ICAEW
REPRESENTATION 54/19

OFF-PAYROLL WORKING RULES FROM APRIL 2020

Issued 23 May 2019

ICAEW welcomes the opportunity to comment on the *Off-payroll working rules from April 2020* published by HMRC on 5 March 2019, a copy of which is available from this link.

This response of 23 May 2019 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business.

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EXECUTIVE SUMMARY

1. ICAEW believes that as a matter of tax policy, there are three interdependent policy issues that need to be resolved:
   a) the tax, national insurance contributions (NIC) and legal status of work should be the same, certain and comprehensible;
   b) the tax and benefit differentials between different types of work need to be addressed; and
   c) off-payroll working in the private and public sectors should be taxed in the same way.

   While the current consultation specifically excludes these wider considerations, and we acknowledge that this will be challenging for government, failing to address these issues will perpetuate the current uncertainty. The Good Work Plan provides an opportunity to enable all stakeholders to work together to reach consensus on employment, tax and national insurance law.

2. Our major points include:
   a) *April 2020 is too soon*: Adequate lead time will be needed if off-payrolling changes are made in the private sector, so, if implemented, go-live should not be before April 2021 (see Appendix 2 for operational and system issues that businesses will need to address).
   b) *The carve-out for 'small' engagers is welcome as an interim measure but the definition of 'small' is too complicated*: Until the wider policy issues in paras 1a – 1c are addressed, the small engager carve-out is a welcome attempt to simplify the rules for small business, but should be viewed as a temporary measure. Further consideration must be given to the practical implications of using the definition suggested in the consultation document.
   c) As proposed in the consultation document, the transfer of liability could produce unfair results.
   d) There needs to be a real-time, independent statutory method of appeal.

3. In Appendix 3 we set out our general points which we made in 2018 relating to:
   a) *The tax gap*:
      i. We acknowledge the policing problems faced by HMRC.
      ii. An holistic approach is needed: tax/NIC solutions need to be arrived at alongside employment status solutions.
      iii. We are not convinced that the figure of £410m is a useful one in assessing the real success of the public sector reforms, and believe that a further detailed breakdown of the cost (including employers' NIC) of non-compliance in the private sector should be provided.
   b) *Tax differentials*: the cost imbalance between different categories of work needs review.
   c) *Off-payroll working in the public sector:*
      i. It is too early to assess the success of the public sector regime as a full year's cycle (including enquiries into employment status etc) has not been completed.
      ii. As a matter of priority, practical problems with the public sector off-payrolling regime need to be resolved (see ICAEW REP 73/18 letter to FST and ICAEW REP 91/18 letter dated 26 July 2018 to HMRC).
      iii. Members are seeing an increasing number of arrangements following the public sector changes whereby the cost of employer NIC, auto-enrolment costs, apprenticeship levy and holiday pay is being passed on to the contractor.

4. We are concerned that even after the proposed changes neither the public sector off-payrolling regime nor the proposed private sector regime will meet our *Ten Tenets for a Better Tax System* by which we benchmark the tax system and changes to it (summarised in Appendix 1), especially Tenets 2, 3 and 4, ie certain, simple, and easy to collect and to calculate.

MAJOR POINTS

5. We welcome the opportunity to comment on the consultation document *off-payroll working rules from April 2020*, published by HMRC on 5 March 2019.
6. As a matter of tax policy, there are three interdependent policy issues (see below) which are fundamental to this consultation and which must be addressed:
   a) The tax, NIC and legal status of work should be the same, it should be certain, and the consequences should be comprehensible to the engager and worker. There are a number of possible options to explore which would achieve this and these must be considered in conjunction with employment rights to arrive at a balanced and coherent position. We would welcome the opportunity to work with government to develop this.
   b) Work should be taxed in the same way, regardless of the wrapper or status. While we understand that government policy appears to be to provide an incentive for those in self-employment (via lower rates of tax and NIC), we believe there should be a debate about how much such an incentive should be and how it should be targeted. We also understand the government's reluctance to tackle the disparity between the total tax paid by and on behalf of the self-employed and employees; however, the differential remains at the heart of the problem and should be addressed through an informed national debate. We strongly believe that addressing the differential would be the most robust long-term way to restore equilibrium of workers' employment status in the jobs market and to protect Exchequer revenues.
   c) Off-payroll working in the public and private sectors should be taxed in the same way. Having different tax rules is unsustainable in the longer term, leading to greater complexity, unfairness, a greater administrative burden and the likelihood of more mistakes and ultimately non-compliance. However, the changes introduced in 2017 for the public sector are continuing to cause problems and these must be resolved before the same system is extended to the private sector (see our letter to HMRC of 26 July 2018 (ICAEW REP 91/18) for issues in the public sector).
7. We understand that dealing with the above is going to be challenging for government and businesses and we acknowledge that there will be winners and losers. However, failing to address these issues will only add to the current uncertainty faced by businesses and workers. In the absence of a definitive and workable solution the UK will be revisiting the status of work and off-payroll working every few years. We welcomed the government publishing its Good Work Plan on 17 December 2018. We believe that this should be used as an opportunity for all stakeholders to work together to ensure consensus in building a roadmap which provides clarity and consistency and also levels the playing field in terms of the amount of tax paid by, and benefits and rights afforded to, people in similar situations, while ensuring parity across both the public and private sectors, and compliance with our Ten Tenets for a Better Tax System summarised in Appendix 1.
8. In our response to HMRC's May 2018 consultation (ICAEW rep 94/18) we asked that any change to the private sector should not be introduced until April 2020 at the earliest, to allow sufficient time for HMRC to provide guidance and software specifications based on enacted legislation and for businesses to review their internal processes, amend current systems or purchase and test appropriate software. We are pleased that the government listened. However, the current consultation document was not published until four months after the Budget 2018 announcement was made, thus eroding much of the benefit of the

postponement to April 2020. We strongly believe that a further postponement to April 2021 is required to give businesses adequate time to prepare for the new rules especially given the need to resolve the issues that have arisen within the public sector implementation.

