



HM Revenue
& Customs

Off-payroll working in the public sector: reform of the intermediaries legislation

Summary of Responses
December 2016

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1. Introduction

Background

At Budget 2015 the government announced that it proposed to reform the intermediaries rules, often known as IR35¹. HMRC published a discussion document [Intermediaries legislation \(IR35\): discussion document](#) in July 2015 which set a framework for discussions including the rationale and options for reform. The government received 162 written responses and held 14 roundtables and other events with interested parties.

After consideration of issues raised as part of that discussion, the government announced at Budget 2016 that the rules would be reformed in the public sector. HMRC consulted on the detail of this reform over the summer of 2016. A consultation [Off-payroll working in the public sector: reform of the intermediaries legislation](#) was published on 26 May 2016 with a closing date of 18 August 2016.

The consultation set out the government's proposal to move responsibility for determining whether the off-payroll rules apply to a contract, and deducting and paying the associated tax liability, to the public sector body or agency engaging the worker through their personal service company (PSC). It sought views on the detail of the policy design, asking sixteen questions (detailed in Annex B) covering:

- Definition of the public sector
- Information sharing
- 5% deduction
- Making the decision
- Transfer of liability
- Costs

HMRC received 188 responses to the consultation from a wide range of stakeholders, including public sector organisations, agencies, representative bodies, the recruitment sector, payroll professionals, trade unions, contractors and businesses. In addition, HMRC hosted over 30 stakeholder events across the UK to discuss the proposals and officials presented at a number of external events.

This document:

- summarises the responses received during this consultation;
- highlights key themes;
- details the government's response to the points raised, and
- provides details of next steps.

¹ ITEPA 2003, Part 2 Chapter 8, sections 48 to 61 and Social Security Contributions (Intermediaries) Regulations 2000 (SI 2000 No. 727)

2. Summary of consultation responses

188 written responses were received. This was in addition to comments received in roundtables and other stakeholder events.

The government is grateful for the detailed consideration and comments provided in response to the consultation. These have been fully considered and the key themes and the government's responses are set out below. Overall the government has concluded that:

- Responsibility for deciding whether the off-payroll rules for engagements in the public sector apply will move from the PSC to the public sector body, agency or third party engaging them;
- The public sector body or agency will be responsible for deducting and paying associated employment taxes and National Insurance Contributions (NICs) to HMRC;
- The 5% allowance currently available to those who apply the off-payroll rules will be removed for those in the public sector;
- Public sector bodies will be required to provide information to agencies and workers about whether engagements are within the rules.

2.1 General comments

The need for reform

Consultation response

Most responses agreed that it was necessary to reform the rules and with the principle underlying the need for the rules: one public sector body commented that '[we agree] wholeheartedly with the principle that people who do the same job in the same manner pay broadly similar amounts of income tax and National Insurance...'. Some were concerned that the changes would be a blueprint for reform to the private sector and others questioned why the reform targeted the public sector alone.

Several respondents, whilst agreeing that there is an issue with the levels of compliance with the legislation, thought that there were other options to tackle the problem, such as a new tax status for freelancers. A few responses called for the government to undertake a fundamental review of employment status to take account of 'the rapidly changing world of work'.

Government response

The government agrees that reform of the off-payroll rules is needed.

It is important to ensure that public funds are correctly used and that those in receipt of them are paying the correct taxes. Some public sector bodies are already required to check that some of their off-payroll workers are paying the correct taxes under the off-payroll assurance processes introduced by HM Treasury in 2012. These are limited to engagements of over six months and over £220 per day.

Although public procurement rules encourage engagers to take on a greater role in tax assurance, compliance across the wider public sector remains low and presents a significant fiscal risk.

The criteria for deciding whether the rules apply will remain the same for both the private and public sectors. The reform means that the public sector engager (or agency in the chain if there is one) will be responsible for applying the rules and liable for paying any associated tax and NICs to HMRC. For private sector engagers the PSC will still be responsible for applying the rules. The government has no current plans to extend the reform beyond the public sector.

