



A GUIDE TO CONTRACTOR SOLUTIONS IN THE UK

This guide provides information to those heading to the UK and considering contracting. It provides a background to the options available to contractors to co-ordinate their tax and administration responsibilities, as well as answers to some frequently asked questions.



Like the majority of Antipodeans who head to the UK, you will probably end up contracting. Contracting has its advantages, the best being the ability to reduce your tax which can be as high as 53.8% for permanent employees. To do this most contractors use contractor solution providers, like everything though there are some key questions around contractor solutions:

- **How much can I reduce my tax?** You have the opportunity to reduce your tax through deductions and the way you are paid – each option will result in different amounts of tax.
- **What are the implications?** Is it legal? There are laws and tax rules to consider and some solutions may not be compliant.
- **What are my responsibilities?** You are responsible for ensuring you complete timesheets, but responsibilities such as issuing invoices and chasing payment will depend on the solution you choose.

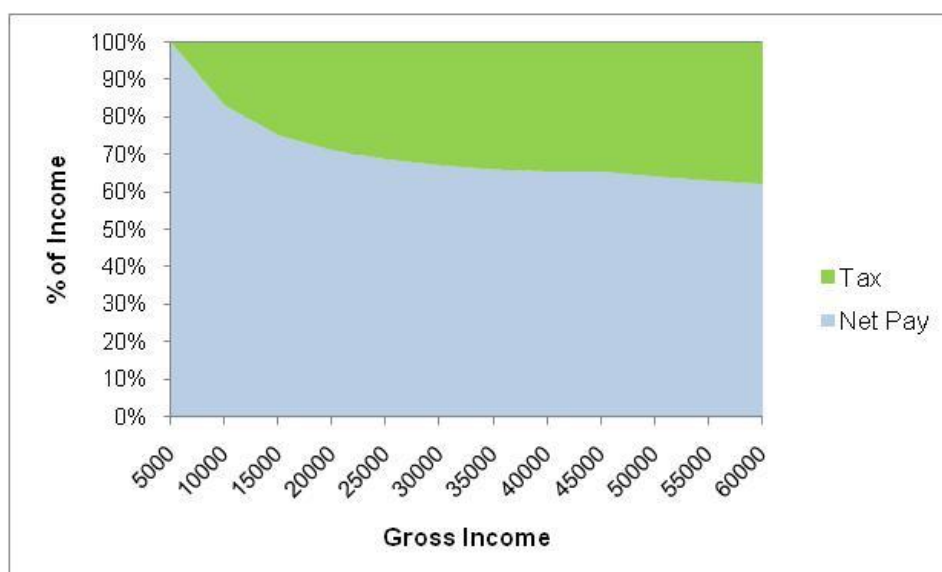
This guide provides information on types of contractor solutions available, so that you can choose the right option for you.

A BRIEF OVERVIEW OF TAX AND NATIONAL INSURANCE

In order to understand the ins and outs of the options, you need to know a little about the UK tax system. There are two types of salary based tax:

1. **National Insurance:** (NI) is paid by both employees and employers. The levy funds state benefits like pensions and unemployment. The employee rate is up to 11% and the employer rate is up to 12.8%.
2. **Pay As You Earn:** (PAYE) works similar to PAYE in NZ and PAYG in Australia. PAYE is calculated based on your gross earnings after the deduction of pension contributions. It is a tiered tax rate system with a top rate of 40%.

The following illustrates your expected take home pay and average tax rate (PAYE and NI) for varying levels of income:





CONTRACTOR SOLUTIONS OPTIONS

When you are contracting you have options as to how and through whom you are paid.

Your options are:

1. 'Umbrella' Company
2. Limited Company
3. Agency PAYE

You need to consider the merits of each option and whether it provides good tax benefits, is legally compliant and minimises your administration effort. Our understanding of how each of the options addresses these attributes is:

	Umbrella Companies	Limited Companies	Agency PAYE
Tax Benefits	✓	✓	✗
Legally Compliant	✓	?	✓
Minimal Administration effort	✓	✗	✓

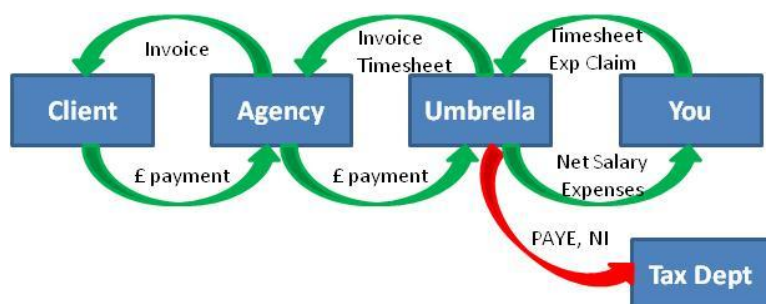
We recommend use of umbrella companies. While offering tax and administration benefits, these products are also compliant with recent changes to the tax rules.

