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## IR35 - What Will 2012 Bring?!..

Our final piece in 2011 on IR35 was a suggestion to let sleeping dogs lie as compliance activity by HMRC in this area was low; only 23 new enquiries opened in the previous year. This was also on the back of The Office of Tax Simplifications suggestion, which was confirmed by The Chancellor, that there would be no changes to the IR35 legislation.

Whilst there are no changes to the IR35 legislation what we are likely to see in 2012 is a significant change in how HMRC select and target contractors for IR35 enquiries.

We understand that a new process is to be launched which will allow HMRC to send thousands of contractors questionnaires. How you respond to the questionnaires will determine how you are viewed by HMRC from an IR35 risk perspective.

Whilst, in theory, this could allow some contractors to achieve a low risk profiling; as their responses will demonstrate they are 'in business in their own account', it will also mean that thousands will be identified as medium or high risks. Where a contractor is identified as a higher risk this is likely to result in further questions and possibly a formal enquiry in to their IR35 status being opened.

As a direct result we are likely to see a significant increase in compliance activity in this area.

Contractors must remember that HMRC will have the ability to

review past contracts up to at least 6 years ago.

Once the final details are announced and we can assess the impact more fully we will be issuing guidance to contractors. In the meantime we suggest that if you have any doubt about your status you should obtain a professional assignment review.

There are many types of reviews available on the market and we advise that when selecting a provider you obtain written confirmation from them on the following key points:

- What does the review assess - contract only or contract and working arrangements? - we advise that it must assess both the written contract as well as the actual working arrangements and relationship between yourself and the end client.
- Does their review provide a written conclusions report supporting the status outcome reached? - we believe that all providers should supply this so you can demonstrate reasonable care and protect yourself from significant penalties if the status is successfully challenged.
- Can you provide a copy of the report to HMRC if requested? - some providers specifically prohibit you supplying a copy of their report to HMRC and if you do so they claim it voids any insurance you may have.
- Will they defend their position if it is challenged by HMRC? and How much will that defence cost? - many of the top providers will defend their advice to you.

Professional Passport has an arrangement with Bauer and Cottrell to supply assignment reviews to our members which also includes a years free Professional membership - find out more here.

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## Umbrella Charges - Do You Understand What You Are Really Being Charged?

Some umbrella providers have used the changes they have had to introduce as a result of The Agency Workers Regulations to also amend their charging models. This has resulted in confusion and in some cases claims of a lack of transparency; with many contractors unaware of the total charges that are being applied and how these are worked out.

In this article we attempt to explain the charging models in the umbrella market and the difference that each means for contractors.

You will need to understand that the term margin is the terminology used by umbrella providers to describe their income, what you will know as their charges.

The first point to make is that whatever margin an umbrella company feels they wish to apply is not in itself a compliance issue as they are free to set their margin at whatever level they feel they can commercially justify; but remember you have choice and if you don't like the charge or feel it unreasonable you are at will to select a different provider.

In some cases your recruitment company will provide a list of umbrella companies that you must operate through, they too

are perfectly entitled to do this. Usually there will be more than one so whilst you have limited choice you still have a choice if you do not like a particular provider.

This article aims to help you decide whether you feel you are obtaining value for money from a provider by understanding what they are actually charging you which maybe different from what they state their charges to be.

Remember all umbrella companies have to apply the same tax calculations so one of the important considerations is their charges as this will affect what you take home in your pocket.

As highlighted in our Contractors Guide to The Agency Workers Regulations the majority of umbrella companies follow a similar, and widely recognised, process for calculating their workers pay and taxes. In simple terms this can be described as:

Paying the worker the equivalent of National Minimum Wage for the hours worked. Then adding in their holiday pay, expenses reimbursement and a bonus that is calculated as the remainder of any monies after the umbrella has taken their margin and applied the **actual** employers National Insurance costs applying to the pay elements of the workers income.

The key part of this process is that the umbrella applies the 13.8% Employers National Insurance calculation only to those parts of pay that it applies to; ie **NOT** expenses.

continued on page 2 >

## IT Contractors

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It is important to understand that allowable expenses are not earnings and therefore no tax or National Insurance, employers or employees, is payable on any allowable expenses.

Employers National Insurance is charged on weekly earnings in excess of £136 per week.

A new structure that has emerged differs as it applies a charge, equivalent to Employers National Insurance, of 13.8% to monies where Employers National Insurance would not normally apply.

In this new charging regime this basic tax principle seems to be ignored and an equivalent charge of Employers National Insurance is being applied to expenses claimed by workers.

To help clarify this here is an example that shows the difference between the traditional method and an example post AWR charging models.

A worker invoices £1,000, the umbrella weekly margin is £27.50, weekly earnings threshold of £136 applies and the worker has £150 of allowable expenses that can be claimed.

In this example the traditional method of calculating employment costs would be:

$$1000 - 27.50 - 150 - 136 = 686.50$$

Employers National Insurance would apply to the £686.50 at 13.8% giving an actual employment cost of £83.25.

The post AWR increased employment cost calculation applied by some umbrella providers would return:

$$1000 - 27.50 - 136 = 836.50$$

An employment cost of 13.8% would be applied to this giving an actual cost of £101.43.

### An increased cost of £18.18 per week.

This difference is the additional costs to the contractor in using an umbrella that applies this example charging structure; remember these cost are additional to their costs so in the above example

**the actual total cost to the contractor for that week is £45.68.**

These additional costs significantly reduce the benefits when using higher charging umbrellas and in some circumstances could leave you worse off than joining your agency's payroll.

Contractors should ask their umbrella providers to clarify that you are receiving the benefit of the National Insurance savings on all your expenses.

You should ensure that any charges, however described, are clearly presented and explained in their entirety.

There have been a number of threads posted on the forum pages of Contractor UK on this subject.

[forums.contractoruk.com/umbrella-companies](http://forums.contractoruk.com/umbrella-companies)