A new online tool will be available by April 2017 for all to use and will make it easier to apply the rules regardless of sector.

The Prime Minister has recently asked Matthew Taylor to lead an independent review into how employment practices need to change in order to keep pace with modern business models. The government awaits the outcome of that review with interest.

Impact on the UK's labour market and the public sector

Consultation response

Some respondents were concerned that the reform would stop people working through limited companies and this could negatively affect the flexibility of the UK labour market, with a small number suggesting that the government's purpose was to stop people using this company structure.

Many contractors and their representatives said they would choose not to work for the public sector as a result of the reform. Some contractors said they would have to consider whether their rates would need to change to take account of the increased tax and NICs that would become due. They said that if rates rise this could lead to skills shortages in key sectors such as IT and engineering and increase public sector hiring costs.

Government Response

The government recognises the benefit to the economy of having a flexible labour market and has no intention of stopping people from working in this way. Public sector bodies will continue to be able to hire contractors, including those who choose to operate through their own company.

The government is not increasing the numbers of people who should be subject to the off-payroll legislation: the changes are intended to improve compliance with the current rules where they are not being operated correctly.

However, the government does not believe that choosing to work through a limited company should necessarily affect the amount of tax and NICs an individual pays.

Where an individual would have been taxed as an employee had they been engaged directly, rather than through an intermediary, it is right that they should pay broadly the same tax as an employee. Individuals doing the same job should be treated similarly, regardless of whether or not they work through a company.

People who are genuinely self-employed – and so outside the intermediaries rules – will not be impacted by this change.

Implementation date

Consultation response

Respondents commented on the date for implementation of the reform and challenged whether it was deliverable in the proposed timescale. Some public sector organisations said that changes to processes would be costly and time-consuming and would not be ready in time for April 2017. Others commented that it would be simple to manage processes where they engaged smaller numbers of contractors. A few organisations said that the reform should be delayed until the online tool is fully ready, as making the decision would be overly burdensome without it.

Government Response

It is important to implement reform as soon as possible to protect the Exchequer. However the government is aware that this will require changes to systems and processes. The government engaged early, and has been talking to stakeholders about reform of the off-payroll rules since last summer. HMRC has consulted extensively with payroll providers, public sector employers and agencies as part of this consultation. HMRC will be providing guidance prior to implementation in April, which will help affected stakeholders to prepare.

The government has already committed to providing a digital tool to help engagers decide whether they need to apply the rules and pay employment taxes and NIC, and has engaged with stakeholders on the detail of the tool design.

HMRC is grateful to respondents for detailed comments on the questions for the new tool. The government will continue to work with stakeholders over the coming months to develop the design and content of the new tool to ensure it is ready for April.

Fiscal impact

Consultation response

A few respondents questioned the basis of the figures quoted in the discussion document, including the cost of non-compliance. A small number expressed the view that there was inconsistency with the Public Accounts Committee report about compliance with Treasury rules which suggested 90% assurance was received.

Government Response

The numbers and costing quoted in the consultation were certified by the independent Office for Budget Responsibility at Budget 2016.

The Public Accounts Committee report looked at temporary staff across government departments and connected government agencies. HMRC figures are for personal service companies only and look across the public sector as a whole.

The Public Accounts Committee report concluded that departments are not doing all they can to ensure that temporary staff pay the right tax and recommended that all departments should review whether their off-payroll staff should be treated as employees and taxed through Pay as You Earn (PAYE).

