

FINAL INTERNAL AUDIT REPORT
CHIEF EXECUTIVE'S DEPARTMENT

REVIEW OF COMPLIANCE WITH THE INTERMEDIARIES LEGISLATION (IR35)

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REVIEW OF COMPLIANCE WITH THE INTERMEDIARIES LEGISLATION (IR35)

INTRODUCTION

1. This report sets out the results of our systems based audit of compliance with the Intermediaries Legislation (IR35). The audit was carried out in quarter 3 as part of the programmed work specified in the 2017-18 Internal Audit Plan agreed by the Section 151 Officer and Audit Sub-Committee.
2. The controls we expect to see in place are designed to minimise the Council's exposure to a range of risks. Weaknesses in controls that have been highlighted will increase the associated risks and should therefore be corrected to assist overall effective operations.
3. The original scope of the audit was outlined in the Terms of Reference issued on 30 October 2017.
4. The IR35 is a tax law. It is properly known as the Intermediaries Legislation and came into force in April 2000 as part of the Finance Act. It is designed to combat tax avoidance by workers supplying their services to clients via an intermediary, such as a limited company, but who would be an employee if the intermediary was not used. Such workers are called 'disguised employees' by Her Majesty's Revenue and Customs (HMRC).
5. Public authorities are responsible for deciding if off-payroll working rules apply in the public sector. If the rules apply, the public authority, agency or other third party who is responsible for paying the worker's intermediary must deduct employment tax and Class 1 NICs and pay and report them to HM Revenue and Customs (HMRC).

AUDIT SCOPE

6. The scope of the audit is detailed in the Terms of Reference issued on 30 October 2017.

AUDIT OPINION

7. Overall, the conclusion of this audit was that Substantial Assurance can be placed on the effectiveness of the overall controls. Definitions of the audit opinions can be found in Appendix C.

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MANAGEMENT SUMMARY

8. We confirmed with the Director of HR during our audit that oversight responsibility for compliance with the legislation rests with HR. We established that IR35 assessment checks should be carried out by managers before asking for a new supplier for the engagement of additional resources to be set up by Liberata. Every two months, HR receive a report from the Finance Directorate and check to identify any supplier set up during that period which is a Personal Services Company (PSC) or a self employed worker. HR then establish whether or not an IR35 assessment has been completed by the manager concerned and also a business case completed and signed.
9. HR provided us with information showing that during the period 1 April 2017 to 31 January 2018 there were 3 out of 232 new suppliers set up who were identified by HR as a 'Personal Services Company' or a self employed worker and where an IR35 assessment had not been completed. When these 3 cases were identified, HR informed the appropriate manager and requested that IR35 assessment check was completed, together with a completed and signed business case.
10. We have therefore made a Priority 1 recommendation for HR to remind managers to ensure that IR35 assessment checks on new suppliers of additional resources, to confirm that they are IR35 compliant, are carried out by the relevant managers before they are formally engaged and set up on the Oracle financial system. HR should escalate immediately to the relevant Director any incident of non-compliance identified, to consider what action should be taken.
11. There are also 10 Independent Social Workers (ISWs) whose cases are under consideration. We were informed by HR that these ISWs are part of the sample originally tested by the HMRC and who the HMRC thought should be classed as 'office holders'. There is however no clear rationale for this classification and this has been queried with the HMRC by HR. An officer at HMRC is pursuing the Council's request with the HMRC policy unit that the ISWs are not designated as office holders for IR35 purposes.
12. In the meantime, these 10 ISWs have been paid by invoice through the accounts payable system while awaiting the outcome of the HMRC decision. We were informed by HR that that course of action was agreed by the Deputy Chief Executive and Executive Director of ECHS, Director of Finance and Portfolio Holder for Resources at an ad-hoc meeting held. There are, however, no documented minutes of that meeting available.
13. Controls noted to be in place and working well included:
 - The Council has a defined policy on implementation of IR35;
 - The Council provides training and supporting information to managers on the requirement to comply with IR35;

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- The Council liaises with intermediary agency suppliers to confirm their IR35 arrangements; and
- The Council performs bi-monthly checks of postings to budget codes to identify payments to undisclosed Personal Service Companies.

14. However, we would like to bring to management attention the following issues:

- IR35 assessment checks are not always performed on new suppliers of additional resources prior to them being engaged and set up on the Oracle financial system;
- Guidance and procedure notes relating to compliance with the IR35 legislation do not have review dates or a responsible officer for the documents cited;
- The Council does not maintain a single source record listing all of its agency workers, interims and contractors or Council workers operating as a Personal Services Company (PSC);

SIGNIFICANT FINDINGS (PRIORITY 1)

15. IR35 assessment checks are not always performed on new supplier requests prior to suppliers being set up on the Oracle financial system.

