Inland Revenue

Supplying services

through a limited company or partnership

We produce a wide range of leaflets, booklets and Helpsheets designed to explain different aspects of the tax and National Insurance systems in plain English and to assist in the completion of tax returns. Most of them are free. Some you might find particularly helpful are listed below.

IR20	Residents and non-residents - Liability to tax in the United Kingdom
IR56	Employed or self-employed? A guide for tax and National Insurance
CWG2	Employer's further guide to Pay As You Earn and National Insurance contributions
480	Expenses and benefits. A tax guide
490	Employee travel. A tax and NICs guide for employers

Our leaflet IR120 'You and the Inland Revenue' tells you more about the standard of service you can expect and the steps to take if you want to comment on the service you receive, or complain about the way we have handled your tax and National Insurance affairs.

Our IR List 'Catalogue of leaflets and booklets' gives further information about our publications, most of which you can get from any Inland Revenue Enquiry Centre, Tax Office or Inland Revenue National Insurance Contributions Office. Addresses are in your local phone book under 'Inland Revenue'. Most offices are open to the public from 8.30 am to 4.30 pm, Monday to Friday and some are also open outside these hours.

Your local library or Citizens' Advice Bureau may also have copies of our leaflets.

You can also get most of our leaflets by

- calling our Orderline on **0845 9000 404** between 8.00 a.m. and 10.00 p.m., seven days a week (except Christmas Day). Orderline calls are charged at local rates

- fax on **0845 9000 604**

- e-mail on **saorderline.ir@gtnet.gov.uk**

Many leaflets are also available on the Internet at

www.inlandrevenue.gov.uk

Tax Bulletin

This is produced six times a year and shows some of our current thinking on technical aspects of taxation. The bulletin is available on the Internet and in paper format by annual subscription. For further information contact

Inland Revenue (Tax Bulletin)
Room 530
22 Kingsway
London WC2B 6NR

Tel. 0207 438 7700

Do you use a limited company or a partnership to provide your services to clients? If so, you need to know about new tax and National Insurance Contributions (NICs) rules introduced from 6 April 2000.

This leaflet will help you find out

- whether the new rules apply to you, and
- what to do if they do apply.

It also answers some common questions and tells you where to get advice if you are still unclear on any point.

Do the rules apply to me?

The rules will apply to you if you answer ‘yes’ to both the following questions.

- Would you be an employee if you worked for your client directly and not through your company or partnership?
- Does the company or partnership you work through meet the conditions set out below?

These questions are explained in more detail below.

Would I have been an employee of my client?

The rules only apply if you would have been an employee of your client, had it not been for the existence of your company or partnership.

If you can answer 'yes' to the following questions, you would probably have been an employee of your client for the contract in question and therefore within the new rules.

- Do you work set hours, or a given number of hours a week or a month?
- Do you have to do the work yourself rather than hire someone else to do the work for you?
- Can someone tell you at any time what to do or when and how to do it?
- Are you paid by the hour, week or month?
- Can you get overtime pay?
- Do you work at the premises of the person you work for, or at a place or places he or she decides?
- Do you generally work for one client at a time, rather than having a number of contracts?

If you can answer 'yes' to the following questions, you would probably **not** have been an employee of your client and therefore outside the new rules.

- Do you have the final say in how you do the work for the client?
- Can you make a loss on the contract?
- Do you provide the main items of equipment you need to do the job for the client, not just the small tools many employees provide for themselves?

- Are you free to hire other people on your own terms to do the work you have taken on? Do you pay them out of your own pocket?

- Do you have to correct unsatisfactory work in your own time and at your own expense?

- Do you have a number of customers at the same time?

You will have to think about each contract individually. Some people will find that they have some contracts which would have been employment and so come within the rules, and others which do not.

The number of clients you have **may** be relevant to the decision whether your work for each is as an employee, or as a self employed person. If you have many different clients this **may** indicate self employment, and be a factor that should be considered in addition to the actual details of each contract. If you have a number of different clients, but are unsure whether you are within or outside the rules, you may wish to talk to your local Tax Office.

More information about employment status can be found in leaflet IR56, 'Employed or self-employed', the February 2000 edition of 'Tax Bulletin', the Employment Status Manual as published on the Inland Revenue website **www.inlandrevenue.gov.uk,** or by contacting your local Tax Office.

