

# IR35

Guidance for KCC Schools



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## What is IR35?

IR35 is tax legislation that is designed to combat tax avoidance by workers supplying their services to clients via an intermediary, such as a limited company, but who would be an employee if the intermediary was not used.

'Disguised employment' can save the engaging organisation a significant amount of money as they do not have to pay employers' NICs, and it also means they do not offer any employment rights or benefits.

It has been in place officially since 1999, however it has been heavily criticised and therefore has been reviewed by HMRC. Changes have been made impacting the public sector.

## Summary of Changes

- New HMRC legislation comes into effect on 6 April 2017
- The responsibility for determining employment status within the public sector changes from the worker to the end-client. The end-client is KCC
- HMRC deem the public sector to be all organisations subject to the Freedom of Information Act.
- This legislation affects all payments made on or after 6 April 2017. Whether the work has actually been completed or not is irrelevant
- All assignments need to have their employment status checked using a new tool provided by HMRC
- The new tool is on the HMRC website and called the Employment Status Service (ESS). It can be accessed at the following address:

<https://www.tax.service.gov.uk/check-employment-status-for-tax/setup>

Key terminology can be found in [Appendix A](#)

## Overview of the Employment Status Service (ESS)

The ESS tool will ask a series of questions around the assignment before providing a final answer as to whether the employment is considered employment, or not.

The answers will be one of the following:

- In scope of the intermediaries legislation (i.e. this means the assignment is considered by HMRC to be employment)
- Outside scope of the intermediaries legislation (i.e. this means the assignment is considered by HMRC to be self-employment)
- Undecided (i.e. not enough information can be provided for the assignment to make a definite decision)

More detail around the key questions used in the ESS are in [Appendix B](#)

## **In Scope of the intermediaries legislation**

If the outcome of the test states the assignment is in scope of the intermediaries legislation, then payments made to the worker must be considered employment.

**This means that Income Tax (PAYE) and Employee's National Insurance needs to be deducted, and Employer's National Insurance and the Apprenticeship Levy paid by the employer (KCC).**

## **Outside Scope of the intermediaries legislation**

If the outcome of the test states the assignment is outside the scope of the intermediaries legislation, then payments made to the worker are considered to be self-employed.

**This means invoices can be paid as normal, and there is no change.**

## **Undecided**

If the outcome of the test is indecisive, the assignment requires further investigation. Guidance is provided in [Appendix C](#), but advice should be sought from the Chief Accountant Team.

## **Types of Engagement**

Engagements with workers are made either:

- directly with the worker, or
- through an agency

## Direct Engagements

The ESS tool must be used to assess current and new assignments. This is to ensure that any changes to the way workers are paid can be made.

### Inside Scope Direct Engagements

If a direct engagement is considered inside scope, they can no longer be paid directly by KCC, as Income Tax PAYE and National Insurance must be accounted for.

The worker should be advised, using the letter in [Appendix D](#), that they should join an agency. We suggest Connect2Kent, as the preferred Agency. The worker may benefit from seeking advice from their accountant and Connect2Kent staff can advise the best way forward.

### Outside Scope Direct Engagements

If a direct engagement is considered outside scope, payments can be made in the same manner as they have previously.

The worker should be advised, using the letter in [Appendix E](#), that there will be no change to the way they are paid.

## Agency Engagements

The ESS tool must be used to assess current and new assignments. This is to ensure that any changes to the way workers are paid can be made.

### **The Agency must be informed of the result.**

This is so they can make the appropriate Income Tax and National Insurance deductions as required.