9. ICAEW welcomes the exemption for small engagers as an attempt to simplify the rules. However, we strongly believe that having different tax rules for some engagers in the private sector is unsustainable in the longer term, leading to greater complexity, unfairness, a greater administrative burden and the likelihood of more mistakes and ultimately non-compliance. Meanwhile the definition of ‘small’ is too complicated. The exemption should be viewed as an interim measure to alleviate the considerable administrative burden for small engagers, until such time as the government has addressed the wider policy issues noted at paras 1a-1c. There are a number of practical considerations that require further consideration for the exemption to be workable, including at which point in time the test should be performed together with when the new rules should be operated - for example at the start of the following tax year. Also how the size of the engager is communicated down the labour supply chain and by when. It will be necessary to consider anti-avoidance rules to prevent the fragmentation of a large client into many small entities who could then engage all the contractors and supply them to the fragmented client.
10. As proposed, the transfer of liability is likely to result in unfair outcomes in particular where the end client has taken reasonable care to ensure it only engages with reputable third parties. We believe the transfer of liability needs further consideration and stronger safeguards.

GENERAL COMMENTS

April 2020 is too soon

11. The timing of any change in the private sector must be considered carefully. UK businesses are already having to implement software and process changes for Making Tax Digital (MTD) and the full extent of the impact of Brexit is still unknown. In ICAEW rep 94/18 we asked that any change to the private sector should not be introduced until April 2020 at the earliest, to allow sufficient time for HMRC to provide guidance and software specifications based on enacted legislation and for businesses to review their internal processes, amend current systems or purchase and test appropriate software. We are pleased that the government listened. However, the consultation document was not published until four months after the Budget 2018 announcement was made, thus eroding much of the benefit of the postponement to April 2020.
12. Members are telling us that engagers will require at least 12 months to amend their systems and link payroll with the systems that pay contractor invoices and ensure that the correct VAT is paid.
13. Draft legislation is not expected to be published until Summer 2019 and it is only from this point that businesses are likely to invest in software and the process changes needed to comply with the new rules. It seems likely that draft legislation will need to be supplemented by extensive HMRC guidance. We have a number of concerns with this:
    a) The rules should be in legislation rather than guidance.
    b) Recent experience has shown that guidance is not usually available until some months after the draft legislation has been published. For example, the termination payment guidance was not available until the day the legislation entered in to force.
    c) The guidance, when published, is unlikely to be comprehensive nor to cover all the issues within the legislation. Again for example, see the termination payment guidance.
14. The guidance should ideally be published for consultation in draft form. Issuing the draft guidance alongside the draft legislation would enable a more comprehensive review. We consider this to be particularly important as very many of those who will need to understand and rely on it will not be tax specialists.

15. We are aware that the check employment status tool (CEST) is being updated, and ICAEW has worked closely with HMRC on this project. We understand that the updated version of the tool is due to be released in March 2020. This is too close to the start date and does not give businesses adequate time to review the employment status of the individuals they engage. As a result some contracts will be put on hold pending the release of CEST which will negatively impact on the productivity of UK business and there will be a commercial advantage to small engagers who will not require use of CEST.
16. The overall package is therefore unlikely to be known until very close to the April 2020 implementation date. As such, we strongly recommend that the government considers a further postponement to the start date of the reform to April 2021 at the earliest.

The carve-out for 'small' engagers should be an interim measure and the definition of 'small' is too complicated

17. The consultation proposals have attempted to simplify the impact of the change by excluding contracts undertaken with smaller clients. This will mean that smaller organisations taking on workers off-payroll will continue to follow the existing rules.
18. We welcome the government's attempt to simplify the current proposals for the off-payroll rules by excluding smaller engagers however we do not think this carve-out is an appropriate long-term solution.
19. The UK will continue to have two systems for dealing with off-payroll working. The dividing line will now be within the private sector, based on the size of the client, rather than having the public/private sector division introduced in April 2017. Contracts with larger private sector clients will use the same rules as public sector clients, leaving those with small clients using the existing rules. The size definition, responsibility for determining the size of a client, and communicating it to all parties, therefore becomes a fundamental part of the system.
20. Off-payroll working in the public and private sectors should be taxed in the same way. Having different tax rules is unsustainable in the longer term, leading to greater complexity, unfairness, a greater administrative burden and the likelihood of more mistakes and ultimately non-compliance.
21. The exemption for small engagers should be implemented as an interim measure until such a time that the government has reached a national consensus on the wider policy issues included in paras 1a-1c.
22. We note the proposal to use the definition of small as per s382, Companies Act 2006 to determine whether an engager is small or not and so where the responsibility to assess the employment status of individual contractors lies. We are concerned that the consultation document has over simplified the tests contained in s382.
23. For example, this test must be performed using accounts of the current and prior years. As written, the proposal appears straightforward when in practice it will be more complicated for a business to determine which system applies in time to operate any necessary withholding.
24. In addition, the consultation does not state at which point the test should be performed, nor does it take into account that there will be a time lag before the status can be known. The filing deadline for private company accounts is 9 months after the end of the accounting period and 6 months for plcs. It is not clear from the consultation document how the rules will work where there is a change of accounting date. We presume the rules would apply from the start of the following tax year rather from the start of the new accounting period.
25. For example, a company with a 31 December 2019 year end will not need to file its accounts until 30 September 2020. It would therefore be impractical for the company to use the December 2019 accounts to determine its size for the tax year starting on 6 April 2020. As such we recommend that the test should be performed based on the company's accounts filed prior to the start of the tax year. In this example that would be the accounts to 31 December 2018, filed on 30 September 2019 being used to assess the size of the engager for the tax year starting on 6 April 2020. We have, however, heard conflicting views from HMRC on how this test would work including that you could cease to be small within a tax

