

CHANGE IS GOOD

WHY **IR35** PRESENTS OPPORTUNITIES FOR
BUSINESS AND CONTRACTORS



A Sullivan & Stanley Report

INTRODUCTION

The trouble with taxation changes is that many businesses and consumers see them as negative.

This has certainly been the case with reform of IR35. The Government's decision to extend the policy to the private sector from April 2020 has caused unease for contractors and the organisations that employ them.

There's confusion over how to correctly determine employment status for contractors; the cost of making changes; fear of getting it wrong and being hit with fines; a lack of clarity over which department should be responsible; and losing great people from the team.

Much of the commentary from media, business owners and the freelance workforce has focused on these issues. But at Sullivan & Stanley, we think IR35 can be hugely positive for commerce and contractors. We don't believe it's HMRC's intention to shut down an appropriate route to strategic support, which is also a blossoming part of the economy.

Instead, we see great opportunity. From revolutionising operating models that future-proof firms, to giving freelance experts the recognition they deserve, business can change for the better.

We're already talking to organisations, across multiple sectors, that understand the value of our transformation model that draws on some of the brightest minds in the business. Understanding the changes is only the starting point. Implementing and managing new processes to deal with the updated legislation will be critical to the future of many organisations.

We wanted to look in depth at how the wider business community feels about IR35. So we surveyed 500 UK business decision-makers across multiple sectors working in the private sector, in medium and large companies.

This report sets out the compelling results of our research - and proves once and for all that the extension of IR35 is to be cheered as much as feared. If you embrace IR35 and adopt the right approach to implement it, then your business can benefit now and in turn be fit for the future.



IR35

06/04/20

THE CHANGES

APRIL 6, 2000

The tax law that became known as IR35 entered the statute books. It was introduced to counteract the avoidance of employed levels of tax and national insurance by individuals providing their services through intermediaries (Personal Services Companies or PSCs - limited companies). In short, it was intended to stop contractors reaping the same benefits as a permanent employee but also enjoying the tax and National Insurance saving opportunities that came with being a limited company.

APRIL 6, 2020

Exactly 20 years later, medium and large companies will become responsible for determining the tax status of contractors to the private sector - finally closing loopholes that remained.

In the public sector, the burden of determining employment status shifted from contractor to organisation - and became mandatory - in April 2017. The private sector is now following suit.

It's true there have been some teething issues in the public sector. But those obstacles serve as learnings for extension across the private sector.

There's trouble in store for organisations that continue to flout the legislation. HMRC will have the power to claim missing taxation and in some cases, fine those caught doing wrong.

Most taxation law comes with grey areas, and IR35 is no different. That means businesses stand at risk of wrongly determining employment status. They could receive significant claims of incorrect tax and National Insurance submissions - leaving them open to punishment.

Before we look at some great ways to mitigate the risks - and realise the benefits - of IR35, let's examine what business leaders told us about how it will affect their organisation.

Are they prepared, will they make changes and who's overseeing the process?





KEY INSIGHTS

To understand businesses view on the updated IR35 legislation, we polled 500 business decision makers at private-sector companies deemed medium to large.

We asked a range of questions, from current concerns to potential cost and perceived benefits. Here's what they told us and what it reveals about their perceptions of the barriers and benefits of IR35.

INSIGHT 1

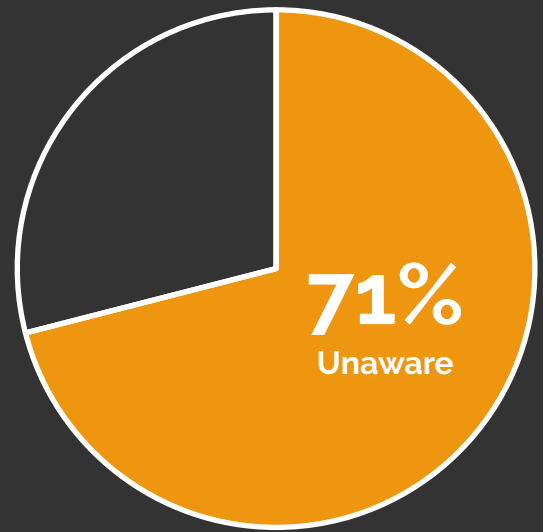
GET THE DATE IN THE DIARY

A surprising 71% of respondents were unaware that the IR35 changes come into effect on April 6, 2020.

