**LETTER TO CONSULTANT WORKER (OPERATING THROUGH A PERSONAL SERVICE COMPANY) TO ACCOMPANY IR35/OFF-PAYROLL EMPLOYMENT STATUS DETERMINATION STATEMENT**

**GENERAL DRAFTING NOTES**

**Legal background**

* IR35 tax rules were introduced in 2000 to target tax avoidance by workers who claim to be self-employed, providing their services through an appropriate intermediary (usually a personal service company or PSC) but who are, in reality, deemed employees of their client. If, but for the existence of the PSC, a worker would have been a deemed employee for tax purposes, IR35 requires the PSC to operate PAYE payroll and deduct income tax and employee’s National Insurance Contributions (NICs) as well as paying employer’s NICs on the fees received for the worker’s services.
* Changes to IR35 and the ‘off-payroll working rules’, which sit over and above IR35 (together, the ‘IR35 tax regime’), come into force on 6 April 2021 (having been delayed for a year due to the Covid-19 pandemic). The new rules will shift the responsibility for determining the employment status of a worker operating through a PSC to its client in the private sector (unless a small business exemption applies). A similar change already took place in the public sector when the off-payroll working rules were first introduced in 2017.
* In cases where the client falls within a small business exemption, the PSC will continue to be responsible for determining the worker’s employment status for tax purposes and declaring this to HMRC, under IR35.

**Client’s obligations under IR35 tax regime from 6 April 2021**

* In summary, the new rules under the IR35 tax regime, which come into force on 6 April 2021, require medium and large sized companies in the private sector (click [here](https://www.gov.uk/hmrc-internal-manuals/employment-status-manual/esm10006) for details of how size is determined) who are ‘the client’ in receipt of a worker’s services to:
* determine, using reasonable care, the employment status for tax purposes of every worker who is working through a PSC (click [here](https://www.gov.uk/hmrc-internal-manuals/employment-status-manual/esm10003) for details of appropriate PSCs and other intermediaries). This will need to be done on a ‘contract by contract’ basis, for each contractual engagement in respect of the worker as some contracts may fall within the new rules and others may not;
* produce an employment status determination statement (SDS) setting out the worker’s employment status for tax purposes (giving the reasons for the status conclusion) and pass a copy to the worker and, where applicable, any agency or other organisation that the client contracts with to supply the worker’s services;
* keep detailed records of the worker’s SDS, including the reasons for the determination and fees paid;
* establish a process for dealing with disagreements in relation to the worker’s SDS;
* confirm the size of the client, if asked by the worker or any agency or other organisation that the client contracts with to supply the worker’s services; and
* in cases where the client is the ‘deemed employer’ (see below) of the worker, the client will be responsible for the operation of PAYE payroll and will have to deduct and pay tax and NICs to HMRC (including, where relevant, payments of the apprenticeship levy).
* If working practices or contractual arrangements change in relation to the worker and its PSC, the client must check the rules to see if the worker’s SDS is still accurate or if it needs to be updated and re-issued.

**Using this template**

* This template letter is intended to accompany a worker’s SDS, being sent by a client (referred to as ‘the Company’ throughout the template) to a worker that is supplying their services to the client through its PSC (either directly or via an agency that contracts with the client).
* The template has been drafted on the basis that there is a private sector client company that is not subject to a small business exemption. It is also drafted on the basis that all of the parties are resident in the UK and that the services are being provided in the UK. Note that where a medium or large-sized private sector client company is based wholly overseas, so there is no UK connection immediately before the beginning of the tax year because it is not UK resident (and does not have a UK permanent establishment), then the new rules under the IR35 tax regime will not apply to the client.
* When the new rules come into force, they will apply to payments made on or after 6 April 2021 but only where the services were also provided on or after 6 April 2021. Clients should issue the SDS on or before the date any payment is made for the worker’s services (otherwise it could result in responsibility for tax and NICs remaining with the client). However, HMRC have confirmed that an SDS can be issued early (i.e. before 6 April 2021) and will be considered valid for engagements carrying on after 6 April 2021, provided that the SDS satisfies the relevant legislative requirements (see below). One advantage of issuing an SDS early is that it may allow for any disagreements to be dealt with and changes to working arrangements to be agreed before April 2021.
* No commercial terms have been included in this template letter. Clients may want to consider adding, for example, their own wording regarding how the parties will absorb any additional costs if the worker’s SDS concludes that their engagement (via their PSC) falls ‘inside’ the IR35 tax regime.