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year and have to operate the off-payrolling rules from a date within the tax year. We do not see this as a practical option.

26. Following discussions with HMRC we understand that it is not proposed to require the engager to pass their size determination on to the individual worker or down the supply chain. As such in respect of the worker there are three possible outcomes:
    a) The worker receives a status determination (because the engager is not small) and will be treated as a deemed employee, or
    b) The worker receives a status determination (because the engage is not small) and will not be treated as a deemed employee, or
    c) The worker does not receive a status determination and should assume this is because the engager is small and therefore the individual is required to determine whether the existing IR35 rules apply.

27. Our concern is that silence will not always mean that the engager is small. For example, the individual responsible for passing on the status determination may be on leave, might have left the organisation, or the email/letter could have been lost etc.

28. Without any formal instruction or guidance individuals in outcome c above will not be aware that they have a responsibility to determine their own employment status. Given the current level of non-compliance in the private sector, possibly due to a lack of awareness of the rules, we believe individuals working for small clients will assume it is “business as usual". This will defeat the purpose of the proposed reform. How will HMRC ensure that these PSCs and contractors are aware of their obligations?

29. In addition, a fee payer may not have received a determination because it has not yet found its way down the supply chain. Unfortunately, under the proposal the fee payer will assume this is because the engager is small. Even though the contractor may have received the determination there is no requirement to tell the fee payer to operate withholding. Under such circumstances where there is a delay in receiving the determination what is the situation regarding the individual’s tax position for the period before the withholding is required? Additionally, what is the situation regarding employer national insurance that should have been paid? The answer to these questions is not clear from the consultation documentation.

30. We believe there needs to be a mechanism in place to ensure that agencies, payroll agencies and workers are informed by the end client whether or not that client is ‘small’. This would enable the worker and the organisation which pays the worker’s personal service company to know which set of rules (ie, new off-payrolling rules or existing IR35 rules) apply. This information should be provided to applicants looking for work and to agencies as part of the job specification.

31. Regarding the definition of ‘small’ itself, we believe an alternative to the Companies Act 2006 definition could be used and we propose some potential alternatives:
    a) A definition based on the number of employees on 6 April, ie, X number of employees or less qualifies for exemption, or
    b) A definition based on turnover ie, turnover less than X qualifies for exemption, or
    c) A definition based on the company’s class 1 secondary national insurance liability as at the end of the prior tax year, noting that from 6 April 2020, employers will need to check whether their class 1 secondary NIC liability exceeds the new £100,000 threshold to assess eligibility for the employment allowance.

32. There may be some engagers, particularly at the larger end of the small cohort, which might prefer to simply move into the large system. This would give them certainty over the regime which they need to implement. Further consideration should be given into whether there is sufficient interest in having such an opt in available, and research should be undertaken to see how many small engagers are on the cusp of being ‘large.’

33. There is a greater prevalence for the use of payroll agents and more than one accountant (who might outsource to a bookkeeper) in the private sector. Having clients who vary in size each year will add complexity and cost to the payroll agent sector

34. We also have concerns about if and how HMRC will police the size determination of the client. Does HMRC intend to check the size of each client? If so, the information required to make the determination should be readily available to HMRC and require little or no interpretation by HMRC compliance officers.

Transfer of liability

35. We appreciate the need for HMRC to address potential non-compliance with the rules and we welcome the opportunity to discuss the transfer of liability, however the proposal in the consultation document is likely to produce unfair results.
36. Illustration B in the consultation document proposes that the liability should move down the chain as each party fulfils its obligations, with liability ultimately resting with the end client if other parties fail. We are concerned that this approach could result in an innocent party having an unexpected liability. It relies on smooth communication flows throughout, possibly quite long, supply chains and it would be impractical for HMRC to police this.
37. One suggestion that has been made is that the liability for the employee's income tax and employee NIC might rest with the worker given the purpose of the rules is to ensure the tax almost mirrors that of an employed individual. This has the advantage that the worker will have received a determination from the engager and should, therefore, know whether the fee-payer should operate PAYE. However, HMRC would need to give further consideration to the different scenarios that are likely to occur in practice, including for example:
    a) A "deemed employee" status determination has been made by the client and PAYE and NIC have been deducted by the fee-payer but not yet paid over to HMRC.
    b) A "deemed employee" status determination has been made by the client and PAYE and NIC have been deducted by the fee-payer and paid over to HMRC.
    c) An individual is treated, incorrectly, as being an off-payroll worker and has therefore been paid gross by the fee-payer.
38. We do not believe that it is reasonable for the end client to become liable where they have taken reasonable care to ensure they engage with only reputable third parties. For example, we do not think it is reasonable for the engager to be responsible for failures further down the supply chain where they have engaged workers through gangmasters licensed by the Gangmaster and Labour Abuse Authority (GLAA).
39. Equally we do not believe it would be fair that a contractor who has had tax withheld, but that tax has not been paid to HMRC by the fee payer, to be liable for the tax not paid over. This would be analogous to the situation involving PAYE and an employee.
40. We do, however, believe that if the fee payer and the contractor contrive not to withhold tax when a determination has been made that tax should be withheld, the contractor should not be able to escape any liability for the tax not withheld. This appears to be a weakness in the current proposals.
41. In summary we think that liability and penalties should remain with the person who is responsible for any mischief and not be able to be transferred to persons who have taken reasonable care.

