



Accountancy Co-operative

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The IR35 5% Expenses Rule

Introduction

Contractors caught by IR35 who use a limited company payment structure need to take into account a HMRC 5% expense allowance rule.

This Help Sheet explains the 5% rule and how it should be applied.

Yearly calculation

Contractors and other service companies which receive income caught by the rules of IR35 must carry out a deemed salary/Schedule E calculation each tax year, based on income received from relevant engagements.

HMRC allow an expense allowance equal to 5% of the income received from relevant engagements in calculating the deemed salary. This is intended to cover the following 'administration' costs where applicable:

- Premises costs including home as office
- Administration and secretarial support
- Accountancy and tax advice
- Costs of seeking contracts
- Printing, postage and stationery
- Employer's and Public Liability Insurance
- Training costs
- Computer equipment (if not eligible for capital allowances)
- Bank and overdraft interest
- Hire purchase payments

The 5% deduction is given at a flat rate on gross fees receivable and is not available to employees as an expense, which they can draw from the company.

It is simply allowed in the deemed calculation of IR35 salary as a fixed and limited claim against the above expenses.

In granting the 5% allowance, HMRC do not require proof of expenditure and the full 5% is granted, even if there is no actual expenditure whatsoever.



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Other expenses

Note that the 5% allowance is only for "administration" and is to cover the ten points above. In addition to the 5% for administration costs, a contractor can also claim direct costs such as travel (trains etc), computer costs (Laptop etc), subsistence (food and accommodation when travelling overnight, or away from your HOME/OFFICE, direct training, sub contractors, etc.

Allowances for corporation tax

The 5% is in respect of the deemed salary calculation only and is not taken into account when preparing the company's accounts and corporation tax computation.

The company accounts will take into account the actual expenses only, which may be higher or lower than the 5% allowance.

Contractors using PAYE Umbrellas

If a contractor is caught by IR35 and using a PAYE umbrella, then the 5% rule is unlikely to apply, since they will not have "administration" expenses, apart from the umbrella company fee which is deducted from the salary in any event.

The actual costs of travel, subsistence, computers, etc., can be claimed in full and tax/national insurance relief obtained on them.



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