



OSK Submission

**Public Consultation on the
Use of Intermediary-type Structures and Self-employment Arrangements**

Department of Finance and Department of Social Protection

Consultation Paper, January 2016

Contents

- 1. OSK..... 2
 - 1.1 Who are OSK..... 2
 - 1.2 Providing Services to Contractors 2
 - 1.3 Our Submission..... 2

- 2. Summary of OSK submission on the options at section 8 3

- 3. OSK Submission..... 4
 - 3.1 Section 8: Options (i) and (ii) 4
 - 3.2 Section 8: Options (iii) and (iv)..... 5

- 4. Benefit to the Exchequer and the Economy: Growing Trend in Contracting 5

- 5. Perceived Loss to the Exchequer..... 6

- 6. Feedback from our Contractor client base 7

- 7. Conclusion..... 8



1. OSK

1.1 Who are OSK

OSK have been providing quality and professional business advice to Irish businesses since 1985. Based in Dublin, we specialise in progressive owner managed businesses and our clients include SMEs, multi-national groups; government bodies, sole traders and contractors.

We deliver excellent quality taxation and accounting services through understanding our clients and their needs. Our services include taxation, audit and accounting, accounting for contractors, company secretarial, small business support, company set-up, taxation, payroll, bookkeeping and management accounting.

1.2 Providing Services to Contractors

With almost 20 years' experience advising contractors in the contracting market in Ireland, OSK understand and has advised on perhaps all issues relevant to contractors.

1.3 Our Submission

Given our experience in advising contractors, OSK is well placed to respond on the consultation paper on the use of Intermediary-type Structures and Self-employment Arrangements. Our submission addresses the options at section 8.

2. Summary of OSK submission on the options at section 8

1. Contractors are not employees of the end user and should not be taxed as such.
2. There is no obligation on the end-user to offer work and there is no obligation on the contractor to accept work, thus there is no contract of service.
3. Providing flexibility to employees is essential to attract inward investment and job creation.
4. To treat a contractor as an employee of the end-user may have a detrimental impact on all the industry sectors that use contractors. Thus, there would be a negative impact on the economy.
5. Legislation is already in place under S.440/S.441 TCA 1997 to apply a surcharge to undistributed income of professional service companies.
6. Contractors generally do not build up reserves. The combined Corporation Tax, Professional Services Surcharge and Capital Gains Tax would more or less equal or in some cases exceed the taxes due under the PAYE system.
7. The perceived loss to the Exchequer needs to be quantified: -
 - (a) Contractors are generally paid more than full time employees and they pay proportionally more taxes and almost always at the higher rates of income tax and universal social charge.
 - (b) The Department of Social Welfare does not pay benefits to contractors.

3. OSK Submission

The stated purpose of the consultation paper is to invite submissions on possible measures to address the loss to the Exchequer that may arise under arrangements (i) where an individual who would otherwise be an employee, establishes a company to provide his or her services and (ii) where an individual, who is dependent on, and under the control of, a single employer in the same manner as an employee, is classified as self-employed. Submissions are invited, in particular, on the options at section 8.

3.1 Section 8: Options (i) and (ii)

The first two suggested options for addressing the perceived loss to the Exchequer involve charging income tax under Schedule E and paying Class A social security. Taxing payments under Schedule E and paying Class A social security only apply where an employer/employee relationship exists. So the net issue to be addressed is whether or not the individuals in question are employed or self-employed, i.e. are they working under a contract *of* service or a contract *for* service. A contract *of* service implies a contract of employment whereas a contract *for* services implies the service provider is self-employed. The terms “employed” and “self-employed” are not defined in the taxes acts but we can turn for guidance to case law^{1, 2}; the Revenue Code of Practice for Determining Employment or Self-Employment Status of Individuals³ and the Report of the Employment Status Group⁴ for guidance. The many factors and criteria to be taken into account are outlined in the documents mentioned and are not repeated in this submission. It is not just a matter of calculating the sum total of the factors but it is the overall effect that is important. The decision as to which category an individual belongs must be arrived at by looking at what the individual actually does, the way he or she does it and the terms and conditions under which he or she is engaged.⁵ Where the evidence balances evenly then the question can be decided by the intention of the parties. Once the job as a whole is looked at, including the working conditions and the reality of the relationship, and a conclusion is reached then the correct tax treatment will be applied. It is not fair or realistic to deem all contractors to be employees of the end user and charge tax under schedule E and charge Class A social security.

