



Select Committee on Economic Affairs

Finance Bill Sub-Committee

Draft Finance Bill 2019-20: Off-Payroll working rules

Monday 16 March 2020

3.20 pm

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Members present: Lord Forsyth of Drumlean (The Chair); Lord Bridges of Headley; Baroness Kramer; Lord Rowe-Beedoe; Lord Tyrie.

Evidence Session No. 5

Heard in Public

Questions 52 – 62

Witnesses

I: Lindsey Whyte, Director, Personal Tax, Welfare and Pensions, HM Treasury; Paul Riley, Director, Tax Administration, HMRC; Cerys McDonald, Director, Off-Payroll Reform Programme, HMRC.

II: Carl Vincent, Chief Financial Officer, NHS Digital.

Examination of witnesses

Lindsey Whyte, Paul Riley and Cerys McDonald.

Q52 **The Chair:** Ms McDonald, Ms Whyte and Mr Riley, welcome to the Finance Bill Sub-Committee. We are very grateful to you for coming along this afternoon.

Perhaps I might begin by asking a slightly more topical question. We have had quite a lot of evidence, and I am sure you have been following what has been said. Indeed, I spent most of the weekend reading 700 written submissions we have had, mainly from people who are directly affected by the proposed changes. A summary of what is being suggested by many contractors is that they are going to find themselves under very severe pressure financially as a result of the changes. I wondered whether Her Majesty's Revenue and Customs had considered, given the enormous financial impact we are about to experience as a result of coronavirus, whether it might be sensible for you to defer introducing the changes for at least six months, if not a year.

Cerys McDonald: Thank you. It might be better for Lindsey to speak to that, because it would be a matter of policy for Ministers.

Lindsey Whyte: As the Committee will be aware, the Chancellor confirmed in the Budget last week that it would still go ahead from April 2020. Alongside that, the Chancellor announced quite a significant package of support for public services, individuals and businesses in responding to the coronavirus outbreak. I am very happy to say a bit more about what was in that to support individuals. The Government are acutely aware that this is going to be a difficult time for many people and businesses, and have sought to put in place a whole series of measures to provide that support.

The Chair: I am asking you whether you might decide not to go ahead with a measure that our evidence indicates will have a very damaging effect on the incomes of many self-employed and contractors. Has it been considered?

Lindsey Whyte: As I said, the Chancellor announced in the Budget that it is going ahead.

The Chair: I know what he said in the Budget. I am asking whether it was considered.

Lindsey Whyte: I cannot comment on policy advice that might or might not have been given; I can only tell you that it was announced that it is going ahead.

The Chair: The Budget speech would have been written somewhat in advance of its delivery, and that decision would have been taken. Knowing what we know now about the catastrophic effect that coronavirus will have on the economy, do you think it would be sensible to consider deferring this?

Lindsey Whyte: That is a question for Ministers to determine. Over the past many months, most particularly recently in the course of undertaking the review on implementation of IR35, Ministers received representations about whether or not to proceed with the reform, and the Government determined that it was still the right thing to proceed with the reform from April 2020. We received evidence that a number of businesses that are well prepared for the reforms, after many consultations and lots of engagement, would now find it harder in some cases not to proceed. We are doing everything we can in response to that review to smooth the implementation and support for individuals and businesses operating the rules. Cerys can say a bit more about what we are doing to support that.

The Chair: If I am a contractor who has to go to an umbrella company and as a result I lose 30% of the revenue I expect, and as a result of coronavirus my ability to generate revenue is severely depleted, what is being done by the Government when this comes into effect on 6 April to compensate for that?

Cerys McDonald: At a macro level in the support we offer individuals?

The Chair: No. I am a contractor faced with a problem that has been created by your policy change. You are saying that the Government have thought about what might be done to help those people. What are you going to do to help me in those circumstances?

Lindsey Whyte: I think the wider set of responses for individuals and businesses is very relevant to individuals employed by personal service companies in this space.

The Chair: Except that they are not affected by this.

Lord Bridges of Headley: The Chancellor's precise words were that he wanted to ease the burden on business. How does pressing ahead help to ease the burden on business?

Lindsey Whyte: The IR35 reforms have been consulted on and in train for a number of years. They will remove the obligation from a number of personal service companies to undertake the assessment themselves, and will mean that, from now on, large and medium-sized organisations are responsible for undertaking the assessment. We have exempted small businesses from doing that, so they will be protected, but it is worth saying that within the wider coronavirus response package there are a number of measures that will also provide support to all small and medium businesses and for which personal service companies will also potentially be eligible.

Lord Bridges of Headley: I hear all that. I think we would all agree that the pharmaceutical companies are in the front line in the fight against coronavirus. How is this helping companies like GlaxoSmithKline? I gather that HMRC has sent warning letters to nearly 1,500 self-employed contractors at GlaxoSmithKline. How is that helping to ease the burden

on that business?

Cerys McDonald: I want to make a distinction between the report you referred to about the letters issued last summer, which are routine compliance activities operating under the existing IR35 rules, and the reforms that come into play from April going forward. HMRC has taken significant steps to put together a package of support for businesses. We are holding one-to-one calls with every large business to talk them through how the changes are expected to roll out, to ensure that they are putting in place the right systems and processes and to answer any questions they have.

Lord Bridges of Headley: You are holding those calls now.

Cerys McDonald: We are.

Lord Bridges of Headley: Is that a good use of their time in the middle of a crisis like this?

Cerys McDonald: The calls are not mandatory for businesses; they are offered to businesses, and we stand ready to support them.

Lord Bridges of Headley: Maybe I can ask the Treasury. Is that a good use of businesses' time at a time like this? Is people having those conversations with HMRC what we mean by easing the burden on business?

Lindsey Whyte: The support is there for them if they need help in implementing the reforms. There is also a considerable amount of further support available to businesses through Time to Pay; there is a new small business support scheme and there is lending support. The package which the Chancellor set out alongside the Budget includes quite significant extra support for businesses, because we recognise that this is going to be a very difficult time.

As you mentioned pharmacy in particular, it is worth saying that the Department for Health and Social Care is working very closely with the Pharmaceutical Services Negotiating Committee and the NHS to make sure that we prioritise the right services for community pharmacy to provide to ensure that they are the most important things for supporting patients through the current outbreak, and we are suspending other things to try to relieve that pressure.

Lord Bridges of Headley: Given that you mentioned healthcare, let me read to you what the secretary-general of the Independent Health Professionals Association said: "What we are seeing in Italy is that intensive care beds quickly fill up. There is some capacity to expand these, however this will be of no use if we cannot adequately staff these additional beds. Rishi Sunak stated in a Sky News interview ... that he will give the NHS whatever it needs. It is now vital to patient safety that these reforms are suspended and I call upon him to make good this promise for the safety of our patients". What do you say to that?

Lindsey Whyte: I would point to the support which the Chancellor has announced. The Chancellor is very clear that the NHS will get all the funding that it needs to ensure it can cope with the coronavirus outbreak. We announced a specific pot of money in the Budget as part of that follow-up, but the Chancellor is very closely involved in all the conversations with the Department for Health and Social Care to make sure that we provide the right support. All I can say is that the position on IR35 is as was set out in the Budget, and beyond that it is really a question for Ministers. I am afraid I cannot go beyond that.

The Chair: Perhaps it might be a good idea to suggest to Ministers that, if their words mean what they are meant to mean, it might be sensible to suspend implementation of this change because of the impact it will have on those businesses. It is generally acknowledged that what is being proposed in the Budget is inadequate for the scale of the crisis, and it seems rather perverse to add an additional burden of this kind on business that could easily be deferred for six or 12 months.

