

IR35 Overview

This legislation was brought in with effect from April 2000. Basically it attempts to cut off the advantages of a limited company which are mainly in saving National Insurance and to some extent personal tax. It says that if the limited company was ignored would the relationship between contractor and client be considered one of employment or self employment. If employment then the legislation applies. The tests for determining employment/self employment status have been built up through case law. Although it is possible to go through a list of these ticking them off as you go the Courts maintain that this is not the correct approach and we are left with a very subjective exercise in determining if the legislation applies. This provides difficulty for the contractor but still more difficulties for the Revenue. The Contractors Accountant Ltd can provide guidance on your position and how to minimise your chances of being subject to the legislation.

The Revenue has issued their guidance notes, which, if you would like further background, can be found on <http://www.hmrc.gov.uk/ir35/>. This gives an outline of the law as they see it and is specious to say the least. Even so it should be possible for most IT contractors and other professionals to negotiate their contracts to fall outside of the scope of the legislation following their guidelines, let alone what the law says. Most agencies have contracts that can avoid IR35 if appropriate. We set out below our suggestions on the construction of contracts. Bear in mind that these suggestions are from a taxation point of view and if you are in any doubt about your contractual obligations you are advised to consult a solicitor. We can recommend a solicitor if required.

The Contract

The legislation refers to the 'arrangements' under which the assignment is undertaken. Having examined the written contract you have to look beyond to see what the underlying relationship is, although a well drafted contract is more than a good start.

We set out below some suggestions for contract clauses although in practise most agencies will have something like this in their contract. The particular area will have a number after it indicating the importance. A **10** indicates the most important. The italics are our comments. This will address the client's concerns and how these may be mitigated. It would be helpful if you are working through an agency for their contract with the client to mirror your contract with the agency. In practise you will not be privy to this. Please note that we have prepared these clauses rather than a lawyer so they will require putting into legalese.

Substitution Clause (10):

Ideally no person should be named in the contract. If no-one is named then the requirement to have an obligation to perform the services personally, which the legislation requires, is difficult to prove.

Otherwise you clause enabling someone else, other than the named contractor, to perform the services is very helpful. The less fettered the right to put someone else in place the better.

Control (10):

You will not be deemed an employee if there is no right of control. Control means what, where, when and how. The fewer stipulations in this area the better, particularly on how the job will be carried out. Surely your clients employ you for your knowledge and experience? They will not be telling you how to do your job.

What you should do is:

- Have the precise services that your company will provide set out in the contract.

- Do not have the times you will attend specified.
- Try to avoid clauses that stipulate that you must work at the client's premises even though this is what is intended.
- Do not have a job title stipulated in the contract nor have anything like a job specification included.

The deliverables in the contract should be enough comfort to the client that you will be attending their offices. Be careful to ensure that the client does not have the right to direct you to work in areas other than those stipulated in the contract.

Now your agency or client may not like something as non-specific as we are advocating but you are contracted to provide professional services that will be specified. It should be obvious that you will have to attend the client's premises in order to fulfil your obligations. With regard to the hours that you put in, the reason that you have entered into the contract is that you want to work and the client wants you to work. Do you need to have this specified? We see the concept of an obligation to work a "professional day" in some contracts which is quite good.

Having established the services to be provided then you should have a clause stating what should happen if such services are not provided. For example, " In the event that the company, in the opinion of the agency / client fails to provide the services contracted for, then the agency / client will one week after the failure write to the company pointing this out". Notice of such failure should not be served on the "agreed consultant". See the section on financial risks for a more comprehensive clause covering both areas.

From the previous paragraph it follows that there is no control of the consultant. All services are agreed in the contract, which the consultant will carry out. If there is a problem the client goes back to the company who can then decide how to rectify this - they may want to change the consultant. But no control over the consultant is exercised. If you ever get to this situation with your client you probably have a problem anyway. Another positive point for the agency / client, in theory.

Mutuality of Obligation (10)

Basically this means are you obliged to provide services and/or is the client obliged to take the services that you provide. If not then there is no Mutuality of Obligation(MOO). If there is no MOO then this is an overriding test and IR35 does not apply. This can be achieved by either, but preferably both, parties having the right to give immediate notice of termination.

By way of example the Revenue attempted to have a building labourer we dealt with put on employment status. He failed all other tests except that if he turned up in the morning and it was raining he would not be taken on that day. As there is no MOO he could not be considered an employee.

Do you take on a financial risk or risk your own money (8):

Usually other than a bad debt risk the answer is no, although it can be argued that by entering into this arrangement the employment legislation requirements are transferred to your company . A fixed price contract would pass this test. Similarly a requirement to carry professional indemnity insurance "or otherwise make provision to cover the costs of negligent work" would be a relatively inexpensive and convenient way of showing risk is taken. Interestingly the Revenue is recognising training as an intangible asset risking your money.

A clause along the following lines is helpful: "Where the company has been notified of a failure in accordance with

clause xx the client may request from the company that they, at their expense, and as specified by the client, reschedule and perform the services"

Clearly the agency or client will not have a problem with this. You may have but if the client is invoking this you have a problem anyway and so do they.

Although this pointer has a high rating it is unlikely that you will achieve a high 'score' and will you need to compensate for this on the other pointers.

Payment (8):

Avoid mention of overtime, holidays and sickness. If you can try to avoid contracts where you are obviously paid by the hour and if you can agree a fixed fee for a given task then this would be a very compelling indicator of self-employment.

Other minor pointers (4 each):

You should operate like a business with a business like approach to obtaining work including maintain an office (at home) with a PC etc. The more separate sources of income the better. Demonstrate that you market your business when out of contract, a website could be a good demonstration. Of course you will have an accountant! Having to provide significant amounts of equipment is help in establishing self-employed status but for professional services not essential.

A training programme would be helpful.

You should avoid being seen to be part and parcel of the organisation: try to avoid having to manage the client's staff (other than contractors who fall outside IR35). The contract should ideally state that the deliverable is a particular piece of work or project rather than an ongoing one providing service.

How Do We Help?

As well as a free contract review we work closely with one of the leading legal specialists in the area who can undertake a review of your working practices and offer insurance against being caught subsequently. Depending on the gravity of any attack from the Revenue we can deal with this or call on their skills, where they have an excellent record. However the Revenue are finding it difficult to make an impression on professional contractors as it requires a great deal of resource. If having taken our advice you are caught by the legislation then we undertake the necessary administration to ensure that you comply with the Revenue requirements in this area. Please note that the advice above is provided for IR35 purposes only and you should take proper legal advice in respect of other aspects of any contract.