

**Office of Tax Simplification (OTS) – Employment Status Review
Comments from the Low Incomes Tax Reform Group (LITRG)**

1 Executive Summary

- 1.1 We discussed this review with the OTS in a plenary session on 5 December 2014. This paper records some key points from that discussion and contributes additional thoughts.
- 1.2 We believe a key part of the problem concerning employment status for low-income workers is confusion as to the potential different types of status (eg employed, self-employed, worker, casual worker, agency worker) and that the definitions can be different for different purposes (eg tax, employment law and National Minimum Wage regulations). There is much misinformation – for example some prospective ‘employers’ advertise positions on the basis that the successful candidate **will be** self-employed, regardless of the facts of the situation if considering the traditional ‘tests’ of status.
- 1.3 Part of the problem is that many people think they have a choice in their status as against it being determined by actual circumstances. Even if they suspect they should be treated as an employee rather than self-employed, financial need often forces those on low incomes to accept work on any terms they can get.
- 1.4 The rise in ‘false self-employment’ may have been exacerbated by additional burdens on employers such as automatic enrolment into pensions, more regular Pay As You Earn (PAYE) reporting requirements under Real-Time Information (RTI), and the removal of the Percentage Threshold Scheme for statutory pay. The difference between total class 2 and 4 National Insurance contributions (NIC) compared to class 1 primary and secondary NIC is also an obvious ‘attraction’ towards self-employment, as are the differences in rules for claiming deductions as a self-employed person compared to an employee. This may make it all the easier for a prospective employer to ‘sell’ the benefits to the prospective employee of instead setting up as self-employed and working on a ‘freelance’ basis.

- 1.5 We highlight some specific issues for those working in the care sector and those seeking to engage the services of a carer or personal assistant (be it using private means, an Access to Work Grant or direct payments/personal budgets for independent living). These issues may spill over to others providing 'domestic' services, such as gardening or child-minding.
- 1.6 We recommend that the guidance on employment status be reviewed and we highlight an example where current information on GOV.UK may be confusing for those potentially considering status issues (the guidance describing the relationship between 'business' and 'worker', thus excluding those who may be a prospective employer in a personal capacity).
- 1.7 Interactions between tax rules and welfare benefits also need careful consideration, and we make particular points as to a lack of joined-up thought between HM Revenue and Customs (HMRC)/HM Treasury (HMT) and the Department for Work and Pensions (DWP) in some areas – including Universal Credit (UC) and the Access to Work scheme.
- 1.8 We note an increasing trend for older people to bridge the gap between their full-time working lives by doing 'small jobs', perhaps as part-time employees or on a self-employed basis (but with the potential for confusion as to status). We recommend the OTS considers systems in other countries that might address some of these issues, such as France's '*chèque emploi*'.
- 1.9 As always, we are happy to discuss anything raised in this paper in more detail.

2 About Us

- 2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HM Revenue and Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 General comments

- 3.1 LITRG welcomes the OTS review of employment status, as we think there is a clear need for action – even if a change in the law is not achievable in the short term, clarification and clearer demarcation of the existing rules is needed.
- 3.2 Low-income workers are at a particular disadvantage in terms of status confusion. The well-paid ‘consultant’ working at a skilled level is likely to be professionally advised such that they structure their business and contracts in a tax-efficient way, and keep records that support their status. (Though we do appreciate this is an area in which tax advisers might themselves welcome further clarity.)
- 3.3 By contrast, those on low incomes may not know there is even an issue in the first place. They may not be given a choice by those using their services about whether they are employed or self-employed – they may simply be told ‘you are self-employed’ and have to deal with the tax consequences accordingly. LITRG has seen examples of where jobs that are seemingly an employed position are advertised on these terms – ie, stipulating that the successful candidate **will be** self-employed!
- 3.4 This practice has the tendency to give the impression to low-income workers that they have a choice in whether they are self-employed or employed, rather than that in fact it is dictated by the reality of the circumstances of their work and contract terms. Even if the worker suspects they should be treated as an employee, but their ‘employer’ is insisting that they work for them on a ‘self-employed’ basis, many will go along with it and register for self-employment. They are forced to do so on the basis of financial need – essentially, being faced with the decision of not being engaged for work at all or being taken on under the wrong employment status equates to a decision of being able to afford to live and to care for their family or not.
- 3.5 Employment status is also an issue that increasingly crosses the divide between tax and benefits, given the rise in the numbers of low-income self-employed. Indeed there has been a push in recent years to encourage self-employment as a means back into work – for example, for the long-term unemployed, and for people with disabilities. The ability to work more flexibly as a self-employed person than an employee may be particularly attractive to the latter.

