

Period at one site (actual or expected period of time)	Extent of duties at one site Length of time Less than 40%	Extent of duties at one site Length of time Greater than 40%
Less than 24 months	YES	YES
Greater than 24 months	YES	NO

The following examples may assist with interpreting the above:

Emma works through her own company as a computer consultant specialising in banking systems. She spends 18 months working full time at a bank in Lombard Street in the City of London. She then moves next door designing a new system for a different bank, where she expects to stay for 22 months. After that contract she moves to a nearby bank for 17 months.

Emma is not entitled to tax relief for her travel from home to work because the nature of her work is such that she expects to work continuously in the "Square Mile"; her travel will be broadly the same every day, year in year out.

David is a computer consultant. He works full time at a site for 18 months, the work is then extended for another 18 months at the same workplace, and the extension is the subject of a separate contract.

As long as David did not expect to be working on the site for more than 24 months, he is entitled to relief for travel from home to work. Once his company enters into a new contract David expects to be working on site for more than 24 months, so from the new contract he is not entitled to relief for his journey.

To benefit from the above rules it is essential that an accurate mileage/travel log be kept.

The cost of travelling to a temporary place of work will be able to be claimed as a valid expense with no personal tax liability.

As soon as it is known that you will be at the same site for two years the claims will cease. It may be wise to negotiate any contract extension to take the contract up to 23 months so as to maximise the benefits available.

Most people will find the most efficient method of reimbursing travelling expenses will be to run your car privately and 'charge' the company a mileage rate using the Inland Revenue's 'Fixed Profit Car Scheme' (FPCS). The FPCS rates are tax-free and are based upon the engine size of the car. Remember that the car will continue to be your car and you should pay all the related costs.

Fixed Profit Car Scheme 2006/07 rates

First 10,000 miles in tax year

40p

Additional miles in tax year

25p

Accommodation Expenses

Temporary accommodation, such as bed and breakfast and hotels, can be allowable as an expense provided it only covers Monday to Friday accommodation. As with travel, this is not available after 24 months (see above).

The allowance will not cover accommodation such as a rented flat; this would be classed as “a benefit in kind” and taxed accordingly.

Insurance

By law, every employer must take out a policy for employer’s liability insurance, which covers the employer against claims by the employee for injury etc. This cover is still legally required for one-person companies.

Other insurance's that you may consider taking out include:

- ◆ Public Liability Insurance – to insure you against claims from third parties that may sue if they have suffered from your actions.
- ◆ Professional Indemnity Insurance – to insure you against any claims made against you, for example, if software written by you does not work.

Pensions

Whilst retirement may seem a long way off it is important to start providing for your future pension as soon as possible.

The company, subject to certain restrictions may pay pension contributions.

It may also be possible to provide Pension linked life cover, again paid by the company.

Salary & Expenses for contracts caught by IR35

Under regulations (commonly known as IR35), there are restrictions on what expenses etc can be claimed by you through the company. The qualifying expenses are as follows:

- ◆ Travelling, accommodation and subsistence expenses that are allowable (see section on travelling expenses on pages 5-7)
- ◆ Employer contributions to approved pension schemes
- ◆ Professional Indemnity Insurance costs
- ◆ Subscriptions to approved professional bodies
- ◆ A further flat rate of 5% of the gross payment from the contracts. This does not have to be accounted for to calculate the “deemed salary”; the 5% allowance will be allowed in all cases. Expense receipts/claims will be required to reclaim any VAT and to claim against Corporation Tax.
- ◆ Employer National Insurance contributions

The total of the above items will be deducted from the income from the contract(s) and this net amount will be paid as a salary to you. This salary is subject to tax and National Insurance in the normal way.

When the accountants receive your monthly invoices, expense claim form and copy bank statements they will send you a report on what you have spent etc. and send you a payslip showing your salary and tax deductions.

Income tax and National Insurance contributions will be deducted as with any salary. The tax and National Insurance contributions will usually be paid quarterly, the accountants advise how much to pay and when it should be paid. All you have to do is send a cheque!

