

A Guide to IR35

Whether you're starting out in a contract or freelance career, or have been doing it a while, it's important you familiarise yourself with the basics of IR35



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What is IR35?

IR35 is a legislation designed to prevent contractors enjoying self employed tax privileges when working in a way that HMRC consider to be disguised employment. If it wasn't for the fact a worker was being paid gross through their limited company, would the relationship be one of employment?

Introduced in 2000, the legislation was introduced as a response to a growing number of people leaving their jobs, only to return to the same business to do the same work as contractors. By setting themselves up as personal services companies (PSCs), these people were able to increase their take home pay through low salaries offset by large dividends.

This makes employers happy too, as their ex-employees' new status as contractors release them from many obligations of employment law.

Faced with a potentially huge loss of receipts, the government decided to take action. Being found to be inside IR35 would make contractors subject to the same tax and NI liabilities as their PAYE colleagues.

Whats happens if I'm caught

If HMRC determine that the contractor falls within IR35, and is what they refer to as a 'disguised employee', they will then demand all backdated tax and NI that the contractor would have paid had they been a permanent employee of their client for the duration of their contract.



IR35 and our Limited Company Service

At Boox, not only do we offer a unique online accounting service, we are here to help you understand IR35 and how it can impact you ahead of your initial steps in the contracting world. We offer an initial contract review as part of our service.

Risks and Impact of IR35

The Risks of IR35

Any contractor operating outside of IR35 and taking dividends from their company runs the risk of an IR35 enquiry, where HMRC will conduct a full review of the contractor's situation.

- IR35 determines whether contractors are "disguised employees" or genuinely self-employed.
- IR35 determines your employment status and, how much tax you have to pay.
- Being 'inside IR35' means that a contractor is liable for full PAYE and NIC deductions.
- HMRC can look 6 years into your employment history and contracts.

The Potential Impact of IR35

For all contractors, being caught 'inside IR35' is likely to have a significant impact on their financial position, highlighting the importance of IR35 awareness and protection.

The increase in tax due if caught inside IR35 is down to the additional employee and employers N.I. contributions, along with income tax payable at the full rate., plus penalties and interest.

		Outside IR35	Inside IR35
Total Revenue		£41,250	£41,250
Personal Taxes	PAYE	0	0
	Employers N.I.	£5.28	£5.28
	Dividend Taxes	0	N/A
Company Taxes	Employers N.I.	0	0
	Corporation Tax	£6,050	N/A
Taxes on Payments	Additional PAYE	N/A	£4,552
	Additional Employers N.I.	N/A	£3,417
	Additional Employees N.I.	N/A	£2,971
TOTAL TAXES		£6,055	£10,947
% of revenue		14%	26%

Example of an individual earning £25 per hour and the impact on their tax obligations of being inside or outside IR35.

Your IR35 Status

Are you inside or outside?

If you're subject to an IR35 investigation from HMRC, your case will be looked at and judged on the basis of the details you provide. Interpretation of IR35 is reliant on historical case law and as a result, some factors on the legislation and their prominence in certain cases influence how IR35 is upheld in new rulings.

Your written contract between your Limited Company and your agency or end client, along with your actual working practices will be the two main drivers of any decision about your IR35 status.



Your Written Contracts

You will be asked to supply all of your written contracts relating to the period which HMRC are investigating. There are a number of key aspects which will determine your IR35 status.



Your Working Practices

How you work with your client will ultimately carry more weight when it comes to the investigation, and it is important your written contract mirrors your working arrangements.

What helps your status

Ensuring you're 'outside' IR35

To avoid the significant impact on your finances and avoid being counted as a 'disguised employee' check out these tips which could help ensure you are on the right side of the line.



Act like a business

Remember why you decided to contract in the first place. You are providing your services to your clients – don't forget that. Operate in a proficient manner and follow normal business practices.



Use 'badges of business'

Consider investing in business stationery, create a business and marketing plan. You should look to purchase your company web domain and create a website to promote your company and look to acquire new clients.



Review all written contracts

Make sure you are happy with each of your contractual agreements and consider seeking professional advice. Also get a signed letter of confirmation from your client which sets out the actual working practices of the engagement.



Consider your right of substitution

Is this in your contract? One of the key indicators for IR35 is the ability to send someone in your place in case of absence. It will be worthwhile for you to exercise this right as well as evidence to support your case.



Equipment & Work Locations

Don't tie yourself to your individual clients. Ensure that you use all of your own equipment when it comes to fulfilling your contractual obligations. Also consider working in different locations and/or renting your own office space.

Dealing with an enquiry

How IR35 investigations are initiated

If HMRC believe your situation merits an investigation, you will receive an initial review letter which will request the following information:

- A complete breakdown of your Limited Company's income for a specific accounting period(s).
- Copies of all contracts which are associated with your income.
- Any evidence and information to support your opinion that your contract(s) is outside of IR35.

Be aware that HMRC have powers to obtain any information they need as part of the investigation. This may include approaching your end client directly to ascertain how they view and treat you as a supplier.

What to do next

You have approximately one month in order to supply HMRC with all of the information they request, but it will be important to take the following steps on making sure you are fully prepared:



- If you already have any IR35 insurance, contact your provider.
- Contact your accountant (if you have one) to start the process of pulling together all your financial information. Remember though it's likely they will charge you for time taken to represent you at a HMRC hearing.

Boox Tip



If you're concerned about your IR35 position - we have a Fee Protection Service which provide you with insurance cover to protect you in the result of any investigation, including IR35, by HMRC. Contact us directly to find out more.

Be prepared

Getting to grips with IR35

What's most important is that you don't bury your head in the sand when it comes to IR35.

Clearly, no freelancer or contractor wants to be subject to the IR35 rules. At the same time, this piece of legislation is complex. You may find it difficult to work out if it applies to you or not – and what steps to take to protect yourself from IR35.

1

Familiarise yourself with the legislation

There's plenty of advice online about IR35 and guidance on how to prepare yourself whether you're new to contracting, or simply taking on a new client.

Use specialists to help

Get both your contracts and your working practices reviewed by an accountant and even better, an IR35 specialist. They may also look at any older contracts.

2

3

Get everything in writing

Ensure that you get written opinions from any reviewer who provides advice on IR35, your contracts and your working practices.

Check policy wording on any insurance

Ensure the policy you've paid for covers you for both the initial letter process and any subsequent enquiry which comes of it.

4

5

Re-look at previous contracts

Remember that HMRC can go back and look at up to six years history. Note any differences between contractors and the clients employees, and ask for client confirmation on your working practices.

Find us online



Ready to get started?

For a no obligation discussion about our service, or the best route for your freelance career, get in touch using the details below:



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