Q53 **Lord Rowe-Beattie:** A statement has been made that non-compliance with the off-payroll rules is widespread. What evidence do you have for that?

Cerys McDonald: That assessment has been based on our analysis of tax receipts and tax return data. In addition, we have looked at evidence from our front-line compliance staff. It is also an assessment that we hear played back to us from stakeholders and businesses who observe non-compliance in their own supply chains. In the evidence that has been presented to this Committee and the feedback we have had in numerous consultations on it, I have not seen anyone argue strongly to the contrary—that non-compliance is not widespread.

Lord Rowe-Beattie: That is interesting, but how does it come about? We have heard that non-compliance is widespread. You are saying that you have no evidence at all.

Cerys McDonald: No. We absolutely have evidence that non-compliance is widespread. I am saying that I share that view.

Lord Rowe-Beattie: I misunderstood you.

Cerys McDonald: HMRC's very firm position, and the motivation and rationale for the reforms, is to address the widespread non-compliance that we observe. Indeed, HMRC has put forward evidence of its estimate that nine in 10 personal service companies are not correctly operating the rules at the moment.

Q54 **Lord Rowe-Beattie:** Your plan is to shift responsibility for regulatory oversight in operating the rules to the clients. Is that a good idea?

Cerys McDonald: The burden for operating the rules, as you rightly point out, currently sits with individuals, and non-compliance is high and has been high for some time. We are changing the obligation and putting it on the client.

It is worth reflecting a little on the challenges that we have as a tax administration department in the context of a very significant shift in the way our labour market is operating. Clearly, the increase in the number of self-employed and owner-managed businesses presents different challenges which HMRC has to step up to and address. This particular measure is a good example of the types of steps HMRC needs to take to protect the tax base, stop the tax gap increasing and improve the trust of our customers in what we do to ensure that there is a level playing field.

Deduction at source, collecting tax and information in real time, and using intermediaries to collect tax on our behalf are all design features that support good tax administration, make things easier for our customers and reduce the risk of error and wider non-compliance. For example, the tax gap figure for PAYE is just 1%, compared with the tax gap figure for self-assessment, which is currently estimated to be 17%. The reform moves away from a self-assessment-style model, where the obligation is on individuals to assess their tax status and report it, and instead puts the responsibility on individual employers to ensure that the employment taxes that are due are paid. We believe that the reform is a good strategic improvement in the way we ensure that we collect the right employment taxes.

Lord Rowe-Beattie: Going back to the comments made by Lord Bridges, is this the appropriate moment to put a further burden on the “employer”?

Cerys McDonald: I hear the Committee’s arguments on that, but at the moment the burden is sitting with 170,000 personal service companies and individuals who are responsible for operating the rules. Yes, we are moving responsibility at the supply chain to the end engager, but we argue that those organisations are better equipped to operate the rules correctly than what we have seen to date, and that is what the evidence suggests.

The Chair: If you have been following the evidence to the Committee, it shows that, rather than looking at those 170,000, or whatever it is, on an individual basis, large employers are simply taking a blanket view and, as a result, are telling them to go to an umbrella company or go elsewhere. That is added to their cost. You talk about a level playing field, but, although the people concerned may be paying tax and national insurance on the same basis, they do not have the same employment rights and the same ability to claim sick pay, holiday pay and so on. It is hardly equitable.

Cerys McDonald: On the blanket assessment point, it is important that we are very clear in our terminology. The wording “blanket assessment” and all the reporting of it is being used to describe a wide range of behaviours. At one end of the spectrum, large organisations are looking at their workforce strategies and how they augment their current labour force using personal service companies. They are reviewing that and, in some cases, taking decisions to operate differently: bringing people in-house, or looking to engage people via an umbrella company. I

acknowledge that that is a consequence of the reform, but those decisions are commercial decisions.

A second set of behaviours has also been reported.

The Chair: Before you go on to the second set of behaviours, you say that those decisions are commercial decisions. If I am running a big organisation, have lots of subcontractors and have to take the liability and look at all of them, I can see why I would be tempted to say, "You know what? We don't want to have anything to do with this any more". That appears to be the evidence we are receiving as to what is happening. It might be a commercial decision, but it has been a commercial decision as a result of the change you have made.

Cerys McDonald: These changes are designed to ensure that we collect taxes that are currently properly due. It is important to remember that we are not changing the underlying tax rules. The individuals affected who ought to be within the IR35 rules and where there is non-compliance are currently having a subsidy from the taxpayer.

The Chair: But you are assuming that the people concerned are all fiddling their taxes.

Cerys McDonald: That is not what I am saying.

The Chair: If they are not, you are imposing a change that results in their commercial relationship being destroyed.

Cerys McDonald: I accept that, because of the way the rules have operated over 20 years, industry practices have become well established. There are ways in which the labour market has adapted to those changes, and to an extent there is a level of non-compliance in that area. It is right that the Government are taking action to address that. It is forecast that the cost to the public purse will be £1.3 billion in two years' time. We are trying to find a better mechanism for collecting the taxes due.

Can I move quickly to deal with blanket status assessments as well, because that is the second category people have raised concerns about? I absolutely share the Committee's concerns about any instances where firms blanket-assess the status of individuals. The legislation is very clear that that is not lawful, and we expect large and medium-sized businesses to take reasonable care in individual assessments.

The Chair: What is the remedy if they do not?

Cerys McDonald: There are a couple of points. HMRC's overriding objective is to make sure that the right tax is paid. If there are instances where an individual has been incorrectly assessed, our priority will be to ensure that that individual gets their tax position corrected, because they will have overpaid tax in that instance.

The Chair: How will you do that if the company, as a matter of policy,

has decided not to deal with those contractors, which it is entirely able to do commercially?

Cerys McDonald: That is why it is important to make the distinction between a commercial decision about changing the way you augment your labour force and a decision to assess somebody as being within or outside IR35 without taking reasonable care.

Baroness Kramer: It sounds as though you are not taking responsibility for the unintended consequences of your policy, which is quite interesting. Could I press you on the issue of non-compliance? Looking at the number suggested by HMRC, only about 10% of contractors who should be within IR35 are operating within the rules. From what you were saying, did I understand that as largely anecdotally based? In other words, if I asked you to pass to this Committee the hard analysis that gets us to around that 10% mark, could you do that?

Cerys McDonald: That figure of 10% is based on a survey of our self-assessment system, so it is not anecdotal and drawn from just a survey of compliance officers; it is drawn from HMRC's systems that provide a lot of the analysis on which we base our policy decisions.

Baroness Kramer: It might be quite interesting to see that. You are suggesting that it is rigorous and scientific, so we ought to be able to pick that up very quickly by looking at it and you should have no difficulty giving that to us. Would you be able to do that?

Cerys McDonald: I can provide the Committee with a note that explains how we came to that conclusion.

Baroness Kramer: That would be helpful. I want to clarify something further. When you refer to non-compliance in those terms, are you talking about non-compliance with HMRC's judgment or with the kind of judgment that the court would deliver if it looked at this situation? I ask that question because there seems to be quite wide divergence between HMRC's interpretation of the law and the court's interpretation of it, which is why HMRC loses so many cases when it takes them to court. Are we talking about non-compliance with a verdict that the court would give or non-compliance with what HMRC would like to see?

Cerys McDonald: I would not recognise the assessment that HMRC's position shows wide divergence from the court. HMRC's role is to enforce legislation. A very small number of cases, which tend to be the most complex ones, go to a tribunal. It is right that in this country there is independent arbitration to test HMRC's position, but a very small number of cases find their way to the court. There are 30 million employees in this country and 4.5 million self-employed people whose employment status is very clear-cut, so we are talking about a very small proportion of the labour force in the greyer area, and a microscopic number of those end up in the courts.