The accountants also complete the PAYE annual returns, including P35, P60, P14 and P11d's.

Although the level of expenses is restricted it is still beneficial to trade through a limited company than remain a permanent employee.

From experience with existing clients other benefits include:

- ✓ Being paid for any overtime worked
- ✓ Greater freedom of choice
- ✓ Greater variety of work
- ✓ Free of “office politics”

Already contracting with your own limited company?

Transferring from your current accountant (or even if you do not have an accountant) is very easy. Just complete the application form with some basic details, together with the items listed below to start the transfer.

Documents needed from you:

1. Copy of the Certificate of Incorporation
2. Copy of the Memorandum and Articles of Association
3. Copy of the latest Annual Accounts (if prepared)

Any other required details will be requested directly from your old accountants.

Once the needed details are received they be checked to ensure that the accounts are in order including checks on the VAT account, PAYE/NIC payments, Corporation Tax etc.

As soon as the transfer is complete you can start to enjoy all of the benefits of the service as listed on page 1.

How much will it cost?

There are no transfer fees or charges.

Assuming take-over at the start of your new financial year the fees will be simply £60.00 + VAT (£70.50) per month.

If the take-over part is way through the financial year the fee will be £60.00 + VAT (£70.50) from starting to act for the company PLUS £30.00 + VAT (£35.25) for each month from the start of the financial year to when they started to act for you. Please contact the office if you wish to discuss what fees would be payable.

How much can I expect to earn through my own Limited Company?

All examples assume a single person allowance of £5,035, claiming 10,000 miles per annum by car and are based on the 2006/07 tax rates.

	£	£	£
Net Annual contract	50,000	75,000	100,000
Add Flat Rate VAT saving*	1,700	2,550	3,400
Gross Salary	10,000	10,000	10,000
Employer NIC	635	635	635
Mileage Allowance	4,000	4,000	4,000
Accountancy Fees	846	846	846
Total Costs	15,481	15,481	15,481
Pre Tax Profit	36,219	62,069	87,919
Corporation Tax @ 19%	6,882	11,793	16,705
Profit After Tax & Available for Dividends	29,337	50,276	71,214
Income for Contractor			
Dividends	29,337	50,276	71,214
Net Salary	8,620	8,620	8,620
Mileage Allowance	4,000	4,000	4,000
Less Higher Rate tax On dividend income	(959)	(6,194)	(11,428)
Total Net Income (After all taxes)	40,998	56,702	72,406
Take Home Pay as a % of Gross Income	82.0%	75.6%	72.4%

All cases will be different but the above examples provide a guide to what you can expect to earn through a limited company.

* - This is the Year 1 saving of 3.4%, after year one the saving reduces to 2.225%

Your Questions Answered by our Recommended Accountant

Q. I am new to contracting and I do not even have a company set up?

A. We offer a FREE Limited Company to all new contractors who use our services for at least twelve months. (We charge just £69 for the company if you stop using us within the first twelve months).

Q. I live 125 miles away from your office, am I too far away?

A. No. We offer a nation-wide service to contractors; all our work can be carried out at the office using the fax, postal service and e-mail.

Q. What happens if I need help?

A. You may email, telephone, fax or write with any query, we will respond as soon as we can, usually the same day.

Q. What if the "IR35" rules do not apply to my company?

A. No problem. If, after reviewing your contract and work situation, you feel that the IR35 rules will not apply to you, simply let us know and we will deal with your accounts accordingly.

Q. Will I need an audit?

A. Limited companies with an annual turnover below £5.6 Million do not need to have an audit.

Q. How much notice must I give if I want to stop using your services?

A. In the unlikely event of you wishing to stop using our service, all we would require is one month's notice.

Q. How quickly can I start to use you?

A. Simply return the form (or a copy) enclosed with this pack. As soon as we receive the completed forms, we will set you up and contact you for anything further that we may need.

