I’d like to explore some of the problems a practice owner might face if one of their associates turned out to be an employee. It may be putting the cart before the horse to look at problems before examining the causes, but it will help focus on the importance of getting the principal/associate legal relationship right, at the outset.

An increasing number of associates, who although their status has apparently been that of self-employed, are raising employment law claims that might not be possible if they were self-employed. A reduced number of associateship posts, commercial pressures on practices, and a heightened awareness of legal rights, are all beginning to raise question marks about the legal status of some associateship arrangements.

There are also significant tax implications for practice owners, when it turns out that a self-employed taxpayer should have been subject to the PAYE scheme. Many practice owners are aware of such potential problems that may exist with self-employed hygienists and therapists, but how much longer will it be before HM Revenue and Customs (HMRC) start to eye-up the legal and tax status of some associates?

Against a background of high public expenditure and reduced tax revenues, and with the likelihood of such pressures continuing for some time in the future, can we expect to see HMRC starting to raise challenges to the tax status of self-employed associates?

The employer’s position

Problems employers face where such challenges are mounted include HMRC trying to revisit the tax position by re-categorising the self-employed individual as an employee and seeking to levy extra tax, going back up to six years (or more in some cases).

Indeed, following the Demi-bourne case, (which involved a self-employed worker who, the Special Commissioner decided was in fact an employee) it was held that, in such cases, the whole amount of back-tax and National Insurance (NI) con-
Contributions over the period of ‘self-employment’, was due from the employer. No credit was given for the tax and NI that the worker had already paid.

Some light relief
Some relief from this draconian state of affairs was reached in April 2008 when the Income Tax (PAYE) Amended Regulations 2008 came into effect. These regulations enable HMRC to issue directions, both to the employer and the employee concerned, so that where an employee has paid tax on earnings under self-assessment (rather than PAYE), then the employee may be able to claim some PAYE credit and the employer may be relieved of some PAYE liability for the amount of tax specified in the direction. However, practice owners who find themselves in this situation still face the problem that:

1. A direction by HMRC will not cover any penalties for which the employer may be liable for breaches of the PAYE Regulations (by not making the PAYE deductions) (although, fortunately, no interest will be charged)
2. There are likely to be limits to the amounts of such credits.

Since one of the perceived advantages of associates being self-employed is a favourable tax regime, it is quite likely that there will be excess to be paid by the practice owner.

NI shortfalls
The other problem that practice owners face in such circumstances is that the regulations only cover PAYE. They do not cover NI shortfalls, which will also have to be made up by owners. And of course, HMRC may decline to make the appropriate directions, and seek to collect the whole of the tax from the employer (which they can do in certain circumstances).

If HMRC does collect all the outstanding tax and NI contributions from the practice owner, you might think that all the practice owner has to do is recover it from the (usually former) employee/associate. Think again – surprisingly it is not entirely clear whether a practice owner does have a legal right to make such a recovery.

Of course, the associateship agreement may contain a contractual provision to enable recovery. However, if there is no such written agreement, although there is some recent case law to suggest that the practice owner might have the right to require ‘restitution’, from the former employee/associate, the process is still unclear (and potentially legally expensive). The position about the recovery of NI contributions is even less clear.

Suitable arrangements
It is not all doom and gloom on the horizon, though. Provided that there are properly and carefully considered (and the strong advice is – written) arrangements in place to ensure the legal and tax status of the parties, then these problems may be avoided.

The next article in the series will explore some of the employment law implications when an associate claims to be an employee.

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