ANSWERS TO SPECIFIC QUESTIONS

DEFINING THE SCOPE OF THE REFORM

Question 1: Do you agree with taking a simplified approach for bringing non-corporate entities into scope of the reform? If so, which of the two simplified options would be preferable? If not, are there alternative tests for non-corporates that the government should consider? Could either of the two simplified approaches bring entities into scope, which should otherwise be excluded from the reform? Is it likely to apply consistently to the full range of entities and structures operating in the private sector? Please explain your answer.

42. We agree that a suitable test needs to be in place for non-corporate engagers. We suggest that this test should mirror the test in place for corporate engagers rather than introducing another set of rules. Our preference would be for the corporate engager test to be simplified as per one of the suggestions in para 31 above with the non-corporate engager test mirroring this.
43. Alternatively, bearing in mind that the absence of a balance sheet on the part of a non-corporate is what drives this question (something only likely to be a consideration for sole traders as partnerships will generally have balance sheets), one possibility would be that, in the absence of a balance sheet, the balance sheet should be assumed to be £5.1m (and thus in the new regime).

INFORMATION REQUIREMENTS

Ensuring information is shared appropriately

Question 2: Would a requirement for clients to provide a status determination directly to workers they engage, as well as the party they contract with, give off-payroll workers certainty over their tax position and their obligations under the off-payroll reform? Please explain your answer.

44. Yes, this would provide certainty to both the party the end client contracts with and the worker.
45. We do however have concerns regarding the practicalities of this working in practice, particularly with regards to timing. The consultation document is silent on when the client would be obliged to do this but we assume the intention is to mirror the current rules in the public sector, ie, for the information to be passed on before the work begins.
46. It is unclear how the worker would dispute the status determination at this point in time. There needs to be an independent and real-time process in place to allow for this that will resolve the status dispute including income tax and NIC issues in one process.

Question 3: Would a requirement on parties in the labour supply chain to pass on the client's determination (and reasons where provided) until it reaches the fee-payer give the fee-payer sufficient certainty over its tax position and its obligations under the off-payroll reform? Please explain your answer.

47. Frequently, senior and highly-skilled off-payroll workers are engaged quickly in response to an emergency situation, for example unforeseen financial losses, sudden departure of key personnel, breakdown of customer relationships, or projects going off-track. In these circumstances, the end-client needs a skilled person to move in rapidly and work intensively on the business problems, not to worry about administrative issues, and it is likely that issues such as status determinations would be pushed to the background, to be resolved later. Trying to resolve these retrospectively could generate substantial conflict and ill-feeling between the parties. Equally, trying to resolve them proactively will delay the engagement starting, delay the start of work which is vital to the business, and undermine the entire rationale for engaging an outside expert quickly to solve a business issue.
48. In marginal cases, of which there would be many where personal service companies are involved, it is unlikely that certainty over the tax position would be achieved. If the client passes on a determination, made in good faith, that a contract is outside the scope of the rules and HMRC disagrees with this, then (if HMRC is correct) it is the fee-payer and not the client that is liable for the shortfall. Bearing in mind that the fee-payer will have virtually no knowledge with which to determine whether HRMC is correct or not, this seems to be an inappropriate outcome.
49. Furthermore while we accept that it might be best practice for all parties in the supply chain to be provided with the status determination we again have concerns over the practicalities of this occurring in reality. Some chains can be particularly long and complex, perhaps including overseas agencies. The passing of information through the chain will rely heavily on smooth communication flows. There could also be lengthy delays in the information reaching the next

party in the chain for reasons outside that party's control. Again, the consultation is silent on time frames for doing this.

50. We would suggest that once the end client has passed the determination on to the worker that the worker passes the information up to the fee-payer. Penalties could be used to enforce compliance, where appropriate.

51. HMRC will need to consider how it expects the information to be passed on ie, via an email, a letter, or a certificate etc and by when. Clearly verbal communication would not be appropriate and a written record of some sort should be on file. Will HMRC specify how this is to be done?

52. Finally, we see this as causing major enforcement problems for HMRC. Fee-payers will not generally have much money with which to pay HMRC any shortfall, as their business is to pay out what they take in, whereas clients generally will. Also, establishing who the defaulting party is in a complex supply chain will require investigating more than one party in it and possibly all of them, which will take time and resource.