2.2. Response to questions in the consultation document

Definition of the public sector

Question 1: *Are there other easily understood definitions that work better than the FOI Act and the FOI (Scotland) Act?*

Question 2: *Are there any other public sector bodies which are not covered by the FOI Acts which should be included in the definition for the proposed rules?*

Question 3: *Should private companies carrying out public functions for the state be included in this definition? Why?*

Question 4: *Are there any public bodies caught by this definition who would face particular impacts which should be considered?*

Consultation response

The government proposed using the definition of public sector set out in the Freedom of Information Act 2000 and the Freedom of Information (Scotland) Act 2002 (the FOI Acts). The majority of respondents supported this proposal. A few proposed alternative definitions such as the ONS definition of the public sector or that in Article 13(1) of the VAT Directive.

Some suggested HMRC should publish a list of those included in the legislation, or should impose an obligation for the public sector organisation to tell the engager (where there is an agency or other third party involved) that it was covered by the FOI legislation.

Most did not think private companies carrying out public functions for the state should be included, because this would blur the line between those who work in the public sector and those who work in the private sector even within the same company.

Government Response

The government agrees that this definition of the public sector is appropriate for the purposes of the change. It covers what most people would recognise as the public sector, is a stable list that rarely changes and organisations will know whether or not they are subject to the FOI Act.

The government also agrees that the reform should not be extended to private companies carrying out public functions.

HMRC will provide guidance to cover the process for the small minority of cases where it may not be clear that an organisation is within the public sector.

Information

Question 5: *Are rules needed to ensure that engagers have the information they need to make the decision? If so, what should they be?*

Consultation response

Some were concerned that it could be difficult to get the information needed to complete the online tool, so they would not be able to get an accurate assessment of whether the rules applied. Many felt that clear rules were needed about what information should be shared, particularly between public sector engagers and agencies.

Some respondents suggested that the government should introduce a legal duty on the engager to pass on the information required to enable a decision to be made, with guidance setting out the information which should be shared. This view was most prevalent from the agency sector, who felt that any agency was 'wholly dependent on third parties' to supply relevant information. They also felt it would be appropriate to impose a sanction on an engager who did not supply information when asked.

Many were concerned that this information would not be readily available at the start of an engagement. They said that working practices are not always established before work started, and 'it will be necessary to seek confirmation that the actual working arrangements reflect the terms of the contract'. Some respondents said that the nature of the work can change throughout the life of the contracts so the decision made at the start might not be valid over time. One response said that the decision on whether the rules applied should be reviewed on a regular basis, such as after three months.

Government Response

The government agrees organisations will need to share information about whether the rules apply. It is therefore introducing a provision to facilitate information sharing between parties in a chain.

Engagers will be required to inform the relevant party, such as an agency, whether the off-payroll rules should apply and will be liable for this decision. HMRC will publish guidance about the information needed which will also cover what engagers should do if working practices change.

5% allowance

Question 6: *How would accounting for the 5% allowance work in practice?*

Question 7: *Are there business costs specific to PSCs that are covered by the 5% that aren't covered under the usual business expense rules?*

Consultation response

Respondents said that while in theory accounting for the 5% allowance would be mathematically simple, to account for it in payroll software would require an update which would be costly and time-consuming. Most organisations, particularly those in the public sector, said that accounting for the allowance would be 'bureaucratic and expensive' and to keep it was 'illogical' and complex, particularly as they could not understand the rationale for retaining it.

A small minority, mostly contractors and their representative bodies, said the allowance should be retained, with one suggesting that it should be increased as expenses sometimes exceed 5%.

Government Response

As there was a strong call from many respondents to remove the 5% allowance the government has decided to remove it for PSCs with engagements in the public sector only. This will make calculating deductions of tax and NICs simpler and less burdensome for engagers and reflects the fact that PSCs will no longer bear the administrative burden of deciding whether the rules apply.

The government recognises that some currently compliant contractors will experience a reduction in take-home pay as a result of the withdrawal of the 5% tax-free allowance. PSCs will, however, still be able to claim allowable business expenses and those available to employees.

Making the decision

Question 8: Does the first part of the test work to quickly rule out engagements that are clearly out of scope?

Question 9: Are these the right questions in the right order of priority?

Question 10: Are the questions simple to understand and use?