Does the company or partnership I work through meet the following conditions?

If your services are supplied through a company.

The rules apply if

- you (or your family*) control more than 5 per cent of the ordinary share capital of the company, or

- you (or your family*) are entitled to receive more than 5 per cent of any dividends from the company, or

- you receive, or could receive, payments or benefits from the company which are not salary, but could reasonably be taken to represent payment for the services you provide to clients.

If your services are supplied through a partnership of which you are a partner.

The rules apply if

- you (or your family*) are entitled to 60 per cent or more of the profits of the partnership, or

- all or most of the partnership's income comes from providing services to a single client, or

- the profit sharing arrangements in the partnership are designed to ensure that you receive an amount based on the payments received for your services to clients.

(* family includes an unmarried partner)

What happens if the rules apply to my contract?

Your company/partnership should operate Pay As You Earn (PAYE) and pay NICs on any payments of salary during the year in the usual way.

You may also have to pay an additional amount of tax and NICs, based on the payments received by your company or partnership for your services, at the end of the tax year or earlier, if you break your connection with the company or partnership during the year (see ‘Common questions’). Your company or partnership will also pay employer’s NICs on the same amount. The following section tells you how to calculate any end of year payment.

What should I do at the end of the tax year?

At the end of the tax year you will need to check that you have paid the correct amount of tax and NICs. If not, you may have to pay additional tax and NICs.

To calculate if any tax or NICs are due at the end of the year.

1. Add up all the payments your company or partnership has received for your services, under contracts to which the rules apply.

2. Deduct 5 per cent from this total. This is to allow for the costs involved in running your company or partnership. There is no need to show how this money is used.

3. Add any other payments and the value of any benefits in kind (such as the use of a car) you have received directly, not through your company or partnership, for services provided under the contract, if they are not already taxable.

4. Deduct any allowable expenses met by your company or partnership (see ‘Common questions’).

5. Deduct any earnings that you have received from your company or partnership in the tax year on which PAYE has been operated and NICs have been paid, and the value of any benefits in kind (such as a car) provided by your company or partnership on which tax and NICs are payable.

6. Deduct the employer’s NICs that your company or partnership has paid on the earnings (but not employee NICs) and Class 1A contributions due on the benefits in kind. NICs should be calculated on an annual basis, whether or not you are a director of the company, (see CWG1

‘Employer’s Quick Guide to Pay As You Earn and National Insurance Contributions’, Card 12 Company Directors - National Insurance contributions).

7. Work out the amount which, together with the employer’s NICs due on it, comes to the amount calculated after Step 6. The result is known as the ‘deemed payment’. If the deemed payment is greater than zero you will need to pay more tax and NICs and you should include it in the calculation of PAYE and NICs for the pay period in which it falls. (See ‘Common questions’). There is an example of how to calculate a deemed payment at the end of this leaflet.

Common questions

Does the deemed payment have to be paid as salary on 5 April?

No. The deemed payment is simply a means to calculate the tax and NICs due, whether or not any payment is actually made to the worker. It can be paid as salary, but the rules do not require this to happen. It may be given to the worker (or others) in the form of dividends, or may be retained in the company.

You will not have to pay tax twice on the deemed payment if it is paid as dividends. Your Tax Office can explain to you how the tax payable on the dividends can be offset.

The deemed payment and employer’s NICs due on it can be deducted when calculating your company’s corporation tax.

Companies should be aware an extra payment of tax and NICs may be due at the end of the tax year and budget accordingly.

When must I pay any additional tax and NICs?

Any tax and NICs due at the end of the tax year as a result of the calculation of the deemed payment should be paid according to the normal PAYE and NIC payment rules. The amount of the deemed payment and the tax and NICs due on it should, if possible, be included in the PAYE return by 19 April and in the Employer's Annual Return (Form P35), which has to be sent to the Inland Revenue by 19 May.

Most of the information needed to calculate the final tax and NICs liability should be available before 5 April and it should be possible to make an estimate of the tax and NICs due at that point. It will be important to keep records of relevant income and expenditure so that you can do this.

However, if it is not possible to calculate the correct amount by 19 April, the Inland Revenue will accept a payment of a lower amount on account of the tax and NICs due, as long as it is made clear on the Employer's Annual Return (P35) that the amount is provisional.