Question 4: What circumstances might result in a breakdown in the information being cascaded to the fee-payer? What circumstances may result in the contractual chain making a payment for the off-payroll worker's services but prevent them from passing on a status determination?

53. There are various scenarios that could lead to a breakdown in communication including office personnel changing or being on leave. It will often be the case that the individual dealing with the payment will be different to the person dealing with the status determination.

54. Under the current proposal, a delay in the determination reaching the fee-payer could be interpreted as no determination being sent and therefore the client being 'small'. This would mean the fee-payer is not required to withhold tax and NIC. However if the fee-payer subsequently receives a determination which states that withholding is required, it is not clear whether they would only withhold on subsequent payments or previous payments too. How is the lack of withholding on prior payments dealt with?

Simplified information flow

Question 5: What circumstances would benefit from a simplified information flow? Are there commercial reasons why a labour supply chain would have more than two entities between the worker's PSC and the client? Does the contract between the fee-payer and the client present any issues for those or other parties in the labour supply chain? Please explain your answer.

55. Yes there are commercial reasons why a labour supply chain would have more than two entities between the worker's PSC and the end client. Regardless of the reasons why, the legislation needs to be able to deal with these modern working practices.

Question 6: How might the client be able to easily identify the fee-payer? Would that approach impose a significant burden on the client? If so, how might this burden be mitigated? Please explain your answer.

56. Our proposal, as per para 50 above, is for the worker to pass the determination up to the fee-payer. As such the client would have no need to identify the fee-payer. This would require enforcement, perhaps via a penalty regime, and there would need to be effective policing by HMRC.

Working for a small organisation

Question 7: Are there any potential unintended consequences or impacts of placing a requirement for the worker's PSC to consider whether Chapter 8, Part 2, ITEPA 2003 should be applied to an engagement where they have not received a determination from a public sector or medium/large-sized client organisation taking such an approach? Please explain your answer.

57. Yes. As per paras 27-29 above, we do not think that silence is acceptable. The end client should be required to communicate their size to the individual worker by a certain date and HMRC would need to consider how best this should be done. For example, via an HMRC-prescribed certificate.

Addressing non-compliance

Question 8: On average, how many parties are in a typical labour supply chain that you use or are a part of? What role do each of the parties fulfil? In which sectors do you typically operate? Are there specific types of roles or industries that you would typically require off-payroll workers for? If so, what are they?

58. We are responding to this consultation as a professional body representing over 150,000 members many of whom act as professional advisors to over 1.5m businesses. This question is therefore not specifically relevant to ICAEW to answer as a business. However, the legislation must be able to cope with the diversity of our membership which ranges across services including retail, construction, manufacturing and farming.

Question 9: We expect that agencies at the top of the supply chain will assure the compliance of other parties, further down the labour supply chain, if they are ultimately liable for the tax loss to HMRC that arises as a result of non-compliance. Does this approach achieve that result?

59. Reputable businesses will only knowingly engage with reputable businesses and no process can ever ensure that in all cases there will not be a failure.
60. HMRC can pursue debts for up to six years. Businesses that were once reputable may cease to be so after the worker has completed their work but before HMRC investigates – for example, because of a change of ownership.
61. We remain of the view that an innocent party should not have to bear a tax cost due to unforeseen circumstances. If the end client has taken reasonable care they should not be subject to a tax cost because of a failure or mistake further down the supply chain. This is particularly so when the end client is engaging with agencies licensed by the government – for example gangmasters licenced by the GLAA.
62. We suggest as a possibility that HMRC should only have power to transfer liability in cases of fraud and gross negligence, established by a special unit with HMRC, as is currently done for transferring liability for unpaid NICs on to directors of defaulting companies.
63. It should also be noted that excessive compliance requirements placed on agencies could be anti-competitive, as agencies will then only take on other intermediaries whom they know and with whom they feel comfortable. This will make it difficult for start-ups to gain entry into this market. We recommend that this issue be further explored.
64. The client may not know who the fee-payer is in respect of a particular contractor. This is particularly in the case where there are complex supply chains due to the need to include specialised agencies for recruitment of particular labour.
65. We think that the proposal in the consultation document regarding of transfer of liability could produce unfair results and needs further consideration.

Question 10: Are there any unintended consequences or impacts of collecting the tax and NICs liability from the first agency in the chain in this way? Please explain your answer.

66. The agency, as well as the contractor, needs a right of appeal. Where the agency is operating withholding on the basis of a determination it does not agree with there needs to be an independent dispute process. For example, the client may on the basis of reasonable answers they have entered in to CEST reach a determination that withholding is due. The agency and the contractor may reach the conclusion that withholding is not due. The different results could be due to the fact that the client only knows about the contractor’s relationship with them but the agency and the contractor are both aware of other clients for whom the worker provides services. This is particularly likely given that CEST does not currently take

"being in business on one's own account" into consideration. These other services may be sufficient to make the difference in the determination. The agency and the contractor may also not be able to tell the client about these other services due to client confidentiality, formal security clearances, court injunctions and data protection laws. The only solution is for an independent appeals process that is not hampered by the data protection laws.

Question 11: Would liability for any unpaid income tax and NICs due falling to the engager (if it could not be recovered from the first agency in the chain) encourage clients to take steps to assure the compliance of other parties in the labour supply chain?

67. We do not think it is reasonable to expect the end client to bear the liability where they have taken reasonable care to use accredited agencies and have performed due diligence work on the agencies they engage with.

