



MODERN WORKING PRACTICES: EMPLOYMENT STATUS RULES FOR EMPLOYMENT RIGHTS AND TAX/NIC

Issued 25 April 2018

ICAEW welcomes the opportunity to respond to the **Employment status** rules for employment rights and tax consultation published by BEIS, HMT and HMRC on 7 February 2018 as part as the **government's response** to the Taylor 'Good Work' report and the joint BEIS and Work & Pensions Select Committee report on modern working practices.

This response of 25 April 2018 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business.

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EXECUTIVE SUMMARY

1. The current situation is one of multiple definitions for employee rights, tax, NIC, pensions, etc. We are concerned that this position is unsustainable in the medium to longer term. We therefore believe that the government should encourage and facilitate an informed national debate on the future of how work should be taxed, together with the associated rights and benefits. The changes needed for a sustainable system will affect more than one generation of worker and should explore not only employment and pension rights etc but also the principles that should underpin the tax and NIC treatments faced by businesses and the workers they engage. The review should consider whether the definitions should change, and identify and explain why such changes are needed.
2. Such a debate, which should include the public, would be able to explore radical, and potentially challenging, policy options. For example, these could range from simpler tests for employment status, through tax/NIC-based solutions which would harmonise hirers' costs between employees and non-employees and remove incentives for workers to be hired other than as employees, to default requirements. Such a debate would also consider the extent to which different types of worker should be entitled to which rights.
3. In the meantime, we suggest that government makes no legislative changes in this area, and in particular does not codify the existing law, pending the agreement of sustainable solutions on employment rights and tax/NIC.
4. Furthermore, for the reasons outlined in our letter dated 5 April 2018 to the Financial Secretary to the Treasury ([ICAEW REP 40/18](#) – see further below), we do not think that extending the public off-payrolling rules from the public to the private sector is currently feasible.

GENERAL COMMENTS

5. We welcome the government's response to the reports from Matthew Taylor and the joint BEIS/DWP parliamentary select committee and the four consultation documents.
6. We understand and appreciate the political sensitivities underlying the government's decision not to address the disparities in the rates of NIC paid by and in respect of employees and those paid by the self-employed. We also recognise that government may as a matter of policy wish to provide recognition in the tax system to those in self-employment.
7. However, the imbalance between NIC costs in respect of employees – especially employers (ie, secondary Class 1) NIC – and non-employees continues to distort how some workers are hired, or choose to be hired. The current position, which is by no means new but which is being highlighted by the ability to harness information technology to set up new platforms through which to hire and pay workers, is we believe unsustainable in the medium to longer term.
8. We believe that the government should work with stakeholders and business to try and identify a suitable solution which is straightforward and complies with our *Ten Tenets for a Better Tax System* (outlined in Appendix 1) and therefore can be easily and robustly enforced. Taking forward the Taylor and joint BEIS/DWP select committee reports provides an opportunity for the government to host an informed debate to

explore the principles that should underpin employment rights, pensions and the tax and NIC treatments faced by businesses and the workers they engage.

9. The debate needs to consider whether for ease of administration there should be the same definition covering both employment rights and tax/NIC (so a worker is either an employee or self employed for both rights and tax/NIC) or whether the economy is better supported by having separate definitions. The debate should identify and explain why changes are needed so that the UK workforce can also participate in the discussion. To facilitate this, government could undertake an extensive communications exercise about a more level employment rights and tax/NIC playing field post-Brexit for workers and businesses.
10. A wide-ranging debate would usefully explore other, radical and potentially challenging, policy options. These could include:

simpler tests for employment status

eg,

- a worker receiving a given proportion, say 75%, of their income in a given period, say nine months, from one organisation – although this test would not give hirers certainty as to whether a worker should be subject to PAYE at the start of the contract,

tax/NIC-based solutions which would harmonise hirers' costs between employees and non-employees

eg,

- abolishing employer NIC lower earnings thresholds,
- introducing withholding tax/NIC where non-employees undertake work for organisations, similar to the construction industry deduction scheme,
- replacing employer (secondary) NIC with, say, an engagers levy payable by organisations – or even individuals – that hire labour regardless of whether or not the workers are employed, self employed or work via a company or intermediary,

default requirements

eg,

- an organisation which is benefitting from a worker's services must treat the worker as an employee for tax and rights even if the worker is working via an agency or personal service company.
11. We put forward the ideas in the previous paragraph as matters that we believe should be considered in an informed public debate and we do not necessarily endorse them.
 12. Mathew Taylor's report considered the concept of a special category of worker where there is an acceptance that the worker is being paid – where withholding could apply – but there is no automatic requirement for employment rights. What happens if people find themselves in multiple pensions, holiday/sick pay schemes, etc? This whole area should be debated.