Question 11: Do the two parts of the test give engagers certainty on day one of the hire?

Question 12: How can the organisation completing the tests ensure they have the information to answer the questions?

Question 13: How could the new online tool be designed to be simple and straightforward to use?

Consultation response

Respondents supported the government's aim to make the test determining whether the rules apply simple to use and understand from day one of an engagement.

However, many had reservations about the proposed gateway tests. Some said the test questions were too narrowly defined, as they only looked at substitution and control. Many said that the two parts of the proposed test did not provide certainty. As one commented, ‘these new rules need to have clear and simple procedures to enable an engager to be sure they have operated them properly...’

Some were concerned about engagers or agencies taking an overly cautious approach to minimise their risk of liability. A few suggested that public sector organisations would put all contractors on payroll to minimise any risk. They thought this could result in genuinely self-employed workers having to pay employment taxes, leading to a rise in appeals against the decision. They also said that HMRC would be faced with an increase in the numbers of people reclaiming tax paid at the end of the tax year, and as a consequence greater administrative costs and burdens to the engager and PSC. A few suggested HMRC would need to create a new process to ensure those caught by the rules, who shouldn’t have been, could reclaim tax at a faster pace than usual.

The proposal for a new digital tool was generally welcomed. Some questioned whether it was feasible to build a digital tool which would cover every situation. Most agreed that there was a tension between providing a tool to cover every circumstance and reflecting complex case law.

There were differing views on how the questions in the tool should be presented. Some wanted simple questions so that people without expertise in employment status could use the tool, but others thought more detailed questions would lead to more accurate outcomes. Many said the questions should only allow for unambiguous answers, otherwise the tool would be seen as too subjective. A majority thought guidance would be necessary, otherwise non-experts would not understand how to answer some of the questions.

A few respondents thought the tool should be mandatory and almost all thought it was fundamental to the successful delivery of the proposal.

There were some reservations about whether the tool could achieve the government’s aim of providing certainty on day one of the contract, either because working practices would change over time, or because working practices could not be known for certain until work had actually started.

Government Response

Following representations, the government has decided not to introduce the separate gateway tests outlined in the consultation document. The government agrees that the proposed gateway tests only work as designed if the person using them already understands employment status case law – and that most people would still need to go on to carry out the full test.

Instead, engagers and agencies will be able to use the online tool alone; providing simplicity and certainty from day one of the contract.

As the government is involving customers in the design of the tool, it is confident it will enable public sector engagers and agencies to accurately determine at the start of a contract whether the rules apply in the majority of cases, reducing the risk of making an incorrect decision.

The questions in the tool will be based on case law and HMRC will provide clear and simple guidance explaining technical terms, how the questions might apply and what to do if the circumstances of the contract change. The tool will be updated to reflect any new case law.

In a very small number of exceptional cases where the tool cannot provide a definitive answer, guidance and support will be available from HMRC as it is now.

The government is grateful to respondents for their input to the digital questions. The government is working with a specialist digital team to develop the tool, and in collaboration with stakeholders to develop the content and design.

Transfer of liability

Question 14: *Where should the liability for tax and National Insurance (and penalties and interest where appropriate) fall when the rules haven't been applied correctly?*

Question 15: *Should the liability move to the PSC where the PSC has given false information to the engager?*

Consultation response

Most thought that liability should fall on the party at fault when the rules had not been applied correctly. For example, some said that where the PSC has given false information to the engager, liability should move to the PSC. As one organisation said, 'it would be unfair for the engager to be penalised in cases where it was subsequently determined that the rules had not been applied correctly because of...mis-information'.

Government Response

The government agrees that when a person working through a PSC provides the public sector body or agency with fraudulent information intended to constitute evidence that the off-payroll rules do not apply, that person should be personally liable.

Legislation will be introduced that will allow liability for tax and NICs to be moved to the person who provided fraudulent information.