**Agency communications**

* An optional paragraph ‘Agency communications’ has been included for cases where the worker’s services (provided through their PSC) have been supplied to the client by an agency. This paragraph makes it clear to the worker that the client is required to provide a copy of the worker’s SDS to the agency that the client contracts with. It also explains that where a labour supply chain exists (e.g. a chain of separate contracts between several agencies or organisations, from the client to the worker’s PSC) the SDS may be passed along the chain (see below).

**Option A**

* If, having taken reasonable care to assess the worker’s employment status for tax purposes, the client determines that the worker is not in deemed employment with the client (i.e. the worker’s engagement is ‘outside’ of the IR35 tax regime), Option A of the template should be chosen to confirm this conclusion. Even though the worker’s engagement is not ‘inside’ the IR35 tax regime in these circumstances, note that the client must still produce the SDS, confirming this outcome (along with its reasons) and pass it on to the worker (and, where relevant, the agency that the client contracts with).

**Option B**

* Alternatively, if the worker is found to be, effectively, in deemed employment with the client for tax purposes (i.e. an ‘off-payroll worker’ who is ‘inside’ the IR35 tax regime) Option B(1) or B(2) should be used, as appropriate. Note that the responsibility for deducting tax and NICs and paying these to HMRC remains with the client until it passes on the SDS to the worker and, where relevant, to the agency providing the worker’s services to the client.
* Option B(1) provides for situations where the client is the ‘fee-payer’ (i.e. ordinarily, this is the party paying fees to the worker’s PSC for the worker’s services). Provided that there are no other qualifying persons that sit in a labour supply chain between the client and the worker’s PSC (e.g. an agency), the client will also be the ‘deemed employer’. The deemed employer is responsible for deducting and paying tax and NICs to HMRC. HMRC guidance on identifying who is a fee-payer and qualifying conditions for being a deemed employer can be found [here](https://www.gov.uk/guidance/fee-payer-responsibilities-under-the-off-payroll-working-rules#check-if-youre-the-fee-payer).

* Option B(1) also specifies that the client’s obligations relate to payments made on or after 6 April 2021 but only where the services were also provided on or after 6 April 2021. If the services were all provided prior to 6 April 2021, but the payment was made on or after 6 April 2021, the payment would not be subject to the new rules. Instead, the pre-6 April 2021 rules would continue to apply for payments made in these circumstances.
* Option B(2) provides for situations where an agency is the ‘fee-payer’. Provided that the agency satisfies certain qualifying conditions (see above), when it receives the SDS, the agency will become the ‘deemed employer’ who is responsible for tax and NICs payment obligations.
* Option B(2) also provides for situations where a labour supply chain exists and the SDS must be passed on by each party until it reaches the lowest party in the chain immediately above the worker’s PSC. This person will normally be the fee-payer and, provided qualifying conditions are met (see above), it will also be the deemed employer who is responsible for tax and NICs payment obligations. Note that a failure to pass on the SDS, where required, can result in the tax and NICs payment obligations remaining with the party that fails to pass it on.
* HMRC advises that both the client (and, the agency that it contracts with) should take steps to understand what the labour supply chain looks like (particularly if there are any offshore agencies in the chain who may not be

subject to the IR35 tax regime obligations) and check the integrity and credibility of the parties in the chain. This can help prevent liability being recovered from the client where a party further down the chain is not compliant. Note that the presence of offshore employment agencies can affect where the responsibility for tax and NICS payments lie in the contractual chain. In this situation, please contact your Make UK adviser for further guidance.