Baroness Kramer: If I may invert it, you just said that 90% of

contractors should be within IR35 operating the rule, so it is not a tiny number you have a dispute with. You may have taken only a tiny number to court.

Cerys McDonald: A tiny number end up going to court, and obviously the party in question can choose to take it to court.

Baroness Kramer: As a sample of that group, you are losing about 40% of cases, or is it higher than that?

Cerys McDonald: It depends on what period you look at.

The Chair: We have seen the figure of 80%.

Cerys McDonald: I do not recognise 80%, but on the 40% I reiterate that these are the most difficult and complex cases and they are finely balanced. That is why they go to litigation, and that is right in a country where we have the rule of law that we do.

Baroness Kramer: You are just ignoring the other cases, because you say that the overwhelming majority of people are outside—

Cerys McDonald: A large number of cases will settle with us based on an inquiry rather than go through the courts.

Baroness Kramer: They are paying the right amount.

Cerys McDonald: There will be cases where we come to an agreement with an individual. They may not have assessed themselves as coming within IR35 and our compliance officers come to a different view. That goes to a negotiation and the case is settled. Those types of cases never go to the tribunal.

Baroness Kramer: I will stop there, but you can see why I am struggling with your numbers. You say that basically only 10% of contractors who should be within IR35 are actually paying it. The consequence of what you are explaining does not seem to fit with that picture at all. You are saying that in most of those cases you deal with it perfectly satisfactorily and end up with a settlement. Only a very small number go to court and you lose about half of those.

Cerys McDonald: The nine in 10 is a top-down assessment derived from our SA return data. HMRC does not and would not have the resources available to it to look individually at every IR35 case; indeed, it may not know about many of them. We are talking about looking at upwards of about 1 million limited companies that are owner managed, and trying to find what proportion of those may be close to the rules and subject to further inquiry. I do not want to give the impression that we are looking individually at every case. The nine in 10 is a macro view and the litigation comes bottom up.

Lord Bridges of Headley: If I may return briefly to the issue of rights and coronavirus and the Treasury, would you agree that the purpose of

the whole policy is to get fairness in the tax system?

Lindsey Whyte: Yes.

Lord Bridges of Headley: We are landing up with a system whereby that fairness may or may not be achieved, given the interactions we have just had, yet there could be a new unfairness in that people will be being paying the same tax at the end of the day but they will not get the same rights, will they?

Lindsey Whyte: You are right that falling within the off-payroll working rules for tax does not automatically change an individual's status for employment rights. There are separate frameworks for determining status for tax and status for rights, and there is no direct link between those two frameworks. There has been an active debate about whether there should be changes made to that, and I am sure the Committee is aware of it. There are mechanisms through which anybody who believes they are not getting the employment rights to which they would be entitled is able to challenge that through an employment tribunal regardless of their tax status.

There are some questions at the moment in relation to the coronavirus response, particularly around statutory sick pay, which I think you are referring to.

Lord Bridges of Headley: Perhaps we could come on to that. It strikes me from your answer, for which I thank you, that, given all these caveats, we are addressing one unfairness but replacing it with another unfairness.

On the issue of the coronavirus measures that the Chancellor announced, there are various stories online. One consultant says, "PSC workers 'inside IR35' are the only section of the working population that the chancellor did not include in the Covid-19 measures for SSP or the Contributory Employment and Support Allowance for the self-employed". Not only are we introducing this new bureaucracy, but these people are not being supported by the Chancellor. Is that right?

Lindsey Whyte: I do not believe it is right. To begin with, this reform is not introducing something new in the difference between status for tax and status for rights. As Cerys explained, it is changing the responsibility for determining status for tax from the personal service company and the individual to the ultimate engager. The difference in status for tax and rights has been in existence for some time. That is not to suggest that there is not a debate about whether it should be changed, but I wanted to make that clear.

In relation to the coronavirus response, individuals who are employed by a personal service company are entitled to statutory sick pay on the same terms as any other employee. I recognise that in practice many may not previously have paid themselves statutory sick pay, because often the individual is both the sole director and the employee, but, if

they are eligible for statutory sick pay within that, we have extended the criteria so that they can now pay it in respect of self-isolation for coronavirus or where somebody is isolating because they are caring for somebody in relation to coronavirus. If they meet the eligibility criteria, the PSC would then be able to claim the refund in the same way as other small and medium-sized enterprises that are able to claim the refund that we are in the process of developing, as was set out in the Budget.

Individuals not eligible for statutory sick pay—for example, if they fall below the lower earnings limit—would be supported by the welfare system, which is why the Chancellor also announced some changes to make it easier and quicker to access employment support allowance, in particular now to be able to access it from the first day rather than waiting until day eight. That is for people who have built up the appropriate national insurance record. People who do not have that national insurance record can go on to universal credit where we have made some changes, including temporarily getting rid of the minimum income floor, for example, to make sure that it is easier and smoother for people to access that.

Baroness Kramer: Could I double-check that? Is that after five weeks?

Lindsey Whyte: For universal credit, advances are available within days of the application. I believe that DWP is also looking at the length of time over which those are repaid to make sure that people can get the funds as quickly as possible. For people who would otherwise have stayed at the minimum income floor level, even though they are not able to work as many hours as would be required by the minimum income floor, the changes to the minimum income floor will mean that it will be lifted so that they benefit from the adjustment in universal credit for those in the system.

Lord Bridges of Headley: Perhaps I could put to you what has been said by an accountant specialising in this area of employment: “The new rules mean that many medium-sized companies have pre-emptively taken on previously contracted workers as employees, swelling the numbers on their payroll. Some will now be too big for reliefs, like the sick pay refund, but would have been eligible had IR35 [reform] been delayed. These companies will miss out on any meaningful support”. What do you say to them?

Lindsey Whyte: We have set out the eligibility criteria for businesses and employers, not just business employers, with fewer than 250 employees on 28 February, but we are working through the design of the refund system to deliver that and engage with employers in order to do that.

Lord Bridges of Headley: You might address that issue.

Lindsey Whyte: I can only set out the criteria that we set out at the point of the Budget, but I will definitely take away that concern.

Lord Bridges of Headley: Once again, would it not be better just to delay all this rather than go through this uncertainty? We have cases of companies that are now uncertain about their tax. Would it not be better to delay it, given the scale of the problem we are now in?

Lindsey Whyte: I can only go back to the answer I have already given you, but I take the Committee's challenge on that and will of course reflect it back.

The Chair: Perhaps I am being a bit thick. Listening to your answers, I keep coming back to the point that you say nothing has changed about the rules of self-employment and all you are doing is putting in place a more effective collection system. I can see how from HMRC's point of view you are shifting the administrative burden away from yourselves. I understand that you have had cuts in your resources and everything else, and it is tempting to pass the buck on to employers to deal with that.

If in practice large companies respond by saying to their previous contractors, "We're going to have to treat you as employed persons, which means we will have to pay employers' national insurance"—national insurance is the key point—"so that will cost us an extra amount and, therefore, we are going to cut what we pay you", the little person at the end of this, the contractor, finds they are being paid less than was previously the case and are not in a position to challenge that. They are a contractor and, if they challenge it, the employer can say, "Well, like it or lump it". Can you not see that this is imposing an enormous hardship on honest contractors who may perfectly well be operating under the rules as they previously did, or am I missing something?

Lindsey Whyte: There is quite a lot in the question. It is not that we are shifting the burden for conducting the assessment from the Government to businesses. At the moment, it is the personal service company and the individual who has to assess and self-report their tax.

