IR35 and intermediaries: have we lost the plot?

Peter Vaines bemoans the lack of clarity and uniformity when it comes to decisions around individual's tax bills – particularly when it comes to the infamous off-payroll working rules

The recent decision in HMRC v Barnes [2024] UKUT 262 (the outcome hardly matters) is the latest in the increasingly absurd saga of IR35 and the intermediaries legislation in sections 48 to 61 ITEPA 2003, and the equivalent provisions for NIC in Regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000.

This won't be the last. In fact, this litigation will continue indefinitely until this wasteful and damaging legislation is amended to something workable.

The absurdity and wastefulness comes from the fact that the courts are able to come to opposite conclusions on virtually, if not exactly, the same facts. There are so many decided cases that HMRC can look at the list and see loads of them which support their view and the taxpayer can do exactly the same. Both sides are therefore encouraged to litigate (and to appeal) and we end up with cases like 'Atholl House', where the taxpayer won in the FTT, won again in the Upper Tribunal but then the Court of Appeal remitted the case to the FTT to start all over again. The costs involved exceeded the tax at stake. This means that both sides ended up losing; not for the first time, the only winners were the lawyers. (See also the note below on the decision of the Supreme Court in 'Professional Game Match Officials Ltd v HMRC [2024]UKSC 29', which has just been published.)

The inconsistency is not only a colossal waste of time, but it undermines the authority of the Tribunals to have so many cases that are in direct conflict with each other. It is also frustrating for taxpayers and their advisers who do not know where they are – quite apart from the significant question of costs, not least from the public purse. In any other walk of life, the words "not fit for purpose" would spring to mind, and so would the words "something must be done".

This situation is the result of legislation that seeks to tax people on the basis of a fantasy. A person may enter into a bona fide commercial contract with another person but as far as tax is concerned, this is ignored. The legislation assumes that there is a different contract on different terms with somebody else, and HMRC then charges tax on the basis of this fantasy.

We can all understand that where the contract between the parties is not genuine, being some kind of artifice or sham, HMRC are quite properly entitled to disregard the pretense and charge tax on the real commercial relationship. But the intermediaries legislation does not deal with artifice it deals with real, binding contracts that have been vigorously negotiated by lawyers on both sides and there is no doubt about the true commercial relationship. Never mind about that. The legislation enables HMRC to disregard it and to charge tax on the basis of a contract which does not exist (and which neither party intended nor wants nor would have entered into) but is the result of imagination.

Such are our powers of imagination (which is truly a gift, enhancing our lives in so many fields) that it is no wonder that the courts can come to contradictory conclusions.

HMRC are very keen (and rightly so) to insist that people should be taxed on the basis of the legal consequences of their actions and give short shrift to anybody who says they could have done the transaction in a different way with the same result and would have paid less tax. In Boston Khan v HMRC 2020 UK UT 0168 the Upper Tribunal explained that the taxpayer "is to be taxed in accordance with the transaction that he did enter into and not by reference to the transactions that he was about to enter into (but did not) even if they might have left him in the same economic position".

The enthusiasm for contractual integrity seems to run out when it comes to personal service companies, where HMRC seek to charge tax by reference to a transaction that the taxpayer did not enter into and had no intention of entering into if it would yield more tax. (A moment's thought will reveal the enormous tax revenues which could arise from adopting this approach more widely.)

The position is made worse by the difficulty in determining whether a person is employed or self-employed. These are very different concepts giving rise to very different legal consequences. I need not go

into them – they will be well known to anybody with commercial experience of a business. The problem is that in some circumstances they can appear very similar, and nobody knows where the dividing line is.

It ought to be one of legal analysis. I would suggest that some rigour needs to be applied to the distinction between an employment and self-employment. Unfortunately, the tests for distinguishing an employment from self-employment are subject to such variation that they have lost any real meaning, and everybody can come to their own conclusion which they can claim is right. One could equally well ask: is Vivian Richards or Sachin Tendulkar a better batsman than Donald Bradman? Is Ben Stokes a better all-rounder than Ian Botham? There will be many views – and no right answer. It depends on your view about which tests to apply and what weight you give to them. (And if you don't know anything about cricket, it would be even more difficult.)

In the context of employment and self-employment, let us consider the position of a famous concert pianist who is engaged to play Beethoven's Piano Concerto No3 at the Albert Hall. He turns up and he is paid for the performance – so there is your mutuality of obligation. Do they have control over his services? Of course. He must attend at a specific place on a specific day, at a specific time and will play a specific piece on a specific instrument. Indeed, the control is even more profound. The piece he is being paid to play has certain specific notes and he will be told that he must play every one of them the right number of times and in exactly the right order. And at all times he will be under the express direction of a man with a stick. He is not permitted to send a substitute, nor will he provide his own equipment; the piano will be supplied, and all the supporting people in the orchestra will also be provided, and he will not be permitted to hire his own helpers.

On all the tests we are required to consider from the multiplicity of cases (including those relating to personal services companies), the pianist would undoubtedly be regarded as an employee. However, we know with equal certainty that he is not – and that will be the case whether he was directly engaged or whether he provided his services through his personal service company.

This is not a bizarre or contrived set of circumstances; it is a perfectly normal situation which occurs in various ways all the time. Accordingly, the principles which are said to be relevant ought to provide the answer. But they clearly do not. Nowhere near. They just result in a lot of head scratching.

How do we reconcile this with the various FTT and Upper Tribunal decisions? With difficulty. It must partly be the way the principles are applied – or more likely, there are many more factors that ought to be taken into consideration before the right answer can be found. Or maybe HMRC's paranoia about people being self-employed is distorting everything and we ought to return to some proper principles.

Whatever the reason, clearly something has gone wrong. IR35 has grown into a monster which is out of control and gobbling up resources – and interfering with the capacity for reason. It is time for a sensible analysis of the distinction between employment and self-employment and an appreciation of the genuine differences which exist between them – and for the tax rules to be applied in an appropriate way. Without reform, the litigation will simply continue unchecked, to everybody's (well, nearly everybody's) detriment.

Postscript: Supreme Court decision

On 17 September 2024 the Supreme Court released their judgment in the case of 'Professional Game Match Officials Ltd v HMRC [2024]UKSC 29', which related to part-time football referees. This is not an IR35 case because there was no intermediary company, but it is crucial to the intermediaries legislation which always depends on whether or not the hypothetical relationship would represent a contract of employment.

HMRC claimed that the part-time referees were employees. PGMOL said they were not employees by reference to all the conventional tests – mutuality of obligation, control, etc.. The FTT agreed with PGMOL; the Upper Tribunal also agreed; the Court of Appeal did not disagree but were not happy about the manner in which the tests had been applied to the facts and remitted the case to the FTT for reconsideration.

The Supreme Court have now decided that this was the right thing to do – so back it now goes to the beginning for consideration by the FTT, but with some important legal guidance from the Supreme Court on the meaning of mutuality of obligation and control.

(Actually we can forget mutuality of obligation; that only relates to whether a contract exists, and gives no indication of the nature of the engagement. So we are left with control. But we know from 'Ready Mixed Concrete' that "control is not everything" – but – maybe that is an argument for another day).

We seem to be a long way from a conclusion here. Whatever the FTT decide next, the matter seems destined to end up for a second time in the Supreme Court on the substantive issue – after many more years. I will probably read about it in my care home.

• Peter Vaines of Field Court Tax Chambers advises on all areas of personal and corporate taxation. Email pv@fieldtax.com or call 0203 693 3700