



What is IR35? (in 5 minutes)

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Introduction

IR35 is a fundamental issue all contractors/freelancers will need to get to grips with to avoid any future complications if the tax man comes calling. It is worthwhile investing some time and effort into understanding the basic principles of IR35 as so you avoid the many pitfalls presented by it – a good understanding of this legislation can repay many times over in tax, time and hassle saved.

IR35 is a piece of tax legislation aimed at identifying individuals supplying their services via a Limited Company to clients as 'disguised employees' in the eyes of HMRC.

A typical example (again in the eyes of HMRC) of a 'disguised employee' would be a permanent employee in a job, resigns on a Friday, sets up as a Ltd Co on the Monday and returns to the same job at the same place as a contractor.

However, IR35 is a complex issue and we have concisely highlighted it's salient features in this article.



1.0 IR35 Tests

- IR35 status is assessed on a contract by contract basis.
- There is no single factor as to why contracts may be in or out of IR35. The checklist below is designed to help you ascertain indicators in/out of IR35.

Test	Basis	Key Risks Pointing to IR35 Status
Contract	Has the client hired your company or you as an individual?	If a contract is between a client and you as an individual (not your company).
Control	Is the client telling you when, how and where to work?	If you're behaving like an employee and doing what your told to do, when and how and your client is making all the decisions.
Mutuality of Obligation	Are you obliged to accept work offered and is the client obliged to offer you work?	You accept any work given to you and you are obliged to complete it rather than specific projects or assignments.
Right of Substitution	Can you provide a substitute to do your or particular aspects of your work on any particular project?	Not being able to substitute yourself with another contractor with same skill set as you to complete some aspects of the assignment.
Financial Risk	Are you taking a financial risk? Or would you still get paid regardless of the success or failure of a particular project?	Employees are protected from exposure to financial loss of the organisation. Is this the same for your Ltd Co should a particular project go wrong?
Part & Parcel	Are you a fixture of the clients organisation?	If you are listed in your clients directory, use their business cards and/or listed on other pieces of their branded material.
Being in Business on your own Account	Do you have a website, business cards, directory listings for your company?	Not having a website and associated marketing material.
Provision for Equipment	Are you using the clients equipment to complete the task/job?	Using the clients I.T. and other equipment.

The tests on page 2 are used to determine IR35 status for each contract. No one indicator is enough and therefore a combination of all the above is often used to make a decision.

It is case law that is used to determine whether a contractor is either employed (inside IR35) or self-employed (outside IR35). Decisions are made on past cases and a Judge's interpretation of source legislation.

2.0 Pointers & Tips

- IR35 is a legal issue and not an accounting issue (but it has an accounting & tax consequence). Therefore, you are advised to seek independent legal advice.
- When seeking legal advice, make sure you use an IR35 specialist. Your local family solicitor is unlikely to have the necessary experience.
- It is recommended you do not use HMRC's contract review service. How impartial do you think they really are?
- Exercise caution with agencies. They may purport to issue **IR35 friendly contracts** but the onus is on you to check this. After all they are sales people trying to earn commission from placing you with a client and IR35 does not matter to them.
- There are certainly ways you can reduce the risks of being caught under IR35 if you are genuinely a contractor supplying your services through a Ltd Co.



3.0 How can I Test my Contract for IR35 Friendliness?

We at Aidhan Accountancy have partnered with QDOS contractor insurance and legal services specialists.

We recommend a professional IR35 contract review which costs as little as £49.00. The contract review is undertaken by an IR35 legal specialist team and will return an opinion in a report format as to whether your contract is IR35 friendly or not. If it is not, the report will make recommendations as to what clauses or changes to your contract are required in order to make it IR35 friendly.

To find out more about insurance products and services available visit:

aidhan.qdoscontractor.com/insurance



4.0 What Happens if I am Caught Inside of IR35?

If you are caught in IR35 you must carry out a deemed salary/schedule E calculation and pay income tax and national insurance like a permanent employee.

HMRC allows an expense allowance equal to 5% of the income received from relevant engagements. This is intended to cover the following administration costs:

- Premises costs including home office
- Administrative and secretarial support
- Accountancy and tax advice
- Costs of seeking contracts
- Printing, postage and stationery
- Employers and public liability insurance
- Training costs
- Computer equipment & hardware
- Bank & overdraft interest
- HP payments

“ If you are caught inside IR35 your effective rate of tax could end up being 35% +. This is compared to 17 - 25% outside of IR35. ”

Other legitimate expenses can be claimed such as travel, computer costs, training etc.

A typical calculation could be as follows*:

	Inside IR35	
Daily Rate		£300
Number of Weeks Worked		44
Total Income		£66,000
Expenses (5% allowance)	£(3,300)	
Other Legitimate Expenses	£(5,000)	
Taxable Profit		£57,700
Employers NI	£(6,987)	
Deemed Payment		£50,713
Additional Employees NI	£(4,231)	
Income Tax	£(13,285)	
Total Tax & NI		£24,502
Take Home Pay		£41,498

Effective Rate of Tax & NI = **37%**

*for illustrative purposes only

5.0 What is the Current Status of IR35 Legislation?

In our professional opinion, IR35 is less of an issue than the noise surrounding it suggests. Statistically, so few cases have ever reached the courts.

However, it's not to say it should be ignored. It still carries a minimal risk to contractors.

Discussions on IR35 are forever evolving and you can keep up to date by following the recommended and reliable newsfeed as follows:

www.contractoruk.com/news/ir35_news

Alternatively, you can arrange a consultation with one of our experts who can help and guide you further (please go to our website at www.aidhanfinancial.com where you will find an option to book a consultation).



6.0 How can Aidhan Accountancy Help?

As part of our package deals we provide literature and guidance on IR35 matters. We have partnered with IR35 contract specialists QDOS insurance who can provide IR35 contract assessments from as little as £49.00.

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