The Chair: But you are saying that, because you do not have the resources to look at it individually, you are going to ask the large companies to do it. That is a shift in the burden.

Lindsey Whyte: It is a shift to large and medium-sized engagers to do that.

The Chair: Which suits you.

Lindsey Whyte: They are arguably better placed. We think that will improve compliance with the IR35 rules.

The Chair: You are making them tax collectors.

Cerys McDonald: They are already tax collectors for PAYE, which works incredibly well.

The Chair: But they are not. This is in respect of—

Cerys McDonald: This is in respect of employment taxes that are due.

The Chair: But at the moment the responsibility for that lies with the contractor.

Cerys McDonald: Yes.

The Chair: The contractor is either self-employed or not and the responsibility is there. As I am listening to you, you seem to be saying, "We can't possibly police all of that, so we are asking the large employers to do it". We know from the evidence we are getting that large employers are responding by saying, "You have to be employed or you have to come to us through a service company". In both cases, the result is that the person who is actually doing the work finds that their income is substantially reduced, and you are doing that at a time in the economy when their income will be substantially reduced because of what is happening. I cannot understand why you do not see that as ultimately damaging not just to the economy but to the tax flow in the long run.

Cerys McDonald: We do not want to give the impression that we do not understand that this is a significant reform to which the labour market is adjusting at the moment, but the underlying tax that is due is not changing. Individuals who are currently not assessing themselves as being within IR35 are being subsidised.

The Chair: I understand that point. Forgive me for interrupting you. You say that tax due is not being collected. My point is that perfectly honest people who are not due to pay national insurance will actually have that cost deducted from their revenue.

Baroness Kramer: May I put this another way and push you on it? I am a contractor. My personal service company is very careful to make sure I am not covered by IR35, but I am now working with an engager who is damned if they are going to end up in a fight with the IRS. What the heck—why bother with that? They decide either to go in the direction of a blanket company, or to force me into an umbrella company, but they are going to do PAYE because there is nothing worse than being in endless battles with the IRS. That is the philosophy and the approach. The way the engager will offset the fact that they have to pay employer's national insurance is to take it out of the money that otherwise would have gone to the contractor.

Explain to me the equality of arms. If I raise a fuss, will I ever get an opportunity to work again, or will I be labelled a troublemaker? Do I have to take the new arrangement on offer or basically not work? There will be a few people whose skills are so exceptional that they will be able to negotiate their way through the system, but for the vast majority—say, IT contractors—there is always someone else willing to do the work.

I am trying to understand. Are you going to go to court to say, "Here is someone who was paying the right amount but was not an employee for tax purposes and now they have been re-categorised and forced into an

umbrella company"? Is the HMRC going to be out there defending their interests? Are you going to be proactively providing them with support?

Cerys McDonald: I draw the Committee's attention to the fact that employer national insurance is at 13.8%. That is a significant proportion of a company's wage bill. Businesses obviously have a duty to their shareholders to maximise profit, which requires them to minimise costs. I believe large companies are not going to take on that additional tax liability because they do not want to be bothered by the taxman. What the rules do is ask individual companies to look at the status of individuals and treat them as employees, if that is the case. I think that 13.8% is a financial—

Baroness Kramer: I do not know what world you live in, but that is not the world.

Cerys McDonald: I would argue that businesses do not take on unnecessary costs.

Baroness Kramer: They pass it through.

Lindsey Whyte: It is worth reflecting some of the evidence we have from the public sector where this has already been in operation. The evidence we have had from the public sector, both from the very early assessment that was done and since then through engagement with different departments, is that while there has been some renegotiation of fees in different places, and organisations have made different changes in response to operating the rules, a number of people have been brought on to payroll, as you would expect if they had been operating in a job that is effectively an employment for tax purposes.

Some contractors have chosen to leave the public sector. Others have chosen to stay, and in some cases there has been a renegotiation of rates as a result; in other cases there has not been. I flag that, because I do not think there is one specific response; it will vary by organisation and by sector as a result of organisations working out what is the most efficient structure for their workforce.

Both across the public sector, and from what we have heard so far from the private sector, we are not expecting a very significant shift in the demand or supply of contingent labour. It is clear that the public sector is still using contingent labour, but we are going through a period of adjustment to make sure that roles are categorised in the right way within that.

Cerys McDonald: Perhaps I may return to Baroness Kramer's point about the 13.8% being pushed on to individuals. The labour market is also a marketplace, and firms consider their wage or pricing strategy when they are thinking about contingent labour. If they were to push on all the cost and one of their competitors chose not to, that would put them at a disadvantage. You need to think about the market impacts of this as well.

The Chair: Have you read the evidence that we have received?

Cerys McDonald: Yes.

The Chair: Is there any evidence that what Baroness Kramer is saying is not happening?

Cerys McDonald: I am not saying it is not happening, but I am trying to give a macroeconomic narrative. I understand that you have seen individual cases where people have described those concerns.

Q55 **Lord Tyrie:** Mr Riley, you have not had a look-in so far, so we will see if we can do something about that. You have seen the evidence to which the Chair has just referred. Among other things, it is about the one-off cost of this proposal. You have given your estimate of what you think that would be. Are you sticking by that in the light of the evidence?

Paul Riley: I think Cerys is better placed to talk about that in respect of off-payroll working. My responsibilities are for tax administration more widely and HMRC powers and safeguards, which I know the Committee has been particularly interested in.

Lord Tyrie: I am doing my best to give you a moment in the sun.

Paul Riley: If you are asking about the costs of the measure, Cerys is the right person to ask.

Cerys McDonald: Perhaps I could come in on that and then maybe Paul can give a wider update on powers. To answer your specific question, I think you are referring to the £14.4 million.

Lord Tyrie: I am. You have seen a lot of evidence about it.

Cerys McDonald: I have seen the evidence the Committee has had.

Lord Tyrie: Are you persuaded by any of that evidence?

Cerys McDonald: I can assure the Committee that I will revisit the assumptions underlying that estimate in light of the evidence you have received. I want to look at it again with the Administrative Burdens Advisory Board.

I want to explain a little how we came to that estimate. HMRC's estimate was published in Budget 2018. We looked at assumptions about the cost to businesses of familiarising themselves with the rules, training their staff, putting systems in place, including IT, carrying out initial independent assessments and the cost of putting the dispute process in place.

However, one of the uncertainties when we made that estimate was lack of evidence or data on the distribution of the use of personal service companies across the 60,000 or so engagers that might be affected by the rules. To what extent is a large percentage concentrated in a small number of those firms? That is something on which we have had limited

data and is one of the things we want to retest when we get more evidence about how the rules have bedded in and we do the external research we have committed to after six months. We want to retest and look at that figure again.

Lord Tyrie: If I could translate that, you accept that £14.4 million is likely to have been an underestimate and that the cost is higher.

Cerys McDonald: I am not going to be drawn on whether it is an underestimate at this point, but I accept the need for us to revisit the assumptions.

Lord Tyrie: Do you think it is possible that you might reduce your estimate of the one-off cost in the light of the evidence?

Cerys McDonald: I will not be drawn on the conclusion, but in response to the evidence that the Committee has received we will revisit some of those assumptions.

Lord Bridges of Headley: If you need to revisit the assumptions, how come it is not a burden on business? It is clearly a burden on business; it could be greater than has been said.

Lindsey Whyte: We recognise that there is an administrative cost for engagers in taking on this responsibility. That is to an extent offset by the reduction in the administrative cost to personal service companies that will no longer be responsible for that. There is an up-front cost in becoming familiar with the system, running it for the first time and training staff, but we think there will be a much lower ongoing administrative cost. That was reflected in the evidence we had from the public sector about its experience of going through this.