Although those at firms with 250 to 300 employees were the most certain (31%) this still points to a worrying lack of knowledge.

Is HMRC's message being communicated clearly enough? More than half (54%) also told us they haven't received enough information, while 52% claimed it is contradictory or confusing.

Regardless, almost three quarters of respondents run the risk of not being ready on time - and that's a concern. Ensuring you have the right advice and support in place to make changes is vital.



71% were unaware of the date that the changes come into effect

INSIGHT 2

IS YOUR PLAN ROBUST ENOUGH?



38% said they'll have a robust strategy

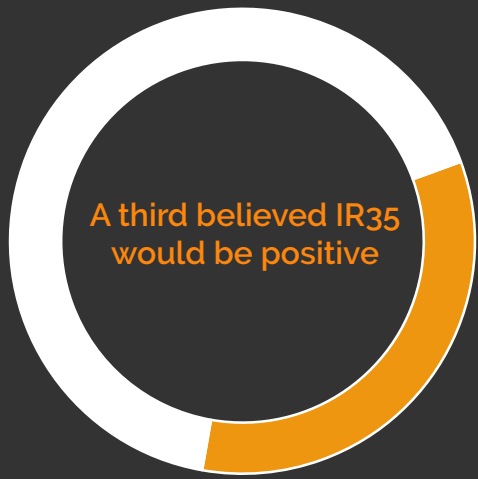
Less than four in ten firms (38%) said they'll have a robust strategy in place by the time IR35 changes kick in.

Larger firms we surveyed were the most confident in their planning: 47% of respondents at companies with more than 500 employees, and 52% at those with turnovers of £500.2m or more, believed they'll be ready.

Meanwhile, a fifth stated they expected to be ready up to three months after April 6; 32% said four to six months after the change date; and nearly one in 10 (9%) think it will take them seven to 11 months beyond April to be up to speed.

This is curious. To use an analogy, most drivers who are warned in advance of a change in the speed limit will adjust before they reach the point where the new limit starts. Why should IR35 be any different?

Even the most confident firms shouldn't rest on their laurels. IR35 is so complex, it's easy to focus on a specific aspect; often this is the financial element. So you may have a plan in place - but it might not be the best one.



IT'S NOT JUST ABOUT THE MONEY

Encouragingly, a third of respondents believed IR35 would be positive for their organisation, compared to 11% negative (41% said "no difference").

Companies with a turnover between £100.2m and £500.1m had the most positive respondents (47%). The important thing to note is that many respondents expected change. But what how will this be manifested?

As noted above, it's important not to conclude that the only benefits will be immediate financial ones. Of course, cost could be removed overnight, especially at firms with a big roll call of contractors.

But surely it's better to understand what those contractors were doing in the first place for example the value they were delivering, how they might be retained or their skills replaced. As we'll see, opportunities stretch far beyond cost cutting.

INSIGHT 4

FIRMS NEED TO TAKE A STEP BACK

One in 10 respondents weren't aware of the potential financial impact of IR35 on their business. A further 48% were unaware, though they are investigating.

Six months before the changes, more than half haven't quantified the cost - whether that's compensating contractors for the losses they face by paying them higher rates, or increasing headcount by taking on more full-time employees.

It's an alarming figure. At this stage, many organisations will be wrapping up financial planning for the new tax year. That means a swathe of medium to larger businesses are unlikely to have allowed contingencies for the extra costs related to IR35.

We've even heard of companies cutting employees to pay for contractors. Firms can be faced with difficult decisions simply because it seems easier to react quickly than take a step back and review their existing operating model. And those knee-jerk actions could cause long-term damage to your organisation if not considered with due care and attention.



One in 10 were unaware of the financial impact

INSIGHT 5

DID YOUR CONTRACTORS WRITE THE CODE?