**Challenging the employment status determination**

* Generally, the worker and, where relevant, any other organisation or agency, provided that it is the deemed employer, can challenge the outcome of the SDS if they disagree with it.
* The client must provide a response within 45 days of receiving a challenge from the worker or agency. Failure to respond within 45 days can result in the worker’s tax and NICs becoming the client’s responsibility. However, the client is only required to respond to representations given before a final payment has been made in relation to the worker’s engagement (as outside of this timeframe there are no further payments on which to operate PAYE).
* The template wording regarding the time limit has been placed in square brackets as the client may prefer to delete it if it is issuing a SDS before 6 April 2021. Technically, if a client receives representations challenging a SDS prior to 6 April 2021, the IR35 tax regime treats the client as receiving those representations on 6 April 2021 (i.e. the 45-day time limit for a response begins on 6 April 2021).

**SDS schedule**

* In summary, a SDS will only be valid if the client has stated whether or not the worker would be an employee for tax and NICs purposes if they were directly engaged by the client; provided their reasons for coming to this conclusion; and taken reasonable care in preparing the SDS.
* This template provides a framework within which to include the worker’s SDS. Producing an SDS will require detailed analysis on a case-by-case basis, applying the principles that govern whether or not a worker is a deemed employee and including the relevant considerations made to provide sufficient clarity around the conclusion. This is a bespoke exercise where it would generally not be appropriate to use a ‘one size fits all’ approach.
* According to HMRC, one example of not taking reasonable care when preparing a SDS would be where every worker is declared as ‘inside’ the IR35 tax regime, without giving any consideration to the specific facts of each individual case. Note that the only time it is likely to be acceptable for a client to make a determination for a group of workers, would be where they are engaged under exactly the same contractual terms and conditions and, in practice, work under the same terms and conditions too.
* The client can use HMRC’s online tool [Check employment status for tax (or ‘CEST’)](https://www.gov.uk/guidance/check-employment-status-for-tax) as an aid to making employment status decisions. If the answers provided to CEST are accurate and in line with HMRC guidance HMRC have stated that they will stand by the outcome, provided this outcome is followed.

**Further support**

* For a template letter to accompany the SDS which must be sent to an agency see template ‘Letter to agency supplying consultant worker (operating through a personal service company) to accompany IR35/off-payroll employment status determination statement’. For guidance on responding to a SDS disagreement see template ‘Letter in response to an employment status determination statement disagreement’.
* If you would like further support regarding the drafting and customising of this template letter, or more strategic advice regarding the IR35 tax regime, determining a worker’s employment status, or generally managing your contractor and consultancy relationships, please contact us:

**Call: 0808 168 5874**

**Email:** [**enquiries@makeuk.org**](mailto:enquiries@makeuk.org)

**www.makeuk.org/HR-services**

[DATE]

**Private and Confidential**

[WORKER NAME]

c/o [PSC NAME]

ADDRESS]

Dear [NAME],

**Changes to IR35 and the off-payroll working rules from 6 April 2021**

From 6 April 2021, changes to HMRC’s IR35 and off-payroll working rules (the ‘IR35 tax regime’) require [COMPANY NAME] (the ‘Company’) to assess the employment status of workers who are providing their services to the Company through an intermediary (e.g. a personal service company or ‘PSC’) and determine if they are self-employed or, effectively, an ‘off-payroll worker’ in deemed employment for tax purposes.

**Your employment status determination**

As required under the new rules, we have carried out a detailed and careful analysis of the work you undertake and the services you provide to the Company through your PSC [PSC NAME] under the [DETAILS OF THE ENGAGEMENT]. Following this analysis, the Company has produced an employment status determination statement (SDS).

Based on our analysis, we have determined that you [are/are not] an off-payroll worker and your engagement [does/does not] fall within the IR35 tax regime. I attach a copy of the SDS (see Schedule 1), for your records, which sets out the reasons for our determination.