Question 12: Are there any unintended consequences or impacts of taking such an approach? Please explain your answer.

68. As above.

HELPING ORGANISATIONS TO MAKE THE CORRECT STATUS DETERMINATIO AND ENSURING REASONABLE CARE

Addressing status determination disagreements between the client and off-payroll worker and/or fee-payer

Question 13: Would a requirement for clients to provide the reasons for their status determination directly to the off-payroll worker and/or the fee-payer on request where those reasons do not form part of their determination impose a significant burden on the client? If so, how might this burden be mitigated? Please explain your answer.

69. Yes providing the reasons would impose a burden although not a significant additional one because in any event the end client should keep records of the reason behind the determination for the purpose of internal audit etc. We believe it is necessary for the worker to receive the reasons for their status determination. Until the government addresses the tax and national insurance differential it will not be possible to avoid the burdens that the off-payroll rules place on business.

70. The requirement for the client to take reasonable care, proposed in the consultation document, will need specific legislation in the private sector, as without it there will be no such obligation (unlike the public sector where this is a matter of public law). This legislation will also need to give the worker recourse to the client if the requirement is breached.

71. As explained above we believe there should be an independent appeals process that can resolve all the tax impacts of a disputed determination, assuming communication of the reasons for the determination has not resolved the dispute. The requirement for the end client to have a dispute resolution process in place is not sufficient (see comments in relation to question 14).

Question 14: Is it desirable for a client-led process for resolving status disagreements to be put in place to allow off-payroll workers and fee-payers to challenge status determinations? Please explain your answer.

72. There needs to be a statutory and independent appeals process to allow the worker and agencies to dispute the employment status determination provided by the end client.

73. We are concerned that a client-led dispute process will not be robust enough and would be unenforceable by HMRC, potentially leaving the worker with no power to appeal the determination. It could also represent a significant administrative burden for engagers, given that it is not clear from the consultation document how the dispute process should be implemented. That said we view a client-led dispute process as merely being the first step in the process, with there also being a need for an independent appeals process to deal with

cases where the end client and contractor continue to disagree. While the end client should provide the reasons for the determination to the worker, if the facts of the case are disputed or the status cannot be readily determined, HMRC will need to determine the status. This has to be the case in order to give the worker the protection that the formal appeals process provides.

74. There is a further issue in that some employment status considerations are known only to the worker, such as the number of clients and the nature of the work performed, when the worker claims to be in business on his own account. This is accepted by HMRC (see the Employment Status Manual, ESM 0514 and ESM 549 to 553. It is not generally appropriate that these should be shared with the client (either in relation to the worker's own affairs or that of his or her clients), and the client would have no means of knowing whether the worker was telling the truth or not without an exhaustive and intrusive inquiry which most clients would be ill-equipped to carry out. We note in particular with reference to this the FTT's decision in the recent case of Atholl House Productions [2019] UKFTT 0242 (TC), where this was the criterion for the decision made and the judges, in their section on this (paragraphs 105 to 114), made no reference to the contract at all. It is therefore essential, at least in cases where being in business on one's own account is claimed to be a factor, that the worker should have direct recourse to HMRC to determine the matter.

75. We note that there is no mention of any penalties that would apply if a business failed to implement a client-led dispute process.

Question 15: Would setting up and administering such a process impose significant burdens on clients? Please explain your answer.

76. As above.

Question 16: Does the requirement on the client to provide the off-payroll worker with the determination, giving the off-payroll worker and the fee-payer the right to request reasons for that determination and to review that determination in light of any representations made by the off-payroll worker or the fee-payer, go far enough to incentivise clients to take reasonable care when making a status determination?

77. Yes, it does however the difficult part is making the status determination in the first place. Most businesses will not have employment status specialists in-house and will need to either train existing staff, recruit specialists or use external expertise, all at a cost.

78. While HMRC has provided CEST as a means to determine employment status, this does not include any questions to determine whether the individual is in business on one's own account (and even if it did, this is not the sort of information a worker would typically share with each end client, as noted above at para 74). We appreciate that work is underway to improve CEST however the rules are too complicated for a yes/no checklist to be able to provide the right answer in all cases.

79. We believe that, where in doubt about the status, end clients are likely to determine that PAYE should be operated. This is because operation of PAYE, while more costly in terms of employer NIC, will remove any future exposure and the uncertainty that accompanies it. Essentially, as businesses require certainty in the tax rules, they will seek to impose this certainty themselves (even at a cost) where the legislation and HMRC tools are ineffective in providing it.

OTHER MATTERS

Pensions

Question 17: How likely is an off-payroll worker to make pension contributions through their fee-payer in this way? How likely is a fee-payer to offer an option to make pension contributions in this way? What administrative burdens might fee-payers face which would reduce the likelihood of them making contributions to the off-payroll worker's pension?

80. We do not think that this is likely to happen in practice.

Other issues

Question 18: Are there any other issues that you believe the government needs to consider when implementing the reform? Please provide details.