One in six aren't considering changing their commercial model

One in six of the respondents' companies aren't considering changing their commercial model to accommodate change. A further third said they have already implemented changes to contractor arrangements.

If companies are content to pass the cost on to contractors in one fell swoop it could quickly cause problems. Contractors have their own financial requirements and may well turn away to roles that don't bring them inside IR35, or pay better - or both.

The knock-on effects could be huge. In sectors where many organisations have rushed to employ an army of contractors - finance or IT, for example - much of the strategic knowledge needed to keep a firm's wheels turning sits with those individuals. In many cases, employees would no longer have strong enough skills to take over.

It's far better to socialise with your contractors to talk through IR35 and confront the issues early.

INSIGHT 6

TIME TO AUGMENT EMPLOYMENT STRATEGY

33%

would consider converting contractors into employees

33% of respondents said their business would consider converting contractors into full-time employees.

That's fine, but it's vital to review the roles they've been fulfilling and what you'll truly need them to do in the future. Is it really worth bringing them inside IR35? How are you measuring the outcomes of your decisions, now and going forward?

Lots of high-profile projects have run over on time and budget because the right management mechanism wasn't in place to deliver the correct outcome. There might be - and usually is - a better way.

All of this means it's time to take a hard look at your operating model, and the opportunities IR35 brings to change it.

THE OPPORTUNITY

The good news is that opportunity around the IR35 changes comes in multiple guises. Respondents told us their key wishes:

47%

Hoped it would bring an opportunity to review and improve systems and clarity around the workforce composition

46%

Desired a clearer working relationship with contractors

41%

Wanted to future-proof their organisation's business model

FOR BUSINESS

TAKE A STEP BACK

In the cut and thrust of everyday business operations, it's easy to lose sight of why your workforce is shaped as it is. IR35 is the best excuse available to stop and take stock of your current situation.

Many organisations settled into a cycle of hiring contractors simply because checks and balances weren't in place to stop the expenditure; it's cultural, with scant requirement for executive sign-off. Firms can also be guilty of failing to properly monitor and measure the performance and effect of their contractors.

Almost a third of our respondents (32%) admitted they were unlikely to rethink contractor arrangements because of IR35. But it's time to draw a line in the sand. Take each contractor in turn, consider whether their role should be brought in-house, and ensure all have determination statements if you believe keeping them on as external consultants is still the best approach.

CHANGE YOUR MODEL

Now is the time to reshape your operating model so your business has the right resources in place to be fit for the future. Many firms still operate a "command and control" model that is no longer relevant for today's economy. More than half (54%) of our respondents are committed to changing their commercial model due to IR35.

Smart organisations will calmly close the loophole that has allowed firms to boost headcount and fill in the gaps in their skillset by bringing someone in through the back door.

In reviewing your existing employment strategy, you'll be able to identify many areas that can be improved. These include: determining exactly what experts and skills you need to drive your business forward; cutting back on overlapping roles; a blended approach to having people available as support, but only using and paying them when they're needed; and, of course, bringing inside IR35 anyone who should be treated as such, to ensure your company remains compliant.

Implementing a new model won't be easy. But if you get it right the first time - and bring along everyone from the board to team managers and the wider business - you should only need to do it once.

REMEMBER YOUR CUSTOMER

IR35 is a business issue, but we're all consumers.

Keep your customer in mind at all times when reviewing and developing your operating model. Consider: is there a direct line of sight from the skills at your organisation to the impact on the customer? How are you going to align those skills to improve the customer experience? Is your team agile enough to respond to rapid changes in consumer demand?

It's a fact that better customer experience leads to longer, more loyal relationships. This, in turn, increases revenue and profit over time. So taking an inside-out approach to building a team that will delight the customer is a win-win for everyone.

IR35 makes many firms uncomfortable because it's forcing them to focus on areas no one has wanted to deal with. It's also frequently unclear who should be in charge of hiring and managing contractors.

Often this has been left to line managers. Problems can arise because it's too easy to hire contractors and their value isn't always measured, or their tenure set in stone.