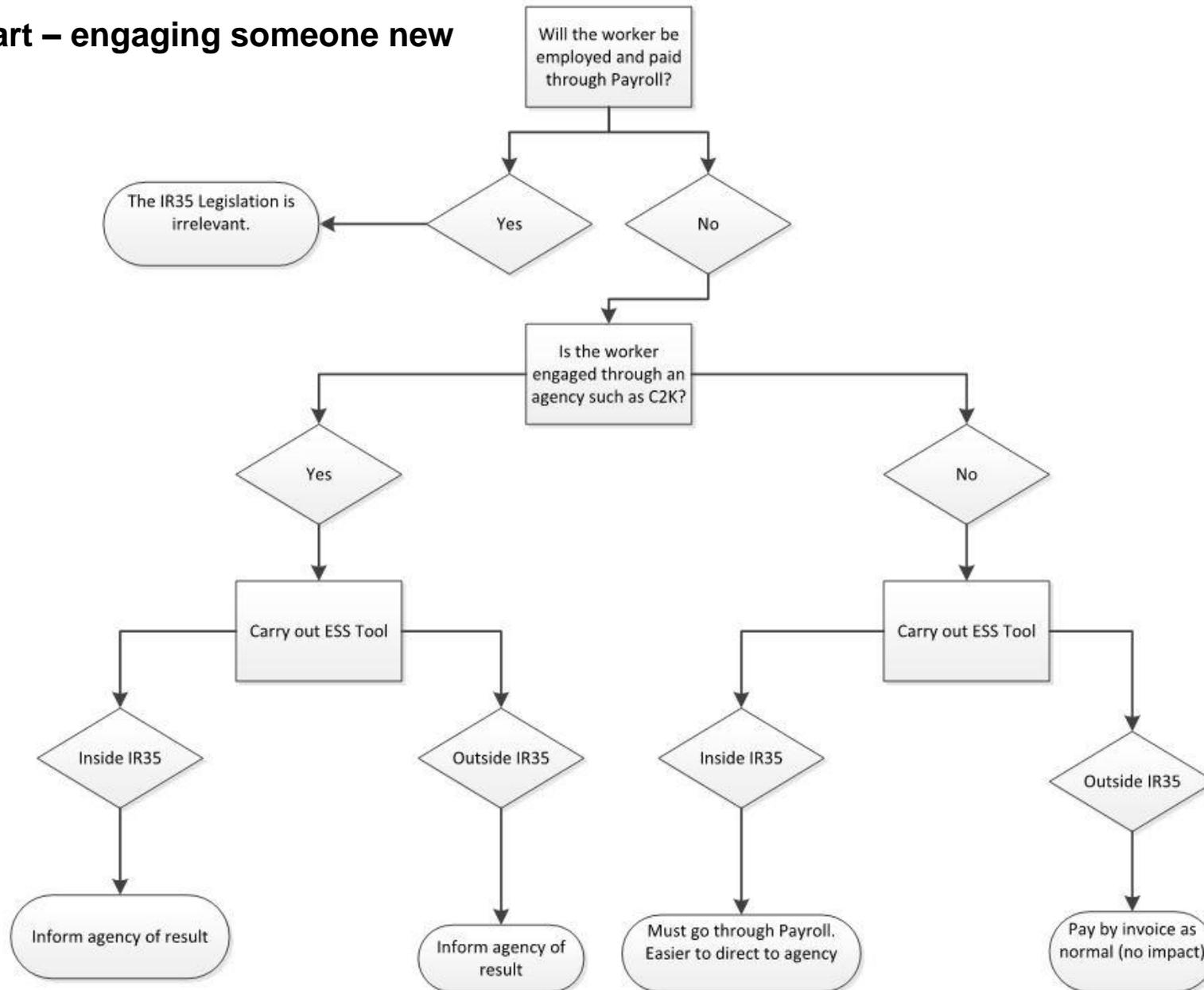
## Potential Penalties

KCC could face penalties from HMRC if we are not compliant with the legislation. This could mean the manager's budget will become liable for the contractor's tax and National Insurance contributions (amount dependent on their tax rate), plus Employer's National Insurance contributions, which could be over 50% of the invoice value. HMRC could also issue penalties and interest charges.

### **Example Penalty**

As an example, on a £50,000 invoice, the total unpaid tax and National Insurance would be £27,500, plus a potential penalty of £8,100, which would be charged to the manager's budget.

# Flowchart – engaging someone new



## Appendix A | Key Terminology

<b>Intermediary</b>	A limited company, partnership, or sole trader who/which is engaged to complete a piece of work / cover a job role
<b>Substantive Post</b>	A permanent position in your organisation, for example Headteacher, Secretary, etc.
<b>Office Holder</b>	<p>A permanent, substantive position that exists independently from the person who fills it.</p> <p>Holding office includes board membership or statutory board membership, or being appointed as a treasurer, trustee, company director, company secretary or other similar statutory roles.</p>
<b>Personal Service Company (PSC)</b>	<p>A limited company that typically has a sole director, the contractor, who owns most or all of the shares.</p> <p>The contractor's PSC generally supplies professional services personally, either directly or via an agency.</p>
<b>PAYE</b>	Pay As You Earn
<b>NI</b>	National Insurance

## Appendix B | Key Questions

### “Which of these describes you best?”

KCC is the end client, so this option should always be used.

### “Is the worker or their business an office holder for the end client?”

An office holder is a statutory appointment, such as a company director, company secretary, board member or trustee.