There will be an interest charge on any of the tax or NICs due on the deemed payment, if it is paid after 19 April. But, if you make it clear on the P35 that the amount is provisional, no penalties will be charged if you pay the correct amount by the following 31 January.

This concession on penalties will apply for the tax year 2000/01 and will be reviewed to establish whether it should continue to apply for subsequent years.

If you do not send the final amount by 31 January following the end of the tax year, the Inland Revenue will take steps to collect any unpaid tax or NICs, and any interest due. In addition penalties may be sought in cases of negligent or fraudulent conduct.

What if I stop working through my service company or partnership before the end of the year?

If you stop working through your service company or partnership before the end of the year, the deemed payment should be calculated in the normal way, and will be treated as having been made immediately before you stop. Please contact your Tax Office for further advice.

What expenses can I deduct in calculating the deemed payment?

In addition to the flat rate deduction of 5 per cent, the following expenses can be deducted in the calculation.

- Any expenses met by your company or partnership that an employee of the client would have been able to claim against income tax if he or she had spent the money personally (such as certain travel expenses, professional subscriptions and premiums for professional indemnity insurance). Inland Revenue booklet 480 ‘Expenses and Benefits. A tax guide’ provides full details. More details about travelling expenses are given in the next section.

- Any pension contributions paid by the company to an approved pension scheme for **your** benefit (but not for anyone else).

What travelling expenses are allowed in calculating the deemed payment?

This will depend on your pattern of working. If you work through your company or partnership for a series of clients in different places, you may be able to deduct the costs of travelling to your clients’ places of business. Provided you do not expect to spend more than 40 per cent of your working time at any one site you are entitled to a deduction for all journeys from home to the clients' premises.

If you do spend more than 40 per cent of your time at a single site, but the engagement is both expected to, and actually does, last for no more than 2 years, a deduction for travel costs will also be available. Further details are in Booklet 490 'Employee Travel - a tax and NICs guide for employers'.

What about company cars?

If you use a car owned by your company or partnership for business travel, a deduction can be made in the calculation of the deemed payment for the costs of that business travel met by your company. You may use the actual costs or the Inland Revenue's authorised mileage rates. Expenses incurred in the course of private use of the car cannot be deducted in calculating the deemed payment.

If the company or partnership provides you with a car for your private use, you will have to pay tax on this benefit according to the rules which apply to other employees. The amount of the car benefit charge can be deducted (at Step 5) in calculating the deemed payment. See sections 11 and 12 of booklet 480 - 'Expenses and benefits. A tax guide' for further details.

Class 1A NICs paid on the company car benefit will be deductible in the calculation of the deemed payment, alongside other employer's NICs.

Your company or partnership will be able to set any costs of providing the car, including capital allowances, against its taxable profits.

What do I need to put on my Self Assessment return?

The deemed payment is treated as income from employment with the company or partnership. It should be recorded on your Self Assessment return on the supplementary employment pages. If you have any other income from employment with the same company or partnership you should record the total amount, including the deemed payment.

How do I apportion expenses between engagements that are affected by the new rules and those which are not?

In calculating the deemed payment, you can deduct expenses paid by the company or partnership which you would have been allowed to claim against tax if you had been an employee of the client, and spent the money yourself. These expenses must relate specifically to your engagement with that client. You will have to keep suitable records to be able to identify the correct amounts.

For example, this could be by reference to car mileage to work out what part of the motoring expenses related to engagements affected by the new rules.

If a client makes a single payment in respect of two or more workers, how will the income be split between them?

This will depend on the particular facts and circumstances. If a company or partnership receives a payment in respect of services provided by more than one worker, the payment should be apportioned between them, by the company or partnership, on a reasonable basis. The Revenue will re-apportion any payment if it appears the company's or partnership's basis of apportionment is unreasonable. The company can appeal against the decision of the Inland Revenue.

What are my tax and NICs liabilities if I work overseas?

If you work overseas your tax and NICs liabilities are the same as if you were employed directly by the overseas client. Further information on liability and the rules about residency can be found in the Inland Revenue booklet IR20 'Residents and non-residents. Liability to tax in the United Kingdom' or from your local Tax Office.

Can I avoid the legislation by using an offshore service company?

No. If you would have been liable to UK tax and NICs had you been employed directly by the client, you must pay UK tax and NICs under these rules, whether or not your service company is located in the UK.

