

## Personal Service Companies (IR35)

The Inland Revenue has introduced regulations (announced in the 1999 Budget) to combat tax avoidance by people who supply services through companies, instead of as employees.

It is often very tax advantageous for people to supply their services through *personal service companies* run by them, as tax rates on the companies are often lower than they would be under PAYE. There are also cash flow advantages and a degree of protection against potential personal liability. Whilst such an arrangement can be perfectly proper, the Inland Revenue believes that numerous people who would otherwise be employees (paying tax under PAYE) are taking unfair advantage of the company taxation system, and they want to stamp this out.

In assessing whether an individual is in reality an employee of the personal organisation who has the benefit of his or her services, Inland Revenue will look very closely at the contract between the organisation and the individual, comparing its terms with various guidelines that have been developed over the years. The Inland Revenue will consider:

- the amount of control that the organisation has over the work done by the individual (in terms of time, place and method). If, therefore, the individual is required to attend the organisation's premises on a regular basis between fixed hours and to carry out work in a particular way, it is likely that the Revenue will consider that individual to be an employee, rather than an independent contractor.
- whether the service company is allowed to provide the services by means of other individuals or whether they are tied to using one particular individual. If one particular individual is specified, then this again tends towards the relationship being an employment relationship, rather than an independent contractor.
- who provides any equipment needed to provide the services: if it is the organisation then that is a factor that would indicate that the organisation is an employer and the individual is the employee, rather than that the personal service company is a genuine independent contractor.
- to what extent the personal service company takes a financial risk in relation to the provision of the services: if the personal service company will be paid on the basis of the time spent by the individual then that would tend to indicate an employment contract, whereas if there is a fixed price payable however long the job takes, then that would tend towards a genuine "contract for services".
- the duration of the arrangement and whether notice has to be given by either party to terminate the arrangement will be considered: a long-running arrangement requiring notice to be given by the parties to terminate it would tend to indicate employment, rather than independent contracting.

All this means that it is important that personal service companies ensure that their contracts with their clients are drawn with these tests in mind so that if they are investigated by the Inland Revenue they can satisfy the Revenue that the client is not the employer of the individual.

Failure to succeed in this would mean that the Inland Revenue would collect any unpaid tax and National Insurance contributions on the same basis as for an employee, together with any penalties, interest, etc that fall due for late payment.

It would be the personal service company that would be liable for these payments, not the ultimate client.