UMBRELLA COMPANY – UMBRELLA BY NAME UMBRELLA BY NATURE

Umbrella companies employ thousands of contractors, taking care of their pay, compliance and administration. Signing with an Umbrella means you become an employee of theirs too.

Umbrella's package your pay to reduce tax

Because you are an employee of the Umbrella (and not the agency or end client) they can package your pay into a combination of salary and non-taxable items such as expenses and other employee benefits. This can commonly save between 25% and 50% of your tax bill.



Little work involved in an Umbrella

An umbrella company will undertake the majority of your administration, compliance and earnings tasks. You typically only need to submit timesheets and provide expenses summaries, the Umbrella does the rest.

Umbrellas comply with all UK legislation

Because you are an employee, Umbrella's protect you from most legislation in the UK such as MSC and IR35 (refer to 'limited companies' for an explanation of these).

Other Advantages of an Umbrella Company:

- Provide for continuous employment (from an administrative perspective) regardless of how many contracts you have, making it easier with visa applications like the HSMP
- No set up or exit fees
- Complies with WHV requirements

Other Disadvantages of an Umbrella Company:

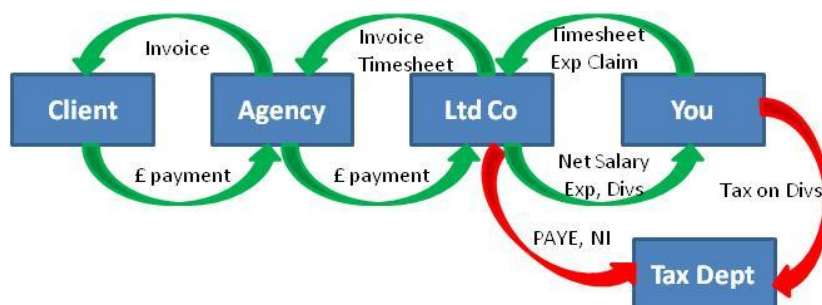
- Tax benefits often less than for a limited company – however this ensures you are tax compliant
- Reduced control – you are effectively an employee and cannot 'custom fit' your solution

LIMITED LIABILITY COMPANY – NOT NECESSARILY LIMITED LIABILITY

Historically the use of limited companies was popular as providers would take care of all the administration and liability. Now new legislation requires you to own, take liability for and run your company using accounting services only as necessary.

Reduces your tax through dividends rather than salary

Companies give you flexibility in how you can structure your earnings due to lower taxes from paying dividends and avoiding National Insurance and PAYE.



Companies are perpetually targeted by the UK Revenue

Two major pieces of legislation have clamped down on companies as a solution for contractors – IR35 and MSC. **IR35** targets people using companies to effectively disguise employment. If caught you must pay tax at the PAYE rate – most Antipodean contractors are caught by IR35. **MSC**, passed in 2007, means no one can manage your company for you and if they do you must pay full tax. As you now must run the company you are also now fully liable.

Limited companies are risky and you should obtain independent (not from your service provider) advice before setting one up.

Visa issues abound

Limited companies can pose difficulties if you require proof of earnings in support of a HSMP visa application or renewal. You cannot set up a limited company on a working holiday visa.

Other Advantages of a Limited Liability Company:

- Can deduct business related expenses
- Full accountability and control

Other Disadvantages of a Limited Liability Company:

- Must operate a separate bank account
- If your accountant (provider) is caught by MSC so are you – even if you did everything by the book, so you must make sure everything is 'whiter than white'

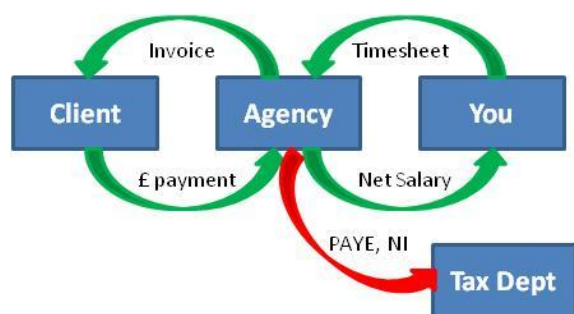
AGENCY PAYE – AND PAYE YOU WILL

If you do not choose a provider you will be paid directly by the Agency who is obligated to ensure that all taxes are deducted prior to you being paid.

No deductions if you go Agency PAYE

You are paid a salary after the deduction of National Insurance (NI) and PAYE. You cannot deduct business related expenses. Agency PAYE provides the lowest net income of the three options.