If an offshore company fails to deduct and account for PAYE tax and NICs under the legislation, liability to pay tax and NICs can be transferred to you. Action to recover employer's NICs not paid by an offshore company could also include action against any assets of that company located in the UK.

The Inland Revenue has powers to obtain details of payments to offshore companies from the records of clients and agencies.

Where can I get advice about whether the legislation applies to my contracts?

Advice can be given on existing contracts only. If you are not sure whether the new legislation applies to a particular engagement, advice will be available from local Tax Offices. They will give a written opinion about employment status for tax and NICs purposes.

The Inland Revenue will review the facts. This will involve looking at whether the relationship between a worker and a client would have been one of employment, if there had been no company or partnership. In order to do this, the Inland Revenue will review the contract or contracts which establish the relationship. They may also talk to you and to others. If you do not agree with the opinion given by the Inland Revenue, and further discussion has failed to achieve agreement, you can request a formal decision against which you can appeal.

If you would like our opinion on a particular engagement you should send your contract(s) to

LP10
IR35 Unit
1st Floor
Tyne Bridge Tower
Church Street
Gateshead
Tyne & Wear
NE8 2DT

e-mail: **IR35@inlandrevenue.gov.uk**

Tel: **0845 303 3535**

Fax: **0845 302 3535**

Example of a calculation of the deemed payment under the service provision rules *

Mr Worker works through his own limited company. He provides services to Mr Client under a contract which falls within the new rules. Mr Client pays £40,000 to Mr Worker's limited company for the services provided by Mr Worker.

Mr Worker does no other work in the year in question. He pays himself a salary of £20,000 during the course of the year and operates PAYE and deducts NICs from that salary in the usual way.

The limited company buys Mr Worker a travel card for £500 to allow him to get to Mr Client's business premises. It also pays £4,000 into Mr Worker's pension scheme.

	£**
Total amount from client (all subject to new rules)	**40,000**
Deduct	
5% to reflect the costs involved in running a company or partnership	2,000
Schedule E expenses related to contract	500
Employer's pension contributions, to an approved scheme, on behalf of worker	4,000
Earnings paid to Mr Worker in year (subject to tax under Schedule E)	20,000
Employer's NICs paid in year	1,840
Total deductions	**28,340**

Balance (£40,000 - £28,340)	**11,660**

Deemed payment =
Balance x100÷(100+11.9)*** (see Step 7) **10,420**

Schedule E tax and NICs are due on the total of the earnings paid in year plus the deemed payment.

Employer's NICs due on the
deemed payment 1,240

Extra tax and employee's NICs may be due on the deemed payment

* The calculation assumes the NICs contribution rates, thresholds and earnings limits for 2001/2002

** Rounded to the nearest whole number.

*** The employer's contribution rate can vary, contracted out or in rates are different. The figure you add to 100 to get the correct divisor should be the contributions rate that is applicable to you. See Inland Revenue National Insurance tables CA38 and Employer's Annual Pack.

Where can I get more information?

The Inland Revenue's web site has more information about the tax and NICs consequences where services are supplied through a limited company or partnership, a copy of the legislation and a list of frequently asked questions with answers. The address is
www.inlandrevenue.gov.uk/ir35

Our service commitment to you

The Inland Revenue and Customs & Excise are committed to serving your needs well by

acting fairly and impartially

We
- treat your affairs in strict confidence, within the law
- want you to pay or receive only the right amount due.

communicating effectively with you

We aim to provide
- clear and simple forms and guidance
- accurate and complete information in a helpful and appropriate way.

providing good quality service

We aim to
- handle your affairs promptly and accurately
- be accessible in ways that are convenient to you
- keep your costs to the minimum necessary
- take reasonable steps to meet special needs
- be courteous and professional.

taking responsibility for our service

- We publish annually our customer service aims and achievements
- If you wish to comment, or make a complaint, we want to hear from you so we can improve our service. We advise you how to do this.

We can provide better service if you help us by

- keeping accurate and up to date records
- letting us know if your personal/business circumstances change
- giving us correct and complete information when we ask for it
- paying on time what you should pay.

Further information on customer service is available at Inland Revenue and Customs and Excise local offices, set out in our Charters, complaints leaflets (IR120 and Notice 1000) and Codes of Practice.

These notes are for guidance only and reflect
the tax and NICs position at the time of writing.
They do not affect any right of appeal.

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