81. **Deemed employment marker** - We have requested on numerous occasions that HMRC issues payroll software IT specifications to ensure that deemed employees are flagged as such on both engager/fee-payer and HMRC systems. This would ensure that deemed employees are not included in certain internal management accounts statistics (ie, gender pay gap reporting) and would prevent student loan deductions being made and auto-enrolment obligations being triggered when they should not be – something which we are aware is happening in the public sector. It would also prevent HMRC helpline staff from telling contractors that they have been incorrectly set up as employees.
82. The alternative is that the contractors who are deemed employees will need to be included on separate PAYE references so that student loan notices etc can be ignored. HMRC would need to issue a great number of PAYE references if this approach was taken. Experience shows that there is greater chance of the employment allowance and the apprenticeship levy being calculated incorrectly the more PAYE references an organisation has. In addition it is also likely that The Pensions Regulator will issue auto-enrolment notices even when there is no auto-enrolment requirement. All these factors will lead to unnecessary work for HMRC, taxpayers, agents and regulators which could be avoided if HMRC amended its systems to allow it to differentiate between real and deemed employees.
83. **Offshore entities** – we recommend that HMRC should make clear what the position is when the OECD Model Tax Treaty is in play. If there is no intermediary, and the client has no tax presence in the UK (unless bearing the cost for a resident party), article 15 specifies that income of someone resident in the foreign state should only be taxed in the UK if that person is in the UK for 183 days or more. In marginal cases – particularly in industries that are project-based, such as construction – the number of days spent in the UK will not be known until close to the year end. If HMRC is expecting a UK-based fee-payer to operate the off-payroll rules irrespective of this, this should be clearly stated. We would welcome a meeting with HMRC to discuss international aspects of the reforms.
84. **Draft legislation** – we request that, where changes are required to other Acts, the text of the existing legislation that is going to be changed is published in track changes alongside the draft legislation to allow everyone easily to identify the amendments.
85. **Guidance** – given some of the delays with the guidance for the reform to the public sector rules and the fact that some guidance is still incorrect despite working with HMRC for over a year now to make the corrections, we would advise that the draft guidance for the private sector is published alongside the draft legislation in the Summer. ICAEW would be very happy to work with HMRC to ensure the guidance addresses the points we would expect it to and is consistent (where appropriate) with the guidance for the public sector.
86. We welcome the recent guidance published by HMRC to increase awareness of the forthcoming changes and the corrections recently made to para 13 of the technical note regarding the accounting entries required in the PSC. However more still needs to be done.
87. **Outstanding issues in the public sector** – We have been working with HMRC for over a year now to improve parts of the reform in the public sector. We highlighted our concerns in our letter dated 26 July 2018 to HMRC (ICAEW rep 91/18) and despite subsequent meetings a number of these remain outstanding. We would welcome an update from HMRC as to how these items are being progressed.

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APPENDIX 1: ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory**: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain**: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple**: the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate**: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted**: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant**: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation**: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed**: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable**: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive**: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see https://goo.gl/x6UjJ5).

APPENDIX 2: OPERATIONAL AND SYSTEMS ISSUES

We set out below some of the key systems and operational issues that businesses will need time to deal with if the public sector rules are extended to the private sector:

Large businesses

1. In larger businesses the data required to set up an employee comes not from a direct input into the payroll software, but typically via a data feed from the human resources (HR) system. The function of the payroll software is essentially to calculate and report real time information as the payment is made and carry essential personal information and details of pay and benefits entitlement. HR systems are likely to also hold this personal information. Businesses will need to assign a new cost centre code to deemed employees to ensure they are not reported internally as true employees. For large employers using ERP systems this will take time and bear a financial cost. A “flag” will also need to be added to the payroll system and Full Payment Submission to alert HMRC to which individuals are deemed employees.
2. For many private sector organisations the HR system will operate globally so any changes must be tested for downstream impact in every geography – one cannot simply tweak the UK system because there isn’t a UK stand-alone system. In order to make changes to a global HR system, one would expect at least six months to escalate the business case to the proper level and then a further 12-18 months for design, testing and implementation.
3. The HR system is one of the core systems within an organisation and much is done with the data. For example statutory reports are made to Regulators such as the SEC, gender pay reporting, country-by-country reporting and headcount forecasting. Head counts are also used in tax where a business claims tax relief dependent on its size, such as the Enterprise Investment Scheme. Having individuals on the HR system who are not employees, potentially affects all downstream data reporting, meaning businesses will need to:
   a) Understand and catalogue the downstream data uses,
   b) Assess whether and to what extent these are impacted
   c) Design and implement fixes.
4. The data feed from HR to the payroll system will cause issues, as non-employees will not have salary data (since they are paid by invoice). Intervention will be required to extract the fees from the invoice which then becomes the ‘salary’, in addition to personal details such as date of birth and NI number which will not be on the invoice. The data feed has a number of automatic checks and safeguards, and these will have to be redesigned in order that false error messages are not being generated by deemed employees.
5. Small business suppliers have often complained that large suppliers take too long to settle their invoices. Some of this delay is systems related. One large private sector company has given us the following systems example to illustrate how the additional step to verify whether or not IR35 applies, interrupts the work flow between receiving an invoice and making payment.

   > *‘The pay data for these non-employees would come from the Accounts Payable (AP) system. In our organisation, invoices must be submitted electronically through a supplier portal (a common global system), and are verified electronically by approvers, who are assigned by expense type and value, before being processed for payment. It would therefore be necessary to insert a holding step after verification to prevent invoices from providers who are identified as within IR35, from being settled automatically. Instead, the VAT-exclusive amount of the invoice would need to be fed into the payroll system at the next available run to serve as pay data, and matched to the right PAYE record. This would require either a direct data link from AP to payroll, which currently does not exist, or at the very least a method of exporting the data from AP in a way that can be imported into payroll (eg, a csv file).’*

In order to complete the export/import, one would need to have a method of identifying the affected suppliers within the AP system, which we don't have at present. The timescale for any changes not already "on-programme" would be 18-24 months as resources are typically committed 18 months ahead in line with the overall business plan. We are also aware that in some sectors, retail in particular, there are software freezes from September to post-Christmas to ensure there is no risk to the IT systems or unexpected down-time during peak-trading.

