's Personal Service Company (PSC) it is presumed that the deemed employer (fee payer) (i.e. the entity responsible for accounting for PAYE and NICs under the OPW rules) will need to regularise the position retrospectively from a payroll perspective, adjusting across tax years where appropriate. And that similar corrections would be required from the perspective of the Personal Service Company (PSC) and the worker's own tax position. HMRC's draft guidance indicates that corrections would, in the first instance, be made through the deemed employer's (fee payer's) payroll but this is likely to only be possible within the same tax year and further guidance from HMRC on the processes for corrections, especially where payments relate to a prior tax year, would therefore be welcome.

Paragraph 16 (Section 61T) –
While a client must take reasonable care when reaching a status determination, there does not appear to be any requirement for them also to exercise reasonable care in considering the representations made by the worker (or deemed employer), both in cases where a decision that the OPW rules apply is affirmed or where it is reversed. We suggest that a requirement for reasonable care be incorporated in the same way as is prescribed for the original decision-making process at section 61NA(2).

Recovery of PAYE debt

Paragraph 19 (Section 688AA) (Workers' services provided through intermediaries: recovery of PAYE) –
This section makes provision for HMRC to amend the Income Tax (PAYE) Regulations 2003 to allow for the transfer of liability to the client or the first agency in a supply chain (i.e. the agency the client contracts with) when there is "*no realistic prospect of recovering [the PAYE debt] from the deemed employer within a reasonable period*". The technical note accompanying the two sets of draft regulations published earlier this year notes (at paragraph 10) that HMRC will not exercise this power to transfer unpaid PAYE and NIC debts in cases of genuine business failure of the deemed employer. This is a welcome clarification, but we consider that, given its importance, it should be reflected in new section 688AA and not left to a technical note.

***Paragraph 19 (Section 688AA)* –**
We consider that where the client, or the agency which the client contracts with (the first agency), has taken reasonable care to ensure the integrity of the supply chain but, for some reason, there is a default and HMRC is unable to recover PAYE/NICs from the party concerned it is not fair or proportionate for the liability to be transferred up the chain to the client or first agency. Rather

we think it right that the transfer of debt provisions should be tempered in cases where the client/first agency has taken reasonable care to ensure the integrity of the supply chain (see below), that PAYE/NIC obligations are complied with etc. but that, notwithstanding this, a default has occurred outside of their control. Accordingly, we recommend that the legislation is amended to prevent the transfer of a tax debt in these circumstances and that, instead, the liability to account for PAYE/NIC reverts to the Personal Service Company (PSC) (i.e. the worker's company) in the same way as would have applied had the client been 'small' and the OPW rules not been applicable.

(NB. Integrity in the supply chain – Many businesses undertake rigorous due diligence activities, including basic tests of financial competence, ownership structure, accuracy of information supplied, etc, with those businesses they engage with both before engaging with them and periodically. They also require any agency they contract with to undertake similar activities with any sub-agency they contract with in longer supply chains – such chains are sometimes inevitable when, for example, a business is seeking to engage a specialist, as that worker/the worker's PSC is likely to be registered with a specialist (and potentially local) agency rather than the (national) agency the business normally contracts with. These checks allow a business to be confident that there is supply chain integrity and that they are dealing with parties that will account for, for example, taxes in accordance with relevant legislation. Where businesses have taken measures to ensure that they are dealing with competent parties it would seem unfair to penalise them in the event that a legitimate business further down the supply chain has for reasons outside their control not been able to pay to HMRC taxes due.)

Research and Development Tax Credits

Paragraphs 21, 22 and 23 (Amendments to CTA 2009 (Additional relief for expenditure on research and development)) –
These paragraphs are new (when compared with the version of the legislation included in the Budget Resolutions). The amendments and additions are aimed at ensuring that relevant payments falling within the OPW rules will be treated as a 'staff provision payment' for the purposes of claims for relief for expenditure on research and development and are a helpful clarification in this respect.

Transitional Provisions

Paragraphs 30, 31 and 32 (Transitional provisions) –
We welcome the confirmation that chain payments, or part of a chain payment, made on or after 6 April 2021 relating to services performed before 6 April 2021 are excluded from the new OPW rules.

Paragraph 33 and 34 (Transitional provisions) –
These provisions allow for Status Determination Statements (SDS) to be validly issued before 6 April 2021 for services that are to be performed on or after 6 April 2021 and for workers etc to dispute those SDSs. This is welcome as it allows for both early notification of status by clients to workers and for workers to engage with such businesses ahead of time where the SDS is disputed. This should help ensure that clients, workers and deemed employers (fee payers) know where they stand in relation to ongoing contracts that span the 2020/21 and 2021/22 tax years.

Further proposal – review of employment status (implementing '*The Good Work Plan*')

We recommend building a roadmap to address the complexity in determining employment status generally.

The 'gateway' conditions as to (i) when the new IR35 off-payroll working rules apply (and who the 'client' is), or (ii) when the old IR35 rules apply, or (iii) when IR35 does not apply to an engagement, are very complex.

Furthermore, determining status (or deemed status in the context of IR35) is also notoriously difficult. Indeed, this complexity has been noted in many recent Tax Tribunal cases with decisions on status running to well over 100 pages of detailed analysis. Businesses cannot be expected to devote the time and expertise required to reach such nuanced decisions. A better way of determining status is needed.

We think there needs to be a wide, open and very public debate on the tax treatment of different kinds of work structures and would urge the government to work with stakeholders, businesses, unions and individuals to facilitate a broader debate to identify what is meant by employment (and self-employment) with a view to agreeing a sustainable solution to how earnings (whether from employment or self-employment or via an intermediary) should be taxed, including how each status should be defined, what rights, benefits and obligations should be associated with each, and to what extent, and how, we might level the playing field.

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