Costs and impacts

Question 16: *What one off and ongoing costs and burdens do you anticipate will arise as a result of this reform?*

Costs for the engager

Consultation response

Some agencies told the government that they do not operate payrolls or have the expertise or software to calculate, deduct and pay employment taxes. They said that they will incur costs as they take steps to align procurement and invoice billing systems with HR and payroll systems. Some larger organisations said that they might have difficulty setting up appropriate controls and processes.

Some engagers and agencies, particularly smaller organisations without in-house tax resource, said that they would not have the knowledge or skills to implement the changes and may need to engage support from advisers.

Government Response

The government recognises that the reform places a new responsibility on engagers and agencies.

Organisations have until April 2017 to prepare, and HMRC will continue to work with interested parties to ensure all are ready to implement the reform. Comprehensive guidance and worked examples will be provided.

HMRC will work to ensure the changes align as closely as possible with existing processes in order to minimise additional costs and burdens for engagers.

Costs to the PSC

Consultation response

Most contractors were concerned that they would suffer increased costs: many said this was because the rules do not apply to them now but would do so after April 2017.

Government Response

This change does not widen the scope of the off payroll rules, but is designed to ensure the current rules work as intended.

The government recognises that some contractors will experience a reduction in take-home pay as a result of the withdrawal of the 5% tax-free allowance. PSCs will, however, still be able to claim allowable business expenses.

Engager obligations

Consultation response

Respondents asked a range of practical questions about obligations under PAYE and accounting practices.

Most expressed concern that the engager, rather than the PSC as is currently the case, would become responsible for paying employer NICs.

They said it was unclear whether the engager would need to enrol workers in their workplace pension schemes.

Respondents also asked questions about how VAT and Corporation Tax would be accounted for, how the rules interact with the CIS scheme, and whether engagers would be liable to pay the Apprenticeship Levy on these payments.

Some respondents in the public sector were concerned that if PSCs were paid through the payroll they would want to claim employment rights such as a right to notice and paid holidays.

Many contractors said that it was unfair to pay someone as if they were an employee without the usual rights that an employee is entitled to. One respondent commented that 'tensions [would arise] between the worker and engager, which in turn will give rise (in all likelihood) to legal challenges'.

Government Response

Comprehensive guidance will be issued to ensure engagers and PSCs understand accounting procedures and the implications of any additional liabilities.

There is no direct link between employment taxes and rights provided by engagers.

4. Next steps

Draft legislation

Draft legislation has been published for consultation. The consultation closes the week commencing 30 January 2016.

Online tool

A specialist digital team is in place to develop the tool and is working in collaboration with stakeholders to develop content and design through to the delivery date in April 2017.

Implementation

The government anticipates these changes will be introduced as part of the Finance Bill 2016 and will be in force from 6 April 2017.

HMRC will issue guidance associated with this measure. New guidance will be published in 2016. HMRC will continue to engage with interested parties over the months leading up to implementation.

Annex A: List of stakeholders consulted

The government is grateful to the following organisations and individuals who responded to this consultation:

1st Option	Dataweaver Ltd
Abbey Tax	Deloitte
ACCA Global	Deloitte on behalf of Employment
Accountax	Businesses in the Health Sector
Adecco	Department for Business, Energy, and
Akarius	Industrial Strategy
Alexander Mann Solutions	Department for Rural Affairs and
Allen Lane	Agriculture
APSCo	Department for Transport
APSE	Department for Work and Pensions
Arras People	Department of Finance, Northern
Association of Accounting Technicians	Ireland
Association of Independent Specialist	Department of Health
Medical Accountants	Devon County Council
Association of School and College	Directors UK
Leaders	Dover Town Council
Association of Taxation Technicians	Driver & Vehicle Standards Agency
Bauer & Cottrell Ltd	Durham County Council
BBC	East of England LGA
BDO LLP	East Sussex County Council and
BECTU	Surrey County Council
Borough of Broxbourne	Employment Lawyers Association
Bradleys Accountants Ltd	Employment Taxes Industry Forum
British Universities Finance Directors	Ernst and Young LLP
Group	Expert Purchasing Solutions
Brookson Group Ltd	FCSA
CACI Ltd	Federation of Small Businesses
Capita	Foreign and Commonwealth Office
Channel 4	Forest Heath District & St
Chartered Institute of Payroll	Edmundsbury Borough Councils
Professionals	Francis Clark (on behalf of a client)
Chartered Institute of Taxation	Francis Clark LLP
Cintra	G4S
Cintra	Galago
Commina Limited	Grant Thornton
Confederation of British Industry	Grants Chartered Accountants
Contractor Calculator	Hays
Crisp Accountancy Ltd	Healthcare Financial Management
Crocus Information Ltd	Association
Crowe Clark Whitehill	HM Treasury
Crunch	Huntingdon District Council
CWC Solutions	ICAEW
Danbro	Institute of Interim Management