An office holder **is not** someone covering a permanent role in your organisation.

### “Would the end client accept the worker’s business sending someone else to do this work instead?”

This is a key question and you should ensure it is answered accurately. Consider whether you would be happy if someone else completed the work who was not who you originally engaged.

It’s also worth noting that the worker would choose the substitute, with no involvement from KCC. The worker would pay the substitute, rather than KCC.

Upon HMRC challenge, if it was found you would not accept a substitute, KCC could become liable for the tax and National Insurance, and face penalties.

### “What does the worker have to provide for this engagement that they can't claim as an expense from the end client or an agency?”

The options are:

- ✓ Materials
- ✓ Equipment
- ✓ Vehicle
- ✓ Other Expenses
- ✓ Not relevant

The expenditure incurred under the headings material and equipment must be significant and not reclaimed as part of the hourly rate / invoice.

The use of a vehicle and other travel related expenditure must relate to work tasks, **not commuting**.

### “What’s the main way the worker is paid for this engagement?”

An hourly, daily or weekly rate is likely to result in the engagement being employment.

However, a fixed price for a piece of work is more likely to deem the engagement to be self-employment.

**“If the end client isn’t satisfied with the worker’s output, when would the worker have to put it right?”**

If the worker would have to rectify any issues, it’s important to note the distinction between two of the options:

“In their usual working hours at the usual rate of pay” is a very strong indication of employment, as they have no financial risk.

“Outside of their usual working hours at additional cost to the worker” is a very strong indication of self-employment, as the worker takes on the risk if work is unsatisfactory or not as per the agreement.

## Appendix C | Employment Status Further Questions

Factor	Self-employed	Employee
<b>Personal service</b>	Will provide own services, but may sub-contract work to others, or have assistance	Only provides own personal services
<b>Mutuality of obligation</b>	Is free to accept or turn down work if he desires. The engager is under no obligation to offer work	The employer is obliged to offer work, and the employee is obliged to accept
<b>Right of control</b>	Likely to be in control of most aspects of the work done	An employer controls what, how, where and when work is done
<b>Right of substitution</b>	May sub-contract work, or bring in assistance	No right to appoint a substitute
<b>Provision of own equipment</b>	Will normally supply all small tools and bring in or hire necessary equipment	Employer will provides necessary equipment
<b>Financial risk/ability to profit</b>	Will quote on a job-by-job basis and is able to make more profit by more efficient working, but may incur loss if overruns on time, or if required to rectify poor work in own time	Paid whatever work is done, statutory holiday entitlement, little risk
<b>Opportunity to profit</b>	Can profit if work is performed efficiently, or from re-charging and making a profit on materials	No opportunity for 'profit', just workplace rewards
<b>Length of engagement</b>	Generally fixed-term or short-term contract.	Permanent contract (no end-date)
<b>Part and parcel of the organisation</b>	May become "a fixture" in that his work brings him to the organisation regularly, but no additional responsibilities	Part of the organisation's structure, capable of being promoted, or manages other staff
<b>Employee type benefits</b>	Unlikely to be entitled to any type of benefits	Pension scheme, canteen, car parking, attends staff functions
<b>Right to terminate contract</b>	If other party is in breach	Would normally give notice
<b>Mutual intention</b>	The intention of the parties should be stated in written contract. This may not be persuasive if in reality the parties behave differently.	If the parties intend the relationship to be one of employment it is difficult for the courts to say otherwise. In most cases the parties will have agreed written terms of employment and the employee will have enforceable rights under employment law

## Appendix D | Template Letter (Direct, In Scope)

Dear **Worker**

Further to your upcoming engagement with Kent County Council, I can confirm that, as a result of the HMRC Employment Status Service, the assignment is considered to be inside IR35 (i.e. deemed to be employment).

As Kent County Council is subject to the Intermediaries Legislation, the authority's preferred method is to engage workers via an Agency.

If you have any queries, or would like to challenge this outcome, please contact me using the contact details provided.

Yours sincerely,

**Your details**

## Appendix E | Template Letter (Direct, Out of Scope)

Dear **Worker**

Further to your upcoming engagement with Kent County Council, I can confirm that, as a result of the HMRC Employment Status Service, the assignment is considered to be outside IR35 (i.e. deemed to be self-employment).

Although Kent County Council is subject to the Intermediaries Legislation, I can confirm that there will be no change in the payment terms of your assignment.

If there are changes to the assignment in the future, the Employment Status Service will need to be used again.

If you have any queries, please contact me using the contact details provided.

Yours sincerely,

**Your details**