Q. What is the cost of closing my company?

A. There is a standard fee to close the company of £141 (inc. VAT), however depending upon how long you have traded, there may be a small additional charge to prepare the final accounts.

Q. What expenses can I use the 5% allowance for?

A. The flat 5% allowance is given in all cases and does not have to be accounted for to calculate the "deemed salary". Any unused balance of the 5% allowance will be declared as profit and be available to be paid as a dividend.

IR35 – What is it?

IR35 was introduced in April 2000 and is designed to combat what the Inland Revenue call “disguised employment”. The aim is to increase the tax paid by people who set up their own company instead of working as a normal employee.

Where a company provides the services of a member of staff to a client (either via an agency or directly) and the terms are such that without the intermediary (company), the individual would be an employee of that client the new tax treatment is triggered.

The deciding factor is to establish whether you are classed as “employed” or “self employed”. There is no statutory definition of employment; however the Revenue will look at several factors to help decide which side of the fence the engagement lays. The relevant factors are:

Direction and Control

The right of direction and control should be considered. It is not necessary to prove that the person carrying out the work is doing so under very detailed supervision because even professional persons can be operating under a general and overall framework of control from the end client.

- a) **What is done** – the right of a client to move the worker to different areas of higher priorities will be a strong indicator of employment.
- b) **When it is done** – control over when the work is done may be an indicator of employment.
- c) **Where it is done** – when you are required to work on your client’s premises this can be an indicator that there will be other control aspects to the engagement. If you can do the work wherever you like, this tends to indicate self-employment.
- d) **How it is done** – this is a very strong indicator of employment; it permits the client to prescribe the way in which the work is to be carried out. However, the absence of this level of control does not necessarily indicate self-employment, it is unusual for someone of a particular skill to be told how to do their work, but this does not make them self employed.

Suggestion – to avoid being caught out, the contract and the actual working arrangements should be as free as possible from aspects of control. Being able to work from your own office (even if only part of the time), be relatively free to decide your own working hours/days will help towards this area being a non-IR35 pointer.

Right of Substitution

Personal service is an essential element of a contract of employment. A person who has the freedom to choose whether to do the task themselves or hire somebody else to do it (on a reasonably unfettered basis) for them, is probably self employed.

Suggestion – a right of substitution written into all contracts, including being acknowledged by the end client and that your company would pay any substitute would help establish your right to substitution.

Provision of equipment

A contractor engaged to undertake a specific piece of work using his or her own tools and equipment will be a strong pointer to self-employment. If the contractor were provided with equipment this would be a pointer to employment.

Suggestion – provision of your own tools, equipment and office facilities can point towards self-employment and show certain financial risk.

Financial risk

An individual who risks their own money, such as buying assets, bearing running costs and paying for overheads, is probably self-employed. The risk of not being paid for an invoice would not qualify; this would be viewed as bad luck. Financial risk could also take the form of quoting a fixed price for a job, with the consequent risk of bearing the additional costs if the job overruns.

Suggestion – working for a fixed price, agreeing to correct defective work (at your cost), providing your own insurance cover will support a case for self-employment.

Basis of payment

Employees tend to be paid by fixed rates, paid weekly, monthly etc. and may also be paid for overtime. Self-employed contractors tend to be paid a fixed sum for a particular job.

Suggestion – if you cannot charge a fixed price, try to issue your own invoice rather than relying on timesheets, steer away from using terms such as “overtime” and try to get any expenses included in the rate. If you must charge for expenses, include on the invoice and do not use the client’s claim forms.

Length of engagement

Long periods working for one client may be typical of an employment but not conclusive. Regular working for the same client may also indicate that there is a single and continuing contract of employment.

A period of notice in the contract is more typical of employment contracts, so an absence of a notice period would point towards self-employment. If you do have periods of notice ensure that it is the same on both sides.

Suggestion – ensure that the contract does not contain any clauses that prevent you from working for other clients at the same time. Having more than one contract on the go will strengthen the case towards self-employment.