4 The rise of false self-employment

- 4.1 LITRG works with other voluntary and community sector organisations. From this involvement and from direct reports from members of the public to our website, we believe there has been an increasing trend towards some employers trying to make people self-employed in order to rid themselves of the responsibilities they have under employment law to their employees (for example, to avoid auto enrolment into pensions and other statutory pay obligations). Some may even make employees ‘redundant’ one day and take them on again the next on a ‘freelance’ basis.

- 4.2 Other driving factors in this trend include avoiding NIC. The difference between the combined levels of classes 2 and 4 NIC for a self-employed person and class 1 primary and secondary contributions for an employee is an obvious 'attraction' towards self-employment if considering the overall net cost of using a person's services.
- 4.3 Other reasons for people to 'prefer' self-employed status need to be examined as part of the OTS's review and whether, given modern working practices (such as the rise of digital technology giving many the ability to work from home), there is justification for maintaining the status quo. Here we are thinking of the different bases for allowing deduction of expenses for the self-employed as against the employed, and the gaps created between 'wholly and exclusively for the purposes of the trade' as against 'wholly, exclusively and necessarily in the performance of duties'.
- 4.4 Take the example of a care worker who is self-employed, working for a number of clients, as against one who is employed by a company supplying care services. Both carers incur mileage costs in travelling between those they care for. In this case, neither is paid in any way for that mileage (ie the self-employed person does not charge a specific mileage rate to their customers and the employee is not reimbursed by their employer for this mileage – a common and unfortunate practice in that industry).
- 4.5 How does the net tax and NIC position of the two compare? The self-employed person would be able to claim a deduction in their profit and loss account for the full cost of the mileage – thus giving them income tax and NIC relief on that expense. The employee would be able (if they were made aware of the possibility) to claim income tax relief alone on the mileage. There is no provision for them to obtain a refund of class 1 NIC for the expense they have incurred out of their net salary.

5 Care and support employers/care workers/personal assistants

- 5.1 Before we get to expenses issues for care workers noted above, there is a fundamental difficulty in how to determine the status of people who work in 'personal assistant' roles and in provision of care, when engaged direct rather than through an agency. There is also an unfortunate lack of understanding of the issues by those administering government funding to those who might engage such an assistant, and consequent lack of advice for claimants of funding¹. See our further comments at section 7.3 below.
- 5.2 There has been a substantial rise in the numbers of people employed in care and support/personal assistant roles and it is expected that this trend will only continue. Indeed,

¹ This is something LITRG has itself attempted to rectify for care and support employers by means of our Disability Tax Guide project (<http://www.disabilitytaxguide.org.uk/>), with the assistance of HMRC Grant in Aid funding.

this number could increase significantly as more people take up health personal budgets which also allow people to use Government funding to employ a personal assistant.

5.3 Difficulties arise in determining status because naturally the lives of a carer and the person for whom they care tend to be more closely intertwined than in other industries where the boundaries between employer/employee or engager/contractor are more clearly demarcated. For example, personal assistants/carers may struggle to fall within some of the traditional 'tests' of self-employment status, such as:

- *Right of substitution* – by virtue of the very personal nature of their relationship with their client, it may not be appropriate for an assistant to be able to send someone else in their stead;
- *Where the work is carried out* – this is very likely to need to be at the client's premises;
- *Provision of own equipment* – this may well not be appropriate or necessary as the client may have all the necessary equipment in their own home for use, as it is likely that much will be in the form of adaptations fitted within in the property – lifts, hoists, etc;
- *Control* – given that care needs are usually very specific and the client will have their own needs and care plan, it is unlikely that the carer will have a great degree of control over how the work is carried out. Indeed, they would be at risk of negligence if a care plan had been agreed and they deviated from it without prior agreement/good reason;
- *Payment/acceptance of risk* – most care work is likely to be carried out at an agreed hourly rate.