¹ Henry Denny & Sons (Ireland) Ltdj v. Minister for Social Welfare [1997] IESC 9; [1998] 1 IR 34 (1st December, 1997)

² Sean Tierney v An Post HC

³ www.revenue.ie/en/practitioner/codes-practice.html

⁴ www.revenue.ie/en/practitioner/tech-guide/ppfrep.pdf

⁵ Report of the Employment Status Group

Contracting does not suit everybody. Many contractors cease contracting and seek permanent work because they prefer the security and associated benefits of full time employment. When they return to full time work they express the view that the relationship is completely different as a full time employee. They become part of the team, they receive the associated benefits available to other employees, they receive training and may be considered for promotion, they are part of the organisation– these opportunities are not available to contractors. Contractors play a very different role and they are not employees.

3.2 Section 8: Options (iii) and (iv)

There is already legislation in place under s. 440/s441 TCA 97 to apply a surcharge to undistributed income of service companies. In OSK's experience of preparing accounts for contractors, any undrawn earnings are always treated as additional remuneration and payroll taxes applied. Contractors do not generally build up reserves in their companies because it is not tax effective to do so. When you take account of the corporation tax rates, the surcharge under s. 440/441 TCA 1997 and the capital gains tax that would be due on any capital distribution(s) the combined tax burden would more or less equal, or in some cases exceed, the combined income tax, social security and universal social charge due under the pay as you earn system (PAYE). Allowing for the extra compliance costs of extracting reserves from the company, it very seldom, if ever, makes sense for a contractor to leave reserves in the company. All earnings not drawn in the accounting period are accrued as director's remuneration and taxed under the PAYE system. In our opinion, there is no need for any adjustments or changes to the legislation to allow for the suggested options iii and iv as appropriate legislation is already in place.

4. Benefit to the Exchequer and the Economy: Growing Trend in Contracting

Providing flexibility to employers is essential to attract inward investment and job creation. There is a growing trend in particular sectors such as construction, engineering, semiconductor and facilities management where contracting, as opposed to permanent roles, is becoming the default for new roles that are introduced to the market. This approach has many benefits for companies, including allowing them to operate in industries that are becoming more project driven. Many of these industries have adopted lower cost structures to compete for global projects and the nature of this type of operation calls for cyclical headcount models.

A contractor based workforce allows the freedom to provide project work on a short term basis and only for the duration of the project, this allows companies to be much more flexible in reacting to market conditions and changing business challenges; it allows companies to “hire and fire” according to their needs in a much more flexible way than if they had only full time employees that they may not have work for when the project comes to an end. There is no obligation on the end-user to offer work and there is no obligation on the contractor to accept work, thus there is no contract *of service*.

The growing trend in contracting and the expansion of the contracting market would be stifled if contractors were to be treated as employees which would not embrace entrepreneurship. Any aspirations a contractor might have to grow and develop a consulting firm with more than one person would no longer be available. Many large consulting firms grew out of more modest beginnings – beginning with one or perhaps two professionals who had the foresight and vision to develop and expand their business to provide different services and to provide project teams on an outsource basis. The government needs to develop policies to assist the development of small consulting firms and incentivise the entrepreneurial talent in our country to remain strong and competitive in a global marketplace.

Because contractors desire the flexibility of working on a contract basis and the opportunities this provides, quite a few of them would be more than interested in moving abroad to seek consulting work and this would have a negative impact on the IT sector in Ireland.