Lord Tyrie: With the Chair's permission, it might be helpful if, as soon as possible after this meeting, you could send us a note on how you derived the number, with the assumptions you have just described and any weighting between them. I think we should have that in the public domain as soon as possible to enable those who have complained to us about the underestimation of the one-off costs to comment so that they can say whether they think that is a reasonable way to go about the calculation. Would you be prepared to do that, Ms McDonald?

Cerys McDonald: We can certainly provide more information, although, as I said, I think there is a good case—

Lord Tyrie: I have asked for specific information based on your reply. I am asking you whether you are going to provide that to the Committee.

Cerys McDonald: I will take that away and see what we can provide to be as helpful as possible to the Committee.

The Chair: Why can you not be as helpful as possible and just say yes?

Cerys McDonald: I shall need to check with an analyst what information—

Lord Tyrie: You have?

Cerys McDonald: I do not have the detailed calculation in front of me, so I do not want to overcommit to the Committee about what I can share. But what I am able to share, I absolutely will.

Lord Tyrie: Are there any aspects of the way you will have calculated this that need to remain confidential?

Cerys McDonald: No, but I do not want to overpromise something to the Committee. We will share with you as much as we can to be helpful.

Lord Tyrie: It is the “as much as we can” that I am responding to.

Cerys McDonald: Sorry, you can remove the “as much as we can”. I shall share with you what we have that will be as helpful as possible.

Lord Tyrie: You will share with us what you have. Okay, thank you very much. We have got past my first question, which I think will supply us with some information and help. You have estimated your own additional, longer-term costs—HMRC’s costs—at £21 million. What does that cover?

Cerys McDonald: The £21 million covers the IT costs that the department faces in updates to real-time information, our PAYE system and self-assessment. It also funds the creation of a new team that we have set up to support our customers with the rollout of these changes.

Lord Tyrie: We are talking about support to medium-sized and larger businesses, I take it.

Cerys McDonald: Yes.

Lord Tyrie: What would be the split between the two?

Cerys McDonald: In the allocation of resource?

Lord Tyrie: Yes.

Cerys McDonald: I do not have an allocation, because there is a large range of activity that we are currently undertaking, which I shall quickly explain to the Committee. In addition to the one-to-one calls I referred to, which we are offering to large businesses and the largest medium-sized businesses, we have written to all 40,000 medium-sized businesses that we estimate could be affected by these changes, signposting the relevant guidance and the tools available to them. We have carried out seven webinars so far, with a few more planned, which reach out to the full community. We have had workshops around the country, and we have published detailed guidance, factsheets and flowcharts. All of those are available to all the affected population.

Lord Tyrie: It might be helpful if the Committee could also have a

breakdown of how you have arrived at the £21 million for HMRC. Would you be able to provide that?

Cerys McDonald: Yes.

Lord Tyrie: And in enough detail for us to be able to grasp what its substantive components are.

Cerys McDonald: I think what you are driving at, which I can share with the Committee, is what proportion is for IT costs, what proportion is for staff supporting our customers, and what proportion we are spending on a wider comms campaign, if that is helpful.

Lord Tyrie: Well, you will have derived the number on some basis; you will not have plucked it from the air.

Cerys McDonald: No, I have just said how we can break it down.

Lord Tyrie: If those are the three headings—

Cerys McDonald: Indeed.

Lord Tyrie: That is already a step forward. As you have estimated your own costs at £21 million, why do you think that the cost to medium-sized and large businesses will be only £5.3 million?

Cerys McDonald: The £21 million is over five years; it is not annual.

Lord Tyrie: But I am talking about the ongoing cost of around £5.3 million.

Cerys McDonald: The £5.3 million is the gross ongoing running cost for the engagers. HMRC's view is that it is offset by a saving from the—

Lord Tyrie: I am just looking at the gross side. The savings are disputed, so I want to look at something more robust, which we can talk about: the estimate of the gross cost. Why do you think that is only £5.3 million, when you are going to spend £21 million?

Cerys McDonald: The £5 million is an annual cost; the £21 million is spread over five years, so it is not a comparable figure.

Lord Tyrie: Let us add them together. Five times five is 25, so for all those businesses we are now putting in 25 against 21 just for you. Do you think that is a plausible comparison? Think of the number of businesses involved in that number. You are hesitating.

Cerys McDonald: I am hesitating. The Committee has given us a good challenge on administrative burdens, and I have said already that we are going to revisit some of those assumptions. The same description and methodology that I outlined for the £14.4 million will apply to the £5.5 million. If you want me to cover that in the note we have already committed to sharing with you, I can do so.

Lord Tyrrie: You are a highly skilled performer in front of these Committees. I have seen you before in another place, and I mean it genuinely as a compliment that you put the best possible case. If I may say so, what I have heard is that you are acknowledging, although you will not do so today—challenge me if I have got this wildly off-beam—that these numbers were probably underestimates, were they not? Shall I give you your answer? You are going to go away and have a look at it and come back in due course.

Cerys McDonald: That is indeed what I am going to do.

Lord Tyrrie: That is what I heard. Now let us go back to Ms Whyte. What we have heard is that we have an underestimate of the true burden on firms, probably, although not certainly. It is conceivable that you will come back to the same number, having looked very carefully at all the evidence, but it is inconceivable that you will reduce it, since we have tried that one out, and it got a negative.

We know that the number is almost certain to go up, possibly by quite a lot, on the basis of the evidence we have seen, as the best guess for what the burden would be. We know that there is an additional one-off shock coming down the line called coronavirus. Is it not the truth, based on a remark you made very early on, that we are looking at a reform that was always difficult to push through and that you are well down the road of pushing through, and you do not want to see it lost as a consequence of a response to a short-term shock?

Lindsey Whyte: It is worth reflecting that there are a number of very strong reasons for implementing the reform, which is why Ministers have decided to go ahead with it from April this year, after significant consultation, but it is right that we are doing—

The Chair: On that significant consultation, can you remind the Committee when you started it and when you completed the review promised by the Government in the general election campaign?

Lindsey Whyte: The specific review on implementation started on 7 January and was concluded in February.

The Chair: That is fantastic, because this Committee would find it impossible to operate to that kind of timescale.

Lord Tyrrie: Can you say when it was completed in February, roughly?

Lindsey Whyte: It was 23 February, possibly.

Lord Tyrrie: That is the minimum permitted to remain in compliance with the guidelines issued by the Cabinet Office for reviews. Am I correct?

Lindsey Whyte: It was the review to look at the implementation.

Lord Tyrrie: Which is six weeks.

Lindsey Whyte: Alongside that, we have continued to roll out the education and support programme, and all the wider work put in place to help to support people in getting ready for the reform. The review we are talking about follows a whole series of consultations over the last several years.

Lord Tyrie: That is fair enough. I want to get back to this point: it is a very difficult thing to roll out and there is quite a lot at stake, from your perspective; since you have rolled this boulder, Sisyphus-like, almost to the top of the hill, you do not want to lose it just as you think you are within an ace of getting it, as a consequence of a temporary suspension for coronavirus. Is there a shred of truth in anything I have just said, or is it nonsense?

Cerys McDonald: I think I would say that we are—

Lord Tyrie: Could I ask Ms Whyte, because it is a policy question, and she is a bit nearer the policy?

Lindsey Whyte: That is fine. There are good reasons to proceed with this, as we have talked through, and we can say a bit more about that. I absolutely recognise that the coronavirus outbreak is going to be difficult for individuals and businesses, which is why the Chancellor has announced a whole set of other measures to try to support businesses through that, which he set out alongside the Budget. We recognise that we will need to give businesses support with costs and workforce issues around coronavirus. We have a number of measures in place, which all the different types of individuals and organisations we are talking about will be able to access and benefit from.