[*Insert the following paragraph if the Worker has been supplied to the Company by an agency*]

**[Agency communications**

As your services have been supplied to the Company by an agency, [AGENCY NAME] (‘the Agency’), please note that the Company is required, under changes to the IR35 tax regime, to provide the Agency with a copy of your SDS. If the Agency is part of a labour supply chain, we note that your SDS may also be passed along the chain, as required under the new rules.]

[*Delete references to the Agency if not applicable*]

**Future changes**

The Company will review your employment status for tax purposes on [an annual] basis, or earlier, if there is a significant change to the current arrangements. The Company will notify you [and the Agency] if it concludes that your employment status has changed and provide a new SDS.

**Next steps**

[***OPTION A: WORKER IS NOT AN OFF-PAYROLL WORKER (I.E. SELF-EMPLOYED) AND ENGAGEMENT IS ‘OUTSIDE’ IR35 TAX REGIME*]**

The Company has determined that you are self-employed and not an off-payroll worker. As such, your engagement falls outside of the IR35 tax regime and you will be responsible for your own tax and NICs in respect of the services that you provide to the Company through your PSC.

[***OPTION B: WORKER IS AN OFF-PAYROLL WORKER AND ‘INSIDE’ IR35 TAX REGIME***]

The Company has determined that you are an off-payroll worker in deemed employment for tax purposes and your engagement falls within the IR35 tax regime.

[*EITHER (1): where the Company is responsible for deducting tax and NICs and paying these to HMRC*:

[As a result of changes to the IR35 tax regime, the Company is required to deduct tax and National Insurance Contributions (NICs) and pay them to HMRC in respect of fees paid to your PSC on or after 6 April 2021 (but only to the extent that they also relate to services provided by you on or after this date).

Records of payments and the amounts of tax and NICs deducted will be kept for [INSERT RETENTION PERIOD], as required by [law OR [INSERT REFERENCE TO THE COMPANY’S DATA PROTECTION POLICY DOCUMENTATION].]

[*OR (2): where the Agency (or another party in a labour supply chain) is responsible for deducting tax and NICs and paying these to HMRC:*

[As a result of changes to the IR35 tax regime, we trust that the Agency is the appropriate person to be responsible for deducting and paying the relevant tax and National Insurance Contributions (NICs) to HMRC in respect of fees paid for your services.

If, however, the Agency is part of a labour supply chain which provides your services to the Company, we note that these tax and NICs payment obligations may lie with another person in the chain, as required under the new rules.]

[*See drafting notes regarding the time limit for responding to a challenge.*]

**Challenging your employment status determination**

If you disagree with your employment status and would like to challenge the outcome of the SDS, please send your representations (including your reasons for any disagreement) along with any supporting evidence to [me OR NAME] by email [EMAIL ADDRESS]. [Provided that any final payment for your services has not already been made, the Company will respond within 45 days of receiving your representations.]

Thank you for your co-operation with the compliance process required by the changes to the IR35 tax regime and we look forward to working with you in the future.

Yours sincerely

[NAME]

[JOB TITLE]

**SCHEDULE 1: STATUS DETERMINATION STATEMENT**

**CLIENT:** [INSERT DETAILS]

**WORKER:** [INSERT DETAILS]

**WORKER’S PERSONAL SERVICE COMPANY:** [INSERT DETAILS]

[**AGENCY:** [INSERT DETAILS OF AGENCY THAT CLIENT CONTRACTS WITH FOR WORKER’S SERVICES (IF APPLICABLE)]]

**ENGAGEMENT:** [INSERT DETAILS OF THE PARTICULAR ENGAGMENT THAT THIS STATUS DETERMINATION APPLIES TO]

**DATE:** [INSERT DATE]

**STATUS DETERMINATION:** [INSERT DETAILS]

**REASONS:** [INSERT DETAILS]