

# Association of Independent Professionals and the Self-Employed – Written evidence (OPR0024)

## Summary

IPSE (the Association of Independent Professionals and the Self-Employed) is the only representative organisation dedicated solely to supporting and representing the UK's 4.3 million self-employed. IPSE is submitting a response to this inquiry due to the dramatic and damaging impact of reforms to off-payroll legislation on the freelance sector – IPSE is grateful for the opportunity to contribute to this call for evidence.

Our response is based on the representative views of IPSE's membership, as well as [IPSE's research into the impact of reforms to IR35 on freelancers](#) – in particular, a survey of 1,017 freelancers conducted between July and August 2021, to which this submission will frequently refer.<sup>1</sup> This submission will also refer to excerpts of case studies submitted by freelancers in response to a call for views held by IPSE.

We note that the committee is particularly interested to hear the experiences of engagers; insights from IPSE's research into the impact of IR35, whilst focusing on freelancers, nonetheless suggests that it is now more difficult for clients to hire highly skilled freelancers. IPSE's own research into the impact of IR35 reforms on engagers is currently in the field and we will update the committee on the findings as part of our oral evidence.

Further feedback from freelancers in IPSE's network suggests clients are not incentivised to determine an engagement to be anything other than 'outside IR35', regardless of the true nature of the arrangement, due to the risk and severity of reprisals by HMRC. This situation has left many freelancers with little choice but to provide their services through the unregulated umbrella company sector – and sometimes with little or no choice in the umbrella company they can use when working on a contract.

Working within IR35 has also had significant financial consequences for freelancers with four out of five (80%) of those working inside IR35 reporting that they have seen a drop in their quarterly income by an average of 30 per cent. A quarter (25%) even said they had experienced a drop in income of over 40 per cent. A key reason for the significant financial consequences for freelancers seems to be Employers' National Insurance Contributions, with 72 per cent of freelancers working inside IR35 reporting that they were now liable for this and were paying it through a reduction in their day rate.

**Overall, IPSE firmly believes the Chapter 10 reforms should not have been introduced and should be reversed. If that is not possible, government should launch a full review of the impacts of the legislation with a view to making radical changes to alleviate its worst impacts on the self-employed and the industries they work in. Tax and employment**

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<sup>1</sup> [IPSE, Taking stock: Assessing the impact of IR35 reforms in the private sector](#), 2021

**status should be aligned so that where a hirer determines IR35 applies, it should be compelled to employ the individual directly.**

- 1. Has the recent extension of the off-payroll working rules to the private sector made it more difficult for engagers to hire people with the right skills and expertise? To what extent has its introduction contributed to job vacancies?** Our research indicates that where clients had traditionally fulfilled their short-term skills requirements by engaging freelancers, they are now less able to do so as a result of the April 2021 IR35 reforms.
  - 1.1 IPSE research suggests the reforms have led to a reduction in the total number of active freelancers in the market. When surveyed, 18 per cent of freelancers were not working – a majority (72%) cited the introduction of IR35 reforms as the reason for this.
  - 1.2 Since the implementation of the reforms, more than one in three freelancers (35%) report that they have left self-employment – closing their companies for retirement, moving into permanent roles, begun contracting abroad or are simply not working. The changes have also brought about a shift in how freelancers operate, with a third (34%) now working through umbrella companies, eight per cent on agency payrolls and three per cent on client payrolls.
  - 1.3 There is evidence that the reforms have accelerated freelancers’ plans to retire, making their skills inaccessible to clients sooner than would otherwise be the case. In addition, 11 per cent of freelancers surveyed planned to retire following the introduction of the reforms, whilst a further 6 per cent planned to stop working altogether.
  - 1.4 Writing to IPSE in response to a call for views, one freelancer said:

“...IR35 for me is an absolute disaster and as I’m over state pension age, once my current fixed term contract ends, I will be retiring... the skills I have built up over the years will no longer be available. This is not a choice I make lightly as I believe I still have several years in me but I cannot stand the thought of working as an employee.”
  - 1.5 Furthermore, 28 per cent said they would continue to work with small clients, who are exempt from the rules, and 24 per cent stated an intention to seek contracts abroad. This suggests that medium and large sized UK businesses may now find it more difficult to acquire skills from the freelance sector than they previously would have.
  - 1.6 **IPSE research also suggests the reforms have led to a reduction in the availability of contracts.** When asked about the key challenges they have faced since the private sector reforms, the most common response from freelancers was a reduction in work, with many mentioning difficulties in finding “suitable outside-IR35 contracts”. These reports are often accompanied by frustrations that end-clients are now missing out on skills and expertise by implementing blanket bans on engaging company directors or blanket inside-IR35 assessments.
  - 1.7 Responding to IPSE’s survey, one freelancer said:

"Since IR35 was introduced many highly skilled and specialised contractors have left the project I am on and cannot be easily replaced. So much for the flexible and dynamic UK economy."