Lord Tyrie: In the light of what you have heard here today, would you please undertake to ensure that Ministers are given the opportunity at least to consider the suspension of the change as part of the response to coronavirus, to reduce the burden on those businesses?

Lindsey Whyte: I will certainly report back the Committee's very strong views, which you have made clear. I will make sure that I do that.

The Chair: I think your Minister is coming to us next week.

Lindsey Whyte: I believe he is, yes.

The Chair: To go back to the consultation thing, among the hundreds of submissions that I was wading through at the weekend, one alleged that the result of the review was released by HMRC before the conclusion date. Is that correct, or not?

Cerys McDonald: No, it is not.

Lindsey Whyte: No, I do not think it is.

The Chair: All right. Someone just imagined that.

Cerys McDonald: What that individual or business might have been referring to is that HMRC has an employment status manual online, which is the technical detailed guidance that supports our existing regulations on IR35 and is obviously being updated. In the run-up to the review, as we were doing the updates, before we had finalised the changes, a version went up online.

The Chair: Thank you for clarifying that.

Q56 **Lord Bridges of Headley:** Last July, before the review and the changes to the CEST tool, the Chartered Institute of Taxation said that CEST “does not factor in all the criteria established by case law as needing to be considered before its algorithms reach a decision on whether IR35 applies”. In the light of the changes that have been made, do you think that the CEST tool now addresses that criticism fully?

Cerys McDonald: Yes, I do. I fully acknowledge that other parties take a different view, but HMRC is firmly of the view that the enhanced version of CEST published in November is fit for purpose. We engaged with over 300 stakeholders in that enhancement. I accept that many people still feel that there are improvements to be made, but, even in evidence to this Committee, the CBI, CIOT, the Low Incomes Tax Reform Group and ABAB all acknowledged that it had significantly improved.

Lord Bridges of Headley: What about mutuality of obligation? Is that now addressed in the CEST tool?

Cerys McDonald: HMRC has been consistently clear that in our view it is reflected in the CEST tool in two ways, if I may explain. First, at its simplest, mutuality of obligation is the basic agreement for an individual to provide services in return for payment. Therefore, there is a contract that exists between that individual and the engager. All the questions in CEST test the very nature of that contract, so they are testing the existence of mutuality of obligation.

However, mutuality of obligation can also look at the depth of the relationship between an individual and their engager, and there are specific questions in the CEST tool that explore that, including the extent to which the individual is part and parcel of the organisation. HMRC’s position on that is very clear. I know that others take a different view.

Lord Bridges of Headley: If a tribunal comes up with a case that it considers to be not at all borderline, one way or the other, would the CEST tool come to the same conclusion as the tribunal?

Cerys McDonald: Yes.

Lord Bridges of Headley: That is not what a barrister told us. He had a case where the tribunal’s analysis was: “We do not consider this to be a borderline case. After the long-awaited improvement of CEST, I once again ran the facts of the case through the tool. However, CEST still failed to give me the result that the tribunal had resoundingly reached a few months earlier”.

Cerys McDonald: Obviously, I cannot comment on that specific example.

Lord Bridges of Headley: No, you cannot; I understand that. But I do not quite understand why you are convinced that this will actually come up with the same result as a tribunal in a case that is clearly not borderline. That statement sounds at odds with what you are saying.

Cerys McDonald: The CEST tool reflects HMRC's interpretation of case law. When we enhanced the tool back in November, we tested against a number of cases. When we have compared the CEST tool with other commercial tools that are available, it gives equivalent results, so HMRC's assessment is that the tool is effective and we stand by the output of that tool.

Lord Bridges of Headley: It is effective in what percentage of cases? It was effective in 85%. Is it now effective in more?

Cerys McDonald: We have had around 400,000 uses of CEST since we launched the enhanced version. Based on the analysis we have run so far, we think that it broadly hits the same percentage—

Lord Bridges of Headley: The 85%.

Cerys McDonald: In the vast majority of cases.

Lord Bridges of Headley: What are the other 15% going to do? Do they ring you to ask for guidance?

Cerys McDonald: When we enhanced the tool back in November, we published online guidance to help to guide people through the tool. Again, the guidance itself was worked through carefully with our stakeholders; it is designed to help people complete the tool correctly and get the right result. We also have a dedicated helpline that people can call if they are struggling with it. I reassure the Committee that that helpline has not fallen over at all in the run-up to the reform and is servicing the demand well.

Q57 **Baroness Kramer:** Obviously, as we read, quite a number of sectors, such as banking, insurance and pharmaceuticals, have looked at the enhanced CEST tool and looked at the situation they face and said, "Not for me. The only way I'm going to deal with this situation is that I won't directly hire contractors any more". They may put some on payroll, although I gather that is quite an exception; in most cases, they now require them to go through umbrella companies. Would you accept that that is the literature, and those are the articles and statements that they publicly made? We are not in dispute over that.

Lindsey Whyte: We recognise that some organisations have made statements about how they will respond. This goes back to a lot of the discussion that we had earlier. It is a significant reform, and it will result in businesses reviewing their workforce and hiring practices, and some of them will do that in different ways.

Baroness Kramer: Perhaps I could push you just a little bit on the consequences of the much expanded and enhanced role for umbrella companies. I was engaged in trying to deal with a loan charge. I think you had many colleagues who expressed a great deal of disquiet with umbrella companies. Would you comment on that, and, while you are talking about it, could you give me your estimate of the costs of becoming a contractor working through an umbrella company? Can you give me your opinion on what that does to enhance the economy and encourage people to go into freelancing and self-employment?

Cerys McDonald: I will start with the comments you made about the use of umbrella companies. The majority of umbrella companies are legitimate and compliant, but we are acutely aware of non-compliant operators in the market. I know that people have raised those concerns with the Committee, and they have obviously raised them directly with us too, and we acknowledge that new schemes are emerging in response to these reforms.

To give a bit of context, HMRC's view is that tax avoidance schemes are no longer a mainstream product. Their creation and promotion are now moving to the more disreputable and shadier end of the market. At the Budget, HMRC confirmed that it is refreshing the tax avoidance strategy. HMRC will invest more time, money and policy expertise in tackling promoters and enablers, which means tackling schemes at source and trying to identify customers who may be getting pulled into those schemes to see what we can do to help them to get out.

An important aspect of that is how HMRC raises awareness of the schemes among contractors. That is absolutely critical. One thing that was explicitly asked for in the review that we carried out earlier this year was that HMRC needed to do more in that space to raise awareness among contractors of some of the risks of the schemes. So, alongside the review, we published a self-help guide to draw attention to some features of the schemes that people need to be aware of, and we have encouraged as many of our stakeholders as possible to push that out on our behalf. Equally, in our engagement with stakeholders who raised concerns about the schemes that are emerging, we are encouraging people to share those with us, and, indeed, many have. Of course, we will take steps to assess and close them down when we feel that they are not legal.

Baroness Kramer: We could probably have a long conversation on enforcement against promoters, which in the loan charge area is not won yet. It is based on other disguised remuneration issues, but not on that. To move away from that—

The Chair: Before you move away, that is something Mr Riley might be able to comment on.

Paul Riley: We announced in the Budget that we would publish a promoters strategy. That is due to happen on Thursday, so on 19 March that strategy will be published.

Baroness Kramer: That will be interesting to look at. I hope that we then see enforcement action against some very well-known companies with a very wide remit, used extensively by the public sector, which is interesting. Even when we are not talking about someone who basically sees this as an opportunity to sell a lot of new products to an individual, what is your estimate of the administrative cost that falls on a contractor who can no longer work on a self-employed, freelance basis but must now go through an umbrella intermediary before they can have any work opportunity?