5. Perceived Loss to the Exchequer

The perceived loss to the exchequer needs to be quantified. The majority of contractors operate through their own limited company and payroll taxed are paid under the PAYE system. Many issues around payment of expenses have already been addressed by the Revenue as part of the national contractor’s project. Contractors operating through their own companies or via an umbrella company are paying payroll taxes under Schedule E. Because contractors are generally paid more than full time employees it could be argued that the Exchequer is gaining in extra taxes due to this higher rates of pay. Other factors to be taken into account include the fact that the Department of Social Welfare does not pay benefits to contractors who are between work so there is a saving to the Exchequer. In addition, many contractors working in Ireland are “exporting” their knowledge from Ireland to their clients abroad. This occurs when an IT professional is providing IT services to companies that are not based in Ireland.

They are bringing substantial earnings into Ireland that would otherwise not be taxed and spent here. Those overseas clients, some of which are based in EMEA and USA may well decide to source that knowledge elsewhere if they are to become subject to taxes here in Ireland. In addition, the contractors, who have a very flexible approach, may decide to move abroad – if they find themselves between contracts they tend to follow the work and move abroad if necessary, as opposed to staying in Ireland and seeking to claim social welfare benefits.

6. Feedback from our Contractor client base

In preparing this submission, OSK sought and obtained feedback from our contractor client base. The overriding views expressed by those contractors who responded is that they are self-employed. Although, of course, they generally all work through their own limited companies so they are employees of their own companies and pay taxes under Schedule E. The views expressed by the contractors were as follows:

1. Contractors work on a contract basis for the following reasons:
 - a. More freedom in terms of the work that they do.
 - b. Flexibility in working arrangements.
 - c. They have the opportunity to make a profit; the rate of pay is generally considerably higher that it would be if they were employees.
 - d. Many contractors have worked in multiple industries, in multiple countries and for multiple employers. They have a wealth and breadth of experience that many employees would not have. They are truly independent.
2. They take their own professional indemnity insurance, at considerable expense themselves.
3. They provide their own equipment, computers.
4. They provide their own office and internet connections.
5. Contractors pay for their own training.
6. Holidays and sick leave are at their own expense.
7. The work is project related and there is no obligation on the end-user to provide work once the project is completed.
8. They take on the risk, and insecurity, of working on short term contracts that may not be renewed. Contractors have a much higher risk of being let go by the client than employees do. Taking a new contact is a risk because the client can change their mind at any time. Employees are somewhat insulated from economic and technological change, contractors are not and have to compete in a global and ever-changing market.

9. Contractors are subject to “technological change” to a much greater degree than permanent staff because no one will hire them as a contractor in an area where they are not demonstrably expert.
10. They provide the same management consulting service as large consulting firms. Just because there is only one person in their business should not result in different tax treatment from larger consulting firms.
11. In times of recession or if there is a break between contracts there is no financial support available from the Department of Social Welfare. Contractors do not get any benefit from the State when they are between contracts.
12. Contractors do not have a lead in time, they have to hit the ground running. They are consulted for their specialist knowledge and expertise and they have to be productive from their first day. While they do have to follow client standards and practices, they are able to design new ways of solving problems, do the work on their own, follow their own standards and they are expected to bring all their knowledge and experience to bear; they are also expected to pass their knowledge on to their client and be a neutral arbiter in recommending possible solutions.
13. If contractors are to be taxed the same as employees, then they should get all the benefits that they would get working as a permanent employee in the same organisation.

7. Conclusion

In conclusion, legislation and codes of practice should apply equally to all business. It is neither fair nor reasonable to treat contractors any differently to other individuals and consulting firms. All the contractors that I have spoken with genuinely regard themselves as self-employed and they do not share the benefits of permanent work. The perceived loss to the exchequer needs to be quantified to establish if there really is a loss. Contractors are on substantially higher rates of pay so they pay more taxes proportionally. In the majority of cases the uplift in pay can be as much as 30 – 35% so the increased income tax, social security and universal social charge paid on the increased pay is substantially more than the perceived loss to the Exchequer in Class A Social Insurance. Once the uplift in pay is approximately 20%, the increased taxes paid by the contractor will cover the perceived loss of employer’s social security. The contract market in IT and Engineering and in the Pharma sector is an integral part of our economy and any move to tax those working in this sector in ways that are out of line with other businesses generally may be detrimental.