DETAILED FINDINGS / MANAGEMENT ACTION PLAN

16. The findings of this report, together with an assessment of the risk associated with any control weaknesses identified, are detailed in Appendix A. Any recommendations to management are raised and prioritised at Appendix B.

ACKNOWLEDGEMENT

17. Internal Audit would like to thank all staff contacted during this review for their help and co-operation.

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DETAILED FINDINGS

APPENDIX A

No.	Findings	Risk	Recommendation
1	<p><u>Supplier Set-Up</u> Every two months, HR receive a report from the Finance Directorate and check to identify any supplier set up during that period which is a Personal Services Company (PSC).</p> <p>They then establish whether or not an IR35 assessment has been completed by the manager concerned and also a business case completed and signed. This means that IR35 assessment checks are not performed on new supplier requests prior to suppliers being set up on the Finance System.</p> <p>During the period 1 April 2017 to 31 January 2018 there were 3 out of 232 new suppliers set up who were identified by HR as a 'Personal Services Company' and where an IR35 assessment had not been completed.</p> <p>When these 3 cases were identified, HR informed the appropriate manager and requested that an IR35 assessment check was completed, together with a completed and signed business case.</p>	<p>Where there are insufficient controls in place to ensure that the employment status of suppliers are assessed and correctly set up in line with the IR35 requirements, there is the risk of incidents of non-compliance not being addressed.</p>	<p>HR should remind managers to ensure that an IR35 assessment check is carried out on the chosen supplier of a service, by the relevant manager, before the supplier is formally engaged for the role and set up on the Oracle financial system. HR should escalate immediately to the relevant Director any incident of non-compliance identified, to consider what action should be taken.</p> <p>(Priority 1)</p>

Priority 1
 Required to address major weaknesses and should be implemented as soon as possible

Priority 2
 Required to address issues which do not represent good practice

Priority 3
 Identification of suggested areas for improvement

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DETAILED FINDINGS

No.	Findings	Risk	Recommendation
	<p>There were also 10 Independent Social Workers whose cases were under consideration. We were informed by HR that these ISWs were part of the sample originally tested by the HMRC and who the HMRC thought should be classed as 'office holders'. There is, however, no clear rationale for this classification and this has been queried with the HMRC by HR. An officer at HMRC is pursuing the Council's request with the HMRC policy unit that the ISWs are not designated as office holders for IR35 purposes.</p> <p>In the meantime, these 10 ISWs have been paid by invoice through the accounts payable system while awaiting the outcome of the HMRC decision. We were informed by HR that that course of action was agreed by the Deputy Chief Executive and Executive Director of ECHS, Director of Finance and Portfolio Holder for Resources at an ad-hoc meeting held. There are, however, no documented minutes of that meeting available however.</p> <p>There is no requirement in place for Liberata to consider IR35 requirements prior to setting up suppliers on the Finance System.</p>		

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No.	Findings	Risk	Recommendation
2	<p><u>Policies and Procedures</u></p> <p>We noted that there is a manual for the engagement of additional resources and which details the approved procedure to be adopted in the engagement of self-employed individuals, consultants and any other non-standardised workers. This is in draft form having been recently revised, and is currently with the Director of HR for approval.</p> <p>Examination of the manual noted that it is not dated or version controlled.</p> <p>There is also a Managers' Tool Kit in place, which includes practice notes providing guidance on the use of consultants. Examination of the Managers Tool Kit noted that it was last updated in July 2012.</p> <p>The Procedure Guidance Note - Contracting of Professional and Consultancy Services that sets out the stages and process to be followed in the procurement of professional services is not dated or version controlled and, as such, we were unable to determine the age of the document. Examination of the document noted that consideration is not given to compliance with the IR35 requirements.</p>	<p>Where guidance and procedure notes relating to the engagement of self-employed individuals, consultants and any other non-standardised workers are not up to date and do not make appropriate reference to IR35 legislation, there is a risk that tasks are carried out incorrectly resulting in staff not complying with statutory requirements.</p>	<p>The procedure manuals covering key processes relating to the engagement of self-employed individuals, consultants and any other non-standardised workers, should be periodically reviewed to ensure that these are up to date and in line with legislative requirements. All documents should detail the review dates, future review date as well as the officer responsible for the review even when no changes are made. (Priority 2)</p>