5.4 Yet other indicators of self-employment may be present – for example, an ability to decline work on the part of the carer and an ability not to offer work on the part of the person engaging the carer. This might be particularly the case where care is usually provided by family members, and the carer is engaged only in providing additional support at certain times (such as respite care). This may mean there is insufficient mutuality of obligations between the parties to indicate employment – unless they might be considered a 'casual worker'.

5.5 Incidentally, we take this opportunity to note that guidance on GOV.UK may be unhelpful to some in determining employment status – particularly in terms of care and support employers who are engaging an assistant for them personally rather than acting as an employer in the course of business. The page on GOV.UK that describes 'casual or irregular work'¹ consistently refers to a relationship between a *business* and a worker, such that someone engaging an assistant for themselves personally would not necessarily appreciate that the guidance applies equally to them.

¹ See <https://www.gov.uk/employment-status/worker>

- 5.6 We therefore recommend that government guidance on employment status issues be reviewed as part of the OTS review, or that the OTS recommends that guidance is reviewed as part of its report.

6 Interaction of tax employment status with other areas of law

- 6.1 Interactions with other law can cause complexities for employers and individuals alike. As noted above, a common error among employers and employees in the real world (ie outside the world of tax specialists) is to imagine that one can choose whether a contract is one of employment or self-employment, or that the label one attaches to a particular arrangement (employment or self-employment) has no bearing on its actual nature.
- 6.2 In some ways that is understandable because the general law on the distinction between employment and self-employment is so vague – what exactly does mutuality of obligation involve and where does the ‘irreducible minimum’ lie; what degree of control turns a contract from one of self-employment to one of employment; how much weight is to be placed on other factors (eg the presence or absence of a right to send a substitute); and so forth. See for example *Stringfellow Restaurants Ltd v Quashie* [2012] EWCA Civ 1735 (21 December 2012) where a dismissed lapdancer was told by the employment judge that she was self-employed, by the Employment Appeal Tribunal that she was employed, then by the Court of Appeal that she was self-employed¹.
- 6.3 We understand the OTS is engaged with the Department for Business, Innovation and Skills and the DWP on these issues. We would stress that these interactions are key, as simplifying the means of distinguishing employed from self-employed status for tax purposes gets us little further forward unless it will also work for employment law purposes.
- 6.4 There are also the grey areas in between employment and self-employment that need consideration – the position of ‘workers’ for National Minimum Wage law and agency workers, for instance, who sit somewhere in the middle. Confusion is created in itself by virtue of there being three different statuses – employee, worker and self-employed – for employment law, as against the two more distinct categories of employed or self-employed for tax purposes.

¹ <http://www.bailii.org/ew/cases/EWCA/Civ/2012/1735.html>

7 Other cross-departmental issues

7.1 *Universal Credit (UC)*

7.1.1 Even without taking into account that UC has different rules for measuring self-employed income than the tax code¹, the basic definition of what counts as self-employed is different between UC and tax.

7.1.2 The UC Regulations include a concept of ‘gainful self-employment’ as follows:

“Meaning of “gainful self-employment”

64. A claimant is in gainful self-employment for the purposes of regulations 62 and 63 where the Secretary of State has determined that—

- (a) the claimant is carrying on a trade, profession or vocation as their main employment;
- (b) their earnings from that trade, profession or vocation are self-employed earnings; and
- (c) the trade, profession or vocation is organised, developed, regular and carried on in expectation of profit.”²

7.1.3 Thus it would seem that a person might be self-employed and paying income tax and NIC on profits, yet the DWP could determine that they are not *gainfully* self-employed for UC purposes – particularly if the activity is a sideline/supplementary to employed income rather than their ‘main employment’. This is likely to prove a source of confusion for claimants.

7.2 *Tax credits*

7.2.1 A similar issue arises with working tax credit where the test is one of whether the person is self-employed and whether the hours they work are ‘for payment or in expectation of payment’. Furthermore, it was announced in Autumn Statement 2014 that this test will be amended to require the self-employment to also be genuine and effective.