- 1.8 Over one in ten (11%) of freelancers surveyed said that their client insisted they move onto a payroll without assessing the IR35 status – a blanket ban on engaging freelancers.
- 1.9 One freelancer told IPSE:

"Blanket panicked decisions by large organisations, not based on facts or working practices have decimated the market for genuine contractors delivering outcome-based flexible skills and services."
- 1.10 Similarly, another freelancer shared their experience:

"IR35 is severely disrupting the industry and causing skills shortages. Rate increases to compensate for the tax increases are increasing delivery costs. It's the biggest threat to our economic recovery - greater than Brexit or COVID."
- 1.11 Another freelancer outlined their experience to IPSE:

"I cannot say how many agents and clients basically begged me to apply for jobs as they were struggling to get talented people... but were unwilling to shift on changing their 'inside' stance."
- 2. For those engagers (and their advisers) who use the CEST (Check Employment for Tax Status) tool to assess employment status, how effective do you consider it to be? Do you have confidence in its results? If not, what further improvements need to be made to it?** IPSE research suggests that HMRC's Check Employment Status for Tax (CEST) tool is not currently an effective means of assessing the nature of a proposed engagement and can be manipulated by engagers to provide a preferred outcome. The tool also notably fails to account for mutuality of obligation (MOO) – a key determining factor for IR35 status, according to case law.
  - 2.1 From our latest research, just 18 per cent of freelancers stated that their client had used HMRC's CEST tool to assess their IR35 status. Instead, 21 per cent reported that their client had used a third-party company to assess their IR35 status, 10 per cent stated that their client had made the IR35 assessment themselves without using any tools or software whilst a further six per cent indicated that their client used a tool or piece of software other than the CEST tool.
  - 2.2 IPSE is very concerned by reports from freelancers that the tool can be manipulated by risk averse clients and third-party HR/solicitor advisors to produce inside-IR35 determinations, regardless of the true nature of the arrangement, in the interest of ruling out retrospective enquiries by HMRC in future.
  - 2.3 For instance, one freelancer shared their experience of a client using an "underdetermined" assessment through the CEST tool to place them within IR35:

"Clients believe they must use CEST as the assessment tool to be compliant and believe the answer it gives is gospel (and that "undetermined = inside IR35). All clients believe the contractor should pay the additional expenses of a client engaging a contractor through IR35, thereby avoiding their legal obligations."

2.4 Similarly, another freelancer shared their experience of a client using the tool to produce a certain outcome:

"Roles deemed inside without considering any factors related to myself / my company - Client's risk averse so if there is any doubt, they will determine inside IR35 - Client tax departments have a mindset that they are working for HMRC not a commercial mindset (e.g., deliberately answering CEST tool answers with the most conservative approach)."

2.5 Some freelancers are also reporting that the tool can be manipulated through trial and error to produce certain outcomes.

2.6 One freelancer replied to IPSE's survey with:

"The CEST tool is basically useless and is misused. I was told to try filling in different combinations of choices into CEST until I got an "outside IR35" judgement."

3. **What changes have engagers had to make to apply the off-payroll rules to contractors, in terms of systems, personnel and training? By reference to your own experience, to what extent (if any) do you consider that compliance costs have increased because of the changes?**

Commissioned IPSE research into the impact of IR35 on clients is currently in the field and covers the question of compliance costs – IPSE will include the key headlines from this piece of research during oral evidence.

4. **To what extent has the introduction of the new rules generated disputes between engagers and contractors concerning the status of contractors vis à vis the rules and how successfully or otherwise have these been resolved?** Our latest research revealed that, despite medium and large sized businesses being legally required to provide a status determination statement for all freelancers, 38 per cent of freelancers reported that their client had not provided them with a Status Determination Statement (SDS). Just over half (56%) of freelancers surveyed were provided with an SDS and of these 29 per cent disagreed with the determination whilst 69 per cent agreed with the outcome.