Your agency will typically pay you this way until such time as you advise them you wish to choose an alternative (umbrella or limited company) solution.



Some companies and agencies will only use Agency PAYE

A small number of hiring companies and agencies require that contractors are paid via Agency PAYE. This is to assure the hiring company or agency that all relevant taxes are being deducted and paid and so no liability exists for them.

Conversely, some agencies do not offer Agency PAYE and as such an alternative contractor solution is required immediately.

Other Advantages of Agency PAYE:

- Simple, with regular administration restricted to completing timesheets
- 100% compliant solution
- There is no fee payable for the processing of Agency PAYE

Other Disadvantages of Agency PAYE:

- Least tax effective option
- Your agency may not offer an Agency PAYE service



CHOOSING THE RIGHT CONTRACTOR SOLUTION PROVIDER

We recommend you don't look solely at the tax savings offered, but also consider the provider reputation, your visa requirements and product simplicity.

While your friends will all have opinions, the responsibility for ensuring you fulfil your tax and compliance responsibilities is yours and solely yours. So choose wisely. With the right decision you will be able to minimise tax and stay compliant with minimal ongoing effort.

We recommend providers that are reputable and who we have received positive feedback on. We will set up a meeting for you with one of these providers as part of our service.

GET IT SORTED QUICKLY

Increased net pay is the main reason for contractor solutions. So, the sooner you get this sorted the sooner you can reap the benefits.

It can be very hectic when you first arrive, meeting with agencies, deciding where to live and catching up with friends. Getting your contracting sorted may not seem a high priority, but it needn't take up much time.

Talk to us to get your preferred option established so you will be able to get the set-up sorted much quicker and get that valuable first pay cheque in your hands.

You may also be able to claim the costs of your relocation to the UK as your first business expense. So keep those receipts...



FREQUENTLY ASKED QUESTIONS

Why are there rules to restrict my use of a company?

Limited Companies were very popular as any payments in the form of a dividend do not attract National Insurance. The rules were introduced to prevent contractors who are in substance in an employment relationship with their client, using a company as a vehicle for avoiding National Insurance and minimising tax.

Can I still operate my own company?

Yes you can. However you need to consider carefully the implications of doing so. See the questions below.

What if I have my own company and do the accounting myself or employ a private accountant?

If you administer your own company or use an accountant who is not an MSC provider, then you will not be impacted by the MSC legislation. But you will need to consider whether you are caught by IR35. If you are, you cannot pay yourself dividends – which is the primary benefit of having a company. In the event of being investigated, the presumption is that you are caught by IR35 unless you can prove otherwise.

Caution should be taken in using a provider who is in the business of providing managed companies under the guise of 'Accounting Services'. Such providers are likely to be targeted by the HMRC.

Who is the HMRC?

HM Revenue & Customs (HMRC) was formed on the 18 April 2005, following the merger of Inland Revenue and HM Customs and Excise Departments. HMRC:

- Collects and administers direct and indirect taxes,
- Pays and administers tax credits, child benefits and child trust funds, and
- Enforces and administers border and frontier protection, environmental taxes, the National Minimum Wage and recovery of student loans.

What is the impact if I do use an MSC Provider?

If you do use an accountant or person who is an MSC provider, you cannot be paid in the form of dividend and instead must be paid a salary with NI and PAYE deducted. Your IR35 status is not relevant under the MSC rules.

Why is an umbrella structure not caught by the MSC rules?

Umbrella companies are specifically allowed within the legislation. Put simply they are not impacted by the rules as contractors within an Umbrella are employees who are paid a tax deducted salary and no dividends.



What is the best solution to stay legal and within the rules?

This really depends on your circumstances. Agency PAYE and traditional umbrella companies effectively act as employees and are not affected by the IR35 or MSC rules, and therefore should be tax compliant. It is worth checking how the umbrella company pays you as some have more complex arrangements that may be considered tax avoidance regimes. Limited companies paying dividends are high risk and you will not be tax compliant if you use an MSC provider or have a contract (or working relationship) which is that of a disguised employee.

I have a Highly Skilled Migrant Programme Visa. How does my payroll solution choice impact my Visa?

The key question here is whether you plan on renewing your Visa. To do so you need proof of sufficient salaried income:

- *Agency PAYE* – As you are paid all your income as a salary, you will be able to prove your income. However, the more contracts you have had with different agencies the more individual tax forms you will need to produce and collate.
- *Limited Company* – This has proved difficult for a number of contractors and we understand that some have not been able to prove a sufficient level of income. You could pay yourself a higher salary and less dividends, however this may mean an umbrella company is better for you as there is less effort required from you. If renewing a HSMP visa is important to you we recommend you either choose another option, or ensure you have fully researched your decision and are confident that your visa renewal will not be compromised. Losing the ability to work in the UK will quickly make any tax gains seem inconsequential.
- *Umbrella Company* – As you are paid a salary you will be able to prove your income. In fact it is administratively simpler, as the Umbrella remains your employer regardless of how many times you contract, you will have continuity of employment and less forms to collate. A small number of umbrella companies may not pay a traditional salary, utilising some form of offshore payment. Be sure to ask if this income source will meet your visa requirements.