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3	<p><u>Records</u> The Contract Procedure Rules, dated October 2016, paragraph 8.6.3 requires that, 'Records of Consultancy appointments shall be kept in accordance with Rule 6.' We established that there is no single source record maintained in the Council listing all its agency workers, interims and contractors or Council workers operating as a Personal Services Company (PSC). In the absence of a single record, managers should be reminded of the need to ensure that local records of these are maintained.</p>	<p>Where the Council does not identify and recognise its off-payroll engagements, there is a risk of off-payroll engagements not being subject to the correct procedures to manage compliance.</p>	<p>In the absence of a single record, managers should be reminded to ensure that local records are maintained of all agency workers not engaged through the agency staff contractor, interims and contractors who are operating as a Personal Services Company (PSC). (Priority 2)</p>

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APPENDIX B

MANAGEMENT ACTION PLAN

Finding No.	Recommendation	Priority *Raised in Previous Audit	Management Comment	Responsibility	Agreed Timescale
1	<p>HR should remind managers to ensure that an IR35 assessment check is carried out on the chosen supplier of a service, by the relevant manager, before the supplier is formally engaged for the role and set up on the Oracle financial system. HR should escalate immediately to the relevant Director any incident of non-compliance identified, to consider what action should be taken.</p>	1	<p>This is the agreed process as defined in the Procedure for the Engagement of Additional Resources. HR will ensure that managers are reminded of the agreed process through publication of the updated and revised version of the Procedure for the Engagement of Additional Resources.</p> <p>It will be reinforced through various communication channels such as Corporate Leadership Team meetings, Managers' Briefings and Inform.</p>	Director of HR	31 May 2018

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MANAGEMENT ACTION PLAN

Finding No.	Recommendation	Priority *Raised in Previous Audit	Management Comment	Responsibility	Agreed Timescale
2	<p>The procedure manuals covering key processes relating to the engagement of self-employed individuals, consultants and any other non-standardised workers, should be periodically reviewed to ensure that these are up to date and in line with legislative requirements.</p> <p>All documents should detail the review dates, future review date as well as the officer responsible for the review even when no changes are made.</p>	2	<p>The Procedure for the Engagement of Additional Resources has been reviewed and updated following the changes in legislation in April 2017. It now contains a review date and future review date. The Director of HR is the responsible officer.</p> <p>HR will put the updated version on the Managers' Tool Kit on OneBromley and liaise with the Commissioning Team to ensure that the 'Procedure Guidance Note - Contracting of Professional and Consultancy Services' is dated, version controlled with responsibility stated and appropriate referenced to IR35 compliance.</p>	Director of HR	31 May 2018

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Finding No.	Recommendation	Priority *Raised in Previous Audit	Management Comment	Responsibility	Agreed Timescale
3	In the absence of a single record, managers should be reminded to ensure that local records are maintained of all agency workers not engaged through the agency staff contractor, interims and contractors who are operating as a Personal Services Company (PSC).	2	HR obtain confirmation from managers using other agencies that they have written evidence that the agency is deducting PAYE and National Insurance. HR will remind managers that local records of all agency workers not engaged through the agency staff contractor, interims and contractors who are operating as a Personal Services Company should be kept and maintained.	Director of HR	31 May 2018

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OPINION DEFINITIONS

APPENDIX C

As a result of their audit work auditors should form an overall opinion on the extent that actual controls in existence provide assurance that significant risks are being managed. They grade the control system accordingly. Absolute assurance cannot be given as internal control systems, no matter how sophisticated, cannot prevent or detect all errors or irregularities.

Assurance Level	Definition
Full Assurance	There is a sound system of control designed to achieve all the objectives tested.
Substantial Assurance	While there is a basically sound systems and procedures in place, there are weaknesses, which put some of these objectives at risk. It is possible to give substantial assurance even in circumstances where there may be a priority one recommendation that is not considered to be a fundamental control system weakness. Fundamental control systems are considered to be crucial to the overall integrity of the system under review. Examples would include no regular bank reconciliation, non-compliance with legislation, substantial lack of documentation to support expenditure, inaccurate and untimely reporting to management, material income losses and material inaccurate data collection or recording.
Limited Assurance	Weaknesses in the system of controls and procedures are such as to put the objectives at risk. This opinion is given in circumstances where there are priority one recommendations considered to be fundamental control system weaknesses and/or several priority two recommendations relating to control and procedural weaknesses.
No Assurance	Control is generally weak leaving the systems and procedures open to significant error or abuse. There will be a number of fundamental control weaknesses highlighted.