Intouch Accounting
i-PAYE
IPSE
Jake Stupart
Joint response from seven NHS trusts:
Devon Partnership NHS Trust, Kent &
Medway NHS & Social Care
Partnership Trust, Norfolk Community
Health & Care NHS Trust, Northampton
General Hospital NHS Trust, St Helens
& Knowsley Teaching Hospitals NHS
Trust, University Hospitals of Coventry
and Warwickshire NHS Trust,
University Hospitals of Leicester NHS
Trust
Kent and Medway NHS & Social Care
Partnership Trust
Kettering Borough Council
Kettleburgh Parish Clerk
KPMG
LA International Computer Consultants
Ltd
Leeds City Council
Leicester City Council
Liberty Bishop
Local Government Association
London Borough of Bexley
Manchester City Council
Mazars LLP
Ministry of Defence
Ministry of Justice
Morgan Hunt
Morson International
MPI Ltd
My Digital Accounts
National Union of Journalists
Network Rail
New Romney Town Council
NHS Wales
North East Procurement Organisation
Northern Ireland Water
Number Mill
Odgers Berndtson
Office of Tax Simplification
Orange Genie Group

Parity Professionals
Parity Solutions
Payroll Alliance
Pinsent Masons
Pocket Accounts
PRISM
Prisma Recruitment Limited
Public Service People Managers'
Association
PwC
QDOS
Recruitment & Employment
Confederation
Reducing the Deficit Ltd
Resource Solutions Group
RSM UK Tax and Accounting Limited
Sellick Partnership
SEPA
Serocor Group
Servoca plc and TLT
Sheldon Phillips Ltd
Society of Welsh Treasurers
Sopra Steria
St Albans District Council
TaxLocal Accountants
The Association of Recruitment
Consultancies
The Institute of Chartered Accountants
of Scotland
The Technical Infrastructure
Partnership Ltd
Torfaen County Borough Council
Transport for London
UK Debt Management Office
Unitum Ltd
Universities and Colleges Employers
Association
Warwickshire County Council
Welsh Local Government Association
Whitefield Tax Ltd
44 responses from individuals

Annex B: Consultation Questions

Definition of the public sector

Question 1: Are there other easily understood definitions that work better than the FOI Act and the FOI (Scotland) Act?

Question 2: Are there any other public sector bodies which are not covered by the FOI Acts which should be included in the definition for the proposed rules?

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5% deduction

Question 6: How would accounting for the 5% allowance work in practice?

Question 7: Are there business costs specific to PSCs that are covered by the 5% that aren't covered under the usual business expense rules?

Making the decision

Question 8: Does the first part of the test work to quickly rule out engagements that are clearly out of scope?

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Question 14: Where should the liability for tax and National Insurance (and penalties and interest where appropriate) fall when the rules haven't been applied correctly?

Question 15: Should the liability move to the PSC where the PSC has given false information to the engager?

Costs

Question 16: What one off and ongoing costs and burdens do you anticipate will arise as a result of this reform?