4.1 In terms of actively disputing their client's determination, over three quarters (77%) of those who disagreed with their IR35 status determination challenged the outcome whilst a quarter (23%) reported that they did not challenge the determination despite disagreeing with the assessment. Overall, 79 per cent of those who challenged their status determination reported that there had been no change as a result of their challenge, however, 17 per cent reported that their IR35 determination was successfully changed.

4.2 One limited company director currently in between contracts outlined their experience of disputing a determination with a client:

"I was working with a client outside IR35 until they panicked in late March and told me that they had decided I would have to move inside IR35. They didn't provide an SDS but did offer a choice of temporary employment or to carry on as a contractor. I asked for an SDS and challenged the outcome. It was completed by head office solicitors/HR management with no knowledge of how I was working. My own assessment was outside IR35 with strong indicators such as being in control of how I do the work. The company is very risk-averse and used the CEST tool with answers to suit the required outcome rather than the reality (which they had no interest in understanding)."

5. **What behavioural effects have resulted from the introduction of the new rules in the private sector in terms of arrangements adopted in hiring contractors?** In terms of how end-clients have altered their behaviour since the changes, the most notable example is the increase in 'inside IR35' determinations – with one in three freelancers (36%) now working in engagements that have been deemed 'inside IR35'.
  - 5.1 Freelancers have reported shifts in how clients are now determining status, with 21 per cent of freelancers reporting that their client had simply determined all engagements as inside IR35 – a blanket assessment. A further 11 per cent of freelancers reported that their client had insisted that they move onto a payroll without assessing the IR35 status of the engagement – a blanket ban.
  - 5.2 Similarly, the increase in inside IR35 roles has also resulted in 34 per cent of freelancers now operating via an umbrella company – considerably higher than anticipated prior to the reforms (19% expected to be operating through umbrella companies)<sup>2</sup>.
  - 5.3 The increase in umbrella company use is particularly concerning given that we know that almost two-thirds (63%) of freelancers reported that they had some level of choice but were given a limited range of umbrella companies to choose from. Worryingly, five per cent stated that they were unable to choose their umbrella company and had to operate through one allocated to them.
  - 5.4 One freelancer shared their experience of operating through an umbrella company:

"The day rate is now subject to Umbrella Fees and deduction of employment costs (employers NI etc), something which is an extra tax from my day rate on top of my normal PAYE taxes and NI. I am therefore now paying nearly 50 per cent tax overall from my contract day rate and I am unable to plan / control my personal income and unable to retain profit for out of contract periods to live on. It has destroyed my ability to operate as an independent contractor."
  - 5.5 In addition, for those freelancers that continue to operate outside IR35, many are now reporting that they have had to cover the liability for any retrospective HMRC investigation with the imposition of indemnity clauses within contracts or being advised or forced to take out additional insurance that some are concerned may not cover the whole supply chain.
  - 5.6 One freelancer outlines this process here:

<sup>2</sup> IPSE, The impact of IR35 changes on the self-employed in 2021, 2021

“End client only prepared to work outside IR35 as an exception as critical to key delivery this year. New agency insisted my company was liable for taxes if HMRC viewed IR35 assessment to be wrong. Agency insisted my company take out additional insurance to cover their or end client tax liability. Received confirmation that insurance would pay out in this instance. Don't know if this is legal and would truly work as does not align with new IR35 laws, think this will only be proven by being challenged in courts.”

