

YOU AND YOUR FAMILY

# Freelancers and Contractors: Tax, Status and Getting Paid

How to work out whether you are self-employed or an employee for tax, how to choose a way of working, and how to avoid the common traps.

FOR: FREELANCERS, CONTRACTORS AND THE BUSINESSES THAT HIRE THEM • SOME EXPERIENCE

## Employed or self-employed?

Many people now earn a living by selling their time and skills to businesses on a flexible basis: consultants, designers, developers, tradespeople, interim managers, and many more. Whether you are an employee or self-employed matters a great deal: it decides the tax, the national insurance, the rights you have, and the paperwork. The label in the contract does not decide it. What matters is how the relationship works in practice.

### The main tests

- **Control.** Does the client decide how, when and where you do the work, or do you?
- **Substitution.** Can you send someone else to do the work in your place?
- **Mutual obligation.** Must the client offer you work and you accept it?
- **Financial risk.** Do you bear the cost of mistakes and supply your own equipment?
- **Integration.** Are you part of the client's organisation, or in business on your own account?
- **Length and exclusivity.** Is it a series of short projects, or a long-term role for one client?

No one test decides. Courts and HMRC weigh them together. Tax status, employment-law status and status for the off-payroll rules are tested separately, and can give different answers.

## Ways of working

- **Sole trader.** You invoice clients directly, and you are taxed through Self Assessment. Simple, but you are personally liable.
- **Limited company.** You invoice through your own company, and take pay as salary and dividends. You get limited liability and flexibility, with more admin.
- **Umbrella company.** You are employed by a company that invoices the client, and pays you after deductions. Simple, but you receive employee-style treatment.
- **Employee.** If the arrangements are really employment, then you should be on the payroll.

### Who this is for

- Contractors starting out
- Freelancers moving between clients
- Businesses hiring self-employed people

### Key points

- The facts decide status. The contract label does not.
- Different regimes test status separately.
- Larger clients decide status under the off-payroll rules.
- Set tax aside from every invoice.
- Review status when the work changes.

## Off-payroll working

Where you work through your own company, the off-payroll working rules, often called IR35, ask whether you would be an employee of the client if you were engaged directly. If so, the tax and national insurance of an employee must be accounted for. For medium and large private-sector clients, and for the public sector, it is the client who must decide status and tell you the result, with reasons. For small clients, your own company decides. If you disagree with a client's decision, there is a process to challenge it. Ask about the size thresholds that apply.

### Questions to ask

- Who controls how I work?
- Can I send a substitute?
- Do I take financial risk?
- Which way of working suits me?
- Is the client large or small for IR35?
- Have I set tax aside?

## Practical tax points for freelancers

- **Set money aside.** Move a fixed share of each payment into a separate account for tax.
- **Plan for payments on account** under Self Assessment, which can make the second year's bill much larger than the first.
- **Check VAT.** If your income passes the registration threshold, you must register, and the flat-rate scheme may help.
- **Claim your costs** properly. See our guide on business expenses.
- **Save for a pension and for periods without work.** No employer will do it for you.
- **Insurance.** Professional indemnity, public liability and income protection.

## Contracts and getting paid

Agree the scope, the price, the payment terms, who owns what you create and who is responsible if something goes wrong. Invoice promptly, charge late payment interest where it applies, and chase quickly. Late payment is the commonest cause of cash problems for freelancers.

## If you hire freelancers

Make sure the working arrangement is what the contract says. If a freelancer works like an employee, the business can be liable for the tax and national insurance, with penalties. Review long-running engagements, and keep a record of your status decisions.

## Related guides

If this is useful, you may also want:

- Registering your business
- Personal tax planning
- VAT

### How King Street can help

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We help freelancers and contractors choose a structure, set up and run a limited company, deal with off-payroll status questions, plan their tax and pay, and file their returns. For businesses that hire contractors, we review arrangements and advise on status.

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