How is an umbrella company beneficial when I cannot receive the tax benefits of dividends?

The merits of an Umbrella encompass other financial and non financial benefits:

- Reduced time and effort to administer particularly compared to running your own company. After the initial set-up your only requirement for the Umbrella is to prepare timesheets and expense summaries.
- Financial benefits from the ability to claim expenses under an Umbrella's expense dispensation, plus the bundling of your professional insurances and having one ongoing employment relationship.

An umbrella company is also likely to be your most tax efficient solution if you are caught by IR35.



I am only going to work in the UK for a short time. What type of product is best for me?

Umbrella companies and Agency PAYE do not have set-up costs whereas a company does. This combined with the documentation and effort required to administer then deregister means that it is most likely that Agency PAYE or an umbrella company will be right for you.

I understand I can get a contract that is worded to fall outside of IR35?

You can get a contract with wording that falls outside of IR35. However the HMRC will be interested in substance over form, so if your contract is worded outside of IR35 but the substance of your working relationship is inside IR35, you will most likely be deemed inside IR35 and liable for calculation of taxes on your deemed salary.

When is Agency PAYE right for me?

Agency PAYE is most suitable for you if you do not have the time or inclination to investigate and select an alternative provider or you do not wish to offset expenses against your income. You can take peace of mind that you are meeting your tax obligations.

When is a limited liability company right for me?

A limited liability company will generally be suitable if:

- You have a contract and working relationship that is outside the IR35 rules, thereby enabling you to legitimately pay yourself dividends; and
- You are comfortable with the level of administration and compliance effort required.

However ensure that you do not use an accounting services provider that is an MSC. If you use an MSC, then you will be deemed liable for PAYE and NI, and not eligible to make dividend payments.

When is an umbrella company right for me?

An umbrella company is suitable for any contractor, but is most optimal for you under ANY of the following situations:

- You have a contract or working relationship that is likely to be caught by IR35;
- You are working under a HSP visa which will require renewal;
- You are working and travelling under a WHV; or
- You want to keep your administrative work to a minimum.

What is PAYE?

PAYE (Pay as you Earn) is the income tax paid by all employees in the UK. It is similar to the primary income tax regimes in place in NZ and Australia.



What are the PAYE Tax Rates in the UK?

The UK has a tiered tax system – the more you earn, the higher the tax rate. The rates and thresholds are subject to change, with the thresholds being reviewed each year. For current rates refer to www.HMRC.gov.uk.

What are National Insurance Contributions?

National Insurance is a government scheme where people in work make compulsory contributions which go towards funding the state benefits system in the United Kingdom. These benefits include the UK state pension and the unemployment benefit.

The compulsory contributions are called National Insurance Contributions and are deducted directly from your pay by your employer. These payments are additional to PAYE.

However, just because you pay National Insurance Contributions does not mean that you are entitled to use the benefits system in the United Kingdom that National Insurance funds. The availability of the benefits will depend on your visa status (e.g. working holiday visa holders are not entitled to the unemployment benefit) and the length of time you stay in the UK (e.g. you must live in the UK for 17 of 20 years prior to retirement, to be entitled to the state pension).

Who pays National Insurance Contributions?

Every employee and employer in the UK is responsible for paying National Insurance Contributions as long as the employees pay is over the specified threshold. This means that unlike PAYE, the employer is also paying National Insurance on your pay as well as yourself.

How much are National Insurance Contributions?

That is dependent on your level of salary. The employer pays at a rate of 12.8% of your salary for all earnings you the employee have over the minimum threshold. You, as the employee, also pay National Insurance at a rate of 11% of your earnings between given thresholds plus 1% for earnings above the maximum threshold. For current rates and thresholds refer to www.HMRC.gov.uk.

Why do I need a National Insurance Number?

National insurance numbers are the unique identifier for tax purposes and are legally required if you are in the UK for more than a year. You need to apply for a NI number as soon as you have a job in the UK. If you do not have one, you will be put onto an emergency tax rate, which is higher than you will normally pay.

For more information see www.dwp.gov.uk/lifeevent/benefits/ni_number.asp.

Why do the agencies quote me a PAYE rate and a Company rate?

The company rate is the rate that they would pay to a company you are working through. The PAYE rate is the rate is the same as the company rate but with the employers National Insurance Contributions deducted off by the agency.