13. Such a debate would also consider the extent to which different types of workers should be entitled to different rights.
14. Codifying existing case law would be very difficult. In Appendix 2 we provide an example of how one might define a contract of employment at a high level on the basis of existing case law. However, we think that codification would raise new issues of interpretation which would give rise to new case law. Codifying the present rules is not in our opinion a sustainable solution as it would perpetuate current difficulties and could reduce the ability of the courts and tribunals to address particular circumstances. Guidance would be also be needed to supplement any new legislation.
15. Similarly, extending the April 2017 public sector off-payroll regime to the private sector, while potentially benefitting exchequer cash flow, would not provide a sustainable solution and is likely to impose on the private sector the numerous practical problems and consequential compliance costs now being faced by organisations and workers in the public sector. These include lack of transparency for workers, problems in accounting for fees in personal service companies, inability in payrolls to distinguish deemed from actual employees (and thence automatically suppress eg, student loan notices, auto-enrolment processes, etc), and the inaccuracy of HMRC's check employment status tool (CEST). If this scheme is to continue in the public sector, these issues must be addressed as they are imposing unnecessary burdens on those involved.
16. We suggest that the government makes no legislative changes in this area pending adopting sustainable solutions on employment rights and tax/NIC following public debate.

DETAILED COMMENTS

17. We agree the synopsis of the current legislation and frameworks noted in the consultation document at Chapter 3: *The current legislation and frameworks* and with the summary of the difficulties in Chapter 4: *Issues with the current employment status regimes* (namely, open to interpretation, complexity and difficulties in resolving disputes). However, any consideration of modern working practices and changes to employment status rules needs to be undertaken in the context of how imbalances in the tax/NIC system (especially employer NIC) drives workers to be hired other than as employees.
18. Codifying the present rules as suggested in Chapter 5: *Legislating for the current employment status tests* would not provide a sustainable solution. As stated above, the problems arise from tax/NIC imbalances and difficulties arising from different employment rights definitions, and, as noted in the consultation document, codification may make it more difficult for the courts and tribunals to exercise judicial flexibility to accommodate different circumstances. We therefore believe that, before undertaking codification, an informed debate to enable sustainable solutions to be identified is needed. Once a national debate has arrived at sustainable solutions for rights and tax, then codification would be the logical next step.
19. Without wishing to pre-empt the outcome of any debate, we suggest that codification of employment status rules would best be incorporated into the Interpretation Act 1978 if definitions of rights and tax are to be consistent. If possible and practicable, the same regime should apply throughout the United Kingdom (eg, by way also of incorporation into the Interpretation Act (Northern Ireland) 1954). Given the wide range of

stakeholders and situations to be addressed, any codification would need to be supported, perhaps by regulations and also by detailed guidance.

