**LETTER IN RESPONSE TO AN EMPLOYMENT STATUS DETERMINATION STATEMENT DISAGREEMENT**

**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’ 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).\*

\* Note that the client will not necessarily be the deemed employer if there is a labour supply chain in place (i.e. a chain of separate contracts between one or more agencies or other organisations, from the client to the worker’s PSC) and there is, for example, an agency in the chain who qualifies as the worker’s ‘fee-payer’ and ‘deemed employer’ instead of the client. HMRC guidance on identifying who is a fee-payer and the 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).)

* 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.

**Minimum requirements for a client-led status disagreement process**

* The IR35 tax regime requires clients to have a status disagreement process in place to deal with disputes regarding a SDS by the worker and/or the deemed employer. The client can decide who is the appropriate person or people to deal with disagreements. HMRC suggests that this could, for example, be the person who issued the original SDS to the worker.
* In summary, under a disagreement process the client must:
  + consider the worker’s and/or the deemed employer’s representations (which may be made verbally or in writing);
  + respond to the worker and/or the deemed employer’s representations within 45 days, beginning with the day the representations are received, not from when the SDS was issued;
  + inform the worker and/or deemed employer that EITHER (1) it has considered their representations and decided that its original SDS was correct (and provide reasons why) OR (2) that the original conclusion was wrong,
  + in cases where the client concludes that the original SDS was wrong, it must, taking reasonable care, produce a new SDS and pass it to the relevant parties (i.e. the worker, the deemed employer and, if relevant, any other party that the client contracts with for the supply of the worker’s services). The new SDS must provide the client’s reasons for reaching its conclusion; state the date when this new SDS became applicable; and also state that the previous SDS is withdrawn.
* Workers and deemed employers are entitled to raise a disagreement if they believe that either the client’s original conclusion in a SDS is incorrect for the whole period of the engagement, or because they believe the contractual terms and/or working practices have changed over time.
* Representations from the worker or deemed employer should contain the reasons why they disagree with the client’s SDS, providing sufficient information for the client to consider the representations. Representations can also be made even if the client did not actually issue a SDS (although in these circumstances the normal 45-day time limit will not apply). The client will be responsible for tax and NICs payment obligations if the engagement is one to which the rules apply so it is prudent for the client to consider any representations received.
* In terms of timing, representations can be made by a worker or deemed employer at any time. However, the client is only required to respond to representations made before a final chain payment is made in relation to a particular engagement (otherwise there would be no further payments on which the client could operate PAYE).
* If the client issued a SDS early (i.e. before 6 April 2021, which is permitted under the rules) and the worker or deemed employer also made representations before 6 April 2021, they are treated as having been received on this date. The effect of this is that the 45-day time limit the client has to respond to representations will only begin on 6 April 2021 (even if the client receives representations before that date).
* If the original SDS stated that the new rules applied and the engagement was ‘inside’ the IR35 tax regime, the deemed employer will remain responsible for tax and NICs payment obligations throughout the disagreement process. This remains the case unless, and until, the client decides that the worker does not fall under the rules. Equally, if the original determination was that the engagement was ‘outside’ the IR35 tax regime, this can be followed unless, and until, the client decides the worker falls within the rules. If any corrections are necessary, these should be made through payroll.
* If, at the end of the status disagreement process, a dispute still exists over the SDS and a worker considers that they have been taxed incorrectly as a result, HMRC states that the processes for [Self-Assessment](https://www.gov.uk/hmrc-internal-manuals/self-assessment-manual/sam110000) and [National Insurance](https://www.gov.uk/hmrc-internal-manuals/national-insurance-manual/nim37000) can be followed as a next step.
* Failure to comply with the minimum requirements of the disagreement process means that responsibility for tax and NICs payment obligations will transfer to the client. This will generally be the case, regardless of whether the client took reasonable care in making its determination.

**Using this template**

* This template letter is intended to provide a response to a challenge regarding the outcome of a worker’s SDS, as required under a client-led disagreement process. The IR35 tax regime stipulates that clients must have this process in place to deal with SDS disagreements. A challenge can be made by the worker and/or any third party who is the deemed employer (e.g. an agency) responsible for deducting and paying tax and NICs to HMRC.
* This template assumes that the client is a private sector company that is not subject to a small business exemption (referred to as ‘the Company’ throughout the template).
* The template 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.
* As appropriate, this template letter should be addressed to the person making the representations which challenge the SDS i.e. the worker and/or the deemed employer (which is most likely to be an agency in a labour supply chain who is also the worker’s fee payer). However, note that an agency who is not the deemed employer in a labour supply chain does not have the right to use the client-led disagreement process.

**Option A**

* Option Ashould be used in cases where the client, having considered the representations made by the worker and/or the deemed employer, decides that its original SDS is correct. The client must provide its reasons for reaching this conclusion.