Cerys McDonald: I do not have an estimate that I can share with the Committee at this point.

Baroness Kramer: But you have surely researched it, because it is an environment that you are creating.

Cerys McDonald: I do not have a figure to hand. Of course, there is a wide variety of different models in the umbrella market, which in itself is competitive. I can take that away and see if there is anything further we could share with the Committee that would be helpful. Obviously, the regulation and policy responsibility for umbrellas more generally is a BEIS matter, but we work closely with both BEIS and the Employment Agency Standards Inspectorate in looking at that area.

Baroness Kramer: Would you accept that freelance work in the kinds of skills in the creative sector, the IT sector or highly specialist design is very often the cutting-edge driver of growth in the economy? What have you assessed is the impact of diminishing that sector as a consequence of shifting the responsibility for making IR35 to entities for which avoiding trouble with the IRS is more significant than building competence among the freelance and contractor industry?

Lindsey Whyte: The OBR has not assessed there to be a significant macroeconomic impact of these changes. We are not stopping anybody operating through whatever structure is most efficient for them and for businesses. We have not seen that this will have a significant impact on the overall demand and supply of many skills; it is just that some of them will be categorised in a different way for some of the employments where they are found, effectively, to be doing a role that is an employed role.

The Chair: You will be relieved to hear that I think we have run out of time. Thank you so much. There are one or two questions that we have not had a chance to ask, but our Committee clerk, Tristan Stubbs, will send them on to you, and perhaps you can respond in writing. Thank you very much indeed.

Examination of witness

Carl Vincent.

Q58 **The Chair:** Mr Vincent, welcome to the Committee. I am sorry that we

have run over time, but, as you saw, there was quite a lot of material to cover. I begin by asking the first question, which we heard earlier. HMRC's position is that, despite some teething issues with the initial implementation of IR35 in the public sector, overall the reforms have been a success. How do you feel about that?

Carl Vincent: HMRC's measure of success would obviously be whether it has achieved the tax that it was setting out to do, and all those sorts of things, and I find it hard to comment on that. I have more of a view about the practical implementation, and I would say that it was extremely difficult to start with.

We found it very difficult to interpret the regulations and found that, using the original CEST tool in particular, we came up with results that HMRC subsequently, when it reviewed our approach, disagreed with. Even with the more recent CEST tool, although things have improved, we still feel that we need to use methodologies on top of it to make sure that we are reaching conclusions that we believe HMRC will be comfortable with.

We have got to a position where we think we are making assessments that HMRC will be comfortable with, but we have not yet settled the historical position. The real test for us will be whether HMRC ultimately agrees that we have settled the historical position. We have got to a place where we think we are compliant, albeit using methodologies beyond the CEST tool.

Baroness Kramer: You feel, as you say, that you are in a situation where you have satisfied HMRC. What impact have you seen on the contractor workforce? If you could take us through some of that, it would be extremely helpful.

Carl Vincent: There was an initial period when it was very unsettling, and the market was settling into a new position. After the first few months it settled down; we managed to get the contractors we sought, and the market has not materially changed. In implementing the guidance over the last few months in particular, we have brought a few contractors in scope and, in that position, we have had to pay more to the ones we felt we had to keep. In due course, we are not clear what we will have to pay them, because the market will settle again. After that initial period, we managed to secure the resources we needed.

Baroness Kramer: Can I check one thing? From what you are saying, most of your contractors were effectively in compliance when they made their own assessment.

Carl Vincent: No. To go back to when the new regulations were implemented, most if not all of our contractors treated themselves as out of scope. We have reached a position now where about 10% are out of scope. It is a different 90% from the ones at the start, but about 90% were incorrectly out of scope, according to our current assessment or treatment.

Q59 **Lord Bridges of Headley:** You obviously heard the discussions we have had. Can you talk about the costs of getting ready for IR35? I was interested in your evidence, for which thank you very much, where you say that you found it “very difficult, based on HMRC guidance and their feedback, to understand the intentions of the legislation”. Can you go into a little more detail on those two points—costs and the interpretation of the legislation?

Carl Vincent: Absolutely. We set up a project team initially to get ourselves ready, and in the six months prior to the regulations our estimated costs were about £150,000 of internal staff time. Subsequent to that, we probably spent about another £450,000 or £470,000 over a three-year period to implement the regulations. I expect the ongoing cost to be much lower, once we have a settled opinion and approach, but over that period, we were still working on it, having ongoing dialogue and putting forward proposals, which HMRC disagreed with. It has been a fairly active three years, which is why the costs have been higher than they otherwise would be. Once we get to BAU, the costs will be much lower.

As to how difficult we found it, we did the preparation before the regulations. We went to workshops and the like, and we heard that, if you used the CEST tool objectively, the outcome was the answer you should use in determining the tax treatment of individuals. But there are subjective questions in the CEST tool. As you work through, you have to make judgments, and with the first CEST tool we were making judgments that HMRC disagreed with.

The biggest assessment of all is, “Has the contractor got unfettered right of substitution?” That is by far the biggest assessment. Can the contractor say, “I’m going to bring in a substitute to deliver this work, so it won’t be me any more”? In our contracts, we believed that they had that right, and we have examples of people doing that, so we put that together. When the CEST tool asked whether contractors had that right, generally we said that they had the right of unfettered substitution, but HMRC challenged us on that.

We moved on and changed the contract, but there is still a subjective judgment, not about whether people have the right of substitution, but about whether it is an unfettered right. There are other subjective questions in the tool, and we are making an honest judgment based on those questions. We have not gone into all the detail on some of them, but it is apparent that HMRC does not always agree with our assessment of each of those questions.

Lord Bridges of Headley: Before we get into the CEST tool, let us deal with the overall experience you went through. In light of the review, how much do you think HMRC and HMT have taken on board about the experience of the public sector, and yours in particular?

Carl Vincent: Certainly the CEST tool is an improvement, so I assume that they have had feedback. We have not settled on our historical

position yet, but when we do I will be interested in how HMRC approaches it. Will it penalise us for making, in good will, judgments or assessments that it ends up disagreeing with, or is it going to say, "We understand it was complicated and it was a bit of a moving feast, so you need to pay the back tax but we are not going to apply penalties"? That will be a big test of whether it has reflected on that period in the way I hope it does.

The Chair: The view expressed to us earlier was that 90% or so, or a very large proportion of people, were behaving as if they were self-employed or as contractors, but in fact their real status was employed. Was that your experience?

Carl Vincent: That is our current position. Our current position is based on using the CEST tool and our own questionnaire, which puts people in scope even if the CEST tool says that they are not. Our current position is that about 90% of our contractors are in scope of IR35, and before the regulations were changed virtually none of them was.

The Chair: So HMRC was quite correct in its assessment.

Carl Vincent: Yes, it is consistent with our pool.

Baroness Kramer: If I understand correctly, most of this was an issue about unfettered substitution.

Carl Vincent: That was a big part of it.

Baroness Kramer: Presumably, it is quite a subjective test. Do you have any awareness of whether, if it went before a court, the court would support the view taken by your contractors before the reforms or insist on the standard that HMRC is now requiring you to implement today, even though, intuitively, it is not where you would put the benchmark?

Carl Vincent: The truth is that I do not. I am sorry.

Baroness Kramer: I can see why you would not have explored it.

Q60 **The Chair:** What was the impact on the NHS?

Carl Vincent: On us, as an organisation, the main impact was the amount of effort we made in getting ourselves to a position where we now believe we are compliant. It was a management distraction, and it had some costs on us.