6. **The Government is proposing a new employment body with powers to enforce employment rights, including for those engaged by agencies and umbrella companies. How effective do you think such a body will be in ensuring workers, particularly the lower paid, are treated fairly?** IPSE's own research has highlighted that those operating via an umbrella company are particularly dissatisfied with management of business expenses (55% stated they were either somewhat or very dissatisfied, including 37% who were very dissatisfied) and handling of employer's NI and apprenticeship levy deductions (33% reported that they were either somewhat or very dissatisfied including 25% who were very dissatisfied).
  - 6.1 IPSE feels strongly that umbrella companies should be much more closely regulated. There have been well publicised issues dating back many years of systematic tax avoidance facilitated by non-compliant umbrellas and more recent concerns over poor treatment of umbrella employees e.g., withholding of holiday pay. The Single Enforcement Body proposed by the Government is a welcome step in the right direction, but it must be properly funded and given the resources that it needs to ensure that any non-compliant umbrella companies are prevented from operating.
  - 6.2 Although better regulation of umbrella companies would be a positive development, IPSE ultimately believes that no one should be forced to work via an umbrella company against their will. As we said in our response to the consultation on the off payroll working reforms, clients that determine that IR35 applies to an engagement should be compelled to employ individuals directly.
  - 6.3 After all, they have in essence determined that this role is best suited to an employee – they should therefore employ the individual that will fill the role. If, however they do not want an employee, and they would prefer to engage someone on a freelance basis, then they should make that clear from the outset and IR35 should not apply.
7. IPSE received many case studies from freelancers as part of a call for views in preparation for this inquiry, whilst it would not be practical to include them all, we believe the following case study exemplifies the significant challenges faced by both engagers and freelancers since the implementation of the reforms:
  - 7.1 “I have operated via my Limited Company as a contractor since 2008 and have worked hard to build up my network and client base. I have also always used due diligence and independently had contracts assessed to determine my IR35 status, which has been outside of IR35. When the IR35 rules were delayed last April due to covid the company I was contracted to put an immediate blanket ban on all limited company directors and my contract along with 20 other contractors was terminated as we refused to go via an umbrella company when we have our own payroll systems set up.

Then due to lockdown I was unable to engage any contracts for 5 months. No pay, no furlough, no government support. One of the "Forgotten Limited". Finally in August 2020 I was able to engage a contract with a previous client I had worked for. I assessed my contract using IR35 Shield and was determined outside of IR35. I remained with this client until the end of March 2021 and only left as they had deemed all contract roles as inside IR35 via CEST when they clearly were not.

I managed to find a contract outside IR35 but that was only for 3 months from June to September 2021. Since that contract finished last month, I have been trying to find another contract but job advert after job advert that match my skill set of Business Transformation or Cyber Security are all stating Umbrella Only, which I feel is wrong. Another client contacted me last week and has offered me a 6-month contract but have stated that the role is inside IR35 and an Umbrella Company is the only option for this engagement. I have not had a one-to-one status determination conducted, just told that the role is inside and they will not increase the day rate to compensate me for my loss of earnings. The company are even telling me which Umbrella Company I am to use.

Today I have had a profile of "take home" pay from the said Umbrella Company and I can't believe how low my monthly salary will be. Employers NI, Apprenticeship Levy and their cut makes for very sad reading. But sadly, I now have no choice but to take it. I am skint and eating into my now very limited pension savings due to no work or furlough. I am gutted and can't understand how this has been allowed to happen. How can I be forced into using an umbrella company with no employment rights while having to use my own laptop and mobile phone. I am either an employee or I am not? I am a Professional who feels exploited by this ruling.

I also feel worthless and am beginning to think there is no point in contracting anymore. We work hard with no security, no holiday or sick pay, no pensions, no employment rights and other benefits of permanent employment. It's a sad day for me today. I feel that the government have won and there is nothing we can do about it. This ruling is grossly unfair and I can't believe it is happening in my country. Just because it is law it doesn't make it morally right!!!"

7.2 "The impact on us of this odious legislation has been immense. We were a small (30 person) UK-based software development company focusing on international transactional and business intelligence systems and had established a very good track record. To achieve this we had spent nearly 10 years enhancing and training our staff to use the highest analysis, design and software development standards.

Many (more than half) of our staff were from Europe living in the UK. Brexit caused a small number of our former staff to relocate back to Europe but this was small compared to the number who left as a result of IR35 which was the last straw for them; including two directors of the company which, as a result caused the closure of the company. We who are left in the UK, continue to recommend our former, but now Europe-based staff as they were excellent and highly skilled. Now, although not working through the same company we all use the same advanced information, systems and technology (IST) development standards which represents a massive cost and quality advantage for

customers. This is also good for our Europe-based colleagues as it is far more profitable to work from Europe and not out of the UK and in most situations it is perfectly feasible for them to do so.

So in our case, the only thing IR35 has achieved is to push the revenue the country and HMRC would otherwise have earned to Europe. This legislation has absolutely damaged UK business operating flexibility, as previously, non-essential staff requirements would have been filled by contractors that can be given reasonably short notice when adverse business conditions arise. This is especially important in the IST development environment where short-term increases in project staff are frequently required.

To the British Government on this, all I can say is "Very badly done"! (In fact, in my opinion, this legislation borders on lunacy)."

*15 November 2021*