Even if your firm is determined to change, who should take charge of the process? We believe this is an issue that goes beyond traditional recruitment and management consultancies. It requires a cross-functional combination of procurement, HR, finance and possibly others. Our research backs this up: perceived responsibility was split between management (49%), HR (45%), finance (32%) and others.

Each of these teams will likely have their own focus and - with the best will in the world - gaps in knowledge around IR35. That's why it's important to consider external support from experts who know the facts, can bring people together, co-creating an operating model that quickly drives through transformation at lower cost and with a better outcome. Some 53% of our respondents said they already intend to seek expert help.

FOR CONTRACTORS

Largely due to media coverage and conflicting advice, many contractors are fearful about the changes to IR35 and what it means for their livelihoods. But managed correctly, there are clear benefits:

- The best aspects of the gig economy are highlighted - firms get to work with experts who are still allowed to share their vast skills and experience on multiple projects, driving the right outcomes for the company and the wider UK economy
- The chance to be measured against deliverable outcomes - rather than just having a timesheet signed off (if at all), increasing personal satisfaction and respect from the organisation and industry at large
- The ability to earn more - this may spell the end of the day rate, as companies agree to a specific budget for a project. That also means a defined timeline, which could help contractors complete it and move on to new work more quickly

WHO ARE S&S AND HOW CAN WE HELP?

OUR MODEL

We recognise that the dynamics of business have changed and the days of the long-term, large-scale transformation programmes are no longer working. The wide use of technology has reduced the barriers to entry and as a consequence, industries are being disrupted by competition they didn't see coming.

This is where Sullivan & Stanley come in. With access to our network, known as The Change Society, we help businesses solve the most complex challenges they face.

The Change Society is Sullivan & Stanley's global movement of individuals who are the top 5% of business experts, fully vetted as the best professionals in their fields. They have vast experience on the frontline of business transformation, and the battle scars to prove it.

We co-create with organisations to help tackle any business requirement, from tech and growth, to strategy and architecture, our experts deliver sustainable change.

Ultimately, we will deliver a new outcome: the future proofing companies need, and experts the opportunity to continue working in a way that suits them.

HELPING YOU MANAGE IR35

We believe IR35 is an opportunity to close the capability gap that hinders business transformation.

Our experts are available on-demand. We won't come in, develop a strategy in the background, give you a PowerPoint presentation then leave.

Nor will we outstay our welcome or blow your budget. We're with you for as long as you need us, rather than seeing a "land and expand" approach from the outset.

We'll work with you to ensure everyone in your organisation understands the issues associated with IR35; implement correct and sustainable processes to manage them; and realise the broader benefits of transforming your business in response.

HOW IT WORKS

As a hybrid-service organisation, we help firms get to the root of their complex business problems by breaking it down into manageable chunks. We then build the best teams around the problem, to deliver a successful outcome. We achieve this in 90-day cycles:

Day 1 - an immersive session with a small group of our experts to identify the root problem(s)

Day 15 - on-site discovery activity to develop a solution

Day 90 - a team of our experts work collaboratively with your team to deliver tangible business value

By working in 90-day cycles, it gives you the flexibility to check you're on the right path, the speed to keep up with the business world and the freedom of not being pinned down by a fixed, long-term strategic plan.

Sullivan & Stanley also operates this model for our own business, transforming every 90 days.

IN SUMMARY

Time is running out to make crucial changes necessary to meet the challenges of IR35 - but it's not too late to be ready on time, or be fit for the future.

In making change, it's important to take a long-term view. Take a step back, call on the help of external experts, and grab the chance to inspect and disrupt your operational model.

Clearly, the private sector can't simply flick a switch and expect everything to be done and dusted by April 6, 2020. It will be an evolution, one that mirrors the constant change business faces. But if your firm hasn't started or finalised its plans, now is the time to reconsider whether you're taking the best approach.

Contrary to what you might have been told, we believe IR35 really can usher in the best of times, not the worst of times, for your organisation.





THE CHANGE SOCIETY

To speak with an S&S expert on IR35, email us at
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www.sullivanstanley.com