After the initial period of impact on the labour and contractor market, it has settled down and we have access to contractors, albeit that we now pay more for a small number than we did. I do not know whether that will be short or long term. For example, if it rolls out to the private sector and the private sector takes the sweeping approach that, broadly speaking, everybody is in scope, I assume that will change the labour market and how much we have to pay. The future is uncertain. At the moment, for a small number we are paying around 25% more than we previously were.

The Chair: Your costs have gone up by 25%.

Carl Vincent: Yes, for a small number of contractors. We felt we had to pay more to keep them, both because they have crucial skills and for business continuity reasons.

The Chair: The other ones you have just squeezed.

Carl Vincent: We have either brought them in scope and not paid them more, or they have left.

The Chair: Right. What sort of number is 25%?

Carl Vincent: Our contractor base is somewhere between 60 and 100; it fluctuates up and down, so 25% could be—

The Chair: No, I meant the cost in pounds.

Carl Vincent: It could be £1 million a year.

The Chair: I see.

Baroness Kramer: For the individuals to whom you are not paying any more, are you paying the cost of the employer's NIC, or are you subtracting that from the money that heads down towards those individuals?

Carl Vincent: We secure contractors through an agent; it is a government framework. That is how we do it, and the PAYE and tax is sorted by that agent. There is an agent fee; we have not paid any more to the agent. How much the agent has sorted out with them, we are not sighted on.

The Chair: It is an umbrella company, effectively.

Carl Vincent: Yes.

The Chair: You said that only in a small number of cases, where it was vital to you, you paid more, but otherwise not. Does it follow that those contractors will have got less because the umbrella company will charge them for those services?

Carl Vincent: I think so, yes. I am certain that is the case.

The Chair: Plus they will be paying national insurance.

Carl Vincent: I am certain that is the case, yes.

The Chair: Right. Does anyone have any other questions?

Q61 **Lord Tyrie:** I have a couple of quick points for clarification. I have been briefed that HMRC launched a review of your implementation in June 2017, and that is still going on. Is that right?

Carl Vincent: Yes.

Lord Tyrie: What on earth is going on? That is nearly three years. We found out that HMRC does reviews in six weeks.

Carl Vincent: The process has been different from a review that we would have with an established tax, or that is my experience. Obviously, HMRC reviews our approach to all sorts of taxes, and generally speaking there is a relatively quick process for looking at what we have done. HMRC agrees or disagrees, we change it, and then we agree the tax element and move on. Some of this is because we have been asking questions of clarification: "Do you really mean this?" HMRC says, "Yes, we really mean that, plus something".

In the first period, from April 2017 to December 2019, we accepted HMRC's position. We said, "We accept that is the position. We didn't get it right. We accept that", and we made an accrual in the accounts but we have not actually paid the money. In the period following that, we have not had a detailed enough discussion with HMRC to get to an agreed position.

Lord Tyrie: My second question is a different one. In your evidence, you said, "It is very difficult to implement the legislation and the HMRC guidance in the way that is intended—that is, on a case-by-case basis". You go on to make a proposal, which is that HMRC should clarify its guidance in a way that forces people to one extreme or the other, as you put it, but from the numbers that you have just given us, which was 90:10 for yourself, they have forced it to one extreme.

Carl Vincent: I think the question was about whether we have any proposals for making it easier. It would be easier if the complexity in the middle between the two extremes was taken away. If you look at the CEST tool, that complexity is still there. There are still 30 questions, or that sort of number, and it asks a whole number of subjective questions about how much control you have over the way the work is delivered, and that kind of thing. You could take that away, say that it is not interesting and assume it is at one extreme or another, and then you would not have to ask those subjective questions.

You could say that, at one end of the spectrum, if they are not getting sick pay and get short notice and that sort of thing, they are out of scope. You could take the other end of the spectrum and say that it is just on outcomes, so if somebody is delivering outcomes and they are paid on the outcome, not on a weekly or daily rate, they are in scope. You could simplify it by taking the extremes; at the moment, it involves quite complex decision-making. That would simplify it.

Q62 **Lord Bridges of Headley:** In your evidence, you say that you have your own external assessment and that you take the advice of tax experts, et cetera. Therefore, I assume that you do not think that the CEST tool in and of itself is fit for purpose.

Carl Vincent: It still leaves us with subjective judgments to make.

Lord Bridges of Headley: It is not really fit for purpose, for your

purposes.

Carl Vincent: It would leave us with more risk than we are willing to manage.

Lord Bridges of Headley: Your advice to a large organisation facing implementation would be, "Don't rely on the CEST tool". Sorry, I am putting words into your mouth, but is that where you are coming from?

Carl Vincent: Sitting here, I am loath to give other people advice. Our approach has been that it is too risky. We ended up having too much risk by using the CEST tool, so, rather than continuing to take risks, we are using the CEST tool but adding our own assessment on top of it, putting a line for people outside scope and making sure that we are on the right side of that, so that we are comfortable that when HMRC comes along and looks at individuals, there will be nobody on the out-of-scope list that it thinks should be in scope.

The Chair: Is that not rather rough justice on people who may genuinely be self-employed?

Carl Vincent: It is, but on the other hand it is less rough justice than taking a sweeping approach and saying that everybody should be in scope.

The Chair: But you have pretty well got there; you said that it was 90%.

Carl Vincent: Well, we have 90:10, but we still have 10% out.

The Chair: Within that 90%, there will be people who are genuinely self-employed, because you have gone to the safest possible position.

Carl Vincent: Yes, we have had to take the safest possible position, because over a period of time it has been very difficult for us to get to a place that we thought was an objective assessment of the correct number of people on either side and get HMRC to agree to that.

The Chair: What sort of response did you get from the people in receipt of that rough justice?

Carl Vincent: It has not been a really terrible kind of response. They either say, "Thanks, but we'll leave", or they say, "Thanks, we'll leave, but we'll stay if you pay us a bit more". Some have said, "Okay, we'll stay. We really like it here", and have taken a pay cut. It has not been a terrible response. We have not had lots and lots of—

The Chair: Except that you have not had the pay cut.

Carl Vincent: Sorry?

The Chair: You have not had the pay cut.

Carl Vincent: No, I am describing the types of responses that we have had. I am not making a judgment.

The Chair: Actually, they do not have much choice, do they?

Carl Vincent: We are one employer of 60 to 100 contractors, and they are not all in Leeds, where we are based. There are lots of other employers, and others have decided to move on. If and when it is applied to the whole economy, there would be a very different position for contractors. At the moment, I think they have a choice.

Lord Bridges of Headley: Can you talk us through the employment rights of the individuals who are found in scope? Have they changed?

Carl Vincent: No.

Lord Bridges of Headley: Not at all. How has that been handled? How has that gone down in the workforce?

Carl Vincent: With the contractors?

Lord Bridges of Headley: Yes.

Carl Vincent: As I said, generally speaking we have not had a huge reaction from them. They have seen the proposal in front of them and either they decided to stay and negotiate an increase or they decided to leave. It might be different if the entire labour market was in the same place, but at the moment there are other employers in Leeds who are mostly using IT contractors.

The Chair: What proportion left?

Carl Vincent: Sorry, I have the numbers, but I cannot think of them off the top of my head.

The Chair: Perhaps you could drop us a note.

Carl Vincent: I am happy to, of course.

The Chair: And what proportion of those did you do a deal with and compensate?

Carl Vincent: From memory, it was about a third. Perhaps I could put it all in a table.

The Chair: Yes, thank you. Are there any other points?

Thank you very much indeed. We really appreciate your coming to the Committee, especially in these hazardous times. Thank you very much.