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Big Bad Wolff Ltd v HMRC

The Upper Tribunal has handed down its decision in a case concerning the interaction of IR35 and the Social Security (Categorisation of Earners) Regulations 1978 ('Categorisation Regulations').

Big Bad Wolff Ltd ('BBW') was a personal service company ('PSC') owned and operated by Mr Robert Glenister and his wife. Payments made in respect of Mr Glenister's acting services were made to BBW, until it ceased to provide Mr Glenister's services in 2013. During the period when BBW provided Mr Glenister's services, it made payments to Mr Glenister, which were subject to both income tax and to National Insurance Contributions ('NICs').

In 1999, the government introduced a package of legislation known as IR35, with the purpose of preventing the use of PSCs to avoid the payment of income tax and NICs by workers who, but for their use of a PSC, would be regarded as employees of the person engaging them. In essence, the legislation posits a hypothetical question: but for the presence of the PSC, would the worker be regarded as employed by the person engaging them? For both income tax and NICs purposes, the answer to this hypothetical question is usually arrived at by the application of the common law test for employment status. If the answer to the hypothetical question is 'yes', the PSC is liable to account for income tax, and for both the employee's and the employer's Class 1 NICs on payments made to the company - as if the payments to the company were a payment of employment income. Significantly, this makes the PSC liable to account for NICs which, had the worker been engaged directly, would normally have been the liability of the employer/producer. In the case of BBW, about 75% of the sums assessed consisted of what would have been the employer's NICs – the liability for which would not have fallen on Mr Glenister, had he contracted directly with producers.

As regards the facts of the case, it was common ground that had Mr Glenister provided his services to producers directly, he would have been regarded as self-employed. But this was not enough to resolve the appeal: the NICs limb of IR35 - contained in the Social Security Contributions (Intermediaries) Regulations 2000 ('Intermediaries Regulations') - asks whether, for the purposes of Parts I to V of the Social Security Contributions and Benefits Act 1992 ('SSCBA'), the worker would be regarded as in 'employed earner's employment.' HMRC decided that IR35 applied to Mr Glenister's use of BBW in respect of NICs (but not income tax), because – by virtue of the deeming effect of the Categorisation Regulations – Mr Glenister 'would be regarded' as in employed earner's employment, i.e. for NICs purposes.

So an issue in the appeal, was whether the deeming effect of the Categorisation Regulations could be read into the counter-factual posited by the Intermediaries Regulations.

The Categorisation Regulations perform a number of functions, including to deem certain persons - who would not ordinarily be regarded as such - to be in employed earner's employment for the purposes of the SSCBA. By this mechanism, certain vulnerable classes of workers were made liable to Class 1 NICs as if they were employees, thereby allowing them access to contributory benefits such as jobseekers' allowance, which is not normally available to the self-employed.

Between 1998 and 2014, the Categorisation Regulations made provision for certain 'entertainers' (e.g. certain actors) to be treated as being in 'employed earners employment' for NICs purposes. Provision was made for 'entertainers' in order to provide protection to them – given that the vast majority of them were not well remunerated and regularly experienced periods between engagements where they had no paying work. The Categorisation Regulations also provided that where an actor was deemed to be in employed earner's employment, it was the producer who was liable to pay employer's NICs. Certain entertainers were excluded from the scope of the rules. Between 1998 (when the rules were first introduced) and 2003 (when they were amended), the 'protection' afforded by the Categorisation Regulations extended only to entertainers who were paid "*wholly or mainly by way of salary*." Since this definition did not achieve its purpose, the definition of "salary" was amended in 2003 to encompass persons who received *any* payment by way of salary.

The Court of Appeal, in *ITV Services v HMRC* [2014] STC 325 found the construction of the (since 2003) defined term "salary" to be a difficult issue, but ultimately adopted a wide construction. This construction has the result of bringing most "entertainers" within the scope of NICs. However, as the working practices of the entertainment industry changed post-2003, it became clear to HMRC that the Categorisation Regulations as then drafted neither achieved their policy objective of providing benefit protection for entertainers, nor dealt effectively with the changes which had occurred since 2003

as regards the ways in which entertainers were engaged and paid. The provisions relating to entertainers were repealed with effect from 6th April 2014. But for individuals engaged prior to 2014 – and applying the meaning of "salary" as found by the Court of Appeal in the ITV Services case - the Categorisation Regulations continued to have a wide scope.

As regards the present appeal, HMRC decided that most of BBW's contracts in respect of Mr Glenister's services were within IR35, because the deeming effect of the Categorisation Regulations could be read into the hypothetical question posed by the Intermediaries Regulations. BBW appealed HMRC's decision on the basis that where the Intermediaries Regulations asked whether a worker "*would be regarded for the purposes of Parts I to V*" of the SSCBA as in employed earner's employment, this question was not to be answered by reference to the deeming provisions contained in the Categorisation Regulations, but - in order to ensure that the package of measures introduced at the same time operated in harmony with the income tax provisions - (broadly) by applying the common law test for employment status.

BBW pointed to certain statutory anomalies in support of its appeal. For instance, s.139 of the Corporation Tax Act 2009 ("CTA 2009") allowed for the PSC to take a deduction in calculating the profits of its trade in respect of the payment which IR35 deemed to be employment income and NICs paid in respect of it, only if the income tax limb of IR35 applied.

BBW argued that this (and other matters) indicated that the package of measures known as IR35 was only ever intended to apply to 'hidden employment'; that this approach to the construction of the provisions was supported *inter alia* by the Explanatory Notes to the enabling provisions, and to the Intermediaries Regulations themselves.

BBW's arguments were rejected by the Upper Tribunal. The Upper Tribunal found that the language of Regulation 6(1)(c) of the Intermediaries Regulations was clear and could not be overridden by other statutory and non-statutory indications.

The outcome of this decision - an informal test case for a number of other appeals - is that where a worker uses a PSC, and would be regarded as self-employed in the absence of that PSC, they will nevertheless be caught by IR35 if the Categorisation Regulations would deem them to be in employed earner's employment. This has the result that the PSC is then liable to pay employer's NICs. This can be contrasted with a scenario where only the Categorisation Regulations, apply, in which case the liability for employer's NICs lies with the producer. At the hearing of the appeal, HMRC confirmed that where IR35 applied only in respect of NICs, then the PSC would be allowed a tax deduction for any NICs paid by the PSC on general principles, even though this was not expressly provided for under s.139 CTA 2009.

The government is currently consulting on reforming IR35 as it applies to the private sector. Its stated intention is to extend the rules which apply to the public sector to private sector engagers which are not small companies. In essence, the changes would require the engager to determine whether IR35 applies to any engagement involving an intermediary PSC, and then to make appropriate deductions from the payments to the PSC for tax and NICs. Under the current proposals (as with the 'public sector' IR35), the party paying the fee to the PSC would be liable to pay the employer's NICs.

The decision of the Upper Tribunal can be found here.

Akash Nawbatt QC represented HMRC.

Marika Lemos and Colm Kelly represented Big Bad Wolff Ltd.

Members of Devereux have appeared in most of the recent IR35 and many of the employment and worker status cases that have been litigated in both the employment and tax tribunals and have extensive experience of advising on IR35 and employment status issues for both tax and employment law purposes.

For more information on Akash, Marika and Colm's latest case highlights, or Devereux's leading tax team, please contact our practice managers on 020 7353 7534 or email clerks@devchambers.co.uk.

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