Mutuality of Obligation (MOO)

Mutuality of Obligation would normally appear in all contracts, i.e. an obligation on each party to provide something.

The internal guides for Revenue staff suggest that they ignore this test when considering the IR35 status of a contract. This is quite a complex test but the Judge was critical of the Revenue's instruction to ignore it. This tests if any obligation exists between the client and the contractor. Contracting via an agency would not result in an actual contract between the client and the contractor although this test sees if there is an imaginary one.

If the client simply pays the contractor or agency for services then it may be that MOO does not exist and so not an "employment" situation.

Suggestion – ensure that the contract clearly sets out what is expected and no additional work is done. Longer, continuous contracts would have a harder time overcoming a self-employment test.

In business on your own account

To show if a person carries out business on their own account, it is necessary to take account of all aspects of the business from an overall view. If your business looks like a real business this will strengthen your case.

Suggestion – aspects that would help towards showing that you are a genuine business include, having your own office and equipment, more than one client at a time, business telephone, stationery, other sources of income etc.

Day to Day working

If the Revenue investigates your contract they may contact the end client and seek information on how you actually work. If you are seen as an integrated part of the organisation this can weaken your case for self-employment status.

Suggestion – try to avoid acting similar to employees of the client, such as:

- ◆ Using staff facilities and benefits such as car parks, canteens etc.
- ◆ Appearing on internal phone lists & email addresses
- ◆ Joining in on staff events such as social events, Christmas parties etc.
- ◆ Managing employees of the client
- ◆ Similar work patterns/holiday leave as employees of the client

If your contract and your actual working practice points towards self-employed status then the IR35 rules will not apply.

You should be targeting the points in the Suggestion boxes above to ensure that self-employed status and exemption from IR35.

Effect of the new rules under IR35

On the assumption that the engagement falls under the new rules, the “deemed salary” will have to be calculated. Certain expenses can be deducted from the income arising from relevant engagements, as follows:

- ◆ Travelling and other expenses covered under Section 198 ICTA 1988
- ◆ Employer contributions to approved pension schemes
- ◆ Employers National Insurance Contributions
- ◆ A flat rate 5% of the gross income from relevant engagements – receipts will still be required for Corporation Tax purposes - the 5% deduction will be allowed in all cases to calculate the deemed salary.
- ◆ Professional indemnity insurance
- ◆ Professional subscriptions

Frequently Asked Questions about IR35

Q Can I get tax relief spent by my company for training?

A No. This is not allowable to normal employees and will not be allowable on its own. You will however be able to utilise the 5% allowance if you choose.

Q Will I be taxed if my clients or agency provide training for me?

A No. Any training provided by clients or agencies will not count as a taxable benefit, and no tax charge will arise.

Q Can I get relief for the cost of seeking contracts?

A The 5% allowance is meant to cover this kind of cost.

Q Service Company workers will be worse off than ordinary employees under the new rules because they will only be able to claim 5% of their expenses.

A. Not correct. Service companies will be able to claim a flat rate deduction of 5% of the gross fees from relevant engagements. This 5% deduction is not available to normal employees.

Q Will travel expenses be allowed?

A The rules that currently apply to employees of service companies which allow them to claim a deduction for travel from their home to place of work will be the same as they are now.

Q What sort of expenses will be covered by the 5% allowance?

A There is no restriction on the use of the allowance, the 5% deduction will be allowed (in calculating the IR35 payments) in all cases.

Q Will the new rules apply to people working for “composite” or “umbrella companies”?

A Yes.

Q Can I continue to pay my partner a salary for acting as Company Secretary?

A Yes, but the amount will be included in the 5% allowance, no additional relief will be allowed.

Q What will happen if someone fails to follow the new rules?

A The Revenue will seek to collect any unpaid tax or NIC's, and any interest due. Additional penalties may be sought in cases of negligent or fraudulent conduct.

Additional information can be obtained at www.hmrc.gov.uk/ir35