If it were possible to calculate the PAYE deductions on the amount of the invoice (excluding VAT), then the net figure would need to come back into the AP system as a company amendment to the invoice and be re-verified before being submitted for payment. Again the link between payroll and AP would need to be a direct data feed or export/import via csv.

A further problem comes when we use the data from the AP system to compile the VAT return. The system has a number of automatic safeguards, and one of these is a reconciliation of taxes to the amounts paid. However, if we have an invoice amount of £100 + VAT (£120), and 20% PAYE withholding has been applied to the £100, we now have a payment of £80 (£100 – £20), and a VAT amount of £20. Naturally the payment of £80 will not reconcile with a VAT payment of £20 as it's not the right VAT rate for the supply. Before compiling the VAT return, we would need to manually reconcile with the payroll data every entry where there is a VAT mismatch. This is potentially thousands of manual reconciliations.'

6. The above illustration is a real case. It hasn't mentioned Making Tax Digital, but this will also require systems change in order to extract and report the correct quarterly VAT totals automatically from April 2019.

Small businesses

7. Smaller businesses with no integrated HR software/payroll software will need to send the data, probably on a spreadsheet, to their payroll agent, detailing the individual's hours charged and relevant data.

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APPENDIX 3: GENERAL COMMENTS

We have reproduced our general comments from ICAEW rep 94/18, our response to the off-payroll working in the private sector consultation published on 18 May 2018.

The tax gap

1. We appreciate the difficulty HMRC has had historically in policing off-payroll working, while also noting that many of the problems stem from the complexity of the rules. This has been exacerbated by lack of HMRC resource.
2. While we support the government's desire to close the tax gap, it is important to adopt a holistic approach to modernising the rules for taxing work. Any changes to the private sector should be considered alongside the outcome of the Matthew Taylor review.
3. It has been quoted that the increase in income tax and NIC receipts following the reform of off-payroll working in the public sector is £410m. We note that the additional net revenue from all sources being brought into the UK Exchequer as a result of the changes will be considerably less than this once the reduction in both corporation tax and tax on dividends paid out by personal service companies (PSCs) are taken into account. Furthermore, the figure does not take account of the loss of VAT that would have been charged on fees where contractors have subsequently been moved to contracts of employment, nor any adjustments where contractors dispute the status allocated to them via self assessment and are ultimately found to be outside IR35. We would therefore challenge whether the figure of £410m is a useful one in assessing the real success of the public sector reforms.
4. We also note that the cost of non-compliance with the off-payroll working rules is projected to increase from £700m in 2017/18 to £1.2bn in 2022/23. We would welcome a breakdown, detailing in particular how much of this is employer NIC.

Tax differentials

5. We note that government is not considering tax, including NIC, rates as part of the employment status consultation nor as part of the private sector off-payrolling consultation. We remain of the view that a divergent tax burden is a major driver behind current hiring practices. This is mainly represented by the 13.8% rate of employer's NIC and 0.5% apprenticeship levy paid in respect of employees and the absence of these costs in respect of the self-employed, although there are other tax differentials too. Other cost differentials include pension costs under auto enrolment, which are currently 2% but will rise to 3% next year, and also holiday pay. We therefore believe strongly that the most robust long-term way to restore equilibrium of workers' employment status in the jobs market and to protect Exchequer revenues is to reduce the differential.

Off-payroll rules in the public sector

6. The reform to the off-payroll rules in the public sector has had a number of teething problems since it was rolled out in April 2017. We strongly recommend that the government addresses these issues in the public sector urgently, regardless of the policy decision taken in regard to the private sector (see ICAEW REP 91/18 for more details).
7. In the event that UK businesses become more risk averse as a result of the off-payroll reform and therefore decide to take on more employees rather than contractors, a significant benefit of flexible labour will be diminished and business costs will rise considerably, so reducing profitability.
8. It is too early to fully understand the impact of the 2017 public sector changes. Until we have seen a full compliance cycle, including company and personal tax return filing, together with resolved enquiries, full assessment of the changes is not possible. Due to the lack of publicity given to HMRC's employment status review facility, individual workers who disagree with their status will need to complete a self assessment tax return and use that return to make a challenge. This will inevitably lead to an increase in workload for HMRC, essentially deferring the problem of final status determination from the initial decision taken by the

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engager to the final resolution through the self assessment tax return process. Other remedies available such as employment tribunals, suing for debt or judicial review will be either considerably more costly and/or even more time-consuming.

9. We are aware that there has been some growth in a number of schemes and our members have already noted the increased use of umbrella companies resulting in a shift of the risk of non-compliance from PSCs to umbrella companies. Agencies supplying workers are putting the individuals into umbrella companies often without telling the individuals, which prevents the agency or the public sector body (PSB) picking up the employer NIC costs and apprenticeship levy. The end result is that these costs are being deducted from the individual's net pay. It seems unlikely that this was Parliament's intention.

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