7.2.2 We have seen tax credit cases where the Tax Credit Office have decided that the person is not ‘self-employed’ in the first part of the test, whereas for tax purposes they are. Similarly we see cases where the Tax Credit Office accept there is self-employment but they do not accept that the hours worked are ‘for payment or in expectation of payment’, suggesting instead that the claimant is pursuing a hobby which then brings into question whether they are actually trading and self-employed for tax purposes. This leads to a confusing situation for claimants when one part of a department is defining self-employment in one way and another part of the same department is making a contrary decision.

¹ Even if the self-employed person adopts the ‘cash basis’ for income tax, differences remain with the UC cash basis.

² Regulation 64, Universal Credit Regulations 2013 - <http://www.legislation.gov.uk/ukdsi/2013/9780111531938/regulation/64>

- 7.2.3 These issues are not limited to UC and working tax credit. Similar issues arise with definitions in Tax-Free Childcare and other DWP benefits.

7.3 ***Government funding of support for individuals which creates status issues***

- 7.3.1 A further consideration is that greater understanding of employment status issues needs to be encouraged outside of HMRC – particularly within the DWP, local authorities and the National Health Service (NHS). HMRC need to work with these other areas of government accordingly, to ensure that correct advice is being given to claimants about the status of the workers they engage.

- 7.3.2 For example, we recently instigated a meeting with the DWP regarding Access to Work – the grant system for assisting people with disabilities to get back into (or in some cases, stay in) work. Applications under the scheme can be made by employees, with grants usually then made to their employers to provide them with the extra support they need; or by the self-employed (including those in partnership with others), with grants then made to the business to provide the support.

- 7.3.3 Status issues can be involved here – for example, if the Access to Work funding is used by a self-employed person to engage a support worker. Currently, the scheme provides no guidance to self-employed individuals that they must consider the employment status of the worker they take on; and anecdotally we believe that some claimants of the grant may even have been encouraged to use the funds to take on people to support them on a ‘self-employed’ basis – without considering the factual position at all.

- 7.3.4 Similar comments apply for local authorities and the NHS where direct payments or personal budgets are made available to individuals who might then engage the services of a support worker and therefore need to consider that person’s working status.

8 **Other trends**

8.1 ***Pensioners***

- 8.1.1 What might have been traditionally considered a person’s ‘retirement date’ is becoming a thing of the past, given changes in the law such as the inability to force workers to retire in most cases and ‘pensions flexibility’ to facilitate a more phased approach to continuing working and partly drawing on pension savings.

- 8.1.2 Pensioners are often in part-time work – perhaps staying on part time in their existing job, retiring from their main job and taking on a different position, or even setting up a small ‘business’ activity (gardening jobs, crafts or dog walking being examples we have seen). Others may get involved in local community activities on a voluntary basis, but as we

highlighted in our 2009 report¹, that in itself can throw up 'status' type issues and problems in determining how reimbursed expenses should be treated.

- 8.1.3 Those who do such 'small jobs' in retirement may not be aware of the status issues that can arise, perhaps especially so if they have been employees throughout their main working life. Whilst solutions to employment status problems along the lines of the Construction Industry Scheme (where a deduction is made by those engaging services before making payment to the service provider) might be part of the OTS's considerations in this review, it is hard to see how such a scheme would operate in terms of more person-to-person or minor engagements.
- 8.1.4 An alternative solution in cases of engaging someone to provide domestic services such as cleaning, gardening, dog-walking, child-minding (and indeed personal care, as discussed above) might be something along the lines of France's '*chèque emploi*' system², through which we understand deductions for tax and social contributions are taken care of before the net payment is made to the service provider. We suggest that this, and other international comparisons, would be worth investigating further as part of the OTS's review.

LITRG
5 January 2015

¹ See 'Bureaucracy, expenses and the low-income volunteer'
<http://www.litrg.org.uk/reports/2009/bureaucracy-expenses-and-the-low-income-volunteer>

² See <http://www.cesu.urssaf.fr/cesweb/home.jsp>