

31 March 2017

Dear Colleagues,

I wrote to Permanent Secretaries last week about the challenges we are experiencing in implementing the changes to the off-payroll rules for contractors engaged through Personal Service Companies (PSCs) and similar intermediaries across Government. I noted that we had identified contrasting outcomes in the decisions departments are making on whether the off-payroll rules apply. The scale of this contrast is such that several departments are indicating that over 80% of contractors are likely to be determined as out of scope, whereas others are indicating that 70-80% of contractors will be in scope of the off pay roll rules. Whilst not all contractors will be within the rules and there may be good reasons for the contrast in outcomes, it does raise concerns where there is evidence that contractors are engaged and work in similar ways.

As government departments, we have a responsibility to implement the reformed off-payroll rules effectively. This means that we need to be confident in the judgements we make on status. I have therefore established a Steering Group to monitor the on-going implementation of the changes across Government with a view to driving overall consistency and providing some assurance to departments on the accuracy of their decisions.

The group met for the first time on Monday 27 March and discussed the causes of the inconsistencies and identified particular issues where departments need to ensure their approach is in line with the guidance. HMRC have tightened the wording of the substitution and working practices questions in the employment status service and will provide additional guidance on the service's results page; ahead of incorporation in the tool this **is attached at annex a.** In addition I have reiterated below key considerations that are pertinent to Civil Service departments. Following these pieces of guidance will provide departments with a higher level of assurance in their determinations.

Decisions should be made in line with the legislation rationale and guidance.

The legislation states that the key test of whether a contractor is in scope of the off-payroll rules is whether, 'if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client or the holder of an office under the client.'¹

Accordingly, engagement decisions should be made 'in the round' and not focusing on individual factors in isolation from each other.

If a contractor is engaged to work in a defined job role that would otherwise be filled by a current or former employee, without substantive changes to the working practices, it is likely that the engagement will be in-scope of the off-payroll rules.

¹ Finance Bill 2017 Part 2, Chapter 10 section 61M

Decisions should be based on actual working practices not contractual terms.

Decisions on whether the rules apply must be made on the basis of actual working practices, rather than contractual terms. It is important that working practices can be evidenced or the feasibility of them explained. This is in line with tax case law.

When considering questions about substitution, departments should consider the situations in which it may be appropriate to cede decisions on who undertakes work to a PSC or other intermediary. This may differ depending on the specific responsibilities or the context of particular roles. For example, where a department decides to hire a specific individual (through their PSC) without any competitive process because the individual has unique skills/experience, it is unlikely that the department would in practice allow substitution. It is also unlikely that departments would wish to allow substitution in respect of contractors working in senior management roles such as SCS, Programme Directors or Heads of Unit.

The key point is that departments making the assessment should consider whether they would, in practice, allow substitution, and not just whether the relevant contract allows a right of substitution.

Conversely, if the only matters a department would in practice require to verify are that a substitute has appropriate security clearance, relevant qualifications and correct level of experience, then the right of substitution is effectively unfettered for the purposes of answering the question in the HMRC assessment tool.

It is important to remember that the substitute must be supplied and paid by the contractor's intermediary company (the PSC). If another body (e.g. an agency) sends a different worker, this will form a new engagement between that body and the department and will not constitute substitution (even if the contractor had referred the new worker to the department).

Decisions should be based on HMRC guidance.

HMRC will stand by the results of the online tool but this must be used in line with HMRCs guidance available at: <https://www.gov.uk/government/publications/off-payroll-working-in-the-public-sector-reform-of-the-intermediaries-legislation-technical-note/off-payroll-working-in-the-public-sector-reform-of-the-intermediaries-legislation-technical-note>

The tool is currently in public beta and we are continuing to improve the wording of the questions and embedded guidance in response to feedback. We will stand by the output of the public beta service subject to the caveats above.

HMRC resources should be the prime source of information for making decisions. If departments require additional help, they are encouraged to seek advice from within government such as through the Tax Centre of Excellence, rather than external agencies.

Communicating decisions

As Accounting Officers, it is important that Permanent Secretaries are briefed on the off-payroll status decisions within their department. Where departments do not provide the body with which they contract (the contractor's PSC or the agency or other body involved) with details of determinations ahead of the first pay date to PSCs, (or do provide details but without taking reasonable care in their assessment), they will be liable for tax and national insurance.

Converting contractors to Temporary Fixed Term Appointees.