**Option B**

* Option B should be used where the client has considered the worker and/or the deemed employer’s representations and decided that its original conclusion was wrong. Taking reasonable care, the client must issue a new SDS to the relevant parties (i.e. the worker, the deemed employer and, if relevant, any other party that the client contracts with for the supply of the worker’s services).
* The final paragraph in Option B clarifies where the responsibility lies for tax and NICs payment obligations before and after the new SDS takes effect. (See earlier comments in ‘Minimum requirements for a client-led status disagreement process’ section on how to decide where this responsibility lies.) It provides drafting alternatives for situations where the client concludes that the original SDS was incorrect for the whole duration of the engagement or where a change has taken place during the engagement which means that the original SDS is only incorrect after a particular point in time.

**SDS schedule**

* If Option B is applicable, the SDS must state the client’s new conclusion (i.e. whether or not the worker would be an employee for tax and NICs purposes if they were directly engaged by the client). It must also include the client’s reasons for reaching its conclusion and make it clear on what date the new SDS is effective from, while also confirming that the previous SDS has been withdrawn.
* Pinpointing the effective date of the new SDS, in Option B, is relevant because a worker (or deemed employer) can raise a disagreement either where they believe that the client’s original conclusion is incorrect for the whole period of the engagement or because they believe that contractual terms and/or working practices have changed over time. (See above for details of wording in the final paragraph of the letter template to reflect this in Option B).
* This template provides a framework within which to include the worker’s new SDS. It is essential that client’s take reasonable care when producing the SDS, especially after a successful challenge to the original SDS. This 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**

* 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]] OR [DEEMED EMPLOYER AGENCY]]

[ADDRESS]

Dear [NAME],

**Employment status disagreement**

I am writing in response to your representations regarding [your employment status determination statement (SDS) OR the employment status determination statement (SDS) of [WORKER’S NAME] (the ‘Worker’)].

The SDS (dated [DATE]) was produced by [COMPANY NAME] (the ‘Company’) in relation to [you OR the Worker] and the services provided through [your OR their] personal service company [PSC NAME] (the ‘PSC’) under the [DETAILS OF THE ENGAGEMENT] (the ‘Engagement’).

As required under HMRC’s IR35 and ‘off-payroll working’ rules (together the ‘IR35 tax regime’), the Company has considered your representations [(made in your capacity as the deemed employer of the Worker)], challenging [your OR the Worker’s] current SDS, under its status disagreement process.

**Conclusion of the Company’s status disagreement process**

[***OPTION A: CLIENT DOES NOT ACCEPT REPRESENTATIONS AND CONFIRMS ORIGINAL STATUS DETERMINATION***]

Having given careful consideration to your representations, the Company has concluded that [your OR the Worker’s] SDS remains valid and correct for the reasons set out below.

[LIST REASONS]

I hope that the reasons stated above provide you with the necessary information to resolve any disagreement regarding [your OR the Worker’s] SDS.

This is the final decision under the Company’s status disagreement process. If you have any other questions regarding [your OR the Worker’s] SDS, you may contact HMRC directly for further clarification.

[***OPTION B: CLIENT ACCEPTS REPRESENTATIONS, WITHDRAWS CURRENT STATUS DETERMINATION STATEMENT AND ISSUES A NEW ONE***]

Having given careful consideration to your representations, the Company has concluded that [your OR the Worker’s] original SDS is no longer valid and correct.

As a result, the Company has withdrawn the original SDS. After conducting a thorough review of [your OR the Worker’s] employment status and the services provided under the Engagement, the Company is issuing a new SDS along with the reasons for its conclusion (see attached Schedule 1) [to you and any other relevant parties,] as required under the IR35 tax regime.

The new SDS will be effective from [DATE]. [*The next sentence can be deleted if the client concludes that the original SDS was wrong for the whole duration of the Engagement.*] [Up until this date, [you OR [INSERT NAME] (the original deemed employer)] will remain responsible for tax and NICs payment obligations in relation to the Engagement.] On or after [DATE], responsibility for tax and NICs payment obligations will sit with [you OR [INSERT NAME] (the new deemed employer)]. Any necessary corrections or adjustments to payroll will be made, as required under the IR35 tax regime.

Thank you for raising your representations with the Company and I trust that this matter has now been resolved satisfactorily.

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)]]

[**NEW DEEMED EMPLOYER**: [INSERT DETAILS OF NEW DEEMED EMPLOYER (IF APPLICABLE)]]

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

**DATE:** [INSERT DATE FROM WHICH THIS STATUS DETERMINATION STATEMENT IS EFFECTIVE AND STATE THAT THE PREVIOUS STATUS DETERMINATION STATEMENT HAS BEEN WITHDRAWN]

**STATUS DETERMINATION:** [INSERT DETAILS]

**REASONS:** [INSERT DETAILS]