**Genesis Initiative Submission to the 10 Downing Street Policy Unit**

**IR 35 – destroying flexible British SME expertise**

**Problem**

For almost three decades, the UK has enjoyed a competitive advantage through its businesses being able to access vital flexible expertise they need to deliver projects and drive the economy forward. The intermediaries’ legislation colloquially referred to as the IR35 tax rules (IR35) undergoes another major overhaul in April 2020. The impact of the changes is likely to be highly detrimental, particularly at a time when the UK economy needs to be nimble on its feet to deal with the potential opportunities and threats posed by Brexit.

Freelancing is a valued business tool. At the top end, Interim management revolves around the provision of specialist resources and skills for a defined project or period. Clients can turn to Interim practitioners for their most complex and top-heavy roles, using a proven heavyweight Interim executive for a short-term assignment to manage a period of growth, transition, crisis or change within an organisation, including start-ups. Similarly, Contractors skilled in a variety of disciplines across all business sectors can be engaged for defined projects to meet a particular need.

Freelancers are businesses on their own account and the vast majority operate through their own personal service companies (PSC). This structure currently enables Clients to engage and disengage a Freelancer at little or no notice. The PSC is an intermediary so, depending on circumstance, IR35 may apply; until April 2020 the Freelancer is primarily responsible for any tax liability if within IR35. From April 2020 the Client is responsible for issuing a status determination statement (SDS) to say if IR35 applies. If it judges incorrectly that the rules do not apply, it becomes primarily responsible for any IR35 tax liability. Human nature suggests that Clients will be risk averse and likely to decide that most assignments will be inside IR35. The Freelancer may continue to work through their PSC and incur the same tax liability as if they were directly on the Client’s payroll but without any entitlement to employment benefits. Alternatively, they can decide not to use their PSC and go direct on the client’s payroll with employment benefits, but the Client has to change the nature of the contract to an employment contract.

Either way, the SDSs issued are likely to put the Freelancer within IR35 even where there is no need, and, in essence, a “worker” tax is applied to a situation where there is a business, not a worker. The Freelancer will suffer a significant unnecessary additional tax burden, which is unlikely to be offset by increased day rates. Many situations will be unclear. A probable outcome is for more Freelancers to return to employment, resulting in a much less flexible workforce[[1]](#endnote-2). Two major high street banks have already announced that, going forward, they will only take on Freelancers working through their PSCs on the basis that the assignments are treated as within IR35. This blanket determination is a direct contravention of the rules to be applied after April 2020.

**Solutions**

As part of Brexit planning, further implementation of the above changes to IR 35 should be suspended for at least 3 years to ensure flexible SME contracting expertise is available competitively to the UK economy. At the same time a research-based review should compare the costs and benefits of employment as against contracting. We suspect that this could lead government to create a level playing field by giving contracting businesses within IR 35 an initial start up exemption to recognise the initial risks of contracting and to encourage the progression that would lead to job creation. The review is required to deal objectively with issue of fairness, since it was the unfair abuse of contracting relationships by some former public sector employees, which provoked IR 35. The situation in the private sector is different.

1. HMRC has developed the ‘Check Employment Status for Tax’ online tool ​(CEST) to help determine whether someone is self-employed or an employee for tax purposes. There are several problems with this tool:

   When tested against the facts of a number of cases decided as outside IR35 by the appeal courts, in a significant number of instances the tool did not give the same result.

   The tool is testing working practices but has to be used before work starts. As a result, many questions are “what ifs” to be answered without reference to reality

   A person who is an “Officer” of a Client company is automatically defined as an employee. Interims in particular require suitably senior authority to manage growth/transition/crisis/change and are unlikely to be able to achieve this if not a Director.

   Contractors become Directors of their Clients not as an end in itself but as something incidental to the task they have to complete. Where the appointment as a Director is not in the normal course of business but is for an alternative purpose, the Interim should not automatically be defined as an employee. [↑](#endnote-ref-2)