Some departments may wish to consider converting contractors to Civil Servant Temporary Fixed Term Appointments (FTAs) as part of their response to the changes. The terms of these must align, where applicable to the DDaT and Commercial reward frameworks. Departments must ensure that this solution is only used where roles are genuinely fixed term and be mindful of the usual employment law principles that relate. Departments must comply with the Recruitment Principles issued by the Civil Service Commission, and if they are using exception 2 to the Principles, no extensions to the maximum 2 year period should be granted. Appointment on merit through fair and open competition must be undertaken for such roles when the initial FTAs using the exception expire. It is important that those who take up a Temporary FTA understand that the Civil Service Code and standard departmental terms and conditions will apply, including rules on conduct, and in particular that they may be required to declare any outside interests.

If departments are seeking flexibility to the Civil Service Recruitment Principles from the Civil Service Commission, I would like my team to be sighted on business cases in advance. Please email these to civilservicepay@cabinetoffice.gov.uk.

Next steps

The Steering Group will meet regularly over coming weeks to monitor the implementation of the changes. I will circulate the minutes from these meetings for your information and action.

I recognise that adoption of the Steering Group recommendations may result in the need for departments to review and adjust their previous determinations. I also recognise the on-going risk of attrition during this period. Where you see such challenges occurring in your department, I ask that you feed that back to me for the Steering Group to consider. We can then identify a consistent response and target support should we need it.

HMRC have led a further series of workshops to help departments and the wider public sector ensure they are implementing the changes correctly. I know many of your HR, Commercial and Finance teams have taken part in these. HMRC will be following up queries and feedback to the tool and guidance which arose from these.

A handwritten signature in black ink, appearing to read 'Rw', with a large, sweeping initial 'R'.

RUPERT MCNEIL

Revised wording of questions in the HMRC Employment Status Service tool

Substitution

HMRC has redesigned the questions on substitution to strengthen it by turning it round to the circumstances in which an engager would reject, rather than accept a substitute, and by unpacking a little more the yes/no answers, to make it clear that only unfettered substitution counts, as follows:

Would the end client ever reject someone else (a substitute) sent to do the work by the worker's business, even if they met all of these criteria?

They:

- are equally skilled, qualified, security cleared and able to perform the worker's duties
- won't be interviewed by the end client before they start (except for verification checks)
- aren't from a pool or bank of workers regularly engaged by the end client
- will do all of the worker's tasks for that period of time
- are being substituted because the worker is unwilling or unable to do the work

Answers:

- Yes - the end client has the right to reject a substitute for any reason, including if it would negatively impact the work
- No - the end client would always accept a substitute who met these criteria (*only this answer is an unfettered right to substitution, all others indicate personal service/fettered right*)

If you answer No, i.e. that there is an unfettered right to substitution, the next question asks would the worker's business (i.e. the personal service company, not the agency) have to pay the person who did the work instead of them? Only where the answer to that question is yes, would the tool then produce an outcome that the worker is outside the rules.

HMRC are also adding additional guidance on the results pages to explain the outcome engagers have got from the tool as follows:

Substitution has happened:

You've told us that the worker's business has arranged and paid for a substitute to work on this engagement, and that the end client accepted it. This suggests that the end client is engaging the worker on a business to business basis, rather than on a personal service basis.

[!] If HMRC investigate this engagement, the worker and the end client will need to demonstrate that paid substitution has happened.

Substitution would happen:

You've told us that the worker's business could arrange and pay for a substitute to work on this engagement, and that the end client would accept it. This suggests that the end client is engaging the worker on a business to business basis, rather than on a personal service basis.

[!] If HMRC investigate this engagement, the end client will need to confirm that they would accept substitution in practice and are not simply reflecting a theoretical contractual

entitlement. They may also be asked to demonstrate that they have accepted substitution on this, or a similar engagement.

Working Practices

The question on putting work right has been revised to make the financial risk associated with this easier to understand.

If the end client isn't satisfied with the work, does the worker need to put it right at their own cost?

Yes – the worker would have to put it right without an additional charge, and would incur significant additional expenses or materials purchases ('materials' would not include stationery, and most likely to be relevant to substantial purchases in the construction industry, significant would not normally include one off costs)

No – the worker has to put it right outside usual hours for no additional charge but without significant additional expenses

No - the worker would put it right in their usual hours at the usual rate of pay, or for an additional charge

No - the worker wouldn't be able to put it right because the work is time-specific or for a single event

No – they wouldn't need to put it right