20. Notwithstanding our reservations about undertaking codification prior to an informed debate, we have in Appendix 2 included as a possible starting point wording to define employment contract based on the existing tests.
21. Chapter 6: *A better employment status test* considers whether new and/or simpler tests are needed. As noted above, the present distortions in hiring practices partly stem from imbalances in the tax/NIC costs of hiring employees when compared to non-employees. New and/or less complex tests would not necessarily resolve this unless they enable hirers to ascertain whether the worker is an employee (and thus liable to PAYE and entitled to employee rights), or not, from the beginning of the contract term. New tests would also mean that employers, workers and advisers would need to learn new rules but, if new rules provided certainty and were simpler, those aspects would be an improvement.
22. New tests would need to be codified to ensure that disagreements can be resolved impartially; we therefore would not favour new tests that are not incorporated in to the legislation. At the same time, non-legislative aids alongside the legislation, such as status tools into which the facts and circumstances can be input, the outcomes of which the owning Department stands by, would be welcome, so long as the tools are reliable and accurate and test against all major relevant factors. (HMRC have stated that HMRC's check employment status tool (CEST) ignores mutuality of obligation because it was designed for the public sector and consequently CEST is not currently suitable for the private sector which has a wider variety of contracts).
23. Chapter 7: *The worker employment status for employment*. As with the employment status test, we recommend no change to the existing law until an informed debate can be had as recommended above.
24. Chapter 8: *Defining working time*. We consider that this is primarily a legal issue and therefore have no specific comments to make here.
25. Chapter 9: *Defining self employed and employers* considers whether 'self employed' and 'employer' should be defined. We consider that, pending a national debate, it is premature to attempt to define these terms given the differences currently between employment rights laws and tax/NIC laws.
26. Chapter 10: *Alignment between tax and rights* asks whether tax and rights tests should be aligned. We believe that employers would welcome one set of rules. A national debate would provide the opportunity to consider whether such tests should extend to deemed employees and whether they should be entitled to the same rights as employees.
27. As to *consultation administration*, an additional final question on the Q&A template seeks comments on the consultation itself. We have stated above that we believe that a public debate is needed to arrive at sustainable long term solutions, so, while we welcome the opportunity to respond to this consultation and that the consultation period is longer than normal (reflecting the complexity and importance of this topic), we suggest that, at this stage, it is premature to hold a consultation and think it would have been better to have framed it as a call for evidence. However, we are happy to help take this review forward.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <https://goo.gl/x6UjJ5>).

APPENDIX 2

POSSIBLE NEW DRAFT SECTION FOR INTERPRETATION ACT 1978

Contract of employment

- (1) A contract of employment shall exist between a person (A) and an individual (B) where:
 - (a) there is mutuality of obligation ,
 - (b) There is no unfettered right of substitution
 - (c) there is a right of control; and
 - (d) none of the conditions in subsections (8) to (10) apply.
- (2) Mutuality of obligation between A and B exists for the purpose of subsection (1) where under the contract between A and B, B is obliged to perform some service for A, A is obliged to remunerate B for performing that service, and A is obliged to provide work to B.
- (3) For the purposes of subsection (1) an unfettered right of substitution exists where:
 - (a) B can delegate the service to be performed for A to some other person, or can procure a substitute to perform that service provided that that right can reasonably be exercised in practice; and
 - (b) that delegation or substitution can be exercised at any time at the option of B, without regard for whether B is able or unable to perform the service.
- (5) A right of control for the purposes of subsection (1) means a right whereby A may exercise control over B as to what service B is to perform on any particular occasion, or where, when or how B is to perform it, subject to subsections (6) and (7).
- (6) A right of control does not exist for the purposes of this section where the level of control derived from it is insufficient to make A master over B.
- (7) A right of control does not exist for the purposes of this section where the control specified is not realistically exercisable in practice.
- (8) The condition in this subsection is that the contract is for B to produce a thing, or a result, for a price, and B is not a rated output worker, ie, a pieceworker.
- (9) The condition in this subsection is that B is in partnership, and acting in the course of that partnership in carrying out his obligations under the contract.
- (10) The condition in this subsection is that B is in business on his own account, and acting in the course of that business in carrying out his obligations under the contract.
- (11) For the purpose of determining whether B is in business on his own account, regard may be had to the following factors:
 - (a) The level of control (if any) in practice exercised by A over B;
 - (b) Any right of substitution that is not unfettered;
 - (c) The length and number of B's engagements;
 - (d) The existence and value of any equipment owned by B in carrying out his obligations under the contract;
 - (e) Whether B is part and parcel of A (if A is not an individual);

- (f) The ability of B to profit from sound management;
 - (g) The risk of B making a loss;
 - (h) Whether B has a business structure;
 - (i) Any prohibitions on B performing services for parties other than A;
 - (j) The terms of payment in the contract;
 - (k) Any contractual right to paid leave, sick pay, or other forms of payment normally associated with employment;
 - (l) Any contractual right not to be unfairly dismissed;
 - (m) Any other matters considered relevant.
- (12) In cases where it is reasonable to doubt whether the requisite conditions apply for there to be a contract of employment, the stated intentions of the parties, where concurrent and freely given, shall determine the matter.
- (13) The parties may state their intentions as to whether or not a contract of employment applies by any means that they see fit, and are not confined to the terms of the contract in so doing.
- (14) For the purposes of this section, A may include a partnership or unincorporated association.